VOLUME 17

Minimum Filing Requirements (G)

AQUA PENNSYLVANIA, INC. & AQUA PENNSYLVANIA WASTEWATER, INC.

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AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR1. Provide capitalization and capitalization ratios for the last 5-year period and projected through the next 2 years (with short-term debt and without short-term debt) for the company, parent and consolidated system.

a. Provide year-end interest coverages before and after taxes for the last 3 years and at the latest date, including indenture and Securities and Exchange Commission (SEC) bases, for the company, parent and consolidated system.

b. Provide year-end preferred stock dividend coverages for the last 3 years and at latest date, including charter and SEC bases.

A. Please see attached Schedule RR1(a) that shows the capitalization and capitalization ratios for the last five-year period (2016-2020) with short-term debt and without short-term debt for the Company, Parent and consolidated system. The forecasts related to the Company for 2021 and 2022 are included. The forecasts related to the Parent and consolidated system for 2021 and 2022 are not available at the present time.

a. Please see attached Schedule RR1(b) that provides year-end interest coverage before and after taxes for the last three years (2018-2020), including Indenture and SEC Bases, for the Company, Parent and consolidated system.

b. There is no preferred stock outstanding for the Company, Parent and consolidated system for the last three years.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
CAPITALIZATION RATIOS

	Actual 12/31/2016		Actual 12/31/2017		Actual 12/31/2018		Actual 12/31/2019		Actual 12/31/2020		Forecast 12/31/2021		Forecast 12/31/2022	
	$	%	$	%	$	%	$	%	$	%	$	%	$	%
Aqua Pennsylvania, Inc.														
Long-term debt (incl. current portion)	1,203,859	45.8%	1,336,761	46.4%	1,487,789	46.5%	1,704,474	48.6%	1,827,113	48.2%	1,915,692	43.8%	2,132,234	45.5%
Short-term debt	5,545	0.2%	3,650	0.1%	15,449	0.5%	25,724	0.7%	49,198	1.3%	50,000	1.1%	50,000	1.1%
	1,209,404	46.0%	1,340,411	46.6%	1,503,237	47.0%	1,730,198	49.4%	1,876,311	49.5%	1,965,692	45.0%	2,182,234	46.6%
Preferred Equity	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Common Equity (incl. minority int.)	1,419,693	54.0%	1,538,172	53.4%	1,695,380	53.0%	1,775,110	50.6%	1,911,851	50.5%	2,403,212	55.0%	2,501,422	53.4%
	2,629,097	100.0%	2,878,583	100.0%	3,198,617	100.0%	3,505,308	100.0%	3,788,162	100.0%	4,368,904	100.0%	4,683,656	100.0%
Excl short-term debt														
Long-term debt (incl. current portion)	1,203,859	45.9%	1,336,761	46.5%	1,487,789	46.7%	1,704,474	49.0%	1,827,113	48.9%	1,915,692	44.4%	2,132,234	46.0%
Preferred equity	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Common Equity (incl. minority int.)	1,419,693	54.1%	1,538,172	53.5%	1,695,380	53.3%	1,775,110	51.0%	1,911,851	51.1%	2,403,212	55.6%	2,501,422	54.0%
	2,623,552	100.0%	2,874,933	100.0%	3,183,169	100.0%	3,479,584	100.0%	3,738,964	100.0%	4,318,904	100.0%	4,633,656	100.0%
Essential Utilities, Inc. (Parent)														
Long-term debt (incl. current portion)	509,867	21.6%	528,758	21.3%	438,760	17.9%	712,371	15.5%	1,043,427	18.2%	N/A	N/A	N/A	N/A
Short-term debt	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	N/A	N/A	N/A	N/A
	509,867	21.6%	528,758	21.3%	438,760	17.9%	712,371	15.5%	1,043,427	18.2%	N/A	N/A	N/A	N/A
Preferred Equity	-	-	-	-	-	-	-	-	-	-	N/A	N/A	N/A	N/A
Common Equity (incl. minority int.)	1,850,068	78.4%	1,957,621	78.7%	2,009,363	82.1%	3,880,860	84.5%	4,683,877	81.8%	N/A	N/A	N/A	N/A
	2,359,935	100.0%	2,486,379	100.0%	2,448,123	100.0%	4,593,231	100.0%	5,727,304	100.0%	N/A	N/A	N/A	N/A
Excl short-term debt														
Long-term debt (incl. current portion)	509,867	21.6%	528,758	21.3%	438,760	17.9%	712,371	15.5%	1,043,427	18.2%	N/A	N/A	N/A	N/A
Preferred equity	-	-	-	-	-	-	-	-	-	-	N/A	N/A	N/A	N/A
Common Equity (incl. minority int.)	1,850,068	78.4%	1,957,621	78.7%	2,009,363	82.1%	3,880,860	84.5%	4,683,877	81.8%	N/A	N/A	N/A	N/A
	2,359,935	100.0%	2,486,379	100.0%	2,448,123	100.0%	4,593,231	100.0%	5,727,304	100.0%	N/A	N/A	N/A	N/A
Essential Utilities, Inc. (Consolidated)														
Long-term debt (incl. current portion)	1,910,633	50.7%	2,143,127	52.2%	2,563,660	55.9%	3,077,400	44.1%	5,630,243	54.2%	N/A	N/A	N/A	N/A
Short-term debt	6,535	0.2%	3,650	0.1%	15,449	0.3%	25,724	0.4%	78,198	0.8%	N/A	N/A	N/A	N/A
	1,917,168	50.9%	2,146,777	52.3%	2,579,109	56.2%	3,103,124	44.4%	5,708,441	54.9%	N/A	N/A	N/A	N/A
Preferred Equity	-	0.0%	-	0.0%	-	0.0%	-	0.0%	-	0.0%	N/A	N/A	N/A	N/A
Common Equity (incl. minority int.)	1,850,068	49.1%	1,957,621	47.7%	2,009,363	43.8%	3,880,860	55.6%	4,683,877	45.1%	N/A	N/A	N/A	N/A
	3,767,236	100.0%	4,104,398	100.0%	4,588,472	100.0%	6,983,984	100.0%	10,392,318	100.0%	N/A	N/A	N/A	N/A
Excl short-term debt														
Long-term debt (incl. current portion)	1,910,633	50.8%	2,143,127	52.3%	2,563,660	56.1%	3,077,400	44.2%	5,630,243	54.6%	N/A	N/A	N/A	N/A
Preferred equity	-	-	-	-	-	-	-	-	-	-	N/A	N/A	N/A	N/A
Common Equity (incl. minority int.)	1,850,068	49.2%	1,957,621	47.7%	2,009,363	43.9%	3,880,860	55.8%	4,683,877	45.4%	N/A	N/A	N/A	N/A
	3,760,701	100.0%	4,100,748	100.0%	4,573,023	100.0%	6,958,260	100.0%	10,314,120	100.0%	N/A	N/A	N/A	N/A

AQUA PENNSYLVANIA, INC. **Schedule RR1(b)**
2021 RATE CASE
INTEREST COVERAGES - INDENTURE & SEC BASIS

	Yr Ended		
	2020	2019	2018
Aqua Pennsylvania, Inc.			
Interest Coverage - Indenture Basis - Before Tax	3.78	3.57	3.79
Interest Coverage - SEC Basis - Before Tax	3.52	3.45	3.60
Interest Coverage - Indenture Basis - After Tax	3.77	3.87	4.12
Interest Coverage - SEC Basis - After Tax	3.52	3.74	3.92
Aqua America, Inc. (Parent)			
Interest Coverage - Indenture Basis - Before Tax	N/A	N/A	N/A
Interest Coverage - SEC Basis - Before Tax	(4.34)	(8.68)	(15.62)
Interest Coverage - Indenture Basis - After Tax	N/A	N/A	N/A
Interest Coverage - SEC Basis - After Tax	(4.52)	(2.24)	(13.80)
Aqua America, Inc. (Consolidated)			
Interest Coverage - Indenture Basis - Before Tax	5.44	4.45	4.74
Interest Coverage - SEC Basis - Before Tax	3.29	2.74	3.30
Interest Coverage - Indenture Basis - After Tax	7.77	4.62	4.94
Interest Coverage - SEC Basis - After Tax	3.29	2.82	3.40

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR2. Provide latest prospectus for the company and the parent.

A. There is no Prospectus for the Company. Please see the attached for the latest Prospectus for the Parent, Aqua America, Inc.

PROSPECTUS

ESSENTIAL UTILITIES, INC.

Dividend Reinvestment and Direct Stock Purchase Plan

6,000,000

Shares of Common Stock

- The Plan gives you a convenient, systematic way to purchase or invest in our common stock.
- You can increase your ownership by reinvesting dividends at a discount of between 0% and 5.0%, as designated from time to time in our sole discretion, and by making optional cash investments with brokerage fees and commissions paid by us.
- You do not need to be one of our existing shareholders to participate in the Plan.
- You can own and transfer shares without holding certificates.
- You can purchase shares through an IRA with a portion of the annual maintenance fee paid by us.

IMPORTANT NOTE: Sales of shares through the Plan are subject to fees and commission charges for which you will be responsible. Please see the "Costs" section of this prospectus for further details regarding these fees and commission charges.

Our common stock is listed on the New York Stock Exchange under the symbol "WTRG." Our principal executive office is located at 762 W. Lancaster Avenue, Bryn Mawr, Pennsylvania 19010-3489 and our telephone number is 610-527-8000.

Investing in our common stock involves risk. See "Risk Factors" on page 2 for certain risks to consider before participating in the Plan or purchasing shares of our common stock.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is July 24, 2020.

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Essential Utilities, Inc. (“we”, “us”, “our”, “Registrant” or the “Company”), a Pennsylvania corporation, is the holding company for regulated utilities providing water, wastewater, or natural gas services to what we estimate to be almost five million people in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana, Virginia, West Virginia, and Kentucky under the Aqua and Peoples brands. One of our largest operating subsidiaries, Aqua Pennsylvania, Inc., provides water or wastewater services to approximately one-half of the total number of water or wastewater customers we serve, who are located in the suburban areas in counties north and west of the City of Philadelphia and in 27 other counties in Pennsylvania. Our other regulated water or wastewater utility subsidiaries provide similar services in seven other states. Additionally, pursuant to the Company’s growth strategy, commencing on March 16, 2020, with the completion of the acquisition of the Peoples Gas companies, the Company began to provide natural gas distribution services to customers in western Pennsylvania, Kentucky, and West Virginia. Approximately 93% of the total number of natural gas utility customers we serve are in western Pennsylvania. Lastly, the Company’s market-based activities are conducted through Aqua Infrastructure, LLC and Aqua Resources, Inc. and certain other subsidiaries of Peoples Gas. Aqua Infrastructure provides non-utility raw water supply services for firms in the natural gas drilling industry.

PLAN OVERVIEW

The Essential Utilities, Inc. Dividend Reinvestment and Direct Stock Purchase Plan (the "Plan") provides you with a convenient and economical way to purchase shares of our common stock and to reinvest your cash dividends in additional shares. The Plan has various features and you can select those features that meet your investment needs.

The Plan is designed for long-term investors who wish to invest and build their share ownership over time. Unlike an individual stock brokerage account, the timing of purchases and sales is subject to the provisions of the Plan.

Please read this prospectus and the documents incorporated by reference herein carefully. If you are a shareholder of record of at least 5 shares of Essential Utilities common stock and wish to participate in the Plan, please sign and execute a Dividend Reinvestment and Direct Stock Purchase Plan Enrollment Form (the "Enrollment Form"). If your shares of Essential Utilities common stock are registered in a nominee name (such as in the name of a bank, broker or other nominee), please see the "Participation and Enrollment" section below for instructions on how to have such shares participate in the Plan. Investors wishing to make an initial investment of not less than $500 should complete the Dividend Reinvestment and Direct Stock Purchase Plan Initial Enrollment Form (the "Initial Enrollment Form"). When completed, the form should be mailed to Computershare Trust Company, N.A. (the "Administrator"). Employees of Essential Utilities who wish to pay for their investment by having a portion of their compensation withheld and applied to the investment should complete the Employee Enrollment Form provided by the Company.

You can also enroll in the Plan and access your Plan account through the Internet at the Administrator's web site, *www.computershare.com/investor*, at any time. In addition, you can authorize one-time initial and subsequent optional cash investments or establish recurring automatic withdrawals from your U.S. bank account.

RISK FACTORS

Investing in our common stock involves risks. Please see the risk factors described in our Annual Report on Form 10-K for the fiscal year ended December 31, 2019, filed with the Securities and Exchange Commission (the "SEC"), and are Quarterly Report on Form 10-Q for the quarter ended March 31, 2020, filed with the SEC, which are all incorporated by reference in this prospectus. Before making an investment decision, you should carefully consider these risks as well as other information contained or incorporated by reference in this prospectus.

FORWARD-LOOKING STATEMENTS

Certain statements in this prospectus, or incorporated by reference into this prospectus, are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 that are made based upon, among other things, our current assumptions, expectations, plans, and beliefs concerning future events and their potential effect on us. These forward-looking statements involve risks, uncertainties and other factors, many of which are outside our control that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. In some cases you can identify forward-looking statements where statements are preceded by, followed by or include the words "believes," "expects," "anticipates," "plans," "future," "potential," "probably," "predictions," "intends," "will," "continue" "in the event" or the negative of such terms or similar expressions. Forward-looking statements in this prospectus, or incorporated by reference into this prospectus, include, but are not limited to, statements regarding:

- recovery of capital expenditures and expenses in rates;
- projected capital expenditures and related funding requirements;
- our capability to pursue timely rate increase requests;
- expectations regarding the impact of the acquisition of Peoples Gas, including statements regarding the impact of the transaction on the Company;
- developments, trends and consolidation in the water, wastewater and natural gas utility and infrastructure industries;
- opportunities for future acquisitions, both within and outside the water, wastewater and natural gas industries, the success of pending acquisitions and the impact of future acquisitions;
- the capacity of our water and natural gas supplies and facilities;
- the availability and cost of capital financing;
- dividend payment projections;
- the impact of geographic diversity on our exposure to unusual weather;
- the impact of conservation awareness of customers and more efficient fixtures and appliances on water usage and gas consumption per customer;
- our authority to carry on our business without unduly burdensome restrictions;

- the continuation of investments in strategic ventures;
- our ability to obtain fair market value for condemned assets;
- the impact of fines and penalties;
- the impact of changes in and compliance with governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- the impact of decisions of governmental and regulatory bodies, including decisions to raise or lower rates and decisions regarding potential acquisitions;
- the development of new services and technologies by us or our competitors;
- the availability of qualified personnel;
- the condition of our assets;
- the impact of legal proceedings;
- general economic conditions;
- acquisition-related costs and synergies;
- the sale of water and wastewater divisions;
- the impact of federal and/or state tax policies and the regulatory treatment of the effects of those policies;
- the amount of income tax deductions for qualifying utility asset improvements and the Internal Revenue Service's ultimate acceptance of the deduction methodology; and
- the impact of COVID-19 or the measures implemented by the Company as a result of COVID-19.

Because forward-looking statements involve risks and uncertainties, there are important factors that could cause actual results to differ materially from those expressed or implied by these forward-looking statements, including but not limited to:

- the diversion of our management's time and resources caused by integration efforts with respect to the Peoples Gas acquisition;
- our ability to manage the expansion of our business, including integrating the Peoples Gas acquisition;
- our ability to treat and supply water or collect and treat wastewater;
- our ability to source a sufficient supply of natural gas to meet demands of our gas utility customers in a timely manner;
- the continuous and reliable operation of our information technology systems, including the impact of cyber security attacks or other cyber-related events;
- changes in general economic, business, credit and financial market conditions;

- changes in governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- changes to the rules or our assumptions underlying our determination of what qualifies for an income tax deduction for qualifying utility asset improvements;
- the decisions of governmental and regulatory bodies, including decisions on rate increase requests;
- our ability to file rate cases on a timely basis to minimize regulatory lag;
- abnormal weather conditions, including those that result in water use restrictions and seasonality effects;
- changes in, or unanticipated, capital requirements;
- changes in our credit rating or the market price of our common stock;
- changes in valuation of strategic ventures;
- the phase-out of LIBOR, or the replacement of LIBOR with a different reference rate or modification of the method used to calculate LIBOR which may adversely affect interest rates;
- our ability to integrate businesses, technologies or services which we may acquire;
- our ability to treat and supply water or collect and treat wastewater;
- the extent to which we are able to develop and market new and improved services;
- the effect of the loss of major customers;
- our ability to retain the services of key personnel and to hire qualified personnel as we expand;
- labor disputes;
- increasing difficulties in obtaining insurance and increased cost of insurance;
- cost overruns relating to improvements to, or the expansion of, our operations;
- increases in the costs of goods and services and commodity prices;
- civil disturbance or terroristic threats or acts;
- changes in accounting pronouncements;
- litigation and claims;
- changes in environmental conditions, including the effects of climate change;
- restrictions on our subsidiaries' ability to make dividends and other distributions; and
- impacts from the global outbreak of COVID-19, including on consumption and collections.

Given these risks and uncertainties, you should not place undue reliance on any forward-looking statements. You should read this prospectus and the documents that we incorporate by reference into this prospectus completely and with the understanding that our actual future results, performance and achievements may be materially different from what we expect. These forward-looking statements represent assumptions, expectations, plans, and beliefs only as of the date of this prospectus. Except for our ongoing obligations to disclose certain information under the federal securities laws, we are not obligated, and assume no obligation, to update these forward-looking statements, even though our situation may change in the future. As you read this prospectus and the documents that we incorporate by reference into this prospectus, you should pay particular attention to the "Risk Factors" included in our most recent Annual Report on Form 10-K and in any filing we make with the SEC after the date of such Annual Report on Form 10-K that is incorporated by reference into this prospectus. We qualify all of our forward-looking statements by these cautionary statements.

A SUMMARY OF IMPORTANT PLAN FEATURES

- *Participation*. You may participate in the Plan if you own at least 5 shares of Essential Utilities common stock that are registered in your name. You may also participate by making an initial minimum investment of at least $500 through automatic withdrawal from your U.S. bank account, by check or by a one-time online bank debit through the Administrator's web site, *www.computershare.com/investor*. Employees of Essential Utilities who wish to pay for their investment by having a portion of their compensation withheld and applied to the investment should complete the Employee Enrollment Form provided by the Company. All U.S. citizens are eligible to join the Plan, whether or not they are currently shareholders. Foreign citizens are eligible to participate as long as their participation would not violate any laws in their home countries or other non-U.S. laws. If your shares of Essential Utilities common stock are registered in a nominee name (such as in the name of a bank, broker or other nominee), please see the "Participation and Enrollment" section below for instructions on how to have such shares participate in the Plan.

- *Automatic Dividend Reinvestment*. You can reinvest all or a portion of the cash dividends received on your first 100,000 shares toward the purchase of additional shares of our common stock, without paying trading fees or commissions. For purposes of the Plan, the term "full dividend reinvestment" means the reinvestment of dividends on all shares held by you in your name under the Plan up to a maximum of 100,000 shares.

- *Electronic Deposit of Cash Dividends*. You can authorize the Administrator to deposit your cash dividends directly into your U.S. bank account.

- *Optional Cash Investments*. As a shareholder, you can buy additional shares of our common stock at any time for as little as $50. The maximum optional cash investment you may make in any calendar year is $250,000. You can pay by check or by a one-time online bank debit through the Administrator's web site, *www.computershare.com/investor*, or have your payment automatically withdrawn from your U.S. bank account. Employees of Essential Utilities who wish to make optional cash investments should complete the Employee Enrollment Form provided by the Company.

- *IRAs*. You may establish a traditional IRA, a Roth IRA or a Coverdell Education Savings Account, which invests in common stock through the Plan. IRA contributions and rollovers do not count against a participant's $250,000 annual investment limitation. There is an annual maintenance fee of forty-five dollars ($45.00) charged by the IRA and Coverdell Education Saving Account Trustee, which we will pay for the first calendar year in which you participate. In all subsequent years, twenty-five dollars ($25.00) of this annual fee will be charged to you, with the balance paid by us.

- *Full Investment*. Full investment of your funds is possible because any initial investment and optional cash investments will be used to buy whole and fractional shares. In addition, the full dividend earned on your shares (up to the first 100,000 shares you own), including fractional shares, will be reinvested or paid out as you designate.

- *Safekeeping of Certificates*. Shares purchased through the Plan for which you request certificates to be issued will be held by the Administrator for safekeeping. You may also deposit any Essential Utilities, or previously named Aqua America, Inc. or Philadelphia Suburban Corporation, stock certificates that you hold for safekeeping, at no charge.

- *Transaction Reporting*. You will receive a statement following each transaction showing the details of, and your share balance in, your Plan account.

- *Internet Account Access*. You can also enroll in the Plan and access your Plan account through the Internet at the Administrator's web site, *www.computershare.com/investor*, at any time. In addition, you can authorize one-time initial and subsequent optional cash investments or establish recurring automatic withdrawals from your U.S. bank account.

ADMINISTRATION

Computershare Trust Company, N.A., administers the Plan and acts as Agent for the participants. Computershare, Inc. acts as service agent to Computershare Trust Company, N.A. in performing certain services for the Plan. These companies purchase and retain shares of our common stock for Plan participants, keep records, send statements and perform other duties required by the Plan.

For information about the Plan, you can contact the Administrator by calling toll-free:

Computershare Trust Company, N.A.	800-205-8314
Outside the United States call collect:	781-575-3100
web site address:	*www.computershare.com/investor*

All written correspondence and optional cash investments submitted without a proper investment coupon, should be submitted to:

By mail:	Computershare Trust Company, N.A. Attn.: Essential Utilities, Inc. Dividend Reinvestment and Direct Stock Purchase Plan P.O. Box 505000 Louisville, KY 40233-5000
By courier:	Computershare Trust Company, N.A. Attn.: Essential Utilities, Inc. Dividend Reinvestment and Direct Stock Purchase Plan 462 South 4th Street, Suite 1600 Louisville, KY 40202

You can contact the Essential Utilities, Inc. IRA Program Administrator by calling toll free 1-800-597-7736. All written correspondence concerning the IRA Program, should be submitted to:

By mail:	The IRA Program C/O Computershare Trust Company, N.A. P.O. Box 2175 Milwaukee, WI 53201-2175
By courier:	The IRA Program C/O Computershare Trust Company, N.A. Attn.: Essential Utilities, Inc. IRA 235 W. Galena Street Milwaukee, WI 53212-3948

Make checks payable to "Computershare-Essential Utilities" in U.S. dollars and drawn on a U.S. bank. The Administrator will not accept cash, traveler's checks, money orders or third party checks for optional cash investments. Please use the cash investment form at the bottom of your statement.

INTERNET ACCESS

You can also obtain information about your account via the Internet at the Administrator's web site, *www.computershare.com/investor*. At the web site, through Investor Center, you can access your share balance, enroll in the Plan, purchase shares (either as a one-time online bank debit or by recurring automatic monthly withdrawals from your U.S. bank account), sell shares, request a stock certificate, change dividend payment options and obtain online forms. To obtain access, click Create Log In, fill in the required information, accept the Terms & Conditions and select a User ID and password.

PARTICIPATION AND ENROLLMENT

If you already own at least 5 shares of our common stock, you are eligible to participate in the Plan.

- If your shares are registered in your name, you can enroll in the Plan through the Internet at the Administrator's web site, *www.computershare.com/investor*, or you can fill out the Enrollment Form and return it to the Administrator.

- If your shares are registered in a nominee name but you wish to participate in the Plan you should instruct your bank, broker or other nominee to have some or all of your shares registered in your name. Simply instruct your bank, broker or other nominee to transfer at least 5 of your shares of our common stock electronically through the Direct Registration System from your brokerage account to a new book-entry account at the Administrator. Please contact your bank, broker or other nominee for more information. Once at least 5 of your shares of our common stock are moved from your brokerage account to a new book-entry account registered in your name with the Administrator, you may then participate in the Plan by enrolling in the Plan as set forth above. Alternatively, you may instruct your bank, broker or other nominee to arrange to have a paper stock certificate issued to you for at least 5 of your shares of our common stock. Once at least 5 shares are registered in your name, you may participate in the Plan by enrolling in the Plan as set forth above. If the shares that you hold are in certificated form, you can deposit these certificated shares in your Plan account for safekeeping. In each instance, any fees or charges assessed by your bank or broker are your responsibility and will not be paid by us.

- If your shares are held through our retirement plans or any of our other employee benefit plans (each, an "employee benefit plan") that participate in the Plan, your participation in the Plan will be through the administrator or trustee of the applicable employee benefit plan and you will be limited to the automatic dividend reinvestment feature of the Plan only. Please contact the administrator or trustee of the employee benefit plan to determine if the plan participates in the Plan. Your participation in the Plan will be subject to the terms and conditions of the applicable employee benefit plan and the administrator or trustee of such plan.

If you do not own any shares of our common stock, or if you wish to establish a separate account, you can go to the Administrator's website, *www.computershare.com/investor*, and follow the instructions provided. You may enroll in the Plan by authorizing a one-time online bank debit from your U.S. bank account for an initial investment of at least $500 or by establishing recurring automatic withdrawals from your U.S. bank account for a minimum of $50 per transaction for at least ten consecutive months. Automatic withdrawal is further described in the "Optional Cash Investments" section of this prospectus. You can also fill out the Initial Enrollment Form and return it to the Administrator. Enclose a check, in U.S. dollars, for at least $500 or, if you are an employee of Essential Utilities and wish to pay for your purchases through the withholding of compensation, fill out the Employee Enrollment Form provided to you by the Company. You can receive an Initial Enrollment Form by contacting the Administrator through the channels outlined in the "Administration" section of this prospectus. If you wish to make your initial investment through automatic withdrawals, you must agree to continue with the withdrawals until the $500 minimum initial investment is reached. Please note, such automatic withdrawals continue indefinitely beyond the initial investment until you notify the Administrator through the Internet, by telephone or in writing to stop such automatic withdrawals.

If you open an account for another person by transferring stock from your account, you must transfer a minimum of 5 shares into that account.

DIVIDEND REINVESTMENT

You may choose to reinvest all or a portion of the dividends paid on your first 100,000 shares of our common stock held in your Plan account or participating in the Plan through our employee benefit plans. Your dividends will be used to buy additional shares of our common stock at a discount between 0% and 5.0%, as designated from time to time by us prior to the purchase of the shares with the reinvested dividends, from the prevailing market price. You have the following options for your dividends:

- *Full Dividend Reinvestment*. Your cash dividends received on shares you own up to 100,000 shares will be used to buy additional shares for you.

- *Partial Dividends Paid in Cash*. If you do not want full dividend reinvestment, select a lower number of full shares on which you want your dividends to be paid in cash. The balance of your dividends will be reinvested.

- *All Dividends Paid in Cash (no dividend reinvestment)*. Your dividends on all of your shares will be paid in cash.

If you do not indicate which reinvestment option you want on the enrollment form, you will be automatically enrolled in full dividend reinvestment.

You may change your reinvestment option at any time by completing and returning a new Enrollment Form (which can be obtained by contacting the Administrator), by accessing your Plan account through the Internet at the Administrator's web site, *www.computershare.com/investor*, by calling the Administrator at 1-800-205-8314 or

by providing written instructions to the Administrator. Dividends will be reinvested or paid on cash in accordance with your most recent instructions received by the Administrator prior to the dividend record date applicable to such dividend.

The 100,000 share reinvestment limitation does not apply to our employee benefit plans.

ELECTRONIC DEPOSIT OF CASH DIVIDENDS

If you are receiving all or a portion of your dividends in cash, you may have them electronically deposited into your U.S. bank account by completing an Authorization for Electronic Direct Deposit Form or by mailing a voided check or deposit slip to the Administrator. Contact the Administrator to receive an Authorization for Electronic Direct Deposit Form. You may also authorize electronic deposit through the Internet at the Administrator's web site, *www.computershare.com/investor*. This feature may be changed or discontinued at any time by notifying the Administrator. If you change your U.S. bank account and fail to notify the Administrator of the change, a check for your dividends will be issued and mailed only after the funds have been returned from the receiving bank.

OPTIONAL CASH INVESTMENTS

Participants in the Plan may buy additional shares of our common stock at any time by investing at least $50. Your total optional cash investment may not exceed $250,000 in a calendar year. Interest will not be paid on amounts held pending investment. Optional cash investments may be made by:

- *One-time online bank debit*. At any time, you may make optional cash investments by going to the Administrator's web site, *www.computershare.com/investor*, and authorizing a one-time online bank debit from your U.S. bank account. Please refer to the online confirmation for your bank account debit date and investment date.

- *Check*. Mail your check with the cash investment form from the bottom of your account statement to the address on the cash investment form. Do not send cash, traveler's checks, money orders or third party checks. All checks should be in U.S. funds and drawn from a U.S. bank. All payments should be made payable to "Computershare-Essential Utilities".

- *Recurring automatic withdrawals from a U.S. bank account*. You can establish recurring automatic withdrawals through the Internet at the Administrator's web site, *www.computershare.com/investor*, or by filling out a Direct Debit Authorization Form for automatic withdrawals. You can receive a Direct Debit Authorization Form by contacting the Administrator through the channels outlined in the "Administration" section of this prospectus. All automatic withdrawal enrollment information must be received at least 30 days prior to the first debit date. Funds will be deducted from your bank account on the first business day of each month. These funds may be commingled with other optional cash investments. Automatic withdrawals will continue at the level you set until you instruct the Administrator otherwise. You can change or stop automatic withdrawals by accessing your Plan account through the Internet at the Administrator's web site, *www.computershare.com/investor*, by calling the Administrator at 1-800-205-8314, by completing and returning a new Direct Debit Authorization Form or by giving written instructions to the Administrator. You must contact the Administrator at least 7 business days prior to the debit date to change or terminate automatic withdrawal. Employees of Essential Utilities who wish to pay for their investment by having a portion of their compensation withheld and applied to the investment should complete the Employee Enrollment Form provided by the Company.

- In the event that a one-time bank debit, check or an automatic withdrawal is not honored for any reason, the Administrator will consider the request for investment of that money null and void and shall immediately remove from the participant's account the shares, if any, purchased upon the prior credit of such money. A fee of $35 will also be assessed against the participant's account. The Administrator will then be entitled to sell those shares to satisfy any uncollected balance. If the net proceeds of the sale of those shares are insufficient to satisfy the balance of such uncollected amounts, the Administrator will be entitled to sell additional shares from the participant's account to satisfy the uncollected balance.

PURCHASE AND SOURCE OF SHARES

Shares of our common stock needed to meet the requirements of the Plan will either be purchased in the open market or issued directly by us. We will pay transaction fees and per share fees (which will include any brokerage commissions the Administrator is required to pay) incurred for the purchase of shares. The Administrator will invest your funds for the optional cash investments as promptly as practicable, at least once each week. However, funds automatically withdrawn from your U.S. bank account will be invested as specified above in "Optional Cash Investments – By automatic recurring withdrawals from a U.S. bank account." Funds may not be returned once they have been submitted to the Administrator. In the unlikely event that, due to unusual market conditions, the Administrator is unable to purchase shares of our common stock within 30 days (in the case of reinvested dividends) or within 35 days after receipt (in the case of cash investments), the funds will be returned to you by check. No interest will be paid on funds held by the Administrator pending investment. All dividends will be invested independently from optional cash investments. Please note that you will not be able to direct the Administrator to purchase shares at a specific time or at a specific price or through a specific broker or dealer.

PRICE OF SHARES

Open market purchases for initial, optional and IRA investments will be at a price equal to 100% of the weighted average per share price of shares purchased by the Administrator to satisfy Plan requirements. If the Administrator purchases shares to meet the dividend reinvestment requirement in the open market, your price per share will be 95% to 100% of the weighted average price of shares purchased, as designated from time to time by us prior to the purchase of the shares with the reinvested dividends. We will pay all transaction fees and per share fees in connection with open market purchases.

For original issue or treasury shares purchased from Essential Utilities for initial, optional and IRA investments (including investments made by employees through compensation withholding), the price per share will be 100% of the average of the daily high and low trading prices quoted on The New York Stock Exchange on the day of purchase (the investment date).

For original issue or treasury shares purchased from Essential Utilities to meet the dividend reinvestment requirement under the Plan, the price per share will be 95% to 100% of the average of the daily high and low trading prices quoted on The New York Stock Exchange for the five trading days preceding the dividend payment date, as designated from time to time by us prior to the dividend payment date.

The discount between 0% and 5.0% on the shares purchased or issued to meet the dividend reinvestment requirement will be designated by us in our sole discretion prior to the purchase or issuance of such shares. We reserve the right to change, reduce or discontinue any discount at any time without notice. We will provide the Administrator with notice of the applicable discount and any change in such discount. Please contact the Administrator with any questions about the discount then in effect. We may also provide notice on our website, but have no obligation to do so. As of the date of this prospectus, the discount is 5.0%.

SALE OF SHARES

You can sell some or all of the shares held in your Plan account by contacting the Administrator. You have choices when making a sale, depending on how you submit your sale request, as follows:

- *Market Order*: A market order is a request to sell shares promptly at the current market price. Market order sales are only available at *www.computershare.com/investor* through Investor Centre or by calling the Administrator directly at 1-800-205-8314. Market order sale requests received at *www.computershare.com/investor* through Investor Centre or by telephone will be placed promptly upon receipt during market hours (normally 9:30 a.m. to 4:00 p.m. Eastern time). Any orders received after 4:00 p.m. Eastern time will be placed promptly on the next day the market is open. The price shall be the market price of the sale obtained by the Administrator's broker, less applicable fees. The Administrator will use commercially reasonable efforts to honor requests by participants to cancel market orders placed outside of market hours. Depending on the number of shares being sold and current trading volume in the shares, a market order may only be partially filled or not filled at all on the trading day in which it is placed, in which case the order, or remainder of the order, as applicable, will be cancelled at the end of such day. To determine if your shares were sold, you should check your account online at *www.computershare.com/investor* or call the Administrator directly at 1-800-205-8314. If your market order sale was not filled and you still want the shares to be sold, you will need to re-enter the sale request. For a market order sale, you will be charged a transaction fee of $25, plus $0.12 per share.

- *Batch Order*: A batch order is an accumulation of all sales requests for a security submitted together as a collective request. Batch orders are submitted on each market day, assuming there are sale requests to be processed. Sale instructions for batch orders received by the Administrator will be processed no later than five business days after the date on which the order is received (except where deferral is required under applicable federal or state laws or regulations), assuming the applicable market is open for trading and sufficient market liquidity exists. Batch order sales may only be submitted in writing. All sales requests received in writing will be submitted as batch order sales, including sale requests for IRA Plan accounts and Coverdell Education Savings Accounts, will be submitted as batch order sale. The Administrator will cause your shares to be sold on the open market within five business days of receipt of your request. To maximize cost savings for batch order sale requests, the Administrator will seek to sell shares in round lot transactions. For this purpose the Administrator may combine each selling Plan participant's shares with those of other selling Plan participants. In every case of a batch order sale, the price to each selling Plan, participant shall be the weighted average sale price obtained by the Administrator's broker for each aggregate order placed by the Administrator and executed by the broker, less applicable fees. For a batch order sale, you will be charged a transaction fee of $25, plus $0.12 per share.

- *Day Limit Order*: A day limit order is an order to sell shares of our common stock when and if they reach a specific trading price on a specific day. The order is automatically cancelled if the price is not met by the end of that day (or, for orders placed aftermarket hours, the next day the market is open). Depending on the number of shares of our common stock being sold and the current trading volume in the shares, such an order may only be partially filled, in which case the remainder of the order will be cancelled. The order may be cancelled by the applicable stock exchange, by the Administrator at its sole discretion or, if the Administrator's broker has not filled the order, at your request made online at *www.computershare.com/investor* or by calling the Administrator directly at 1-800-205-8314. For a day limit order sale, you will be charged a transaction fee of $25, plus $0.12 per share.

- *Good-Till-Cancelled ("GTC") Limit Order*: A GTC limit order is an order to sell shares of our common stock when and if the shares reach a specific trading price at any time while the order remains open (generally up to 30 days). Depending on the number of shares being sold and current trading

volume in the shares, sales may be executed in multiple transactions and over more than one day. If shares are traded on more than one day, a separate fee will be charged for each such day. The order (or any unexecuted portion thereof) is automatically cancelled if the trading price is not met by the end of the order period. The order may be cancelled by the applicable stock exchange, by the Administrator at its sole discretion or, if the Administrator's broker has not filled the order, at your request made online at *www.computershare.com/investor* or by calling the Administrator directly at 1-800-205-8314. For a GTC limit order sale, you will be charged a transaction fee of $25, plus $0.12 per share.

General: All sales requests processed over the telephone by a customer service representative entail an additional fee of $15.00. All per share fees include any brokerage commissions the Administrator is required to pay. Any fractional share will be rounded up to a whole share for purposes of calculating the per share fee. Fees are deducted from the proceeds derived from the sale. The Administrator may, under certain circumstances, require a transaction request to be submitted in writing. Please contact the Administrator to determine if there are any limitations applicable to your particular sale request. Proceeds are normally paid by check, which are distributed within 24 hours of after your sale transaction has settled.

The Administrator reserves the right to decline to process a sale if it determines, in its sole discretion, that supporting legal documentation is required. In addition, no one will have any authority or power to direct the time or price at which shares for the Plan are sold, and no one, other than the Administrator, will select the broker(s) or dealer(s) through or from whom sales are to be made.

If you elect to sell shares online at *www.computershare.com/investor*, you may utilize the Administrator's international currency exchange service to convert the sale proceeds to your local currency prior to being sent to you. Receiving sales proceeds in a local currency and having your check drawn on a local bank avoids the timely and costly "collection" process required for cashing U.S. dollar checks. This service is subject to additional terms and conditions and fees, which you must agree to online. We are not responsible for any costs or fees associated with your use of this service.

If your holdings in any account fall below 5 shares, the Administrator may close that account out of the Plan as described in the "Minimum Account" section of this prospectus.

INDIVIDUAL RETIREMENT ACCOUNTS ("IRA")

You may establish a Traditional IRA, Roth IRA or Coverdell Education Savings Account of our common stock by returning completed Enrollment Forms together with your contribution to the IRA and Coverdell Education Savings Account Trustee. If you are already a shareholder of at least 5 shares, you may open an IRA or Coverdell Education Savings Account with as little as $50. If you are not a shareholder, the minimum contribution to open an account is $500.

You may also open an IRA or Coverdell Education Savings Account to receive a cash rollover or a transfer of Essential Utilities shares from another IRA or qualified retirement plan. The IRA and Coverdell Savings Account Trustee will invest the cash rollovers into shares of our common stock.

There is an annual maintenance fee of $45.00 charged by the IRA and Coverdell Education Savings Account Trustee, which we will pay for the first calendar year in which you participate. In all subsequent years, twenty- five dollars ($25.00) of this annual fee will be charged to you, with the balance paid by us.

IRA and Coverdell Education Savings Account contributions and rollovers will not count against the $250,000 maximum investment limit under the Plan.

If you are interested in opening a Traditional IRA, Roth IRA or Coverdell Education Savings Account, you may obtain the enrollment and a disclosure statement from Computershare Trust Company, N.A., which will administer the IRA and Coverdell Education Savings Account. For information, call the Computershare IRA Department at its toll-free number, 1-800-597-7736.

SAFEKEEPING OF CERTIFICATES AND BOOK ENTRY

For your convenience, shares purchased under the Plan will be maintained by the Administrator in your name in book-entry form. You may, however, request a stock certificate by accessing your Plan account through the Internet at the Administrator's web site, *www.computershare.com/investor*, by calling the Administrator at 1-800-205-8314 or by providing written instructions to the Administrator. There is a $25 fee for certificate issuance.

If you are holding certificates for Essential Utilities, Inc., or previously named Aqua America, Inc. or Philadelphia Suburban Corporation common stock, you may use the Plan's "safekeeping" service to deposit those stock certificates at no cost. Safekeeping protects your shares against loss, theft or accidental destruction and provides a convenient way for you to keep track of your shares. Only shares held in safekeeping or in book-entry form may be sold through the Plan.

To use the safekeeping service, send your certificates to the Administrator at the address listed on page 6 of this prospectus by registered or certified mail, with a return receipt requested or some other form of traceable mail, and properly insured. **YOU SHOULD NOT ENDORSE THE STOCK CERTIFICATE BEFORE YOU SEND IT IN.**

TRACKING YOUR INVESTMENT

The Administrator will send a statement confirming the details of each transaction you make. For market order transactions, the time of sale will be provided. If you continue to be enrolled in the Plan, but have no transactions, the Administrator will mail you an annual statement reflecting your holdings. For shares acquired in the Plan after January 1, 2011, specific cost basis information will be included in your statement in accordance with applicable law.

You should notify the Administrator promptly of any change in address since all notices, statements and reports will be mailed to your address of record.

Please retain your statements to establish the cost basis of shares purchased under the Plan for income tax and other purposes. A $20 flat fee per year requested will be charged for all prior year duplicate statement requests.

You may also view year-to-date transaction activity in your Plan account for the current year, as well as activity in prior years, by accessing your Plan account through the Internet at the Administrator's web site, *www.computershare.com/investor*.

OBTAINING A STOCK CERTIFICATE

To obtain a stock certificate for all or a portion of your full shares, you can contact the Administrator by accessing your Plan account through the Internet at the Administrator's web site, *www.computershare.com/investor*, by calling the Administrator at 1-800-205-8314, by making a written request of the Administrator or by completing the transaction form at the bottom of your statement and submitting it to the Administrator. There is a $25 fee for certificate issuance. No fractional shares of common stock will be issued; instead, the then-current market value of any fractional share sold, less any transaction fees and per share fees, will be paid in cash.

If you want the certificate issued in a name other than your Plan account registration, the Administrator may require you to have your signature guaranteed by a financial institution in the Medallion Guarantee program.

TRANSFERS

You may transfer or give our common stock to anyone you choose by:

- Making an initial $500 cash investment to establish a new account in the recipient's name; or
- Making an optional cash investment on behalf of an existing shareholder in the Plan in an amount not less than $50 nor more than $250,000 in one calendar year; or
- Transferring at least 5 shares from your account to the recipient.

If you would like transfer instructions, please visit the Administrator's Transfer Wizard at *www.computershare.com/transferwizard*. The Transfer Wizard will guide you through the transfer process, assist you in completing the transfer form, and identify other necessary documentation you may need to provide.

DIVIDEND PAYMENT AND RECORD DATES

Normal dividend payment dates are expected to be on the first day of March, June, September and December. The record date usually precedes the dividend payment date by 10 business days.

In order to be the owner of record and eligible to receive the quarterly dividend, your shares must have been purchased and the transaction settled three trading days prior to the record date (the ex-dividend date). We can give no guarantee whatsoever that we will declare dividends in the future.

TERMINATION OF PARTICIPATION

If you wish to stop reinvesting your dividends or to stop automatic monthly investments, please use the transaction form attached to your statement or contact the Administrator by accessing your Plan account through the Internet at the Administrator's web site, *www.computershare.com/investor*, by calling the Administrator at 1-800-205-8314 or by providing written instructions to the Administrator.

In the event you have been reinvesting your dividends and your notice of termination is received by the Administrator near a record date for a dividend payment, the Administrator, in its sole discretion, may either distribute that dividend in cash or reinvest it in shares on your behalf. In the event the dividend is reinvested, the Administrator will process your withdrawal from the Plan as soon as practicable, but in no event later than five business days after the purchase is completed.

MINIMUM ACCOUNT

After you have made your initial contribution of $500 by automatic withdrawals, check or one-time online bank debit, or had at least 5 shares transferred into an account registered in your name under the Plan, you must, at all times you are enrolled in the Plan, keep a minimum number of 5 shares of our common stock in your account. If you keep less than 5 shares in your account, the Administrator may code the account for future dividends to be paid in cash.

COSTS

We pay for all transaction fees and per share fees (which include any brokerage commissions the Administrator is required to pay) associated with the reinvestment of dividends and the making of optional cash investments.

For each batch order sale of whole shares from your Plan account, you will be charged a $25.00 transaction fee and a per share fee of $0.12.

For each market order sale of whole shares from your Plan account, you will be charged a $25.00 transaction fee and a per share fee of $0.12.

For each limit order sale of whole shares from your Plan account, you will be charged a $25.00 transaction fee and a per share fee of $0.12.

For each GTC limit order sale of whole shares from your Plan account, you will be charged a $25.00 transaction fee and a per share fee of $0.12.

All sales requests processed over the telephone by a customer service representative entail an additional fee of $15.00.

There is an annual maintenance fee of $45.00 charged by the IRA and Coverdell Education Savings Account Trustee, which we will pay for the first calendar year in which you participate. In all subsequent years, twenty-five dollars ($25.00) of this annual fee will be charged to you, with the balance of the annual fee paid by us. Fees are collected by the Administrator from your account.

TAXES

All dividends paid to you – whether or not they are reinvested – are considered taxable income to you in the year they are paid. The total amount will be reported to you, and to the Internal Revenue Service, shortly after the close of each year. If you are reinvesting your dividends, the value of the applicable discount from the purchase price of the shares (the calculated fair market value) will also be reported as taxable income.

If you are an employee of Essential Utilities and are paying for shares by having compensation withheld, the amounts withheld will be subject to taxation as ordinary income on the same basis as the portion of your compensation that is not withheld.

All shares of stock that are sold through the Administrator will also be reported to the IRS as required by law. Any profit or loss you incur should be reflected when you file your income tax returns.

In addition, the Internal Revenue Service may require that any per share fees (which include any brokerage commissions the Administrator is required to pay incurred in the purchase of shares and paid by us on your behalf be treated as dividend income to you, in which case such amounts can be included in your cost basis of shares purchased.

Be sure to keep your statements of account for income tax purposes. A fee of $20.00 per year requested may be incurred to furnish historical information. If you have questions about the tax basis of any transactions, please consult your own tax advisor.

VOTING

We will forward to you, either electronically or by mail based on your preference, a proxy for shares of our common stock for which you hold certificates and shares of our common stock credited to your Plan account. The Administrator shall not vote shares of our common stock that it holds for your Plan account except as directed by you.

HANDLING OF STOCK SPLITS AND OTHER DISTRIBUTIONS

In the event we issue a stock dividend or declare a stock split, your Plan account will be adjusted to reflect the receipt of shares paid or distributed. Any stock dividend or stock split shares of our common stock issued with respect to both certificated and book-entry (whole and fractional) shares will be credited automatically to your Plan account in book-entry form.

In the event of a stock subscription or other offering of rights to shareholders, your rights will be based on your total registered holdings (the shares held in the Plan and outside of the Plan). A single set of materials will be distributed that will allow you to exercise your rights.

CHANGES TO THE PLAN

We may add to or modify the Plan at any time. Similarly, we may, at any time, waive, suspend or terminate the Plan, or any provision of the Plan. We will send you written notice of any significant changes, suspensions or termination. The current prospectus is filed with the SEC and available on our website at *www.essential.co* and modifications to the Plan will be reflected in an updated prospectus on our website.

Any modification made to, or waiver, suspension or termination of, the Plan will apply to a participant's holdings in the Plan at the time the modification, waiver, suspension or termination becomes effective and to transactions occurring thereafter, regardless of when or how the shares were acquired. However, any modification, waiver, suspension or termination of the Plan will not affect your rights as a shareholder in any way, and any book-entry shares you own will continue to be credited to your account with the Administrator unless you specifically request otherwise.

We and the Administrator reserve the right to change any administrative procedure of the Plan.

INTERPRETATION OF THE PLAN

We may interpret and regulate the Plan as deemed necessary or desirable in connection with the operation of the Plan and resolve questions or ambiguities concerning the various provisions of the Plan.

RESPONSIBILITIES OF ESSENTIAL UTILITIES AND THE ADMINISTRATOR

Neither we nor the Administrator shall be liable for any act performed in good-faith or for any good-faith omission to act, including, without limitation, any claims or liability: (a) for failure to terminate your account upon your death prior to receiving written notice of such death or (b) with respect to the prices at which shares of our common stock are purchased or sold for your Plan account and the times when such purchases or sales are made or (c) for any fluctuation in the market value after purchases or sale of shares of our common stock. in no event will we, the Administrator or their agents have any liability as to any inability to purchase shares or as to the timing of any purchase.

Neither we nor the Administrator can assure you a profit or protect you against a loss on the shares you purchase under the Plan.

USE OF PROCEEDS

The proceeds from the sale of newly-issued or treasury shares offered by us will be used for general corporate purposes. All other shares of common stock acquired under the Plan will be purchased in the open market, not from us, and we will not receive any proceeds from such purchases.

EXPERTS

The financial statements and management's assessment of the effectiveness of internal control over financial reporting (which is included in Management's Report on Internal Control over Financial Reporting), incorporated in this Prospectus by reference to the Annual Report on Form 10-K for the year ended December 31, 2019 have been so incorporated in reliance on the report of PricewaterhouseCoopers LLP, an independent registered public accounting firm, given on the authority of said firm as experts in auditing and accounting.

Ballard Spahr LLP, our outside counsel, has given its opinion regarding the validity of the common stock covered by this prospectus.

ANTIDILUTION PROVISION

The aggregate number of shares of common stock registered for issuance and purchase under the Plan, as provided in the Registration Statement, of which this prospectus forms a part, the maximum number of shares that may be purchased by a participant and the calculation of the purchase price per share may be appropriately adjusted by us to reflect any increase or decrease in the number of issued shares of common stock resulting from a subdivision or consolidation of shares or other capital adjustment, or the payment of a stock dividend, or other increase or decrease in such shares, if effected without receipt of consideration by us.

WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the SEC. You may read and copy any document we file at the SEC's public reference room at 100 F Street N.E., Washington, D.C. 20549. Copies of such materials can be obtained by mail at prescribed rates from the public reference room. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. You may also obtain our SEC filings from the SEC's web site at www.sec.gov or from our web site at *https://www.essential.co/investor-relations*.

This prospectus is part of a Registration Statement on Form S-3 that we filed with the SEC to register the stock offered under the Plan. As allowed by SEC rules, this prospectus does not contain all information you can find in the Registration Statement or the exhibits to the Registration Statement. The SEC allows us to "incorporate by reference" information into this prospectus, which means that we can disclose important information to you by referring you to another document filed separately with the SEC. The information incorporated by reference is considered to be part of this prospectus and later information fi led with the SEC will update and supersede this information. Any statement so updated or superseded shall not be deemed, except as so updated or superseded, to constitute a part of this prospectus. We incorporate by reference the documents listed below and any future filings made with the SEC under Section 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934, as amended, until our offering is completed.

- Our Annual Report on Form 10-K for the year ended December 31, 2019, including portions of our definitive Proxy Statement for our 2019 Annual Meeting of Shareholders incorporated therein by reference;

- Our Quarterly Report on Form 10-Q for the quarter ended March 31, 2020;

- Our Current Reports on Form 8-K filed with the SEC on January 16, 2020 (Items 8.01 and 9.01), February 3, 2020 (Items 5.03 and 9.01), February 27, 2020 (Items 8.01 and 9.01), March 16, 2020 (Items 1.01, 2.01, 2.03, 3.02, 5.02, 8.01 and 9.01), April 3, 2020 (Items 1.01, 2.03 and 9.01), April 13, 2020 (Item 8.01), April 13, 2020 (Items 8.01 and 9.01), April 15, 2020 (Items 1.01, 2.03 and 9.01), May 11, 2020 (Item 5.07) and May 18, 2020 (Items 5.03 and 9.01); and

- The description of our common stock set forth in our Registration Statement on Form 8-A, including any amendments or reports filed for the purpose of updating such description.

You may request a copy of any documents that we incorporate by reference at no cost by telephoning 1-610-527-8000 or writing us at the following address:

Essential Utilities, Inc.
Investor Relations
762 W. Lancaster Avenue
Bryn Mawr, PA 19010

You should rely only on the information contained or incorporated by reference into this prospectus. We have authorized no one to provide you with different information. You should not assume that the information in the prospectus or incorporated by reference into this prospectus is accurate as of any date other than the date on the front of this prospectus or the date of those documents. Our business, financial condition, results of operations and prospects may have changed since those dates.

ESSENTIAL UTILITIES, INC.

Dividend Reinvestment and Direct Stock Purchase Plan

6,000,000

Shares of Common Stock

PROSPECTUS

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR3. Supply projected capital requirements and the sources of company, parent and consolidated system for the historic test year and each of 3 comparable future years.

A. Please see the Company's historic and projected capital requirements for 3/31/2021, 3/31/2022, and 3/1/2023 below. Please note that projected capital requirements are not yet available for 3/31/2024.

	3/31/2021	3/31/2022	3/31/2023
Debt	$ 1,825,756,444	$ 1,814,370,444	$ 1,998,934,444
Preferred	$ -	$ -	$ -
Equity	$ 1,957,971,316	$ 2,265,829,316	$ 2,345,976,316
	$ 3,783,727,759	$ 4,080,199,759	$ 4,344,910,759

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR4. Provide a schedule of debt and preferred stock of company, parent and consolidated system as of historic test year-end and latest date, detailing for each issue (if applicable):

a. Date of issue.

b. Date of maturity.

c. Amount issued.

d. Amount outstanding.

e. Amount retired.

f. Amount required.

g. Gain on reacquisition.

h. Coupon rate.

i. Discount or premium at issuance.

j. Issuance expenses.

k. Net proceeds.

l. Sinking fund requirements.

m. Effective interest rate.

n. Dividend rate.

o. Effective cost rate.

p. Total average weighted effective cost rate.

A. There is no preferred stock for the Company, Parent or System (consolidated). The schedule of debt for the Company may be found in Schedule 6 of Exhibit 4-A . The attached Schedule RR4 lists the debt details for the Parent as of March 31, 2021.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
AQUA AMERICA LTD - AS OF MARCH 31, 2021

Issuer	Structure	Interest Rate	Issue Date	Maturity Date	Original Amount	LT (excl. CP) Balance @	Due 04/01/21 to 03/31/22	LT (incl. CP)	Weighted Average Interest	Unamortized Debt	Annual Amortization	Effective Interest Rate	Sinking Fund Req't	Issuance Prem/(Disc)
Essential Utilities, Inc.	PNC Revolving Credit Facility	1.23%	12/05/18	12/05/23	1,000,000,000	440,000,000		440,000,000	5,425,200	N/A	N/A	N/A	N/A	-
Essential Utilities, Inc.	Senior Unsecured Notes	3.01%	11/03/16	11/03/31	35,000,000	35,000,000	0	35,000,000	1,053,500	N/A	N/A	N/A	N/A	-
Essential Utilities, Inc.	Senior Unsecured Notes	3.19%	11/03/16	11/03/34	30,000,000	30,000,000	0	30,000,000	957,000	N/A	N/A	N/A	N/A	-
Essential Utilities, Inc.	Senior Unsecured Notes	3.25%	11/03/16	11/03/35	25,000,000	25,000,000	0	25,000,000	812,500	N/A	N/A	N/A	N/A	-
Essential Utilities, Inc.	Senior Unsecured Notes	3.41%	11/03/16	11/03/38	10,000,000	10,000,000	0	10,000,000	341,000	N/A	N/A	N/A	N/A	-
Essential Utilities, Inc.	Senior Unsecured Notes	3.57%	11/03/16	11/03/41	25,000,000	25,000,000	0	25,000,000	892,500	N/A	N/A	N/A	N/A	-
Essential Utilities, Inc.	Senior Unsecured Notes	4.28%	04/26/19	05/01/49	500,000,000	500,000,000	0	500,000,000	21,380,000	N/A	N/A	N/A	N/A	-
Essential Utilities, Inc.	Senior Unsecured Notes	3.57%	04/26/19	05/01/29	400,000,000	400,000,000	0	400,000,000	14,264,000	N/A	N/A	N/A	N/A	-
Essential Utilities, Inc.	Tangible Equity Units	3.00%	04/28/19	04/30/22	119,081,442	10,272,996	40,332,846	50,605,842	1,518,175	N/A	N/A	N/A	N/A	-
Essential Utilities, Inc.	Senior Unsecured Notes	2.70%	04/13/20	04/15/30	500,000,000	500,000,000	0	500,000,000	13,520,000	N/A	N/A	N/A	N/A	-
Essential Utilities, Inc.	Senior Unsecured Notes	3.35%	04/13/20	04/15/50	600,000,000	600,000,000	0	600,000,000	20,106,000	N/A	N/A	N/A	N/A	-
Total Essential Utilities, Inc.						**2,575,272,996**	**40,332,846**	**2,615,605,842**	**80,269,875**	**18,624,218**	**2,096,984**	**3.172%**		**-**

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR5. Supply financial data of company and/or parent for last 5 years:

a. Earnings-price ratio (average).

b. Earnings-book value ratio (per share basis) (average book value).

c. Dividend yield (average).

d. Earnings per share (dollar).

e. Dividends per share (dollars).

f. Average book value per share yearly.

g. Average yearly market price per share (monthly high-low basis).

h. Pre-tax funded debt interest coverage.

i. Post-tax funded debt interest coverage.

j. Market price-book value ratio.

A. Please refer to the direct testimony of Paul R. Moul and the accompanying Exhibit 4-A for the Company's financial data, including the details requested in items (a) through (j).

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR6. Provide AFUDC charged by company at historic test year-end and latest date, explain method by which rate was calculated and provide workpaper showing derivation of the company's current AFUDC rate.

A.

AFUDC is $5,935,981 for the twelve months ended March 31, 2021 and $7,265,303 for the twelve months ended July 31, 2021. The Company utilizes the short-term debt rate for cost of capital used during construction. However, when CWIP exceeds short-term debt, a blended rate reflecting both debt and equity is utilized. The July 31, 2021 current monthly AFUDC debt rate is 0.131984% and the current monthly AFUDC equity rate is 0.310819%.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR7. Set forth provisions of company's and parent's charter and indentures, if applicable, which describe coverage requirements, limits on proportions of types of capital outstanding, and restrictions on dividend payouts.

A. Please see the attached.

Prepared by and Return to:
Mary T. Tomich, Esq.
Dilworth Paxson LLP
1500 Market Street
Suite 3500E
Philadelphia, PA 19102
215-575-7000

FIFTY-NINTH SUPPLEMENTAL

INDENTURE

DATED AS OF SEPTEMBER 1, 2020

TO

INDENTURE OF MORTGAGE

DATED AS OF JANUARY 1, 1941

AQUA PENNSYLVANIA, INC.

TO

THE BANK OF NEW YORK MELLON TRUST COMPANY, N. A., as Trustee

Available Permanent Additions pursuant to the provisions of Section 9 of Article I of the Original Indenture;

(xii) The amount set forth in subparagraph (vi) after deducting the amount, if any, set forth in subparagraph (vii); and

(xiii) That all conditions precedent to the taking of the credit or credits so requested by the Company have been complied with.

(B) In the event that the Officers' Certificate delivered to the Trustee pursuant to the provisions of paragraph (A) of this Section shall state, pursuant to the requirements of subparagraph (vi), the Cost or Fair Value of Available Permanent Additions acquired by the Company during the preceding calendar year, the documents specified in paragraphs 2, 3, 5, 6 and 7 of subdivision (B) of Section 3 of Article IV of the Original Indenture.

(C) An amount in cash equal to the sum set forth in subparagraph (viii) of the Officers' Certificate provided for in paragraph (A) hereof.

SECTION 3. All cash deposited with the Trustee as part of any Maintenance or Improvement Deposit provided for in Section 1 of this Article, may, at the option of the Company, be applied to the purchase of bonds under the provisions of Section 2 of Article X of the Original Indenture or to the redemption of bonds under the provisions of Section 3 of Article X of the Original Indenture or may be withdrawn by the Company at any time to reimburse the Company for the cost of a Net Amount of Available Permanent Additions (excluding, however, from any such Available Permanent Additions all Permanent Additions included in any certificate delivered to the Trustee for the purpose of obtaining a credit against any Maintenance or Improvement Deposit provided for in Section 1 of this Article to the extent that such Permanent Additions have been used for any such credit). The Trustee shall pay to or upon the written order of the Company all or any part of such cash upon the receipt by the Trustee of:

(a) A Resolution requesting such payment; and

(b) The documents specified in paragraphs 2, 5, 6 and 7 of subdivision (B) of Section 3 of Article IV of the Original Indenture, with such modifications, additions and omissions as may be appropriate in the light of the purposes for which they are used.

ARTICLE III.

Covenants of the Company

SECTION 1. The Company hereby covenants and agrees with the Trustee, for the benefit of the Trustee and all the present and future holders of the Bonds, that the Company will pay the principal of and premium, if any, of and interest on all bonds issued or to be issued as aforesaid under and secured by the Original Indenture as hereby supplemented, as well as all bonds which may be hereafter issued in exchange or substitution therefor, and will perform and fulfill all of the terms, covenants and conditions of the Original Indenture and of this Fifty-ninth

Supplemental Indenture with respect to the additional bonds to be issued under the Original Indenture as hereby supplemented.

SECTION 2. The Company covenants and agrees that so long as any of the Bonds are outstanding (a) the Company will not make any Stock Payment if, after giving effect thereto, its retained earnings, computed in accordance with generally accepted accounting principles consistently applied, will be less than the sum of (i) Excluded Earnings, if any, since December 31, 2019, and (ii) $20,000,000; (b) Stock Payments made more than forty (40) days after the commencement, and prior to the expiration, of any Restricted Period shall not exceed 65% of the Company's Net Income during such Restricted Period; and (c) the Company will not authorize a Stock Payment if there has occurred and is continuing an event of default under subsections (a) or (b) of Section 1 of Article XI of the Original Indenture.

For the purposes of this Section 2 the following terms shall have the following meanings:

"Capitalization" shall mean the sum of (i) the aggregate principal amount of all Debt at the time outstanding, (ii) the aggregate par or stated value of all capital stock of the Company of all classes at the time outstanding, (iii) premium on capital stock, (iv) capital surplus, and (v) retained earnings.

"Debt" means (i) all indebtedness, whether or not represented by bonds, debentures, notes or other securities, for the repayment of money borrowed, (ii) all deferred indebtedness for the payment of the purchase price of property or assets purchased (but Debt shall not be deemed to include customer advances for construction or any bonds issued under the Indenture which are not Outstanding Bonds), (iii) leases which have been or, in accordance with generally accepted accounting principles, should be recorded as capital leases and (iv) guarantees of the obligations of another of the nature described in clauses (i), (ii) or (iii) which have been or, in accordance with generally accepted accounting principles, should be recorded as debt.

"Determination Date" shall mean the last day of each calendar quarter. Any calculation with respect to any Determination Date shall be based on the Company's balance sheet as of such date.

"Excluded Earnings" shall mean 35% of the Company's Net Income during any Restricted Period.

"Net Income" for any particular Restricted Period shall mean the amount of net income properly attributable to the conduct of the business of the Company for such period, as determined in accordance with generally accepted accounting principles consistently applied, after payment of or provision for taxes on income for such period.

"Outstanding Bonds" shall mean bonds which are outstanding within the meaning indicated in Section 20 of Article I of the Original Indenture except that, in addition to the bonds referred to in clauses (a), (b) and (c) of said Section 20, said term shall not include bonds for the retirement of which sufficient funds have been deposited with the Trustee with irrevocable instructions to apply such funds to the retirement of such bonds at a specified time, which may

be either the maturity thereof or a specified redemption date, whether or not notice of redemption shall have been given.

"Restricted Period" shall mean a period commencing on any Determination Date on which the total Debt of the Company is, or as the result of any Stock Payment then declared or set aside and to be made thereafter will be, more than 70% of Capitalization, and continuing until the third consecutive Determination Date on which the total Debt of the Company does not exceed 70% of Capitalization.

"Stock Payment" shall mean any payment in cash or property (other than stock of the Company) to any holder of shares of any class of capital stock of the Company as such holder, whether by dividend or upon the purchase, redemption, conversion or other acquisition of such shares, or otherwise.

SECTION 3. The Company covenants and agrees that so long as any of the Bonds are outstanding neither the Company nor any subsidiary of the Company will, directly or indirectly, lend or in any manner extend its credit to, or indemnify, or make any donation or capital contribution to, or purchase any security of, any corporation which directly or indirectly controls the Company, or any subsidiary or affiliate (other than an affiliate which is a subsidiary of the Company) of any such corporation.

ARTICLE IV.

The Trustee

SECTION 1. The Trustee hereby accepts the trust hereby declared and provided, and agrees to perform the same upon the terms and conditions in the Original Indenture, as supplemented by this Fifty-ninth Supplemental Indenture.

SECTION 2. Subject to the provisions of Article XIII of the Original Indenture, the Trustee may execute any of the trusts or powers hereof and perform any of its duties by or through and consult with attorneys, agents, officers or employees selected by the Trustee in its sole discretion. The Trustee shall be entitled to advice of counsel concerning all matters of trusts hereof and the duties hereunder and may in all cases pay such reasonable compensation to all such attorneys, agents, officers and employees as may reasonably be employed in connection with the trusts hereof. The Trustee may act or refrain from acting and rely upon and be free from all liability for so relying upon the opinion or advice of any attorney (who may be the attorney or attorneys for the Company) and shall be free from all liability for any action taken or not taken in reliance on such opinion or advice. The Trustee may act and rely on written opinions of experts employed by the Trustee and such advice shall be full and complete authorization and protection in respect of any action taken, suffered or omitted by the Trustee hereunder in good faith and in reliance thereon. The Trustee shall not be responsible for any loss or damage resulting from any action or non-action in good faith taken in reliance upon such opinion or advice. The Trustee shall not be bound to confirm, verify or make any investigation into the facts or matters stated in any financial or other statements, resolution, certificate, statement, instrument, opinion, report, notice, request, direction, consent, order or other paper or document furnished pursuant to the terms hereof.

IV 3 (4

pany to permit the legal and valid issue and authentication and delivery of the bonds which have been applied for has been duly had and taken;

4. An Officers' Certificate, as herein defined, stating the aggregate principal amount of all bonds at the time outstanding under this Indenture, and, unless the Opinion of Counsel provided for in paragraph 3 of this subdivision (*B*) shall state that the amount of indebtedness or bonded indebtedness which may be incurred by the Company is not then limited by law or by corporate action, also stating that the total amount of indebtedness or bonded indebtedness of the Company outstanding, including the aggregate principal amount of bonds issued and outstanding, as herein defined, under this Indenture plus the aggregate principal amount of bonds applied for in the accompanying application, does not exceed an amount which shall be specified in the Certificate;

5. The officially authenticated certificates or other documents, if any, specified in the Opinion of Counsel provided for in paragraph 3 of this subdivision (*B*), including evidence satisfactory to the Trustee of the payment or provision for payment of any taxes therein referred to;

6. If the bonds, the authentication and delivery of which are then applied for, are not a part of any series then existing, a Resolution or Resolutions and an indenture supplemental hereto, creating the series of which such bonds are a part.

SECTION 3. (*A*) Subject to the provisions of Section 2 of this Article bonds in addition to those provided for in any other Section hereof may from time to time be executed by the Company and delivered to the Trustee

and shall be authenticated and delivered by the Trustee upon the basis of Available Permanent Additions, subject to the conditions, provisions and limitations set forth in this Section. The aggegate principal amount of bonds that may be authenticated and delivered from time to time under the provisions of this Section is limited to seventy per cent. (70%) of the Net Amount of Available Permanent Additions, made the basis of the authentication and delivery thereof certified or provided in subdivision (*B*) of this Section.

No bonds shall be authenticated and delivered under this Section unless the Net Earnings of the Company as shown by a Net Earnings Certificate for a period of twelve (12) consecutive calendar months within the fifteen (15) calendar months next preceding the application for authentication and delivery of bonds, shall have been not less than one and three-quarters (1¾) times the interest requirements for a period of one year upon (*a*) the bonds applied for, (*b*) all bonds outstanding, as herein defined, on the date of such application, and (*c*) all indebtedness outstanding on the date of such application which is secured by any lien for the payment of money or its equivalent prior to or on a parity with the lien of this Indenture other than Permitted Liens, as herein defined.

(*B*) No application by the Company to the Trustee for the authentication and delivery of bonds under this Section shall be granted by the Trustee, until the Trustee shall have received:

1. The documents provided for in Section 2 of this Article;

2. An Engineer's Certificate, as herein defined, dated not more than thirty (30) days preceding the

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AQUA AMERICA, INC.

$125,000,000

$35,000,000 3.01% Senior Notes, Series A, due November 3, 2031
$30,000,000 3.19% Senior Notes, Series B, due November 3, 2034
$25,000,000 3.25% Senior Notes, Series C, due November 3, 2035
$10,000,000 3.41% Senior Notes, Series D, due November 3, 2038
$25,000,000 3.57% Senior Notes, Series E, due November 3, 2041

NOTE PURCHASE AGREEMENT

DATED AS OF NOVEMBER 3, 2016

Default or Event of Default would exist under the terms of this Agreement, and *provided, further,* that once a Subsidiary has been designated an Unrestricted Subsidiary, it shall not thereafter be redesignated as a Restricted Subsidiary on more than one occasion. Within ten days following any designation described above, the Company will deliver to each Purchaser a notice of such designation accompanied by a certificate signed by a Senior Financial Officer of the Company certifying compliance with all requirements of this **Section 9.6** and setting forth all information required in order to establish such compliance.

Section 9.7. Subsidiary Guaranty. (a) If at any time any Subsidiary of the Company shall become a co-obligor under, or guarantor of Debt outstanding under, any Material Credit Facility (a *"Subsidiary Guarantor"*), then concurrently with any such event the Subsidiary Guarantor shall execute and deliver to the holders of the Notes an unconditional guarantee of the Notes which shall be in form and substance satisfactory to the Required Holders, and (b) deliver such proof of corporate or other action, incumbency of officers, opinions of counsel and other documents as is consistent with those delivered by the Company pursuant to **Section 4** on the Closing Date or as the Required Holders shall have reasonably requested.

SECTION 10. NEGATIVE COVENANTS.

The Company covenants that so long as any of the Notes are outstanding:

Section 10.1. Limitation on Debt. The Company will not permit Consolidated Debt (determined as of the last day of each fiscal quarter) to exceed 65% of Consolidated Total Capitalization as of such date.

Section 10.2. Limitation on Liens. The Company will not, and will not permit any of its Restricted Subsidiaries to, directly or indirectly create, incur, assume or permit to exist (upon the happening of a contingency or otherwise) any Lien on or with respect to any property or asset (including, without limitation, any document or instrument in respect of goods or accounts receivable) of the Company or any such Restricted Subsidiary, whether now owned or held or hereafter acquired, or any income or profits therefrom, or assign or otherwise convey any right to receive income or profits, except:

(a) Liens for taxes, assessments or other governmental charges that are not yet due and payable or the payment of which is not at the time required by **Section 9.4**; *provided,* any such tax, assessment or other governmental charge shall be paid prior to the commencement of any proceedings to foreclose any Lien related thereto;

(b) any attachment or judgment Lien, unless the judgment it secures shall not, within 60 days after the entry thereof, have been discharged or execution thereof stayed pending appeal, or shall not have been discharged within 60 days after the expiration of any such stay;

(c) Liens incidental to the conduct of business or the ownership of properties and assets (including landlords', carriers', warehousemen's, mechanics', materialmen's and other similar Liens for sums not yet due and payable or which are being contested in

(xi) Investments in addition to the Investments permitted by the preceding clauses (i) through (x); *provided* that the aggregate principal amount of Investments outstanding pursuant to this clause (xi) shall not at any time exceed 25% of Consolidated Net Worth.

In valuing Investments for purposes of applying the limitations set forth in clause (xi) of this **Section 10.6**, such Investments shall be taken at the original cost thereof, without allowance for any subsequent write-offs or appreciation or depreciation therein, but less any amount repaid or recovered on account of capital or principal.

Section 10.7. Nature of Business. Neither the Company nor any Restricted Subsidiary will engage in any business, other than, when taken as a whole, the general nature of the business in which the Company and its Restricted Subsidiaries are engaged on the date of this Agreement and other energy related regulated business activities and non-regulated business activities that are complementary to the foregoing.

Section 10.8. Transactions with Affiliates. The Company will not and will not permit any Restricted Subsidiary to enter into directly or indirectly any Material transaction or group of related transactions (including without limitation the purchase, lease, sale or exchange of properties of any kind or the rendering of any service) with any Affiliate (other than the Company or another Restricted Subsidiary), except upon fair and reasonable terms no less favorable to the Company or such Restricted Subsidiary than would be obtainable in a comparable arm's-length transaction with a Person not an Affiliate. In addition, the Company will not, and will not permit any Restricted Subsidiary to, make any loan or advance to the Company or any Restricted Subsidiary except in the ordinary course of business and in accordance with the reasonable requirements of the business of the Company or any such Restricted Subsidiary.

Section 10.9. Acquisitions. The Company will not, and will not permit any Restricted Subsidiary to, make any acquisition of all or substantially all of the assets or capital stock of any business entity if at the time of such acquisition and after giving effect thereto, a Default or Event of Default shall exist.

Section 10.10. Unrestricted Subsidiaries. The Company will not at any time permit Unrestricted Subsidiaries to (i) own more than 40% of the Consolidated Total Assets of the Company and its Subsidiaries, or (ii) account for more than 40% of the consolidated gross revenues of the Company and its Subsidiaries, determined in each case in accordance with GAAP.

Section 10.11. Interest Coverage Covenant. Section 6.1(b) (the *"Interest Coverage Covenant"*) of the Bank Credit Agreement in effect on the date of this Agreement (as such covenant may be amended or modified from time to time whether pursuant to an amendment to the Bank Credit Agreement in effect on the date of this Agreement or any new, restated or replacement Bank Credit Agreement) is hereby incorporated by reference into this **Section 10.11**. The Interest Coverage Covenant shall continue in effect until such time as the Interest Coverage Covenant shall have been eliminated from the Bank Credit Agreement or all

indebtedness under the Bank Credit Agreement is repaid in full and all commitments related thereto are terminated; *provided*, that if at the time of any such repayment or the termination of any such commitment a Default or Event of Default shall exist under this Agreement, then the Interest Coverage Covenant shall continue in full force and effect so long as such Default or Event of Default continues to exist. If at any time a Default or Event of Default exists under the Interest Coverage Covenant, no modification or waiver of the Interest Coverage Covenant shall be effective unless the Required Holders shall have consented thereto. Promptly, but in no event more than 5 Business Days following the execution of any Bank Credit Agreement (or any amendment thereto) which changes or eliminates the Interest Coverage Covenant, the Company shall furnish each holder of the Notes with a copy of such agreement.

Section 10.12. Economic Sanctions, Etc. The Company will not, and will not permit any Controlled Entity to (a) become (including by virtue of being owned or controlled by a Blocked Person), own or control a Blocked Person or (b) directly or indirectly have any investment in or engage in any dealing or transaction (including any investment, dealing or transaction involving the proceeds of the Notes) with any Person if such investment, dealing or transaction (i) would cause any holder or any affiliate of such holder to be in violation of, or subject to sanctions under, any law or regulation applicable to such holder, or (ii) is prohibited by or subject to sanctions under any U.S. Economic Sanctions Laws.

SECTION 11. EVENTS OF DEFAULT.

An *"Event of Default"* shall exist if any of the following conditions or events shall occur and be continuing:

(a) the Company defaults in the payment of any principal or Make-Whole Amount, if any, on any Note when the same becomes due and payable, whether at maturity or at a date fixed for prepayment or by declaration or otherwise; or

(b) the Company defaults in the payment of any interest on any Note for more than five Business Days after the same becomes due and payable; or

(c) the Company defaults in the performance of or compliance with any term contained in **Section 8.5, 10.1, 10.2, 10.3, 10.4, 10.5** or **10.11**; or

(d) the Company defaults in the performance of or compliance with any Material term contained herein (other than those referred to in paragraphs (a), (b) and (c) of this **Section 11**) and such default is not remedied within 30 days after the earlier of (i) a Responsible Officer obtaining actual knowledge of such default and (ii) the Company receiving written notice of such default from any holder of a Note (any such written notice to be identified as a "notice of default" and to refer specifically to this paragraph (d) of **Section 11**); or

(e) any representation or warranty made in writing by or on behalf of the Company or by any officer of the Company in this Agreement or in any writing required

thereof at the interest rate implicit in such rentals and otherwise in accordance with GAAP) under the lease relating to such Sale-and-Leaseback Transaction.

"Bank Credit Agreement" means the bank credit agreement dated as of March 23, 2012, between the Company and PNC Bank National Association, as agent, and the banks party thereto, as from time to time amended or restated or any replacement facility which constitutes the primary bank credit facility of the Company.

"Blocked Person" means (a) a Person whose name appears on the list of Specially Designated Nationals and Blocked Persons published by OFAC, (b) a Person, entity, organization, country or regime that is blocked or a target of sanctions that have been imposed under U.S. Economic Sanctions Laws or (c) a Person that is an agent, department or instrumentality of, or is otherwise beneficially owned by, controlled by or acting on behalf of, directly or indirectly, any Person, entity, organization, country or regime described in clause (a) or (b).

"Business Day" means (a) for the purposes of **Section 8.6** only, any day other than a Saturday, a Sunday or a day on which commercial banks in New York City are required or authorized to be closed, and (b) for the purposes of any other provision of this Agreement, any day other than a Saturday, a Sunday or a day on which commercial banks in Philadelphia, Pennsylvania or New York, New York are required or authorized to be closed.

"Capital Lease" means, at any time, a lease with respect to which the lessee is required concurrently to recognize the acquisition of an asset and the incurrence of a liability in accordance with GAAP.

"Capital Lease Obligation" means, with respect to any Person and a Capital Lease, the amount of the obligation of such Person as the lessee under such Capital Lease which would, in accordance with GAAP, appear as a liability on a balance sheet of such Person.

"Change in Control" is defined in **Section 8.7**.

"Closing" is defined in **Section 3**.

"Code" means the Internal Revenue Code of 1986, as amended from time to time, and the rules and regulations promulgated thereunder from time to time.

"Company" means Aqua America, Inc., a Pennsylvania corporation.

"Confidential Information" is defined in **Section 20**.

"Consolidated Debt" means, as of any date of determination, the total of all Debt of the Company and its Subsidiaries outstanding on such date, after eliminating all offsetting debits and credits between the Company and its Subsidiaries and all other items required to be eliminated in the course of the preparation of consolidated financial statements of the Company and its Subsidiaries in accordance with GAAP.

"Consolidated Funded Debt" means, as of any date of determination, the total of all Funded Debt of the Company and its Subsidiaries outstanding on such date, after eliminating all offsetting debits and credits between the Company and its Subsidiaries and all other items required to be eliminated in the course of the preparation of consolidated financial statements of the Company and its Subsidiaries in accordance with GAAP.

"Consolidated Net Worth" means, as of any date of determination, the sum of (i) the par value (or value stated on the books of the corporation) of the capital stock (but excluding treasury stock and capital stock subscribed and unissued) of the Company and its Subsidiaries plus (ii) the amount of the paid-in capital and retained earnings of the Company and its Subsidiaries, in each case as such amounts would be shown on a consolidated balance sheet of the Company and its Subsidiaries as of such time prepared in accordance with GAAP.

"Consolidated Total Assets" means, as of any date of determination, the total amount of all assets of the Company and its Subsidiaries, as such amounts would be shown on a consolidated balance sheet of the Company and its Subsidiaries as of such time prepared in accordance with GAAP.

"Consolidated Total Capitalization" means, as of any date of determination, the sum of (i) Consolidated Funded Debt and (ii) Consolidated Net Worth.

"Controlled Entity" means (i) any of the Subsidiaries of the Company and any of their or the Company's respective Controlled Affiliates and (ii) if the Company has a parent company, such parent company and its Controlled Affiliates. As used in this definition, *"Control"* means the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a Person, whether through the ownership of voting securities, by contract or otherwise.

"Debt" means, with respect to any Person, without duplication,

(a) its liabilities for borrowed money;

(b) its liabilities for the deferred purchase price of property acquired by such Person (excluding accounts payable and other accrued liabilities arising in the ordinary course of business but including, without limitation, all liabilities created or arising under any conditional sale or other title retention agreement with respect to any such property);

(c) its Capital Lease Obligations;

(d) all liabilities for borrowed money secured by any Lien with respect to any property owned by such Person (whether or not it has assumed or otherwise become liable for such liabilities);

(e) all non-contingent liabilities in respect of reimbursement agreements or similar agreements in respect of letters of credit or instruments serving a similar function issued or accepted for its account by banks and other financial institutions;

EXECUTION COPY

AQUA PENNSYLVANIA, INC.

$40,000,000 5.95% Senior Notes
due March 31, 2034

NOTE PURCHASE AGREEMENT

DATED AS OF MARCH 31, 2006

1996608.01.14
162584-7

SECTION 10. NEGATIVE COVENANTS.

The Company covenants that so long as any of the Notes are outstanding:

Section 10.1. Limitation on Debt. The Company will not permit Consolidated Debt (determined as of the last day of each fiscal quarter) to exceed 62% of Consolidated Total Capitalization as of such date.

Section 10.2. Limitation on Liens. The Company will not, and will not permit any Subsidiary to, directly or indirectly create, incur, assume or permit to exist (upon the happening of a contingency or otherwise) any Lien on or with respect to any property or asset (including, without limitation, any document or instrument in respect of goods or accounts receivable) of the Company or any Subsidiary, whether now owned or held or hereafter acquired, or any income or profits therefrom, or assign or otherwise convey any right to receive income or profits, except:

(a) Liens for taxes, assessments or other governmental charges that are not yet due and payable or the payment of which is not at the time required by **Section 9.4**; *provided*, any such tax, assessment or other governmental charge shall be paid prior to the commencement of any proceedings to foreclose any Lien related thereto;

(b) any attachment or judgment Lien, unless the judgment it secures shall not, within 60 days after the entry thereof, have been discharged or execution thereof stayed pending appeal, or shall not have been discharged within 60 days after the expiration of any such stay;

(c) Liens incidental to the conduct of business or the ownership of properties and assets (including landlords', carriers', warehousemen's, mechanics', materialmen's and other similar Liens for sums not yet due and payable or which are being contested in good faith by appropriate proceedings diligently conducted) and Liens to secure the performance of bids, tenders, leases, or trade contracts, or to secure statutory obligations (including obligations under workers compensation, unemployment insurance and other social security legislation), surety or appeal bonds or other Liens incurred in the ordinary course of business and not in connection with the borrowing of money;

(d) leases or subleases granted to others, zoning restrictions, easements, rights-of-way, restrictions and other similar charges or encumbrances, in each case incidental to the ownership of property or assets or the ordinary conduct of the business of the Company or any of its Subsidiaries, *provided* that such Liens do not, materially impair the use of such property and which are not violated in any material respect by the existing or proposed use by the Company and its Subsidiaries of the properties subject to such Liens;

(e) Liens securing Debt of a Subsidiary to the Company or to a Subsidiary;

(f) Liens created under indentures, mortgages and deeds of trust securing Debt of the Company or a Subsidiary;

"Capital Lease" means, at any time, a lease with respect to which the lessee is required concurrently to recognize the acquisition of an asset and the incurrence of a liability in accordance with GAAP.

"Capital Lease Obligation" means, with respect to any Person and a Capital Lease, the amount of the obligation of such Person as the lessee under such Capital Lease which would, in accordance with GAAP, appear as a liability on a balance sheet of such Person.

"Change in Control" is defined in **Section 8.7**.

"Closing" is defined in **Section 3**.

"Code" means the Internal Revenue Code of 1986, as amended from time to time, and the rules and regulations promulgated thereunder from time to time.

"Company" means Aqua Pennsylvania, Inc., a Pennsylvania corporation.

"Confidential Information" is defined in **Section 20**.

"Consolidated Debt" means, as of any date of determination, the total of all Debt of the Company and its Subsidiaries outstanding on such date, after eliminating all offsetting debits and credits between the Company and its Subsidiaries and all other items required to be eliminated in the course of the preparation of consolidated financial statements of the Company and its Subsidiaries in accordance with GAAP.

"Consolidated Funded Debt" means, as of any date of determination, the total of all Funded Debt of the Company and its Subsidiaries outstanding on such date, after eliminating all offsetting debits and credits between the Company and its Subsidiaries and all other items required to be eliminated in the course of the preparation of consolidated financial statements of the Company and its Subsidiaries in accordance with GAAP.

"Consolidated Net Worth" means, as of any date of determination, the sum of (i) the par value (or value stated on the books of the corporation) of the capital stock (but excluding treasury stock and capital stock subscribed and unissued) of the Company and its Subsidiaries plus (ii) the amount of the paid-in capital and retained earnings of the Company and its Subsidiaries, in each case as such amounts would be shown on a consolidated balance sheet of the Company and its Subsidiaries as of such time prepared in accordance with GAAP.

"Consolidated Total Assets" means, as of any date of determination, the total amount of all assets of the Company and its Subsidiaries, as such amounts would be shown on a consolidated balance sheet of the Company and its Subsidiaries as of such time prepared in accordance with GAAP.

"Consolidated Total Capitalization" means, as of any date of determination, the sum of (i) Consolidated Funded Debt and (ii) Consolidated Net Worth.

"Debt" means, with respect to any Person, without duplication,

(a) its liabilities for borrowed money;

(b) its liabilities for the deferred purchase price of property acquired by such Person (excluding accounts payable and other accrued liabilities arising in the ordinary course of business but including, without limitation, all liabilities created or arising under any conditional sale or other title retention agreement with respect to any such property);

(c) its Capital Lease Obligations;

(d) all liabilities for borrowed money secured by any Lien with respect to any property owned by such Person (whether or not it has assumed or otherwise become liable for such liabilities);

(e) all non-contingent liabilities in respect of reimbursement agreements or similar agreements in respect of letters of credit or instruments serving a similar function issued or accepted for its account by banks and other financial institutions;

(f) Swaps of such Person; and

(g) Guaranties of such Person with respect to liabilities of a type described in any of clauses (a) through (f) hereof.

Debt of any Person shall include all obligations of such Person of the character described in clauses (a) through (g) to the extent such Person remains legally liable in respect thereof notwithstanding that any such obligation is deemed to be extinguished under GAAP.

"Default" means an event or condition the occurrence or existence of which would, with the lapse of time or the giving of notice or both, become an Event of Default.

"Default Rate" means with respect to the Notes, that rate of interest per annum that is the greater of (i) 7.66% per annum, or (ii) 2% over the rate of interest publicly announced by PNC Bank, N.A. in New York, New York as its "base" or "prime" rate.

"Environmental Laws" means any and all federal, state, local, and foreign statutes, laws, regulations, ordinances, rules, judgments, orders, decrees, permits, concessions, grants, franchises, licenses, agreements or governmental restrictions relating to pollution and the protection of the environment or the release of any materials into the environment, including but not limited to those related to hazardous substances or wastes, air emissions and discharges to waste or public systems.

"ERISA" means the Employee Retirement Income Security Act of 1974, as amended from time to time, and the rules and regulations promulgated thereunder from time to time in effect.

"Debt" means, with respect to any Person, without duplication,

(a) its liabilities for borrowed money;

(b) its liabilities for the deferred purchase price of property acquired by such Person (excluding accounts payable and other accrued liabilities arising in the ordinary course of business but including, without limitation, all liabilities created or arising under any conditional sale or other title retention agreement with respect to any such property);

(c) its Capital Lease Obligations;

(d) all liabilities for borrowed money secured by any Lien with respect to any property owned by such Person (whether or not it has assumed or otherwise become liable for such liabilities);

(e) all non-contingent liabilities in respect of reimbursement agreements or similar agreements in respect of letters of credit or instruments serving a similar function issued or accepted for its account by banks and other financial institutions;

(f) Swaps of such Person; and

(g) Guaranties of such Person with respect to liabilities of a type described in any of clauses (a) through (f) hereof.

Debt of any Person shall include all obligations of such Person of the character described in clauses (a) through (g) to the extent such Person remains legally liable in respect thereof notwithstanding that any such obligation is deemed to be extinguished under GAAP.

"Default" means an event or condition the occurrence or existence of which would, with the lapse of time or the giving of notice or both, become an Event of Default.

"Default Rate" means with respect to the Notes, that rate of interest per annum that is the greater of (i) 7.66% per annum, or (ii) 2% over the rate of interest publicly announced by PNC Bank, N.A. in New York, New York as its "base" or "prime" rate.

"Environmental Laws" means any and all federal, state, local, and foreign statutes, laws, regulations, ordinances, rules, judgments, orders, decrees, permits, concessions, grants, franchises, licenses, agreements or governmental restrictions relating to pollution and the protection of the environment or the release of any materials into the environment, including but not limited to those related to hazardous substances or wastes, air emissions and discharges to waste or public systems.

"ERISA" means the Employee Retirement Income Security Act of 1974, as amended from time to time, and the rules and regulations promulgated thereunder from time to time in effect.

AMENDED AND RESTATED CREDIT AGREEMENT

among

AQUA PENNSYLVANIA, INC.

and

THE BANKS PARTY HERETO

and

PNC BANK, NATIONAL ASSOCIATION
as Agent

Dated as of November 17, 2016

5.9 Taxes. Pay when due all taxes, assessments and governmental charges imposed upon it or any of its properties or that it is required to withhold and pay over, except where contested in good faith and where adequate reserves have been set aside to the extent required under GAAP.

5.10 Covenants of the Indenture. Comply at all times with the covenants contained in the Indenture, as last supplemented by the Supplemental Indenture, without regard to any amendment of or supplement to the Indenture occurring after October 15, 2010.

5.11 Guarantees of Obligations. It is the intent of the parties hereto that all of the obligations of the Borrower hereunder shall be unconditionally guaranteed by all of its Material Subsidiaries to the maximum extent permitted under any Requirement of Law applicable to any such Material Subsidiary. Accordingly, in the event that any Material Subsidiary shall be formed, acquired or come into existence after the date hereof then the Borrower will cause such Material Subsidiary to (i) execute and deliver a Guaranty Agreement in form and substance satisfactory to the Agent pursuant to which such Material Subsidiary will become a "Guarantor" hereunder, and guarantee the obligations of the Borrower hereunder and under the Notes and other Loan Documents and (ii) deliver such proof of corporate or other action, incumbency of officers, opinions of counsel and other documents as is consistent with those delivered by the Borrower pursuant to Section 4.1 on the Closing Date or as the Agent shall have reasonably requested.

5.12 Anti-Money Laundering/International Trade Law Compliance. No Covered Entity will become a Sanctioned Person. No Covered Entity, either in its own right or through any third party, will (a) have any of its assets in a Sanctioned Country or in the possession, custody or control of a Sanctioned Person in violation of any Anti-Terrorism Law; (b) do business in or with, or derive any of its income from investments in or transactions with, any Sanctioned Country or Sanctioned Person in violation of any Anti-Terrorism Law; (c) engage in any dealings or transactions prohibited by any Anti-Terrorism Law or (d) use the Loans to fund any operations in, finance any investments or activities in, or make any payments to, a Sanctioned Country or Sanctioned Person in violation of any Anti-Terrorism Law. The funds used to repay the Loans will not be derived from any unlawful activity. Each Covered Entity shall comply with all Anti-Terrorism Laws. The Borrower shall promptly notify the Agent in writing upon the occurrence of a Reportable Compliance Event.

SECTION 6. NEGATIVE COVENANTS

The Borrower hereby agrees that, so long as the Commitments remain in effect, any Note remains outstanding and unpaid or any other amount is owing to any Bank or the Agent hereunder, the Borrower shall not directly or indirectly:

6.1 Financial Covenants.

(a) Equity to Capital Ratio. Permit as of the end of any fiscal quarter the Equity to Capital Ratio to be less than thirty eight percent (38%).

(b) Interest Coverage Ratio. Permit as of the end of any fiscal quarter the Interest Coverage Ratio to be less than 1.8 to 1.

6.2 Limitation on Certain Debt. Except for the Loans and Commitments under the Loan Documents and the Term Loan Facilities, at any time enter into, assume or suffer to exist lines of credit or comparable extensions of credit from one or more commercial banks (or their Affiliates) under which the Borrower has incurred or may incur aggregate Debt in excess of $15,000,000.

6.3 Limitation on Liens. Create, incur, assume or suffer to exist any Lien upon any of its property, assets or revenues, including, without limitation, the stock of its Subsidiaries, whether now owned or hereafter acquired, except for:

(a) The following, (i) if the validity or amount thereof is being contested in good faith by appropriate and lawful proceedings diligently conducted so long as levy and execution thereon have been stayed and continue to be stayed or (ii) if a final judgment is entered and such judgment is discharged within thirty (30) days of entry, and in either case they do not materially impair the ability of the Borrower to perform its obligations hereunder or under the other Loan Documents:

(A) Claims or Liens for taxes, assessments or charges due and payable and subject to interest or penalty, provided that the Borrower maintains such reserves or other appropriate provisions as shall be required by GAAP and pays all such taxes, assessments or charges forthwith upon the commencement of proceedings to foreclose any such Lien;

(B) Claims, Liens or encumbrances upon, and defects of title to, real or personal property including any attachment of personal or real property or other legal process prior to adjudication of a dispute on the merits; and

(C) Claims or Liens of mechanics, materialmen, warehousemen, carriers, or other statutory nonconsensual Liens;

(b) pledges or deposits in connection with workers' compensation, unemployment insurance and other social security legislation;

(c) deposits to secure the performance of bids, trade contracts (other than for borrowed money), leases, statutory obligations, surety and appeal bonds, performance bonds and other obligations of a like nature incurred in the ordinary course of business of the Borrower;

(d) easements, rights-of-way, restrictions and other similar encumbrances incurred in the ordinary course of business which, in the aggregate, are not substantial in amount and which do not interfere with the ordinary conduct of the business of the Borrower;

(e) Liens which were in existence on the date hereof and shown on Schedule 6.3 and replacements, extensions or replacements thereof;

"Covered Entity": (a) the Borrower, each of the Borrower's Subsidiaries and all Guarantors and (b) each Person that, directly or indirectly, is in control of a Person described in clause (a) above. For purposes of this definition, control of a Person shall mean the direct or indirect (x) ownership of, or power to vote, 25% or more of the issued and outstanding equity interests having ordinary voting power for the election of directors of such Person or other Persons performing similar functions for such Person, or (y) power to direct or cause the direction of the management and policies of such Person whether by ownership of equity interests, contract or otherwise.

"Daily LIBOR Rate" shall mean, for any day, the rate per annum determined by the Agent by dividing (the resulting quotient rounded upwards, if necessary, to the nearest 1/100th of 1%) (x) the Published Rate by (y) a number equal to 1.00 minus the Eurocurrency Reserve Requirements. The Published Rate shall be adjusted as of each Business Day based on changes in the Published Rate or the Eurocurrency Reserve Requirements without notice to the Borrower, and shall be applicable from the effective date of any such change. Notwithstanding the foregoing, if the Daily LIBOR Rate as determined above would be less than zero, such rate shall be deemed to be zero for purposes of this Agreement.

"Debt": with respect to any Person, at any time, without duplication, all of (i) its liabilities for borrowed money, (ii) liabilities secured by any Lien existing on property owned by such Person (whether or not such liabilities have been assumed), (iii) its liabilities in respect to Capital Leases; (iv) its liabilities under Contingent Obligations; and (v) all other obligations which are required by GAAP to be shown as liabilities on its balance sheet but excluding (x) deferred taxes and other deferred or long-term liabilities and other amounts not in respect of borrowed money and (y) the aggregate amount of accounts receivable sold, factored or otherwise transferred for value without recourse (other than for breach of representations).

"Default": any of the events specified in Section 7, whether or not any requirement for the giving of notice, the lapse of time, or both, or any other condition precedent therein set forth, has been satisfied.

"Defaulting Bank": any Bank, as determined by the Agent, that has (a) failed to fund any portion of its Revolving Credit Loans or participations in Swing Line Loans within three Business Days of the date required to be funded by it hereunder, (b) notified the Borrower, the Agent, the Swing Line Bank or any Bank in writing that it does not intend to comply with any of its funding obligations under this Agreement or has made a public statement to the effect that it does not intend to comply with its funding obligations under this Agreement or under other agreements in which it commits to extend credit, (c) failed, within three Business Days after request by the Agent, to confirm that it will comply with the terms of this Agreement relating to its obligations to fund prospective Revolving Credit Loans or participations in Swing Line Loans, (d) otherwise failed to pay over to the Agent or any other Bank any other amount required to be paid by it hereunder within three Business Days of the date when due, unless the subject of a good faith dispute, or (e) (i) become or is insolvent or has a parent company that has become or is insolvent, (ii) become the subject of a Bail-In Action, or (iii)

become the subject of a bankruptcy or insolvency proceeding, or has had a receiver, conservator, trustee or custodian appointed for it, or has taken any action in furtherance of, or indicating its consent to, approval of or acquiescence in any such proceeding or appointment or has a parent company that has become the subject of a bankruptcy or insolvency proceeding, or has had a receiver, conservator, trustee or custodian appointed for it, or has taken any action in furtherance of, or indicating its consent to, approval of or acquiescence in any such proceeding or appointment (it being understood that a Defaulting Bank shall cease to be a Defaulting Bank if the Borrower, the Agent and the Swing Line Bank shall each agree that such Defaulting Bank has adequately remedied all matters that caused such Bank to be a Defaulting Bank).

"Distribution": in respect of any corporation, (a) dividends, distributions or other payments on account of any capital stock of the corporation (except distributions in common stock of such corporation); (b) the redemption or acquisition of such stock or of warrants, rights or other options to purchase such stock (except when solely in exchange for common stock of such corporation); and (c) any payment on account of, or the setting apart of any assets for a sinking or other analogous fund for, the purchase, redemption, defeasance, retirement or other acquisition of any share of any class of capital stock of such corporation or any warrants or options to purchase any such stock.

"Dollars" and "$": dollars in lawful currency of the United States of America.

"EEA Financial Institution": (i) any credit institution or investment firm established in any EEA Member Country which is subject to the supervision of an EEA Resolution Authority, (ii) any entity established in an EEA Member Country which is a parent of an institution described in clause (i) of this definition, or (iii) any financial institution established in an EEA Member Country which is a subsidiary of an institution described in clauses (i) or (ii) of this definition and is subject to consolidated supervision with its parent.

"EEA Member Country": any of the member states of the European Union, Iceland, Liechtenstein and Norway.

"EEA Resolution Authority" any public administrative authority or any person entrusted with public administrative authority of any EEA Member Country (including any delegee) having responsibility for the resolution of any EEA Financial Institution.

"Environmental Laws": any and all applicable foreign, Federal, state, local or municipal laws, rules, orders, regulations, statutes, ordinances, codes, decrees or binding requirements of any Governmental Authority, or binding Requirement of Law (including common law) regulating, relating to or imposing liability or standards of conduct concerning protection of the environment or public health, remediation of environmental conditions, or damages arising from such conditions, as now or may at any time hereafter be in effect.

"Equity to Capital Ratio": at the date of determination, the ratio of Consolidated Shareholders' Equity to the sum of (i) Consolidated Funded Debt and (ii) Consolidated Shareholders' Equity.

"ERISA": the Employee Retirement Income Security Act of 1974, as amended from time to time.

"EU Bail-In Legislation Schedule": the EU Bail-In Legislation Schedule published by the Loan Market Association (or any successor person), as in effect from time to time.

"Eurocurrency Reserve Requirements": for any day as applied to a Eurodollar Loan, the aggregate (without duplication) of the rates (expressed as a decimal fraction) of reserve requirements in effect on such day (including, without limitation, basic, supplemental, marginal and emergency reserves under any regulations of the Board of Governors of the Federal Reserve System or other Governmental Authority having jurisdiction with respect thereto) dealing with reserve requirements prescribed for eurocurrency funding (currently referred to as "Eurocurrency Liabilities" in Regulation D of such Board) maintained by a member bank of such System.

"Eurodollar Rate": with respect to the Loans comprising any Eurodollar Borrowing for any Interest Period, the interest rate per annum determined by the Agent by dividing (the resulting quotient rounded upwards, if necessary, to the nearest 1/100th of 1% per annum) (a) the rate which appears on the Bloomberg Page BBAM1 (or on such other substitute Bloomberg page that displays rates at which U.S. dollar deposits are offered by leading banks in the London interbank deposit market), or the rate which is quoted by another source selected by the Agent as an authorized information vendor for the purpose of displaying rates at which U.S. dollar deposits are offered by leading banks in the London interbank deposit market (for purposes of this definition, an "Alternate Source"), at approximately 11:00 a.m., London time, two (2) Business Days prior to the commencement of such Interest Period as the London interbank offered rate for U.S. Dollars for an amount comparable to such Eurodollar Borrowing and having a borrowing date and a maturity comparable to such Interest Period (or if there shall at any time, for any reason, no longer exist a Bloomberg Page BBAM1 (or any substitute page) or any Alternate Source, a comparable replacement rate determined by the Agent at such time (which determination shall be conclusive absent manifest error)), by (b) a number equal to 1.00 minus the Eurocurrency Reserve Requirements; provided, however, that if the Eurodollar Rate determined as provided above would be less than zero, such rate shall be deemed to be zero for purposes of this Agreement.

The Eurodollar Rate shall be adjusted with respect to any Eurodollar Borrowing that is outstanding on the effective date of any change in the Eurocurrency Reserve Requirements as of such effective date. The Agent shall give prompt notice to the Borrower of the Eurodollar Rate as determined or adjusted in accordance herewith, which determination shall be conclusive absent manifest error.

"Eurodollar Borrowing": a Borrowing comprised of Eurodollar Loans.

"Eurodollar Loan": any Revolving Credit Loan bearing interest at a rate determined by reference to the Eurodollar Rate in accordance with the provisions of Section 2.

"Event of Default": any of the events specified in Section 7, provided that any requirement for the giving of notice, the lapse of time, or both, or any other condition, has been satisfied.

"Excluded Taxes": as defined in subsection 2.12(a).

"Existing Credit Agreement": as defined in the Background to this Agreement.

"Exposure": as to any Bank at any date, an amount equal to the sum of (a) the aggregate principal amount of all Loans made by such Bank then outstanding and (b) the principal amount of such Bank's pro rata share of Swing Line Loans then outstanding based on its Commitment Percentage.

"FATCA": Sections 1471 through 1474 of the Code, as of the date of this Agreement (or any amended or successor version that is substantially comparable and not materially more onerous to comply with), any current or future regulations or official interpretations thereof and any agreement entered into pursuant to Section 1471(b)(1) of the Code.

"Federal Funds Effective Rate": for any day, the weighted average of the rates on overnight Federal funds transactions with members of the Federal Reserve System arranged by Federal funds brokers, as published on the next succeeding Business Day by the Federal Reserve Bank of New York, or, if such rate is not so published for any day which is a Business Day, the average of the quotations for the day of such transactions received by the Agent from three Federal funds brokers of recognized standing selected by it.

"Federal Funds Open Rate" for any day shall mean the rate per annum which is the daily federal funds open rate as quoted by ICAP North America, Inc. (or any successor) as set forth on the Bloomberg Screen BTMM for that day opposite the caption "OPEN" (or on such other substitute Bloomberg Screen that displays such rate), or as set forth on such other recognized electronic source used for the purpose of displaying such rate as selected by the Agent (an "Alternate Federal Funds Source") (or if such rate for such day does not appear on the Bloomberg Screen BTMM (or any substitute screen) or on any Alternate Federal Funds Source, or if there shall at any time, for any reason, no longer exist a Bloomberg Screen BTMM (or any substitute screen) or any Alternate Federal Funds Source, a comparable replacement rate determined by the Agent at such time (which determination shall be conclusive absent manifest error)); provided, that if such day is not a Business Day, the Federal Funds Open Rate for such day shall be the Federal Funds Open Rate on the immediately preceding Business Day."

"Fee Letter": the letter from the Agent to the Borrower dated November 14, 2016 regarding certain fees payable by the Borrower.

"Fees": as defined in subsection 2.4(a).

"Foreign Bank": any Bank that is not created or organized under the Laws of the United States, any State thereof or the District of Columbia.

"GAAP": at any time with respect to the determination of the character or amount of any asset or liability or item of income or expense, or any consolidation or other accounting computation, generally accepted accounting principles as applied to the public utility industry, as such principles shall be in effect on the date of, or at the end of the period covered by, the financial statements from which such asset, liability, item of income, or item of expense, is derived, or, in the case of any such computation, as in effect on the date when such computation is required to be determined, subject to Section 1.3(b).

"Governmental Authority": shall mean the government of the United States of America or any other nation, or of any political subdivision thereof, whether state or local, and any agency, authority, instrumentality, regulatory body, court, central bank or other entity exercising executive, legislative, judicial, taxing, regulatory or administrative powers or functions of or pertaining to government (including any supra-national bodies such as the European Union or the European Central Bank) and any group or body charged with setting financial accounting or regulatory capital rules or standards (including, without limitation, the Financial Accounting Standards Board, the Bank for International Settlements or the Basel Committee on Banking Supervision or any successor or similar authority to any of the foregoing).

"Guarantor": any Material Subsidiary which becomes a "Guarantor" after the date hereof pursuant to Section 5.11.

"Guaranty": any Guaranty Agreement entered into by a Guarantor pursuant to Section 5.11.

"Indenture": means the Indenture of Mortgage dated as of January 1, 1941 between the Borrower and Chase Manhattan Trust Company, National Association, as successor Trustee, as amended and supplemented.

"Insolvency": with respect to any Multiemployer Plan, the condition that such Plan is insolvent within the meaning of Section 4245 of ERISA.

"Insolvent": pertaining to a condition of Insolvency.

"Interest Coverage Ratio": at the date of determination, the ratio of Consolidated EBIT to Consolidated Interest Expense, in each case for the prior four (4) consecutive fiscal quarters.

"Interest Payment Date": (a) as to any Base Rate Loan or Swing Line Loan, the last day of each month, (b) as to any Eurodollar Loan having an Interest Period of three months or less, the last day of such Interest Period, and (c) as to any Eurodollar Loan having an Interest Period longer than three months, each day which is three months, or a

whole multiple thereof, after the first day of such Interest Period and the last day of such Interest Period.

"Interest Period": with respect to any Eurodollar Loan:

(i) initially the period commencing on the borrowing or conversion date, as the case may be, with respect to such Eurodollar Loan and ending one, two, three or six months thereafter, as selected by the Borrower in their notice of borrowing or notice of conversion, given with respect thereto; and

(ii) thereafter, each period commencing on the last day of the next preceding Interest Period applicable to such Eurodollar Loan and ending one, two, three or six months thereafter, as selected by the Borrower by irrevocable notice to the Agent not less than three Business Days prior to the last day of the then current Interest Period with respect thereto;

provided that, the foregoing provisions relating to Interest Periods are subject to the following:

(i) if any Interest Period would end on a day other than a Business Day, such Interest Period shall be extended to the next succeeding Business Day unless such next succeeding Business Day would fall in the next calendar month, in which case such Interest Period shall end on the next preceding Business Day;

(ii) any Interest Period that begins on the last Business Day of a calendar month (or on a day for which there is no numerically corresponding day in the calendar month at the end of such Interest Period) shall end on the last Business Day of a calendar month;

(iii) an Interest Period that otherwise would extend beyond the Termination Date shall end on the Termination Date; and

(iv) the Borrower shall select Interest Periods so as not to require a payment or prepayment of any Eurodollar Loan during an Interest Period for such Loan.

"Investments": investments (by loan or extension of credit, purchase, advance, guaranty, capital contribution or otherwise) made in cash or by delivery of Property, by the Borrower (i) in any Person, whether by acquisition of stock or other ownership interest, indebtedness or other obligation or Security, or by loan, advance or capital contribution, or (ii) in any Property or (iii) any agreement to do any of the foregoing.

"Law": any law(s) (including common law), constitution, statute, treaty, regulation, rule, ordinance, opinion, issued guidance, release, ruling, order, executive order, injunction, writ, decree, bond, judgment, authorization or approval, lien or award of or any settlement arrangement, by agreement, consent or otherwise, with any Governmental Body, foreign or domestic.

Published CUSIP Number: 03836VAE5
Revolving Facility CUSIP Number: 03836VAF2

CREDIT AGREEMENT

dated as of

December 5, 2018,

among

AQUA AMERICA, INC.,

the LENDERS party hereto

and

PNC BANK, NATIONAL ASSOCIATION,
as Administrative Agent

RBC CAPITAL MARKETS[1],
PNC CAPITAL MARKETS LLC,
MERRILL LYNCH, PIERCE, FENNER & SMITH INCORPORATED
and
COBANK, ACB,
as Joint Lead Arrangers and Joint Bookrunners

RBC CAPITAL MARKETS,
as Syndication Agent

and

BANK OF AMERICA, N.A.
and
COBANK, ACB,
as Documentation Agents

[CS&M Ref. No. 4025-142]

[1] RBC Capital Markets is a brand name for the capital markets activities of Royal Bank of Canada and its affiliates.

SECTION 6.03 Restrictive Agreements. The Company will not, and will not permit any Restricted Subsidiary to, enter into or permit to exist any contractual obligation (other than this Agreement or any other Loan Document) that limits the ability of any Restricted Subsidiary to make dividends or other distributions with respect to its Equity Interests to the Company or any Restricted Subsidiary, unless the Company determines in good faith that such contractual obligations would not materially impede the Company's ability to meet its payment obligations under this Agreement.

SECTION 6.04 Transactions with Affiliates. The Company will not, and will not permit any Restricted Subsidiary to, enter into or cause, suffer or permit to exist any transaction, arrangement or contract with any Affiliate (other than the Company or any Restricted Subsidiary) that is on terms materially less favorable to the Company or such Restricted Subsidiary than those that would be obtained at such time in a comparable arm's-length transaction with a Person other than an Affiliate, provided that the foregoing shall not apply to (a) any payments made and other transactions entered into in the ordinary course of business with officers and directors of the Company or any Subsidiary, and consulting fees and expenses incurred in the ordinary course of business payable to former officers or directors of the Company or any Subsidiary or (b) any other transaction (if part of a series of related transactions, together with such related transactions) involving consideration or value of less than $10,000,000.

SECTION 6.05 Financial Covenant. The Company will not permit the ratio, on the last day of any fiscal quarter of the Company, of (a) Consolidated Funded Debt as of such day to (b) the sum of (i) Consolidated Funded Debt as of such day and (ii) Consolidated Shareholders' Equity as of such day, to exceed 65%; provided that if the PNG Acquisition is consummated, the maximum ratio permitted by this Section 6.05 shall be (a) with respect to the fiscal quarter of the Company during which the PNG Acquisition Closing Date occurs and any subsequent fiscal quarter of the Company that ends no later than 180 days after the PNG Acquisition Closing Date, 80% and (B) with respect to any fiscal quarter of the Company that ends thereafter, 65%.

ARTICLE VII

Events of Default

SECTION 7.01 Events of Default. If any of the following events ("Events of Default") shall occur and be continuing:

(a) the Company shall fail to pay any principal of any Loan or any LC Disbursement when and as the same shall become due and payable, whether at the due date thereof or at a date fixed for prepayment thereof or otherwise;

(b) the Company shall fail to pay any interest or any fee or any other amount (other than an amount referred to in clause (a) of this Section 7.01) payable under this Agreement or any other Loan Document, when and as the same shall become due and payable, and such failure shall continue unremedied for a period of five days;

(c) any representation, warranty or statement of fact made or deemed made by or on behalf of the Company in any Loan Document or in any certificate, financial statement or

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR8. Attach copies of the summaries of the company's projected revenues, expenses and capital budgets for the next 2 years.

A. Please refer to Schedules B-1 and C-1 of Exhibit 1-A for water and Schedules B-1 and C-1 of Exhibits 1-B through 1-G for wastewater for the Company's projected revenues and expenses for the next 2 years. Please refer to RR26 for a listing of the future test year and fully projected future test year capital budget.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR9. Describe long-term debt reacquisitions by company and parent as follows:

a. Reacquisitions by issue by year.

b. Total gain on reacquisitions by issue by year.

c. Accounting of gain for income tax and book purposes.

A. The Company has called certain debt issuances in the past when the decision was to the benefit of the customer to do so.

a. Please see the attached.

b. None.

c. None.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
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Long Term Debt Refunding

Amount	Interest Rate	Maturity Date	Year of Refunding
$ 7,200,000	8.875%	6/1/2010	1992
$ 3,150,000	9.200%	12/15/2001	1993
$ 4,400,000	10.125%	5/15/1995	1993
$ 10,000,000	12.450%	8/1/2003	1993
$ 8,000,000	13.000%	7/1/2005	1995
$ 5,000,000	7.875%	12/1/1997	1996
$ 4,150,000	8.400%	5/1/2002	1996
$ 10,000,000	10.650%	4/1/2006	1996
$ 3,200,000	6.500%	6/1/2010	2002
$ 14,000,000	6.375%	10/15/2023	2004
$ 21,770,000	6.350%	8/15/2025	2005
$ 2,132,180	9.220%	11/15/2019	2007
$ 18,360,000	6.000%	7/1/2030	2010
$ 25,000,000	6.000%	6/1/2029	2010
$ 3,200,000	9.530%	12/15/2019	2012
$ 1,500,000	8.260%	11/1/2022	2012
$ 3,500,000	8.320%	11/1/2022	2012
$ 30,000,000	5.350%	10/1/2031	2012
$ 25,000,000	5.550%	9/1/2032	2012
$ 25,000,000	5.150%	9/1/2032	2013
$ 14,000,000	5.050%	10/1/2039	2014
$ 4,000,000	8.140%	11/1/2025	2015
$ 24,675,000	5.000%	2/1/2035	2015
$ 25,375,000	5.000%	11/1/2038	2015
$ 24,165,000	5.000%	11/1/2037	2015
$ 21,770,000	5.000%	11/1/2036	2015
$ 23,915,000	5.000%	2/1/2040	2017
$ 23,915,000	5.000%	2/1/2041	2017
$ 24,830,000	5.250%	7/1/1942	2018
$ 24,830,000	5.250%	7/1/1943	2018
$ 58,000,000	5.000%	10/1/2039	2019
$ 62,165,000	5.000%	11/15/2040	2019
$ 12,520,000	4.750%	11/15/2020	2019
$ 25,910,000	5.000%	12/1/2033	2020
$ 19,270,000	5.000%	12/1/2034	2020
$ 15,000,000	4.500%	12/1/2042	2020
$ 81,205,000	5.000%	12/1/2043	2020

AQUA PENNSYLVANIA, INC.
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FILING REQUIREMENTS

G. Rate of Return

RR10. Provide the following information concerning compensating bank balance requirements for actual per book test year:

a. Name of each bank.

b. Address of each bank.

c. Type of accounts with each bank (checking, savings, escrow, other services, etc.).

d. Average daily balance in each account.

e. Amount and percentage requirements for compensating bank balances at each bank.

f. Average daily compensating bank balance at each bank.

g. Documents from each bank explaining compensating bank balance requirements.

h. Interest earned on each type of account.

A. None. Compensating bank balances are not required.

AQUA PENNSYLVANIA, INC.
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G. Rate of Return

RR11. Provide the following information concerning bank notes payable for actual per book test year:

a. Line of credit at each bank.

b. Average daily balances of notes payable to each bank, by name of bank.

c. Interest rate charged on each bank note (prime rate, formula).

d. Purpose of each bank note, (for example, construction, fuel storage, working capital, debt retirement).

e. Prospective future need for this type of financing.

A. Please see the attached.

AQUA PENNSYLVANIA, INC.
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Lines of Credit

a. **Bank Name** — **Amount**

PNC Bank Revolver	$ 100,000,000	(includes $10,000,000 Swing Line Loan)

b. **Average Daily Balance for Historical Test Year**

PNC Bank Revolver	$ 43,000,613

c. **Formula Rate as Follows:**

PNC Bank Revolver

LIBOR rate + 65 basis points for 30, 60, 90 or 180 days, or
PNC Bank prime rate, or
Federal Funds rate + 50 basis points
Swing Line Loan: Federal Funds rate + 75 basis points

d. The proceeds of the lines of credit are used for working capital.

e. The Company anticipates that it will utilize bank loans in the future to provide interim funding for capital expenditures and acquisitions.

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G. Rate of Return

RR12. Submit details on company or parent common stock offerings for the past 5 years to present, as follows:

a. Date of prospectus.

b. Date of offering.

c. Record date.

d. Offering period including dates and number of days.

e. Amount and number of shares of offering.

f. Offering ratio, if rights offering.

g. Percent subscribed.

h. Offering price.

i. Gross proceeds per share.

j. Expenses per share.

k. Net proceeds per share in (12.) i and j.

l. Market price per share.

(1) At record date.

(2) At offering date.

(3) One month after close of offering.

m. Average market price during offering.

(1) Price per share.

(2) Rights per share-average value of rights.

n. Latest reported earnings per share at time of offering.

o. Latest reported dividends at time of offering.

A. Please see the attached for the details of the common stock offerings for the last 5 years to present.

Filed Pursuant to Rule 424(b)(5)
Registration No. 333-223306

Title of Each Class of Securities to be Registered	Amount to be Registered[1]	Maximum Offering Price per Unit[1]	Maximum Aggregate Offering Price[1]	Amount of Registration Fee[2]
Common Stock, par value $0.50 per share	37,370,017	$34.62	$1,293,749,988.54	$156,802.50

(1) Assumes full exercise of the underwriters' option to purchase up to an additional 4,874,350 shares of our Common Stock.
(2) Calculated in accordance with Rule 457(r) of the Securities Act of 1933, as amended.

Prospectus Supplement
(To Prospectus dated February 28, 2018)

32,495,667 Shares

AQUA AMERICA, INC.

Common Stock

We are offering 32,495,667 shares of our common stock, par value $0.50 per share (our "common stock"). Our common stock is listed on the New York Stock Exchange under the symbol "WTR." On April 17, 2019, the last reported sale price of our common stock on the New York Stock Exchange was $34.82 per share.

We intend to use the net proceeds from this offering, together with the net proceeds from the other Financing Transactions (as defined herein), to (1) fund the acquisition (the "Acquisition") of all of the issued and outstanding limited liability company membership interests of LDC Funding LLC ("LDC"), the parent of a group of natural gas public utility companies (collectively with LDC, "Peoples"), (2) complete the Company Debt Refinancing (as defined herein) and (3) pay related costs and expenses. This offering is not conditioned upon the consummation of the Acquisition. If the Acquisition is not consummated, we intend to use the net proceeds from this offering for general corporate purposes, which may include the Company Debt Refinancing, the redemption of securities issued in connection with the other Financing Transactions, repurchases of our common stock, debt repayment, capital expenditures and investments. See "Use of Proceeds."

Concurrently with this offering, we have commenced the TEU Offering (as defined herein), which is being made by means of a separate prospectus supplement and not by means of this prospectus supplement. This offering is not conditioned upon the completion of the other Financing Transactions, including the TEU Offering. This prospectus supplement is not an offer to sell or a solicitation of an offer to buy any securities offered in any of the other Financing Transactions.

Investing in our common stock involves risks. See "Risk Factors" on page S-13 of this prospectus supplement, page 8 of the accompanying prospectus and in the documents we incorporate by reference in this prospectus supplement and the accompanying prospectus.

	Per Share	Total[1]
Public Offering Price	$ 34.620	$1,124,999,992
Underwriting Discount	$ 0.779	$ 25,314,125
Proceeds, before expenses, to Aqua America	$ 33.841	$1,099,685,867

(1) Assumes no exercise of the underwriters' option to purchase additional shares, described below.

We have granted the underwriters the option, exercisable in whole or from time to time in part, to purchase up to an additional 4,874,350 shares of our common stock directly from us at the public offering price per share shown above, less the underwriting discount per share shown above, exercisable for 30 days after the date of this prospectus supplement.

Neither the U.S. Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus supplement or the accompanying prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The underwriters expect to deliver the shares of common stock to purchasers on or about April 23, 2019.

Joint Bookrunners

Goldman Sachs & Co. LLC | **Morgan Stanley** | **RBC Capital Markets**
BofA Merrill Lynch | | **Wells Fargo Securities**

Co-Managers

PNC Capital Markets LLC | **Barclays** | **Citizens Capital Markets** | **Huntington Capital Markets**
MUFG | **J.P. Morgan** | **TD Securities** | **Baird**
Boenning & Scattergood | **Janney Montgomery Scott** | | **HSBC**

April 17, 2019

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ABOUT THIS PROSPECTUS SUPPLEMENT

Unless otherwise specified or the context requires otherwise, references in this prospectus supplement to (1) "Aqua America," the "Company," "we," "us," "our" and similar references refer to Aqua America, Inc. and its subsidiaries prior to the proposed Acquisition, (2) the "combined company" refers to Aqua America and its subsidiaries after completion of the Acquisition (as defined herein) and (3) "this offering" refers to this offering of the shares pursuant to this prospectus supplement and the accompanying prospectus.

This document is in two parts. The first part is this prospectus supplement, which describes the specific terms of this offering of our common stock and also adds to and updates information contained in the accompanying prospectus and the documents incorporated by reference in the accompanying prospectus. The second part is the accompanying prospectus, which gives more general information about us, some of which does not apply to this offering of our common stock. To the extent the information in this prospectus supplement is inconsistent with the information in the accompanying prospectus, you should rely on the information in this prospectus supplement.

We have not, and the underwriters have not, authorized anyone to provide you with any information other than that contained or incorporated by reference in this prospectus supplement, the accompanying prospectus or in any free writing prospectus we may provide to you in connection with this offering. Neither we nor the underwriters take any responsibility for, or provide any assurances as to the reliability of, any additional or different information that others may give you. Neither we nor the underwriters are offering to sell our common stock or seeking offers to buy our common stock in jurisdictions where offers or sales are not permitted. You should assume that the information contained in this prospectus supplement, the accompanying prospectus and any related free writing prospectus is accurate only as of their respective dates or as of the respective dates specified in such information, as applicable, and the information contained in documents incorporated by reference is accurate only as of the respective dates of those documents or as of the respective dates specified in such information, as applicable, in each case regardless of the time of delivery of this prospectus supplement or the accompanying prospectus or any such free writing prospectus or any sale of our common stock. Our business, financial condition, results of operations and prospects may have changed since those dates.

The distribution of this prospectus supplement, the accompanying prospectus and any related free writing prospectus and the offering of our common stock in certain jurisdictions may be restricted by law. Persons into whose possession this prospectus supplement, the accompanying prospectus and any such free writing prospectus come should inform themselves about and observe any such restrictions. This prospectus supplement, the accompanying prospectus and any such free writing prospectus do not constitute, and may not be used in connection with, an offer or solicitation by anyone in any jurisdiction in which such offer or solicitation is not authorized or in which the person making such offer or solicitation is not qualified to do so or to any person to whom it is unlawful to make such offer or solicitation. See "Underwriting."

BASIS OF PRESENTATION

Unless otherwise specified or the context requires otherwise, the information in this prospectus supplement and the accompanying prospectus, including the documents incorporated by reference herein or therein, (1) does not give effect to any of the Transactions (as defined below), (2) when giving effect to this offering or the TEU Offering, assumes that the underwriters for this offering and the underwriters for the TEU Offering do not exercise their respective options to purchase additional shares of our common stock or additional TEUs (as defined herein), respectively, from us and (3) when giving effect to the Acquisition, assumes there are no adjustments to the Default Cash Acquisition Consideration (as defined herein) and that the Cash Acquisition Consideration (as defined herein) will therefore be $4.275 billion.

Although (1) the Acquisition has not yet occurred and, if completed, will not occur until after the closing of this offering, (2) this offering and certain of the other Financing Transactions are not contingent upon the completion of the other Financing Transactions, the Acquisition or the Company Debt Refinancing and (3) the indebtedness or other securities to be incurred or issued in certain of the Financing Transactions may not be incurred or issued, or may be redeemed, repaid, or repurchased, if the Acquisition is not consummated or is not consummated by a specified date, the pro forma and certain of the as adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus gives pro forma effect to the Acquisition, the Company Debt Refinancing and the Financing Transactions as if we had completed all such transactions as of December 31, 2018, in the case of balance sheet data, and as of January 1, 2018, in the case of income statement data, unless otherwise specified. The pro forma financial information included or incorporated by reference in this prospectus supplement does not, unless otherwise stated, give effect to our expected issuance of $150 million of the Debt Financing, because we intend to use that portion of the Debt Financing for general corporate purposes, including working capital and capital needs. See “Use of Proceeds.” Moreover, the unaudited pro forma consolidated combined financial information included in our Current Report on Form 8-K/A filed with the U.S. Securities and Exchange Commission (the “SEC”) on April 15, 2019, which is incorporated by reference in this prospectus supplement and the accompanying prospectus and may be obtained as described in this prospectus supplement under the heading “Where You Can Find Additional Information; Incorporation of Certain Documents by Reference,” and certain pro forma and as adjusted information included in this prospectus supplement, have been calculated on the basis of assumptions made by our management at the time such information was prepared. For example, such unaudited pro forma consolidated combined financial information and other adjusted information reflects assumptions regarding (a) the amount of proceeds we will receive from, and certain pricing and other terms of, the Financing Transactions, (b) the number of securities to be issued in connection with the Financing Transactions and (c) the terms on which the Acquisition and the Company Debt Refinancing will be completed. As a result, purchasers in this offering should not place undue reliance on the pro forma and as adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus because this offering is not contingent upon completion of any of the other transactions reflected in that information.

All references to currency amounts included in this prospectus supplement are in U.S. dollars unless specifically noted otherwise.

FORWARD-LOOKING STATEMENTS

Certain statements in this prospectus supplement, the accompanying prospectus and the documents they incorporate by reference contain, and any free writing prospectus we may provide to you in connection with this offering are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act") that are made based upon, among other things, our current assumptions, expectations, plans, and beliefs concerning future events and their potential effect on us. These forward-looking statements involve risks, uncertainties and other factors, many of which are outside our control that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. In some cases you can identify forward-looking statements where statements are preceded by, followed by or include the words "believes," "expects," "anticipates," "plans," "future," "potential," "probably," "predictions," "intends," "will," "continue," "in the event" or the negative of such terms or similar expressions. Such forward-looking statements include, but are not limited to, statements regarding:

- recovery of capital expenditures and expenses in rates;
- projected capital expenditures and related funding requirements;
- our capability to pursue timely rate increase requests;
- the availability and cost of capital financing;
- developments, trends and consolidation in the water and wastewater utility and infrastructure industries;
- dividend payment projections;
- opportunities for future acquisitions, both within and outside the water and wastewater industry, the success of pending acquisitions and the impact of future acquisitions;
- expectations regarding the proposed Acquisition, including statements regarding regulatory approvals for the Acquisition, potential financing transactions related to the Acquisition (including statements regarding the Financing Transactions and the use of proceeds therefrom, including the Company Debt Refinancing), closing of the Acquisition or the impact of the Acquisition on the Company;
- the capacity of our water supplies, water facilities and wastewater facilities;
- the impact of federal and/or state tax policies, including changes in tax laws and policies as a result of the Tax Cuts and Jobs Act of 2017, and the regulatory treatment of the effects of those policies;
- the impact of geographic diversity on our exposure to unusual weather;
- the impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer;
- our authority to carry on our business without unduly burdensome restrictions;
- the continuation of investments in strategic ventures;
- our ability to obtain fair market value for condemned assets;
- the impact of fines and penalties;
- the impact of changes in and compliance with governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- the impact of decisions of governmental and regulatory bodies, including decisions to raise or lower rates and decisions regarding potential acquisitions;
- the development of new services and technologies by us or our competitors;

- the availability of qualified personnel;
- the condition of our assets;
- the impact of legal proceedings;
- general economic conditions;
- acquisition-related costs and synergies;
- the sale of water and wastewater divisions; and
- the amount of income tax deductions for qualifying utility asset improvements and the Internal Revenue Service's ultimate acceptance of the deduction methodology.

Because forward-looking statements involve risks and uncertainties, there are important factors that could cause actual results to differ materially from those expressed or implied by these forward-looking statements, including but not limited to:

- our ability to integrate and otherwise realize all of the anticipated benefits of businesses, technologies or services which we may acquire;
- our ability to manage the expansion of our business, including our ability to manage our expanded operations following the closing of the Acquisition;
- changes in general economic, business, credit and financial market conditions;
- changes in governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- our ability to treat and supply water or collect and treat wastewater;
- Peoples's ability to transport, distribute and store natural gas;
- the profitability of future acquisitions;
- changes to the rules or our assumptions underlying our determination of what qualifies for an income tax deduction for qualifying utility asset improvements;
- conditions to the completion of the Acquisition may not be satisfied or waived on a timely basis, or at all;
- the decisions of governmental and regulatory bodies, including decisions on rate increase requests and decisions regarding potential acquisitions;
- our ability to file rate cases on a timely basis to minimize regulatory lag;
- abnormal weather conditions, including those that result in water use restrictions and seasonality effects;
- changes in, or unanticipated, capital requirements;
- changes in our credit ratings or the market price of our common stock;
- changes in valuation of strategic ventures;
- the extent to which we are able to develop and market new and improved services;
- the effect of the loss of major customers;
- our ability to retain the services of key personnel and to hire qualified personnel as we expand;
- the diversion of our management's time and resources caused by the announcement and pendency of the Acquisition;

- labor disputes;
- increasing difficulties in obtaining insurance and increased cost of insurance;
- cost overruns relating to improvements to, or the expansion of, our operations;
- increases in the costs of goods and services and commodity prices;
- civil disturbance or terroristic threats or acts;
- the continuous and reliable operation of our information technology systems, including the impact of cyber security attacks or other cyber-related events;
- changes in accounting pronouncements;
- litigation and claims;
- changes in environmental conditions, including the effects of climate change;
- restrictions on our subsidiaries' ability to make dividends and other distributions;
- restrictions and limitations that may stem from financing arrangements we enter into or assume in the future, or from the redemptions and repurchases we may undertake if the Acquisition is not consummated;
- dilution to our shareholders related to any financing transactions, including the Financing Transactions; and
- broad discretion of our management to use the net proceeds from this offering if the Acquisition is not consummated.

Given these risks and uncertainties, you should not place undue reliance on any forward-looking statements. You should read this prospectus supplement, the accompanying prospectus and the documents that we incorporate by reference into this prospectus supplement completely and with the understanding that our actual results, performance and achievements may be materially different from what we expect. These forward- looking statements represent assumptions, expectations, plans and beliefs only as of the date of this prospectus supplement, the date of the document containing the applicable statement or the date specified in such statement, as applicable. Except for our ongoing obligations to disclose certain information under the federal securities laws, we are not obligated, and assume no obligation, to update these forward-looking statements, even though our situation may change in the future. For further information or other factors which could affect our financial results and such forward-looking statements, see "Risk Factors." We qualify all of our forward-looking statements by these cautionary statements.

Investing in our common stock involves risks. You should review and consider carefully the risks, uncertainties and other factors that affect our business, financial condition and results of operations and the value of the shares, including those described in the "Business," "Risk Factors," and "Management's Discussion and Analysis of Financial Condition and Results of Operations" sections and other sections in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018, and our Current Report on Form 8-K/A filed with the SEC on April 15, 2019, which are incorporated by reference in this prospectus supplement, and those described in the "Risk Factors" sections and other sections of this prospectus supplement and the accompanying prospectus. You may obtain copies of these reports and documents as described under "Where You Can Find Additional Information; Incorporation of Certain Documents by Reference" in this prospectus supplement. These risks, uncertainties and other factors could cause you to suffer a loss of all or part of your investment in the shares. Before making an investment decision, you should carefully consider these risks, uncertainties and other factors, as well as other information contained or incorporated by reference in this prospectus supplement and the accompanying prospectus and any related free writing prospectus we may provide to you in connection with this offering. However, additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our business, operations, financial condition and financial results and the value of the shares.

MARKET AND INDUSTRY DATA

This prospectus supplement, the accompanying prospectus and the documents incorporated by reference in this prospectus supplement and the accompanying prospectus include, and any free writing prospectus we may provide to you in connection with this offering may include, market, demographic and industry data and forecasts related to our business and to Peoples's business that are based on or derived from sources such as independent industry publications, publicly available information, government data and other information from third parties or that have been compiled or prepared by our or Peoples's management or employees. We do not guarantee the accuracy or completeness of any of this information, and we have not independently verified any of the information provided by third-party sources.

In addition, market, demographic and industry data and forecasts involve estimates, assumptions and other uncertainties and are subject to change based on various factors, including those discussed under the heading "Risk Factors" in this prospectus supplement and under similar headings in the documents that are incorporated by reference in this prospectus supplement and the accompanying prospectus. Accordingly, you should not place undue reliance on any of this information.

SUMMARY INFORMATION

The following summary highlights, and should be read together with, the information contained elsewhere in this prospectus supplement, the accompanying prospectus and the documents incorporated by reference herein and therein. This summary may not contain all of the information that may be important to you, and you should carefully read this entire prospectus supplement, the accompanying prospectus, any free writing prospectus we may provide to you in connection with this offering and the documents incorporated by reference herein and therein before making an investment decision. You may obtain a copy of the documents incorporated by reference by following the instructions in the section titled "Where You Can Find Additional Information; Incorporation of Certain Documents by Reference," in this prospectus supplement. Unless we state otherwise or the context otherwise requires, references appearing in this prospectus supplement to "Aqua America," the "Company," "we," "us" and "our" should be read to refer to Aqua America, Inc. and its subsidiaries.

Aqua America, Inc.

Aqua America, Inc., a Pennsylvania corporation, is the holding company for regulated utilities providing water or wastewater services to an estimated three million people in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana, and Virginia. Our largest operating subsidiary is Aqua Pennsylvania, Inc., which accounted for approximately 53% of our operating revenues and approximately 71% of our regulated segment's income for 2018. As of December 31, 2018, Aqua Pennsylvania provided water or wastewater services to approximately one-half of the total number of people we serve. Aqua Pennsylvania's service territory is located in the suburban areas in counties north and west of the City of Philadelphia and in 27 other counties in Pennsylvania. Our other regulated utility subsidiaries provide similar services in seven other states. In addition, the Company's market-based activities are conducted through Aqua Infrastructure, LLC ("Aqua Infrastructure") and Aqua Resources Inc. ("Aqua Resources"). Aqua Infrastructure provides non-utility raw water supply services for firms in the natural gas drilling industry. Aqua Resources provides water service through operating and maintenance contracts with a municipal authority and another party close to our utility companies' service territory; and offers, through a third-party, water and sewer line protection solutions and repair services to households. In 2017, we completed the sale of two business units that were reported within Aqua Resources, one which installed and tested devices that prevent the contamination of potable water and another that constructed, maintained, and repaired water and wastewater systems. Additionally, during 2016, we completed the sale of business units within Aqua Resources, which provided liquid waste hauling and disposal services and inspection, and cleaning and repair of storm and sanitary wastewater lines.

Aqua America, which prior to its name change in 2004 was known as Philadelphia Suburban Corporation, was formed in 1968 as a holding company for its primary subsidiary, Aqua Pennsylvania, formerly known as Philadelphia Suburban Water Company. In the early 1990s, we embarked on a growth through acquisition strategy focused on water and wastewater operations. Our most significant transactions to date have been the merger with Consumers Water Company in 1999, the acquisition of the regulated water and wastewater operations of AquaSource, Inc. in 2003, the acquisition of Heater Utilities, Inc. in 2004, and the acquisition of American Water Works Company, Inc.'s regulated water and wastewater operations in Ohio in 2012. Since the early 1990s, our business strategy has been primarily directed toward the regulated water and wastewater utility industry, where we have more than quadrupled the number of regulated customers we serve, and have extended our regulated operations from southeastern Pennsylvania to include our current regulated utility operations throughout Pennsylvania and in seven other states. During 2010 through 2013, we sold our utility operations in six states, pursuant to a portfolio rationalization strategy to focus our operations in areas where we have critical mass and economic growth potential. Currently, the Company seeks to acquire businesses in the U.S. regulated sector, which includes water and wastewater utilities and other regulated utilities, and to pursue growth ventures in market-based activities, such as infrastructure opportunities that are supplementary and complementary to our regulated businesses. On October 22, 2018, we entered into a purchase agreement to acquire a group of natural gas public utility companies that we refer to as "Peoples." Peoples serves approximately 740,000 gas utility

customers in western Pennsylvania, West Virginia, and Kentucky. See "—Recent Developments—Proposed Peoples Gas Acquisition" for additional information regarding Peoples and the Acquisition.

Our growth in revenues over the past five years is primarily a result of increases in water and wastewater rates and customer growth. The increase in our utility customer base, as shown below, has been due to customers added through acquisitions, partnerships with developers, and organic growth (excluding dispositions):

Year	Utility Customer Growth Rate
2018	2.3%
2017	1.1%
2016	1.6%
2015	1.9%
2014	1.3%

In 2018, our customer count increased by 22,741 customers, primarily due to utility systems that we acquired and organic growth. Overall, for the five-year period of 2014 through 2018, our utility customer base, adjusted to exclude customers associated with utility system dispositions, increased at an annual compound rate of 1.6%. During the five-year period ended December 31, 2018, our utility customer base, including customers associated with utility system acquisitions and dispositions, increased from 941,008 at January 1, 2014 to 1,005,590 at December 31, 2018. This five-year period includes the impact of the condemnation of our Fort Wayne, Indiana system in 2014, which resulted in the loss of approximately 13,000 connections.

Our principal executive office is located at 762 W. Lancaster Avenue, Bryn Mawr, Pennsylvania 19010- 3489, and our telephone number is 610-527-8000. Our website may be accessed at *www.aquaamerica.com*. The reference to our website is intended to be an inactive textual reference only, and the contents of our website is not incorporated by reference herein and should not be considered part of this prospectus supplement.

Our Business Strategy

Since the early 1990s, our business strategy has been primarily directed toward the regulated water and wastewater utility industry, where we have more than quadrupled the number of regulated customers we serve, and have extended our regulated operations from southeastern Pennsylvania to include our current regulated utility operations throughout Pennsylvania and in seven other states. We are focused on operating our businesses in a safe and efficient manner to provide exceptional service to our customers. Our key strategic priorities are as follows:

Pursue High-Quality, Low-Risk Earnings Growth

Growth in our existing water and wastewater utility business comes from both customer growth and increases in water and wastewater rates, driven by utility infrastructure investment. We expect to invest approximately $1.4 billion into our existing water utility infrastructure over the 2019-2021 timeframe including approximately $550 million in 2019. These estimates exclude planned capital expenditures by Peoples and the costs of new mains financed by advances and contributions in aid of construction. Our investment plans are supported by constructive regulatory environments in the jurisdictions in which we operate, and are expected to result in annual rate base growth over the same time period. Our regulators have a track record of setting rates and establishing terms of service that allow our regulated subsidiaries to obtain a fair and reasonable return on capital invested. Further, several of our regulators have put in place programs that incentivize prudent investments in our utility system by providing for reduced regulatory lag. For example, New Jersey allows for an infrastructure rehabilitation surcharge for water utilities, while Pennsylvania, Illinois, Ohio, Indiana and North Carolina allow for the use of an infrastructure rehabilitation surcharge for both water and wastewater utility

systems. Aqua Virginia is also piloting an infrastructure rehabilitation surcharge for its water and wastewater utilities to be implemented in 2019, pursuant to the final order issued in Aqua Virginia's 2018 rate case.

In addition to our organic infrastructure investment, we expect to continue to actively explore opportunities to expand our operations through acquisitions of government-owned and regulated water and wastewater systems that provide services in areas near our existing service territories or in new service areas. With approximately 50,000 community water systems in the United States, 81% of which serve less than 3,300 customers, the water industry is the most fragmented of the major utility industries (telephone, natural gas, electric, water and wastewater). In the states where we operate regulated utilities, we believe there are approximately 14,000 community water systems of widely-varying size, with the majority of the population being served by government-owned water systems. Because of the fragmented nature of the water and wastewater utility industries, we believe that there are many potential water and wastewater system acquisition candidates throughout the United States. We believe numerous factors will drive continued consolidation of these systems, including the benefits of economies of scale, the increasing cost and complexity of environmental regulations, the need for substantial capital investment and the need for technological and managerial expertise.

Six of the states in which we operate currently have some form of fair market value legislation. This legislation allows the relevant public utility commission to utilize fair market value to set ratemaking rate base instead of the depreciated original cost of water or wastewater assets for certain qualifying municipal acquisitions. We believe that this legislation is another factor that will encourage consolidation in the water and wastewater industry, providing municipalities with an option for exiting the business if they are dealing with challenges associated with their aging, deteriorating water and wastewater assets, do not have the expertise or technical capabilities to continue to comply with ever increasing environmental regulations or simply want to focus on other community priorities. In 2018, we closed six municipal acquisitions with over 13,700 customers and over $100 million of rate base.

Maintain a Low-Risk Regulated Utility Profile

Our core skill set is operating, maintaining and growing a regulated utility platform. The vast majority of our earnings are derived from regulated utilities, and we intend to maintain our focus on regulated utility platforms. As further discussed in "—Recent Developments—Peoples Gas Acquisition—Strategic Rationale for the Acquisition," the Acquisition is consistent with this strategy. Our focus on regulated utilities has contributed to our historically stable earnings and cash flows, which forms the foundation for our dividend policy and has allowed us to raise dividends 28 times in the last 27 years.

Maintain Our Commitment to a Strong Balance Sheet

Our goal is to maintain a strong balance sheet and liquidity position in addition to solid investment grade credit ratings. We believe maintaining these objectives affords us the financial flexibility necessary to take advantage of significant growth opportunities in our regulated utility businesses.

Our Competitive Strengths

We believe that we are well-positioned to meet our obligations to customers, grow our business and create shareholder value because of the following factors:

Extensive Track Record of Operating Stable Utilities

Our earnings are principally derived from the return on investment we earn on our utility assets. We estimate that, as of December 31, 2018, our rate base was approximately $4.5 billion. We estimate that, as of December 31, 2019, assuming consummation of the Acquisition, our rate base will be approximately $7.2 billion. Of the $7.2 billion expected rate base as of December 31, 2019, we estimate that approximately 70%

will be derived from water and wastewater utilities and approximately 30% will be derived from natural gas distribution. We have more than 130 years of service experience and a proven track record of operational efficiency.

Operations in Constructive Regulatory Jurisdictions

We currently have regulated utility operations in eight different states, which have collectively provided constructive regulatory environments for our utility operations, and following the Acquisition will have regulated utility operations in ten different states, which we believe will provide constructive regulatory environments for our expanded utility operations. Two of these ten states have in place rate decoupling mechanisms for water or gas utility businesses, which reduce the dependency of our revenues to the changes in the volume of managed water or natural gas that may result from fluctuations in the weather, gas consumption, water conservation, and other factors. Further, regulators in several of these states have put in place certain programs that incentivize prudent capital investments in our utility system by providing for accelerated recovery of and on capital. The regulatory framework in Pennsylvania, which accounted for approximately 71% of our Regulated segment's income for 2018, is generally considered progressive and is highly rated by Regulatory Research Associates. Pennsylvania's high rating is based on the probable level and quality of the earnings to be realized by the state's utilities as a result of regulatory, legislative and court actions, as well as the utilization of fully forecasted test years, Distribution Systems Improvement Charges and other automatic adjustment clauses that are intended to reduce the gap between the time that a capital project is completed and the recovery of costs in rates. As further discussed in "—Recent Developments —Peoples Gas Acquisition—Strategic Rationale for the Acquisition," the Acquisition would increase our presence in constructive regulatory jurisdictions, particularly in Pennsylvania.

Significant Infrastructure Needs & Core Competency in Infrastructure Investment

According to recent U.S. EPA surveys, there are approximately 50,000 community water systems and approximately 15,000 wastewater systems in the United States, a majority of which are municipally owned, and more than $740 billion will need to be spent to maintain and improve U.S. water and wastewater infrastructure over the next 20 years. We have historically leveraged our expertise in infrastructure improvement and pipeline replacement to improve safety and reliability throughout the states in which we operate. For example, over the last 15 years, our investment in pipe replacement in southeastern Pennsylvania has resulted in a 53% reduction in discolored water-quality-related service orders and a 60% reduction in main breaks. As municipalities face the challenges of replacing deteriorating infrastructure, we provide a viable and valuable solution to communities through our expertise and our economies of scale. In addition, we expect the Acquisition will introduce new infrastructure investment opportunities, as discussed in "—Recent Developments—Peoples Gas Acquisition— Strategic Rationale for the Acquisition."

Consistent History of Dividend Growth. We have paid dividends consecutively for 74 years

In 2018, our Board of Directors raised the quarterly dividend on our common stock by 7%, increasing the effective annual dividend rate to $0.876 per share, beginning with the dividend payment in September 2018. This is the 28th dividend increase in the past 27 years and the 20th consecutive year that we have increased our dividend in excess of 5%.

Experienced Management Team

Our senior management team is highly experienced in the utility industry. The team is supported by a core group of employees in leadership positions with substantial experience in the operation of regulated utility businesses. In addition, as discussed in "—Recent Developments—Peoples Gas Acquisition—Strategic Rationale for the Acquisition," the Peoples's management team has significant experience in the natural gas utility industry. Additionally, the Aqua America CEO serves on the Board of Directors of the National Association of Water Companies.

Recent Developments

Proposed Peoples Gas Acquisition

On October 22, 2018, we entered into a Purchase Agreement (the "Acquisition Agreement") with LDC Parent LLC, a Delaware limited liability company ("Seller"), to acquire all of the issued and outstanding limited liability company membership interests of LDC, the parent of a group of natural gas public utility companies including Peoples Natural Gas Company LLC, a Pennsylvania limited liability company, Peoples Gas Company LLC, a Pennsylvania limited liability company, Peoples Gas WV LLC, a West Virginia limited liability company, Peoples Gas Kentucky LLC, a Kentucky limited liability company, and Delta Natural Gas Co., Inc., a Kentucky corporation, as well as other operating subsidiaries.

The Acquisition, once consummated, will expand our regulated utility business to include natural gas distribution. The cash purchase price for the Acquisition will be an amount equal to $4.275 billion (the "Default Cash Acquisition Consideration"), subject to adjustments for working capital, certain capital expenditures, transaction expenses and closing indebtedness as set forth in the Acquisition Agreement (as so adjusted, the "Cash Acquisition Consideration"). The Company expects to assume, as a result of acquiring Peoples, approximately $1,370 million of Peoples's indebtedness upon the closing of the Acquisition, which would reduce the cash purchase price by approximately $1,370 million pursuant to the foregoing adjustments. See "— Financing Transactions" and "Use of Proceeds" for a discussion of our plans to finance the Cash Acquisition Consideration.

Closing of the Acquisition is subject to customary closing conditions set forth in the Acquisition Agreement, including, among others, (1) the absence of any law or governmental order prohibiting the consummation of the Acquisition, (2) the accuracy of the parties' representations and warranties, subject to customary materiality standards and certain other exceptions, (3) compliance in all material respects of the parties with their applicable covenants under the Acquisition Agreement, subject to certain exceptions, (4) the absence of a "material adverse effect" with respect to LDC and its subsidiaries and (5) receipt of certain regulatory approvals, including from the public utility commission in Pennsylvania and West Virginia. The closing of the Acquisition is not subject to any financing condition. We currently expect the Acquisition will close in mid-2019.

The Acquisition Agreement contains certain termination rights for each of us and Seller. The Acquisition Agreement may be terminated at any time prior to the closing of the Acquisition in the event the Acquisition is not completed by October 22, 2019 (subject to extension, on the terms set forth in the Acquisition Agreement, to April 22, 2020 in order to obtain necessary regulatory approvals) (the "Acquisition Outside Date"). However, neither we nor Seller may terminate the Acquisition Agreement pursuant to the foregoing if our or Seller's respective failure to fulfill any obligation under the Acquisition Agreement was the primary cause of the failure of the closing to occur on or before the Acquisition Outside Date. The Acquisition Agreement may also be terminated at any time prior to the closing of the Acquisition by mutual written consent of us and Seller, and in other customary circumstances. In the event that the Acquisition Agreement is terminated due to certain breaches by us, we would be required to pay a fee of $120 million to the Seller as liquidated damages.

The Acquisition and the Acquisition Agreement are described in more detail in our Current Report on Form 8-K filed with the SEC on October 23, 2018 (the "Acquisition 8-K"), which is incorporated by reference into this prospectus supplement and the accompanying prospectus. The foregoing summary description does not purport to be complete and is qualified in its entirety by reference to the complete text of the Acquisition Agreement, which was filed as Exhibit 2.1 to the Acquisition 8-K.

The Acquisition Agreement has been filed as an exhibit to our public reports filed with the SEC, and has been incorporated by reference into this prospectus supplement and the accompanying prospectus, solely to provide information to current and prospective investors and security holders regarding its terms. The Acquisition

Agreement and the description of certain terms of the Acquisition Agreement appearing in this prospectus supplement and some of the documents incorporated by reference in the accompanying prospectus are not intended to provide any other factual information about Aqua America, Peoples, their respective businesses, or the actual or future conduct of their respective businesses or to modify or supplement any factual disclosures about Aqua America or Peoples included in this prospectus supplement, the accompanying prospectus or the documents incorporated by reference therein or Aqua America's other public reports. The Acquisition Agreement and any descriptions thereof should not be relied upon as representations or warranties about Aqua America or Peoples or, other than with respect to the terms of the Acquisition Agreement, as disclosure about Aqua America or Peoples. No one should rely on the representations, warranties and covenants in the Acquisition Agreement or any descriptions thereof as characterizations of the actual state of facts or conditions of Aqua America or Peoples or any of their respective subsidiaries or affiliates. The representations and warranties contained in the Acquisition Agreement are the product of negotiations among the parties thereto and that the parties made to, and solely for the benefit of, each other as of specified dates. The assertions embodied in those representations and warranties are subject to qualifications and limitations agreed to by the respective parties and are also qualified in important part by confidential disclosure schedules delivered in connection with the Acquisition Agreement. In addition, those representations and warranties were made for the purpose of allocating contractual risk between the parties to the Acquisition Agreement instead of establishing these matters as facts, and may be subject to standards of materiality used by the contracting parties that differ from those applicable to investors and security holders. Moreover, information concerning the subject matter of the representations and warranties may change after the dates contemplated by the Acquisition Agreement, which subsequent information may or may not be reflected in this prospectus supplement or the documents incorporated by reference in this prospectus supplement and the accompanying prospectus or in Aqua America's other public reports. The Acquisition Agreement and any such descriptions thereof should not be read alone, but should instead be read in conjunction with the other information regarding Aqua America or Peoples that is contained in, or incorporated by reference into, this prospectus supplement, the accompanying prospectus and the documents incorporated by reference herein and therein.

The consummation of this offering is not conditioned upon the closing of the Acquisition. There can be no assurance that the Acquisition will be consummated on the terms or by the time currently contemplated, or at all, or, if consummated, that the terms of the Acquisition, including the financing thereof and the closing date, will not differ, perhaps substantially, from those currently contemplated or described in this prospectus supplement or the documents incorporated by reference in this prospectus supplement and the accompanying prospectus. The closing of the Acquisition is subject to, among other conditions, the receipt of regulatory approval by the Pennsylvania Public Utility Commission. We filed an application for approval by the Pennsylvania Public Utility Commission, and several entities have intervened in the proceeding. The procedural schedule requires rebuttal testimony to be filed on April 30, 2019. We have initiated settlement discussions with the intervenors and those negotiations are ongoing. Whether through a settlement agreement or through a litigated proceeding, we may be required to agree to certain actions, undertakings, terms, or other measures, including those that may require increased capital or other expenditures by the Company. See "Risk Factors—Risks Related to the Acquisition and the Financing Transactions" in this prospectus supplement, "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018 and "Risk Factors" in our Current Report on Form 8-K/A filed with the SEC on April 15, 2019 (as updated by annual, quarterly and other reports and documents we file with the SEC that are incorporated by reference in this prospectus supplement and the accompanying prospectus).

About Peoples

Headquartered in Pittsburgh, Pennsylvania, Peoples primarily engages in regulated distribution and transportation of natural gas to approximately 740,000 residential, commercial and industrial customers in Pennsylvania, West Virginia and Kentucky. For the year ended December 31, 2018, Peoples's operating revenues amounted to $914 million.

For a discussion of Peoples's business, operations, financial condition and financial results and the specific risks related to Peoples's business, operations, financial condition and financial results, please see the "Peoples's Business," "Risk Factors related to Peoples" and "Management's Discussion and Analysis of Financial Condition and Results of Operations of Peoples" in our Current Report on Form 8-K/A filed with the SEC on April 15, 2019 and incorporated by reference in this prospectus supplement and the accompanying prospectus.

Strategic Rationale for the Acquisition

We believe the Acquisition is a strategically compelling transaction that brings together two high- quality regulated utility companies in regions with constructive regulatory environments and attractive demographics. Consistent with our strategy of growing our regulated utility platform, we expect that the Acquisition will introduce a new platform for regulated growth, creating a leading water and natural gas utility in the United States with scale across the water, wastewater and natural gas distribution sectors. We believe this enhanced growth platform will present opportunities for the Company to grow our rate base through a wider range of infrastructure investment opportunities. In addition, as a larger publicly traded utility, we expect to have better access to capital to fund our infrastructure and capital expenditure needs. We also believe our enhanced scale and better access to the capital markets will support our commitment to strong investment grade credit ratings.

Both Aqua America and Peoples have demonstrated the ability to earn a return on and recover invested capital, with a history of sustained growth in earnings and cash flow. We believe the Acquisition will diversify the Company's cash flow while preserving our low-risk regulated utility profile, resulting in a multi-platform utility with operations spanning ten states.

We expect that the Acquisition will increase our presence in constructive regulatory jurisdictions, particularly Pennsylvania, where the regulatory framework is generally considered progressive and is highly rated by Regulatory Research Associates. Pennsylvania's high rating is based on the probable level and quality of the earnings to be realized by the state's utilities as a result of regulatory, legislative, and court actions, as well as the utilization of fully forecasted test years, Distribution Systems Improvement Charges and other automatic adjustment clauses that are intended to reduce the gap between the time that a capital project is completed and the recovery of costs in rates. The Peoples's management team will bring significant experience investing in and operating critical energy and safety infrastructure; their experience and knowledge is expected to be highly complementary to our core focus of operating our businesses in a safe and efficient manner to provide exceptional service to our customers.

We expect the Acquisition to increase our scale, cash flow diversity and rate base and strengthen our financial foundation, creating an enhanced platform for long-term growth. However, there can be no assurance that the Acquisition will be consummated on the terms or by the time currently contemplated, or at all, or, if consummated, that we will realize the anticipated benefits of the Acquisition. See "Risk Factors—Risks Related to the Acquisition and the Financing Transactions" in this prospectus supplement and "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018 (as updated by annual, quarterly and other reports and documents we file with the SEC that are incorporated by reference in this prospectus supplement and the accompanying prospectus).

Financing Transactions

In addition to the sale of our common stock in connection with this offering, we expect to obtain additional financing to (1) fund the Acquisition, (2) complete the redemption of approximately $314 million aggregate principal amount of our privately placed notes (such notes, the "PPNs," and such redemption, the "Company Debt Refinancing") and (3) pay related costs and expenses as described below. In addition, we intend to use $150 million of proceeds of the Debt Financings for general corporate purposes, including working capital and capital

needs. For information regarding sources and uses of funds in connection with the Acquisition and the Financing Transactions, see "Use of Proceeds.

TEU Offering

Concurrently with this offering, we are offering, by means of a separate prospectus supplement, 12,000,000 of our 6.00% tangible equity units ("TEUs"), plus up to 1,800,000 additional TEUs that the underwriters of the TEU Offering have the option to purchase directly from us, at the public offering price of $50.00 per TEU (the "TEU Offering"). Each TEU is comprised of two parts: (1) a prepaid stock purchase contract issued by us (a "TEU purchase contract") and (2) a senior amortizing note issued by us (a "TEU amortizing note"). If the TEU Offering is consummated but the closing of the Acquisition has not occurred on or prior to April 22, 2020, or if, prior to such date, the Acquisition Agreement is terminated, we may elect to redeem all, but not less than all, of the outstanding TEU purchase contracts in accordance with the terms thereof (an "acquisition termination redemption"). Upon any such acquisition termination redemption, holders of TEUs would have the right to require us to repurchase their TEU amortizing notes at the relevant repurchase price. Unless earlier redeemed by us in connection with an acquisition termination redemption or settled earlier at the holder's option or at our option, each TEU purchase contract will, subject to postponement in certain limited circumstances, automatically settle on April 30, 2022, and we will deliver a specified number of shares of our common stock per TEU purchase contract based upon applicable settlement rates and the market value of our common stock. The TEU amortizing notes have a specified initial principal amount and a specified interest rate and we will make specified payments of interest and partial repayments of principal on quarterly installment payment dates. The net proceeds from the sale of TEUs in the TEU Offering will be approximately $585.8 million (or approximately $673.7 million if the underwriters of such offering exercise their option to purchase additional TEUs in full).

Private Placement

On March 29, 2019, we entered into a Stock Purchase Agreement (the "CPPIB Agreement") with Canada Pension Plan Investment Board ("CPPIB") pursuant to which CPPIB agreed to purchase an aggregate of 21,661,095 newly issued shares of our common stock at the lower of (1) $34.62 per share and (2) the volume weighted average price per share in our public offerings of Common Stock to fund the Acquisition, the Company Debt Refinancing and pay related costs and expenses related thereto (the "Private Placement").

We expect the Private Placement to close concurrently with the consummation of the Acquisition, subject to certain closing conditions, including the closing of the Acquisition, the completion of additional equity offerings (including this offering and the TEU Offering) which raise gross proceeds in an aggregate amount of at least $1,600 million and the execution and delivery of a shareholder's agreement between CPPIB and the Company. The completion of the Private Placement is not conditioned upon the consummation of the Company Debt Refinancing or the Debt Financings.

Pursuant to the CPPIB Agreement, the shares purchased by CPPIB in the Private Placement will be subject to certain transfer restrictions until the earlier of 15 months following the completion of the Private Placement or specified change of control events with respect to the Company, subject to certain exceptions. In addition, subject to ownership thresholds and other customary requirements, CPPIB will have, pursuant to the shareholder's agreement to be entered into in connection with the closing of the Private Placement, (1) the right to appoint a member of our board of directors, (2) certain pre-emptive rights, (3) certain registration rights in respect of the shares purchased by CPPIB in the Private Placement and (4) certain "standstill" obligations with respect to the Company, subject to certain exceptions. Upon closing of the Private Placement, the Company has agreed to reimburse CPPIB for reasonable out-of-pocket diligence expenses of up to $4 million, subject to certain exceptions.

The foregoing description of the Private Placement does not purport to be complete and is qualified in its entirety by reference to the full text of the CPPIB Agreement, which was filed as Exhibit 10.1 to our Current Report on Form 8-K filed with the SEC on March 29, 2019 and incorporated by reference herein.

Debt Financings

We intend to obtain or otherwise incur up to approximately $1,009 million of senior indebtedness in connection with the Acquisition and the Company Debt Refinancing and approximately $150 million of senior indebtedness to be used for general corporate purposes, including working capital and capital needs. We refer to this $1,159 million of senior indebtedness financing as the "Debt Financings." The Debt Financings may include some combination of the following:

- *Notes Offering.* Subsequent to this offering we expect to offer, pursuant to one or more separate prospectus supplements, one or more series of senior unsecured notes (such notes, the "New Notes" and, such offerings, the "Notes Offering").

- *Bridge Facility.* On October 22, 2018, we obtained a commitment (the "Bridge Commitment") from Goldman Sachs Bank USA and Royal Bank of Canada to provide 364-day senior unsecured bridge loans (the "Bridge Facility"), in an aggregate amount of up to $5,100 million, subject to customary conditions set forth in the Bridge Commitment. As of the date of this prospectus supplement, we have terminated approximately $1,633 million of commitments under the Bridge Commitment in connection with, among other things, the replacement of our prior unsecured revolving credit facility, the expected refinancing of Peoples's revolving credit facility using our senior unsecured revolving credit facility (our "Revolving Credit Facility") and the expected assumption of Peoples's private placement notes. The Bridge Commitment may only be drawn upon to fund the Acquisition, the Company Debt Refinancing and related fees and expenses, and will expire upon the earliest to occur of (1) the termination of the Acquisition Agreement prior to the consummation of the Acquisition, (2) the closing of the Acquisition or (3) the Acquisition Outside Date.

In addition, if and to the extent the TEU Offering and/or the Private Placement is not completed, or such offerings are completed for less aggregate net proceeds than anticipated, we currently intend to fund any shortfall through the issuance of additional shares of common stock or equity-linked securities prior to the consummation of the Acquisition. However, if we are unable to issue such shares or equity-linked securities, we would fund any shortfall with additional debt financings, which may include borrowings under the Bridge Facility and/or the Revolving Credit Facility.

In this prospectus supplement, references to the "Financing Transactions" refer to this offering, the TEU Offering, the Private Placement and the Debt Financings, and references to the "Transactions" refer to the Financing Transactions, the Acquisition and the Company Debt Refinancing, including the application of the net proceeds from the Financing Transactions to complete such transactions, as described herein. In addition, unless otherwise specified or the context requires otherwise, references in this prospectus supplement to the "consummation of the Acquisition" or similar expressions shall be deemed to include the application of the net proceeds from the Financing Transactions to complete such transactions, as described herein, including the consummation of the Company Debt Refinancing.

This offering and certain of the other Financing Transactions are not conditioned upon the consummation of any other Financing Transactions, the Acquisition or the Company Debt Refinancing. In addition, the indebtedness or other securities to be incurred or issued in certain of the Financing Transactions may not be incurred or issued, or may be redeemed, repaid, or repurchased, if the Acquisition is not consummated or is not consummated by a specified date. Accordingly, even if the Acquisition, the Company Debt Refinancing or other Financing Transactions do not occur, the common stock issued in this offering will remain outstanding. Purchasers of our common stock in this offering should not place undue reliance on the pro forma and as adjusted information included and incorporated by reference in this prospectus supplement and the accompanying prospectus because this offering is not contingent upon the completion of any of the other Financing Transactions, the Acquisition or the Company Debt Refinancing, some or all of which are reflected in the adjustments included in that information, and because the actual amount of proceeds from the sale of shares and from any other Financing Transaction, and the actual terms of each of the Transactions, may differ, perhaps substantially, from those reflected in the prospectus supplement. We cannot assure you that we will complete the Acquisition or any of the other Financing Transactions on the terms contemplated by this prospectus supplement, or at all.

THE OFFERING

The following summary contains basic information about this offering and may not contain all of the information that may be important to you. You should read this entire prospectus supplement, the accompanying prospectus, any free writing prospectus we may provide to you in connection with this offering and the documents incorporated by reference herein and therein before making an investment decision.

As used in this section, unless the context otherwise requires, references to "Aqua America," the "Company," "we," "us," "our" and similar references refer only to Aqua America, Inc. and not to its consolidated subsidiaries.

Issuer	Aqua America, Inc., a Pennsylvania corporation
Common Stock Offered	32,495,667 shares of our common stock.
Underwriters' Option	We have granted the underwriters the option, exercisable in whole or from time to time in part, to purchase up to an additional 4,874,350 shares of our common stock directly from us, exercisable for 30 days after the date of this prospectus supplement.
Common Stock to be Outstanding Immediately After this Offering	210,587,288 shares (or 215,461,638 shares if the underwriters exercise their option to purchase additional shares of our common stock in full).
Use of Proceeds	We estimate that the net proceeds from this offering, after deducting underwriting discounts and estimated offering expenses, will be approximately $1,098.3 million (or approximately $1,263.2 million if the underwriters exercise their option to purchase additional shares of our common stock directly from us in full). We intend to use the net proceeds from this offering, together with the net proceeds from the other Financing Transactions, to (1) fund the Acquisition, (2) complete the Company Debt Refinancing and (3) pay related costs and expenses as described below. See "—Recent Developments—Proposed Peoples Gas Acquisition." In addition, we intend to use $150 million of proceeds of the Debt Financings for general corporate purposes, including working capital and capital needs. If for any reason the Acquisition is not consummated, we expect we would use the net proceeds from this offering for general corporate purposes, which may include the Company Debt Refinancing, the redemption of securities issued in connection with the other Financing Transactions, repurchases of our common stock, debt repayment, capital expenditures and investments. See "Use of Proceeds."
Concurrent TEU Offering	Concurrently with this offering of our common stock, we are offering, by means of a separate prospectus supplement, 12,000,000 TEUs, plus up to 1,800,000 additional TEUs that the underwriters of the TEU Offering have the option to purchase directly from us. The net proceeds from the sale of TEUs in the TEU Offering will be approximately $585.8 million (or approximately $673.7 million if the underwriters of such offering exercise their option to purchase additional TEUs in full). Each TEU is comprised of two parts: (1) a

	TEU purchase contract and (2) a TEU amortizing note. If the closing of the Acquisition has not occurred on or prior to April 22, 2020, or if, prior to such date, the Acquisition Agreement is terminated, we may elect to redeem all, but not less than all, of the outstanding TEU purchase contracts in an acquisition termination redemption. This prospectus supplement is not an offer to sell or a solicitation of an offer to buy any securities being offered in the TEU Offering. There can be no assurance that the TEU Offering will be completed. Neither this offering nor the TEU Offering is conditioned upon the consummation of the Acquisition or completion of any other Financing Transactions. See "—Recent Developments—Financing Transactions—TEU Offering."
Private Placement	On March 29, 2019, we entered into the CPPIB Agreement pursuant to which CPPIB agreed to purchase an aggregate of 21,661,095 shares of our common stock at the lower of (1) $34.62 per share and (2) the volume weighted average price per share in our public offerings of Common Stock to fund the Acquisition, the Company Debt Refinancing and pay related costs and expenses related thereto. This prospectus supplement is not an offer to sell or a solicitation of an offer to buy any securities being offered in the Private Placement. This offering is not conditioned upon completion of the Private Placement. The completion of the Private Placement is subject to certain closing conditions, including the closing of the Acquisition, the completion of additional equity offerings (including this offering and the TEU Offering) which raise gross proceeds in an aggregate amount of at least $1,600 million and the execution and delivery of a shareholders agreement between CPPIB and the Company. See "—Recent Developments—Financing Transactions—Private Placement."
Certain United States Federal Income and Estate Tax Considerations	Certain United States federal income and estate tax considerations to non-U.S. holders of purchasing, owning and disposing of our common stock are described in "Certain United States Federal Income and Estate Tax Considerations to Non-U.S. Holders" included in this prospectus supplement.
Listing	Our common stock is listed on the New York Stock Exchange (the "NYSE") under the symbol "WTR."
Dividend Policy	We have historically paid quarterly dividends on our common stock; however, the declaration, amount, timing and payment of any future dividends are subject to the determination and approval of our board of directors based on then-current or anticipated future conditions including our results of operations, capital requirements, financial condition, legal requirements or other factors deemed relevant by our board of directors. See "Listing of Our Common Stock and Dividends."
Transfer Agent and Registrar	The registrar and transfer agent for our common stock is Computershare Trust Company, N.A.
Risk Factors	Investing in our common stock involves risks. See "Risk Factors" in this prospectus supplement, the accompanying prospectus and in the documents we incorporate by reference in this prospectus supplement and the accompanying prospectus for a discussion of some of the risks and other factors you should carefully consider before deciding to invest in shares of our common stock.

In this prospectus supplement, unless otherwise indicated, the number of shares of our common stock outstanding and the other information based thereon is based on 178,091,621 shares of our common stock outstanding as of December 31, 2018, and does not reflect:

- 21,661,095 shares of our common stock issuable upon completion of the Private Placement;
- 17,330,400 shares of our common stock (or 19,929,960 shares of our common stock if the underwriters exercise their option with respect to such offering in full) issuable upon settlement of the TEU purchase contracts, assuming the maximum number of shares issuable upon automatic settlement of such TEU purchase contracts that are components of the TEUs; and
- 18,738,059 shares of our common stock reserved for issuance upon exercise of stock options outstanding, upon vesting of our time based restricted stock units, upon vesting of our performance based restricted stock units or performance share units, as well as additional shares we may issue under our dividend reinvestment program, employee stock purchase plan or 401(k) savings plans.

RISK FACTORS

Investing in our common stock involves risks. You should review and carefully consider the risks, uncertainties and other factors described below and all of the information included elsewhere in this prospectus supplement, the accompanying prospectus, any free writing prospectus we may provide to you in connection with this offering and the documents incorporated by reference herein and therein before deciding to invest in the shares. We also urge you to consider carefully the risks, uncertainties and other factors set forth under the headings "Forward-Looking Statements" and "Market and Industry Data." However, additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our business, operations, financial condition and financial results and the value of the shares.

Risks Related to Our Business

For a discussion of specific risks related to our business, operations, financial condition and financial results, including certain risks related to the Acquisition, please see the "Business," Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" sections in our Annual Report on Form 10-K for our fiscal year ended December 31, 2018, as updated by our annual, quarterly and other reports and documents we file with the SEC that are incorporated by reference in this prospectus supplement and the accompanying prospectus. See "Where You Can Find Additional Information; Incorporation of Certain Documents by Reference," in this prospectus supplement. In addition, we provide the following risk factor.

Changes in our earnings may differ from changes in our rate base.

Our business is capital intensive and requires significant capital investments for additions to or replacement of property, plant and equipment. These capital investments create assets that are used and useful in providing regulated utility service, and as a result, increase our rate base, on which we generate earnings through the regulatory process. Changes in our reported earnings, however, may differ from changes in our rate base in a given period due to several factors, including rate case timing and the terms of such rate cases; over- or under-earnings in a given period due to changes in operating costs; the effects of tax rates or tax treatment of capital investments, including the effect of repair tax; capital expenditures that are not eligible for DSIC between rate cases; and acquisitions which have not yet been included in rate base. We anticipate that we may experience periods in which growth in earnings is less than growth in rate base; such differences may be significant and may persist over multiple reporting periods.

Risks Related to Peoples's Business

For a discussion of specific risks related to Peoples's business, please see "Risk Factors related to Peoples" in our Current Report on Form 8-K/A filed on April 15, 2019 and incorporated by reference in this prospectus supplement and the accompanying prospectus. These risks, uncertainties and other factors are not the only ones that Peoples faces. Additional risks, uncertainties and other factors not presently known to us or that we currently deem immaterial may also impair Peoples's business, operations, financial condition and financial results. Any of these risks could, if the Acquisition is consummated, impair the combined company's business, operations, financial condition and financial results or could otherwise adversely impact our investment in Peoples, in which case you may lose all or part of your investment in the shares.

Risks Related to the Acquisition and the Financing Transactions

Aqua America expects to incur significant additional indebtedness in connection with the Acquisition. As a result, it may be more difficult for Aqua America to pay or refinance its debts or take other actions, and Aqua America may need to divert cash to fund debt service payments.

As discussed herein, Aqua America expects to incur significant additional indebtedness to finance the Cash Acquisition Consideration and the Company Debt Refinancing and pay related transaction costs. Additionally,

in connection with the Acquisition, Aqua America currently intends to assume approximately $1,370 million of Peoples's indebtedness. Moreover, although Aqua America currently plans to fund a significant portion of the Cash Acquisition Consideration and the Company Debt Refinancing through the sales of its equity securities, if and to the extent that such sales are not completed or are completed for less aggregate net proceeds than anticipated, the amount of indebtedness it will incur to finance the Acquisition, the Company Debt Refinancing and associated transactions costs would increase, perhaps substantially. The increase in Aqua America's debt service obligations resulting from additional indebtedness could have a material adverse effect on the results of operations, financial condition and prospects of the combined company.

Aqua America's increased indebtedness could also:

- make it more difficult and/or costly for Aqua America to pay or refinance its debts as they become due, particularly during adverse economic and industry conditions, because a decrease in revenues or increase in costs could cause cash flow from operations to be insufficient to make scheduled debt service payments;
- limit Aqua America's flexibility to pursue other strategic opportunities or react to changes in its business and the industry sectors in which it operates and, consequently, put Aqua America at a competitive disadvantage to its competitors that have less debt;
- require a substantial portion of Aqua America's available cash to be used for debt service payments, thereby reducing the availability of its cash to fund working capital, capital expenditures, development projects, acquisitions, dividend payments and other general corporate purposes, which could harm Aqua America's prospects for growth and the market price of our common stock, TEUs and debt securities, among other things;
- result in a downgrade in the credit ratings on Aqua America's indebtedness, which could limit Aqua America's ability to borrow additional funds on favorable terms or at all (including in order to refinance the Bridge Facility (if drawn) and/or its other debt), increase the interest rates under its credit facilities and under any new indebtedness it may incur, and reduce the trading prices of its outstanding debt securities, common stock and TEUs (see "Summary Information—Recent Developments—Financing Transactions");
- make it more difficult for Aqua America to raise capital to fund working capital, make capital expenditures, pay dividends, pursue strategic initiatives or for other purposes;
- result in higher interest expense, which could be further increased in the event of increases in interest rates on Aqua America's current or future borrowings subject to variable rates of interest; and
- require that additional materially adverse terms, conditions or covenants be placed on Aqua America under its debt instruments, which covenants might include, for example, limitations on additional borrowings and specific restrictions on uses of its assets, as well as prohibitions or limitations on its ability to create liens, pay dividends, receive distributions from its subsidiaries, redeem or repurchase its stock or make investments, any of which could hinder its access to capital markets and limit or delay its ability to carry out its capital expenditure program or otherwise limit its flexibility in the conduct of its business and make it more vulnerable to economic downturns and adverse competitive and industry conditions.

It is possible that the Notes Offering will not be completed or, if completed, will generate less aggregate net proceeds than anticipated, which is a scenario in which we may incur borrowings under the Bridge Facility and/or incur borrowings under the Revolving Credit Facility. It is also possible that this offering, the TEU Offering and the Private Placement will not be completed or, if completed, will generate less aggregate net proceeds than anticipated,

in which case we intend to fund any shortfall through the issuance of additional shares of common stock or equity- linked securities prior to the consummation of the Acquisition, but may ultimately fund any shortfall with additional debt financings (which could include borrowings under the Bridge Facility) and/or borrowings under the Revolving Credit Facility. Any such borrowings under the Bridge Facility or the Revolving Credit Facility may cause us to incur significantly higher borrowing costs than the contemplated long-term financing, which would increase the overall cost of the Acquisition and could harm our business, financial condition, results of operations, and cash flows. Any borrowings under the Bridge Facility will mature 364 days after they are incurred. We may not be able to refinance borrowings under the Bridge Facility on favorable terms or at all before their maturity. In addition, the interest rate applicable to borrowings under the Bridge Facility will increase at the end of each three-month period after the borrowing date. Accordingly, we may incur additional interest expense if we are unable to refinance borrowings under the Bridge Facility before the interest rate increases take effect.

The increased indebtedness in connection with the Acquisition could cause us to place more reliance on cash flow from operations to pay principal and interest on debt and to satisfy our other obligations. Based on the current and expected results of operations and financial condition of Aqua America and its subsidiaries and the currently anticipated financing structure for the Acquisition, Aqua America believes that its cash flow from operations, together with the proceeds from borrowings, issuances of equity and debt securities in the capital markets, and equity sales will generate sufficient cash on a consolidated basis to make all of the principal and interest payments when such payments are due under Aqua America's and its current subsidiaries' existing credit facilities, indentures and other instruments governing their outstanding indebtedness, under the indebtedness anticipated to be incurred to fund the Cash Acquisition Consideration and the Company Debt Refinancing and under the indebtedness of Peoples anticipated to be assumed as a result of the Acquisition. However, Aqua America's expectation is based upon numerous estimates and assumptions and is subject to numerous uncertainties. LDC and its subsidiaries will not guarantee any indebtedness of Aqua America or any of its other subsidiaries, nor will any of them have any obligation to provide funds (nor will we have any ability to require them to provide funds), whether in the form of dividends, loans or otherwise, to enable Aqua America to pay dividends on its common stock or to enable Aqua America and its other subsidiaries to make required debt service payments or meet its other cash needs (including those described above under "Summary Information—Recent Developments"). In addition, as described above in "—Aqua America's ability to pay dividends and to meet its debt obligations largely depends on the performance of its subsidiaries and the ability to utilize the cash flows from those subsidiaries," certain of LDC and its subsidiaries may face limitations on their ability to provide funds to Aqua America. As a result, Aqua America may substantially increase its debt services obligations in anticipation of the Acquisition without any assurance that Aqua America will receive any cash from LDC or any of its subsidiaries to assist Aqua America in servicing its indebtedness, paying dividends on its common stock or meetings its other cash needs. Even if the Acquisition is consummated, Aqua America may not have access to the cash or other assets of certain of LDC and its subsidiaries.

In order to maintain its credit ratings, Aqua America may consider it appropriate to reduce the amount of its indebtedness outstanding following the Acquisition. Aqua America may seek to reduce this indebtedness with the proceeds from the issuance of additional shares of common stock and, possibly, other equity-linked securities, cash on hand and proceeds from asset sales, which may dilute the voting rights and economic interests of holders of Aqua America's common stock. However, the ability of Aqua America to raise additional equity financing after completion of the Acquisition will be subject to market conditions and a number of other risks and uncertainties, including whether the results of operations of the combined company meet the expectations of investors and securities analysts. Aqua America may not be able to issue additional shares of its common stock or other equity securities after the Acquisition on terms that it considers acceptable or at all, and Aqua America may not be able to reduce the amount of its outstanding indebtedness after the Acquisition, should it elect to do so, to a level that permits it to maintain its investment grade credit ratings.

The unaudited pro forma consolidated combined financial information and other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus are presented for illustrative purposes only and do not purport to represent what the financial position or results

of operations of the combined company would have been had the Transactions been completed on the dates assumed for purposes of that information, nor do they represent the actual financial position or results of operations of the combined company following the Transactions, if consummated.

The unaudited pro forma consolidated combined financial information and other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus are presented for illustrative purposes only, are based on numerous adjustments, assumptions and estimates, are subject to numerous other uncertainties and do not purport to reflect what the combined company's financial position or results of operations would have been had the Transactions been completed as of the dates assumed for purposes of that information, nor do they reflect the financial position or results of operations of the combined company following the Transactions, if consummated. Such unaudited pro forma consolidated combined financial information and certain other adjusted information reflects the assumptions of our management at the time that such information was initially prepared, and therefore does not reflect the amount of proceeds we will receive from, and certain pricing and other terms of, each of the Debt Financings, the TEU Offering, the Private Placement and this offering, the number of shares of our common stock sold in this offering and in the Private Placement and the number of TEUs sold in the TEU offering, and the actual amount of costs and expenses and underwriting discounts we will pay in connection with the Transactions. Therefore, actual amounts, including the actual amount of net proceeds from the respective Financing Transactions, may differ, perhaps substantially, from the assumed amounts set forth in the unaudited pro forma consolidated combined financial information and the other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus.

The unaudited pro forma consolidated combined financial information and other adjusted information has also been prepared on the assumption that the Transactions will be completed on the terms and in accordance with the assumptions set forth in such unaudited pro forma consolidated combined financial information or such adjusted information, as applicable. Any changes relative to these assumptions, including, without limitation, any changes in the assumed types or sizes of the Financing Transactions, the assumed interest on debt we will issue or otherwise incur, the assumed number of shares of common stock or TEUs we issue, the assumed amount of our Transactions costs, the assumed amounts of net proceeds we receive from the respective Financing Transactions would result in a change relative to such unaudited pro forma consolidated combined financial information or such other adjusted information, which could be material. In addition, none of the Financing Transactions (other than the Private Placement) will be contingent upon completion of any of the other Financing Transactions, and it is possible that one or more of the Financing Transactions will not be completed. Likewise, because certain of the Financing Transactions are not contingent upon completion of the Acquisition, it is possible that this offering and certain of the other Financing Transactions may be completed even if the Acquisition is not consummated, in which case we may be required to redeem or otherwise repay certain indebtedness or debt securities we may issue in the Debt Financings, and we may elect to redeem all of the TEU purchase contracts (if issued), in which case holders of TEUs would have the right to require us to repurchase their outstanding TEU amortizing notes. It is also possible that this offering, the TEU Offering, the Private Placement and the Notes Offering, if completed, will not generate the anticipated amount of net proceeds, in which case we may draw upon the Bridge Commitment and/or incur borrowings under our Revolving Credit Facility and/or issue additional shares of common stock or equity-linked securities. In any event, our and Peoples's actual financial positions and results of operations prior to the Acquisition and those of the combined company following the Acquisition, if consummated, may not be consistent with, or evident from, the unaudited pro forma consolidated combined financial information or other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus.

For purposes of the unaudited pro forma consolidated combined financial information, the Cash Acquisition Consideration has been preliminarily allocated to the identifiable assets acquired and liabilities assumed based on limited information presently available to estimate fair values. The Cash Acquisition Consideration will be allocated among the relative fair values of the identifiable assets acquired and liabilities assumed based on their estimated fair values as of the date of the Acquisition. The relative fair values of the assets acquired and liabilities

assumed are estimates, which are subject to change pending further review. The actual amounts recorded at the completion of the Acquisition, if completed, may differ materially from the information presented in the unaudited pro forma consolidated combined financial information.

Although the unaudited pro forma consolidated combined financial information and other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus include sensitivity analyses that are intended to assist you in quantifying the impact of changes in certain of the assumptions used in preparing such information, those sensitivity analyses reflect the pro forma impact of only a limited number of those assumptions and therefore do not allow you to quantify the impact of changes in certain other assumptions made in calculating this information. Changes in such other assumptions may have a material impact on such information. Likewise, the sensitivity analyses we have provided do not necessarily address the impact of all possible changes in the assumptions contemplated by such analyses. We do not intend to provide you with updated unaudited pro forma consolidated combined financial information or other adjusted information that reflects the actual size and terms of the Financing Transactions (other than to disclose the actual size and pricing terms of this offering and the TEU Offering in one or more free writing prospectuses) prior to the time you will be required to make a decision whether or not to invest in this offering.

As a result of the foregoing, investors should not place undue reliance on unaudited pro forma consolidated combined financial information and other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus.

We may not complete the Acquisition. If we incur indebtedness or issue debt securities to finance a portion of the Acquisition, and we do not complete the Acquisition on or before a specified date or if other specified events occur, we may be required to redeem or repay any such indebtedness or debt securities. We may not have the financial resources necessary to effect such redemption or repayment. It is possible that our failure to complete Acquisition may have a material adverse effect on our financial condition and the market price of our common stock.

The Acquisition is subject to a number of customary closing conditions. See "Summary Information— Recent Developments—Proposed Peoples Gas Acquisition." Satisfaction of many of these conditions is beyond our control. If these conditions are not satisfied or waived, the Acquisition will not be completed. As a result, the Acquisition may not close as scheduled or at all. Among other conditions, the closing of the Acquisition is subject to the receipt of regulatory approval by the Pennsylvania Public Utility Commission. Whether through a settlement agreement or through a litigated proceeding, we may be required to agree to certain actions, undertakings, terms, or other measures, including those that may require increased capital or other expenditures by the Company. Any additional items we agree to in order to resolve this matter may have an adverse effect on our business, financial condition or results of operations. The closing of this offering is not conditioned on, and is expected to be consummated before, the closing of the Acquisition. Accordingly, if you decide to purchase shares in this offering, you should be willing to do so whether or not we complete the Acquisition.

We expect to incur a substantial amount of additional indebtedness as part of the Financing Transactions. See "Summary Information—Recent Developments —Financing Transactions" and "Use of Proceeds." To the extent we incur indebtedness or issue debt securities as part of the Financing Transactions and we do not complete the Acquisition by a specified date or if certain other specified events, such as termination of the Acquisition Agreement, occur, we expect that we will be required to redeem or repay some or all of such indebtedness and debt securities and that the redemption or repayment price will include a premium.

We will not be required to deposit the proceeds from the Financing Transactions into an escrow account pending completion of the Acquisition or to grant any security interest or other lien on those proceeds to secure any required repayment or redemption of any Financing Transactions. If we are required to redeem or repay any indebtedness or debt securities issued in the Financing Transactions under the circumstances described above, our ability to pay the redemption or repayment price may be limited by our financial resources at the time and the terms of our debt instruments or other instruments and agreements and it is possible that we will

not have sufficient financial resources available to satisfy our obligation to effect such redemption or repayment. Any failure to pay the mandatory redemption or repayment price of any Financing Transactions as and when required could have a material adverse effect on our business, results of operations and financial condition and the market price of our securities, including our common stock, the TEUs being offered in the TEU Offering, or any indebtedness incurred or other securities issued as part of the Financing Transactions. If the Acquisition is not completed, we will not have any obligation to offer to repurchase the common stock sold in this offering. It is possible that our failure to complete the Acquisition, or the expenditure of our funds to redeem or repay any securities issued or borrowings incurred in the other Financing Transactions, may have a material adverse effect on the market price of our common stock and the TEUs issued in the TEU Offering.

Risks Related to Our Common Stock

The price of our common stock may be volatile. This volatility may affect the price at which you could sell our common stock, and the sale or resale of substantial amounts of our common stock could adversely affect the market price of our common stock.

The market price for our common stock has historically experienced, and may continue to experience, volatility. This volatility may affect the price at which you could sell our common stock, and the sale or issuance of substantial amounts of our common stock, or the perception that such sales or issuances could occur, could adversely affect the market price of our common stock. In addition, the availability for sale of substantial amounts of our common stock could adversely impact its market price. In that regard, if we issue TEUs in the TEU Offering, shares of our common stock will be issuable upon settlement or redemption of the TEU purchase contracts and the number of shares may be substantial. The settlement rates for the TEU purchase contracts will be subject to certain anti-dilution adjustments that could increase, potentially significantly, the number of shares of our common stock issuable upon such settlement. Similarly, although CPPIB is currently subject to restrictions on resale, if the Private Placement is completed a significant portion of our common stock will be available for resale into the market by a small number of investors following the expiration of such restrictions. The issuance or sale of shares, or the perception that such issuances or sales could occur, could adversely affect the market price of our common stock, even if our business is doing well. Any of the foregoing may also impair our ability to raise additional capital through the sale of our equity securities.

The market price of our common stock may be influenced by many factors, some of which are beyond our control, including the factors discussed above under “Forward-Looking Statements” and “Market and Industry Data” or elsewhere in this Risk Factors section and the following:

- actual or anticipated fluctuations in our operating results or our competitors’ or peers’ operating results;
- actions by applicable regulatory authorities, including the Pennsylvania Public Utility Commission;
- announcements by us, our competitors or our partners of significant contracts, acquisitions, divestitures or strategic investments;
- our growth rate and our competitors’ or peers’ growth rates;
- the financial markets and general economic conditions;
- changes in stock market analyst recommendations regarding us, our competitors, our peers or the energy infrastructure, gas and electricity services industries generally, or lack of analyst coverage of our common stock;

- sales of our common stock by our executive officers, directors and significant shareholders or sales of substantial amounts of our common stock or securities convertible into or exchangeable for our common stock;
- changes in the amount of our common stock dividends per share, the common stock dividends per share paid by our competitors and interest rates; and
- changes in tax laws and regulations.

The market for our common stock likely will influence, and be influenced by, any market that develops for the TEUs or the TEU purchase contracts. For example, investors' anticipation of the distribution into the market of the additional shares of common stock issuable upon settlement of the TEU purchase contracts could depress the price of our common stock and increase the volatility of the common stock price. The price of our common stock also could be affected by possible sales of such common stock by investors who view the TEUs as a more attractive means of equity participation in us and by hedging or arbitrage trading activity that is likely to develop involving the TEUs, TEU purchase contracts and the common stock. Such hedging or arbitrage activity could, in turn, affect the trading prices of the common stock.

We expect that we will need to raise additional capital, and raising additional funds by issuing additional equity securities or with additional debt financing may cause dilution to shareholders or restrict our operations.

Upon the issuance of the shares of common stock in the Private Placement and the issuance of the TEUs in the TEU Offering, holders of our common stock will incur immediate and substantial net tangible book value dilution on a per share basis. If we are unable to consummate the TEU Offering, the Private Placement or any portion of the Debt Financings, we may issue additional shares of common stock to finance the Acquisition. In addition, we expect that we will need to raise additional capital in the future in order to, among other things, repay indebtedness and fund our operations and future acquisitions, which we may do through equity and equity-linked securities offerings or additional debt financings, as well as borrowings under our credit facilities. Additional issuances of equity securities, including shares of our common stock, or debt or other securities that are convertible into or exchangeable for, or that represent the right to receive, common stock, including the TEUs, could dilute the economic and other rights and interests of holders of shares of our common stock and cause the market price of our common stock to decline. Subject to certain exceptions, such issuances may be made without any action or approval by our shareholders.

Any new debt financing we enter into may involve covenants that restrict our operations more than our current outstanding debt and credit facilities. These restrictive covenants could include limitations on additional borrowings, and specific restrictions on the use of our assets, as well as prohibitions or limitations on our ability to create liens, pay dividends, receive distributions from our subsidiaries, redeem or repurchase our stock or make investments. These covenants could hinder our access to capital markets and limit or delay our ability to carry out our capital expenditure program.

If the closing of the Acquisition has not occurred on or prior to April 22, 2020, or if, prior to such date, the Acquisition Agreement is terminated, we may redeem the TEU purchase contracts, in which case holders of TEUs would have the right to require us to repurchase TEU amortizing notes.

The Acquisition may not be consummated. If the closing of the Acquisition has not occurred on or prior to April 22, 2020, or if, prior to such date, the Acquisition Agreement is terminated, we may elect to redeem all, but not less than all, of the outstanding TEU purchase contracts (if issued). We will pay or deliver, as the case may be, a redemption amount to be determined based on the price of our common stock at that time in cash or in

shares of our common stock in accordance with the terms of the TEU purchase contracts. If we elect to redeem the TEU purchase contracts, holders of TEUs would have the right to require us to repurchase TEU amortizing notes at the relevant repurchase price.

Upon redemption of the TEU purchase contracts, our common stock may incur immediate net tangible book value dilution on a per share basis. In addition, if the TEU purchase contracts are redeemed for cash and holders of TEUs require us to repurchase TEU amortizing notes, we would experience reduced liquidity, which could limit our flexibility in the conduct of our business and make us more vulnerable to economic downturns and adverse competitive and industry conditions.

Anti-takeover provisions in our organizational documents and under Pennsylvania law might discourage, delay or prevent changes in control of our company and may result in an entrenchment of management and diminish the value of our common stock.

Certain provisions of our articles of incorporation and bylaws could have the effect of delaying, deterring or preventing another party from acquiring or seeking to acquire control of us. These provisions are intended to discourage certain types of coercive takeover practices and inadequate takeover bids and to encourage anyone seeking to acquire control of us to negotiate first with our board of directors. However, these provisions could also delay, deter or prevent a change of control or other takeover of our company that our shareholders might consider to be in their best interests, including transactions that might result in a premium being paid over the market prices of our common stock and TEUs, and may also limit the prices that investors are willing to pay in the future for our common stock and TEUs. These provisions may also have the effect of preventing changes in our management.

For example, our articles of incorporation and bylaws include anti-takeover provisions that:

- authorize our board of directors, without a vote or other action by our shareholders, to cause the issuance of preferred stock in one or more series and, with respect to each series, to fix the number of shares constituting that series and to establish the rights, preferences, privileges and restrictions of that series, which may include, among other things, dividend and liquidation rights and preferences, rights to convert such shares into common stock, voting rights and other rights which may adversely affect the voting or other rights and the economic interests of holders of our common stock and TEUs, if issued;

- require that certain fundamental transactions must be approved by the holders of 75% of the outstanding shares of our capital stock entitled to vote on the matter unless at least a majority of the members of the board of directors has approved the transaction, in which case the required shareholder approval will be the minimum approval required by applicable law;

- establish advance notice requirements and procedures for shareholders to submit nominations of candidates for election to our board of directors and to propose other business to be brought before a shareholders meeting;

- provide that vacancies in our board of directors, including vacancies created by the removal of any director, or any increase in the number of directors may be filled by a majority of the directors then in office or by the sole remaining director;

- provide that no shareholder may cumulate votes in the election of directors, which means that the holders of a majority of our outstanding shares of common stock can elect all directors standing for election by our common shareholders;

- require that any action to be taken by our shareholders must be taken either (1) at a duly called annual or special meeting of shareholders or (2) by the unanimous written consent of all of our shareholders

- require action by shareholders entitled to cast a majority of the votes which all shareholders are entitled to cast at the particular meeting in order for our shareholders to call a special meeting of shareholders; and

- provide that a state court located within Montgomery County, Pennsylvania (or, in the event such court lacks jurisdiction over such action or proceeding, the United States District Court for the Eastern District of Pennsylvania) will be the exclusive forum for the adjudication of certain disputes, including derivative actions.

In addition, anti-takeover provisions in Pennsylvania law could make it more difficult for a third party to acquire control of us including, but not limited to, provisions relating to (1) control share acquisitions, (2) disgorgement of profits by certain controlling persons, (3) business combination transactions with interested shareholders, and (4) the rights of shareholders to demand fair value for their stock following a control transaction. Pennsylvania law permits corporations to opt-out of these anti-takeover provisions, but we have not done so. Such provisions could have the effect of deterring takeovers or delaying changes in control or management of us. Additionally, such provisions could limit the price that some investors might be willing to pay in the future for shares of our common stock.

In addition, the TEUs, if issued, will, and the Debt Financings and other debt financings may, include certain terms that may have anti-takeover effects. For example, each holder of a TEU purchase contract will have the right, upon certain "fundamental changes" (including a cash acquisition of us), to require early settlement of such holder's TEU purchase contract at a rate designed to compensate for the lost option value of such TEU purchase contract.

This offering is not conditioned upon the completion of the Acquisition. If the Acquisition is not consummated, we will have broad discretion on the use of the net proceeds of this offering.

This offering is not conditioned upon the completion of the Acquisition. Accordingly, your purchase of our common stock in this offering may be an investment in Aqua America on a stand-alone basis without any of the assets of Peoples or anticipated benefits of the Acquisition. We will have broad discretion to use the net proceeds of this offering if the Acquisition does not occur. If the Acquisition does not occur, we expect to use the net proceeds from this offering for general corporate purposes, which may include the Company Debt Refinancing, the redemption of securities issued in connection with the other Financing Transactions, repurchases of our common stock debt repayment, capital expenditures and investments. See "Use of Proceeds."

We may be unable to, or may choose not to, continue to pay dividends on our common stock at current or planned rates or at all.

Any future payments of cash dividends, and the amount of any cash dividends we pay, on our common stock will depend on, among other things, our financial condition, capital requirements and results of operations, and the ability of our subsidiaries to distribute cash to us, as well as other factors that our board of directors may consider relevant. If we were to reduce the amount of cash dividends per share payable on our common stock, fail to increase the amount of those cash dividends per share in the future or cease paying those cash dividends altogether, it would likely have an adverse impact on the market price of our common stock and any TEUs we may issue. In addition, under Pennsylvania law, our board of directors (or an authorized committee thereof) may not declare and pay dividends on shares of our common stock if, after giving effect to the dividend (1) we would be unable to pay our debts as they become due in the ordinary course of business, or (2) our total assets would be less than the sum of our total liabilities plus the amount that would be needed, if we were to be dissolved as of the date for measuring the dividend, to satisfy the preferential rights upon dissolution of shareholders whose preferential rights are superior to those receiving the dividend.

Aqua America's ability to pay dividends and to meet its debt obligations largely depends on the performance of its subsidiaries and the ability to utilize the cash flows from those subsidiaries.

Aqua America is a holding company substantially all of whose assets are owned by its subsidiaries and substantially all of whose operations are conducted through its subsidiaries. Aqua America's ability to pay dividends and meet its debt and other obligations depends almost entirely on cash flows from its subsidiaries and, in the short term, its ability to raise capital from external sources. In the long term, cash flows from its subsidiaries depend on their ability to generate operating cash flows in excess of their own expenditures, common and preferred stock dividends (if any), and debt or other obligations. Its subsidiaries are separate and distinct legal entities that are not obligated to pay dividends or make loans or distributions to Aqua America (whether to enable Aqua America to pay dividends on its common stock, to pay principal and interest on its debt, to settle, repurchase or redeem its debt (including the TEU amortizing notes) or other securities (including the TEU purchase contracts), or to satisfy its other obligations). In addition, notwithstanding its controlling interest in such subsidiaries, many of them are limited in their ability to pay dividends or make loans or distributions to Aqua America, including, without limitation, as a result of legislation, regulation, court order, contractual restrictions and other restrictions or in times of financial distress. Likewise, certain of LDC and its subsidiaries face similar restrictions that, if the Acquisition is consummated, will limit their ability to pay dividends or make loans or distributions to Aqua America. As a result, the Company may not be able to cause its subsidiaries (including, following the Acquisition, LDC and its subsidiaries) and other entities to distribute funds or provide loans sufficient to enable it to pay dividends and meet its debt and other obligations.

USE OF PROCEEDS

We estimate that the net proceeds to us from this offering, after deducting underwriting discounts and estimated offering expenses, will be approximately $1,098.3 million (or approximately $1,263.2 million if the underwriters exercise their option to purchase additional shares of our common stock in full).

We intend to use the net proceeds from this offering, together with net proceeds from the TEU Offering, the Private Placement and the Debt Financings, to (1) fund the Acquisition, (2) complete the redemption of approximately $314 million aggregate principal amount of the PPNs and (3) pay related costs and expenses as described below. In addition to the $1,009 million aggregate principal amount of Debt Financings we intend to incur to fund the Acquisition, complete the Company Debt Refinancing and pay related costs and expenses, we expect to incur $150 million aggregate principal amount of Debt Financings, the net proceeds of which we intend to use for general corporate purposes, including working capital and capital needs.

This offering and certain of the other Financing Transactions are not conditioned upon the consummation of any other Financing Transactions, the Acquisition or the Company Debt Refinancing. In addition, the indebtedness or other securities to be incurred or issued in certain of the Financing Transactions may not be incurred or issued, or may be redeemed, repaid, or repurchased, if the Acquisition is not consummated or is not consummated by a specified date. Even if the Acquisition, the Company Debt Refinancing and/or other Financing Transactions do not occur, the common stock issued in this offering will remain outstanding. If for any reason the Acquisition is not consummated, we expect we would use the net proceeds for this offering for general corporate purposes, which may include the Company Debt Refinancing, the redemption of securities issued in connection with the other Financing Transactions, repurchases of our common stock, debt repayment, capital expenditures and investments. Pending application of the net proceeds of this offering for the foregoing purposes, the net proceeds may be invested temporarily in investment-grade securities or similar instruments, or be used to temporarily reduce borrowings under the Revolving Credit Facility.

The following table outlines the estimated sources and uses of funds for the Acquisition, the Company Debt Refinancing and the related costs and expenses. The actual net proceeds from the Financing Transactions and the costs and expenses related to the Transactions will likely vary from the estimates reflected in the following table. See "Summary Information—Recent Developments—Financing Transactions."

The following table does not reflect the sale of any shares or TEUs that may be sold to the underwriters of this offering and of the TEU Offering upon exercise of their respective options to purchase additional shares and TEUs. To the extent the underwriters exercise such options, we expect that the net proceeds from such sales will be used to fund a portion of the purchase price of the Acquisition, which would reduce, by a corresponding amount, the amount of the debt we expect to incur to fund a portion of the purchase price of the Acquisition.

Sources of Funds[1]		**Uses of Funds**	
	(in millions)		
Shares offered hereby	$ 1,125	Cash Acquisition Consideration[2]	$ 2,905
TEU Offering	600	Company Debt Refinancing[3]	314
Private Placement	750	Transactions costs and expenses, including	
Debt Financings[4]	1,009	discounts and financing fees	265
Assumption of Peoples's existing debt	1,370	Assumption of Peoples's existing debt	1,370
Total sources of funds	$ 4,854	**Total uses of funds**	$ 4,854

(1) All amounts are estimated proceeds before underwriting discounts and offering expenses. If and to the extent that any of this offering, the TEU Offering or the Private Placement is not completed, or if the aggregate net proceeds from this offering, the TEU Offering and the Private Placement are less than the aggregate amount set forth in this table, we intend to fund any shortfall by issuing additional shares of common stock or equity-linked securities prior to the consummation of the Acquisition. However, if we are unable to issue such shares or equity-linked securities, we would fund any shortfall with additional debt financings, which may include borrowings under the Bridge Facility and/or the Revolving Credit Facility.

(2) Assumes the only adjustment to the Default Cash Acquisition Consideration is a reduction of $1,370 million based upon the assumption by the Company of $1,370 million aggregate principal amount of Peoples's indebtedness upon closing of the Acquisition. To the extent we assume less than $1,370 million aggregate principal amount of Peoples's existing indebtedness, we may issue additional shares of common stock, equity-linked securities and/or New Notes and/or incur borrowings under the Bridge Facility and/or the Revolving Credit Facility.

(3) In connection with the Acquisition and the Financing Transactions, we expect to redeem approximately $314 million in aggregate principal amount of our PPNs prior to the closing of the Acquisition. Estimated premiums payable in connection with the Company Debt Refinancing are included in "Transaction costs and expenses, including discounts and financing fees" above. The PPNs we intend to redeem in the Company Debt Refinancing have maturities ranging from 2019-2037 and interest rates ranging from 3.57-5.83%.

(4) In addition to the $1,009 million aggregate principal amount of Debt Financings we intend to incur to fund the Acquisition, complete the Company Debt Refinancing and pay related costs and expenses, we expect to incur $150 million aggregate principal amount of Debt Financings, the net proceeds of which we intend to use for general corporate purposes, including working capital and capital needs.

CAPITALIZATION

The following table sets forth our consolidated cash and cash equivalents and capitalization as of December 31, 2018:

- on an actual basis;
- on an as adjusted basis to give effect to this offering;
- on an as further adjusted basis to give effect to this offering and the TEU Offering; and
- on a pro forma basis to give effect to the Transactions, including this offering, the TEU offering, the Acquisition, the Company Debt Refinancing, the Private Placement and the Debt Financings.

The following table does not reflect the sale of any shares or TEUs that may be sold to the respective underwriters of this offering and of the TEU offering upon exercise of their respective options to purchase additional shares and TEUs. If the underwriters exercise such options, we expect that the proceeds from such sales will be used to fund a portion of the purchase price of the Acquisition, which would reduce, by a corresponding amount, the amount of the Debt Financings we expect to incur to fund a portion of the purchase price of the Acquisition.

The completion of this offering is not conditioned upon the consummation of any of the other Transactions, including the Acquisition. Accordingly, investors should not place undue reliance on the as further adjusted and pro forma information included in this prospectus supplement because this offering is not conditioned upon the consummation of any of the other transactions reflected in such information. In addition, even if the Transactions are completed, actual amounts may vary from such information depending on several factors, including potential changes in our financing plans as a result of market conditions or the timing of the consummation of the Acquisition.

The following data are qualified in their entirety by our financial statements and related notes and other information incorporated by reference in this prospectus supplement and the accompanying prospectus. This table should be read in conjunction with "Summary Information–Recent Developments—Proposed Peoples Gas Acquisition," "Risk Factors," "Use of Proceeds," and our pro forma and consolidated financial statements and related notes incorporated by reference in this prospectus supplement and the accompanying prospectus, and the other information contained in the documents incorporated by reference in this prospectus supplement and the accompanying prospectus.

(dollars in thousands)	Actual	As Adjusted for this Offering	As Further Adjusted for this Offering and the TEU Offering	Pro Forma for the Transactions
Cash and cash equivalents[1]	$ 3,627	$ 1,101,967	$ 1,687,741	$ 209,100
Debt:				
Long-term debt of subsidiaries[2]	$ 1,604,233	$ 1,604,233	$ 1,604,233	$ 1,604,233
Revolving Credit Facility[3]	370,000	370,000	370,000	370,000
Privately placed notes[4]	589,427	589,427	589,427	275,927
Debt Financings[5]	—	—	—	1,159,000
Assumed Peoples's indebtedness[6]	—	—	—	1,329,227
TEU amortizing notes that are components of the TEUs[7]	—	—	103,549	103,549
Total debt	$ 2,563,660	$ 2,563,660	$ 2,667,209	$ 4,841,936
Equity:				
Preferred stock, $1.00 par value (1,770,819 shares authorized, none issued)	—	—	—	—
Common stock, $0.50 par value (300,000,000 shares authorized; 181,151,827 issued, actual; 213,647,494 issued, as adjusted and as further adjusted and 235,308,589 issued, pro forma)[8]	90,576	106,824	106,824	117,654
Capital in excess of par value[8][9]	820,378	1,902,470	2,387,198	3,104,807
Retained earnings[10]	1,174,245	1,174,245	1,174,245	1,130,168
Treasury stock, at cost (3,060,206 shares)	(75,835)	(75,835)	(75,835)	(75,835)
Total stockholders' equity	$ 2,009,364	$ 3,107,704	$ 3,592,432	$ 4,276,794
Total capitalization	$ 4,573,024	$ 5,671,364	$ 6,259,641	$ 9,118,730

(1) As adjusted amount reflects the impact of the net proceeds of $1,098.3 million from this offering. As further adjusted amount additionally reflects the impact of the net proceeds of $585.8 million from the TEU Offering. The pro forma amount additionally reflects Peoples's cash balance of $13.7 million as of December 31, 2018, the estimated net proceeds from the Private Placement of $728.4 million and the estimated net proceeds of the Debt Financings of $1,149.4 million, less the estimated cash purchase price of Peoples of $2,945.8 million (see Note 6), the estimated amount of the Company Debt Refinancing of approximately $314 million (see Note 4) and additional estimated acquisition-related payments for expenses of $110.3 million. Cash and cash equivalents may increase or decrease depending on, among other things, actual costs and expenses incurred in connection with the Transactions.

(2) Such amounts do not include subsidiary debt that is reflected in "Privately placed notes" or in "Assumed Peoples's indebtedness".

(3) In December 2018, we entered into a five-year $550 million unsecured Revolving Credit Facility, which replaced our prior unsecured revolving credit facility. Subject to customary conditions, we may request that the lenders under the Revolving Credit Facility provide an incremental unsecured revolving credit facility of up to $450 million upon the closing of the Acquisition. As described below in note 6, at the closing of the Acquisition, we expect to borrow $270 million under the Revolving Credit Facility in order to repay $270 million under the Peoples's revolving credit facility that is expected to be assumed at the closing of the Acquisition and terminated .

(4) In connection with the Acquisition and the Financing Transactions, we expect to redeem approximately $314 million in aggregate principal amount of our PPNs, of which $150.9 million in aggregate principal amount is indebtedness of our subsidiaries, prior to the closing of the Acquisition.

(5) The pro forma amount of $1,159 million represents the assumed aggregate principal amount of the Debt Financings, including the $150 million aggregate principal amount we intend to use for general corporate purposes. If we do not consummate the TEU Offering or the Private Placement, or if such offerings are completed for less aggregate net proceeds than anticipated, we may issue additional shares of common stock or equity-linked securities prior to the consummation of the Acquisition. However, if we are unable to issue such shares or equity-linked securities, we would fund any shortfall with additional debt financings, which may include borrowings under the Bridge Facility and/or the Revolving Credit Facility.
We expect the terms of one or more series of New Notes issued in the Debt Financings will include a special mandatory redemption provision requiring us to redeem such New Notes if the Acquisition is not consummated by a specified date. If the Acquisition is not consummated, we do not expect to incur any borrowings under the Bridge Facility.

(6) The pro forma amount reflects approximately $1,329 million aggregate principal amount of Peoples's existing indebtedness expected to be assumed in connection with the Acquisition as of December 31, 2018. We expect the amount of such assumed debt will be $1,370 million as of the closing of the Acquisition. Of the $1,370 million of expected assumed Peoples's indebtedness at closing, $270 million is expected to be borrowings under the Peoples's revolving credit facility which is expected to be repaid at the closing of the Acquisition with borrowings under the Revolving Credit Facility and terminated.

(7) Each TEU will include a TEU amortizing note, as described in "Summary Information—Recent Developments—Financing Transactions—TEU Offering." Approximately 17.3% of the stated amount of the TEUs, $103.5 million, will be represented by the TEU amortizing notes.

Under certain conditions, if the TEU Offering is consummated but the Acquisition does not occur, we may elect to redeem all, but not less than all, of the outstanding TEU purchase contracts in accordance with the terms thereof, in which case holders of TEUs would have the right to require us to repurchase their outstanding TEU amortizing notes at the relevant repurchase price. See "Summary Information—Recent Developments—Financing Transactions—TEU Offering." We would not have the option to redeem the TEU amortizing notes.

(8) As adjusted, as further adjusted and pro forma share numbers and amounts ($16.2 million with respect to "Common stock" and $1,082.1 million with respect to "Capital in excess of par value") with respect to this offering reflect related underwriting discounts and estimated offering expenses.

The pro forma share number and amount also reflects the expected issuance of 21,661,095 shares in the Private Placement at an offering price of $34.62 per share (an incremental $10.8 million with respect to "Common stock" and an incremental $717.6 million with respect to "Capital in excess of par value") and reflects placement agent fees and other estimated issuance costs. In addition to other closing conditions, the completion of the Private Placement is conditioned upon the completion of at least $1.6 billion in common stock and equity-linked securities offerings and the consummation of the Acquisition.

If and to the extent that any of the TEU Offering or the Private Placement is not completed, or if the aggregate net proceeds from such offerings is less than anticipated, we currently intend to issue additional shares of common stock or equity-linked securities prior to the consummation of the Acquisition. However, if we are unable to issue such shares or equity-linked securities, we would fund any shortfall with additional debt financings, which may include borrowings under the Bridge Facility and/or the Revolving Credit Facility.

Share numbers and amounts do not reflect shares of our common stock issuable upon settlement of the TEU purchase contracts, shares of our common stock reserved for issuance upon exercise of stock options outstanding, shares of our common stock reserved for issuance upon vesting of our time based restricted stock units (including reinvested dividends), shares of our common stock reserved for issuance upon the vesting of our performance based restricted stock units or performance share units or additional shares we may issue under our dividend reinvestment program, employee stock purchase plan or 401(k) savings plans. See "Summary Information–The Offering"

(9) Each TEU will include a TEU purchase contract. We will account for the TEU purchase contracts as equity and will record the initial fair value of the TEU purchase contracts, net of the related underwriting discounts and estimated offering expenses allocated to the TEU purchase contracts, as capital in excess of par value, $484.7 million. The exact amount we record as capital in excess of par value will not be determined until our determination of the final offering expenses related thereto. See note (7) above.

Under certain conditions, if the TEU Offering is consummated but the Acquisition does not occur, we may elect to redeem all, but not less than all, of the outstanding TEU purchase contracts in accordance with the terms thereof. We will pay a redemption amount to be determined based on our common stock price at the time in cash and/or shares of our common stock in accordance with the terms of the TEU purchase contract. If we elect to redeem the TEU purchase contracts, holders of TEUs would have the right to require us to repurchase their outstanding TEU amortizing notes at the relevant repurchase price. See "Summary Information—Recent Developments—Financing Transactions—TEU Offering."

(10) The pro forma amount, a reduction of $44.1 million, reflects the payment of additional Acquisition-related expenses and the write-off of unamortized debt issuance costs.

LISTING OF OUR COMMON STOCK AND DIVIDENDS

Our common stock is listed on the NYSE under the symbol "WTR." As of March 31, 2019, there were (i) 178,369,078 shares of our common stock outstanding and (ii) options to acquire 1,112,210 shares of our common stock outstanding.

On April 17, 2019, the last reported sale price of our common stock on the NYSE was $34.82. As of December 31, 2018, there were approximately 23,476 holders of record of our common stock.

We have historically paid quarterly dividends on our common stock; however, the declaration, amount, timing and payment of any future dividends are subject to the determination and approval of our board of directors based on then-current or anticipated future conditions including our results of operations, capital requirements, financial condition, legal requirements or other factors deemed relevant by our board of directors. See "Risk Factors—Risks Related to Our Common Stock—We may be unable to, or may choose not to, continue to pay dividends on our common stock at current or planned rates or at all."

CERTAIN UNITED STATES FEDERAL INCOME AND ESTATE TAX CONSIDERATIONS TO NON-U.S. HOLDERS

The following is a summary of certain United States federal income and estate tax consequences of the purchase, ownership and disposition of our common stock as of the date hereof. Except where noted, this summary deals only with common stock that is held as a capital asset by a non-U.S. holder (as defined below).

A "non-U.S. holder" means a beneficial owner of our common stock (other than an entity treated as a partnership for United States federal income tax purposes) that is not, for United States federal income tax purposes, any of the following:

- an individual citizen or resident of the United States;
- a corporation (or any other entity treated as a corporation for United States federal income tax purposes) created or organized in or under the laws of the United States, any state thereof or the District of Columbia;
- an estate the income of which is subject to United States federal income taxation regardless of its source; or
- a trust if it (1) is subject to the primary supervision of a court within the United States and one or more United States persons have the authority to control all substantial decisions of the trust or (2) has a valid election in effect under applicable United States Treasury regulations to be treated as a United States person.

This summary is based upon provisions of the Internal Revenue Code of 1986, as amended (the "Code"), and regulations, rulings and judicial decisions as of the date hereof. Those authorities may be changed, perhaps retroactively, so as to result in United States federal income and estate tax consequences different from those summarized below. This summary does not address all aspects of United States federal income and estate taxes and does not deal with foreign, state, local or other tax considerations that may be relevant to non-U.S. holders in light of their particular circumstances. In addition, it does not represent a detailed description of the United States federal income and estate tax consequences applicable to you if you are subject to special treatment under the United States federal income tax laws (including if you are a United States expatriate, foreign pension fund, "controlled foreign corporation," "passive foreign investment company" or a partnership or other pass-through entity for United States federal income tax purposes). We cannot assure you that a change in law will not alter significantly the tax considerations that we describe in this summary.

If a partnership (or other entity treated as a partnership for United States federal income tax purposes) holds our common stock, the tax treatment of a partner will generally depend upon the status of the partner and the activities of the partnership. If you are a partner of a partnership holding our common stock, you should consult your tax advisors.

If you are considering the purchase of our common stock, you should consult your own tax advisors concerning the particular United States federal income and estate tax consequences to you of the purchase, ownership and disposition of our common stock, as well as the consequences to you arising under other United States federal tax laws and the laws of any other taxing jurisdiction.

Dividends

In the event that we make a distribution of cash or other property (other than certain pro rata distributions of our stock) in respect of our common stock, the distribution generally will be treated as a dividend for United States federal income tax purposes to the extent it is paid from our current or accumulated earnings and profits, as determined under United States federal income tax principles. Any portion of a distribution that exceeds our current and accumulated

earnings and profits generally will be treated first as a tax-free return of capital, causing a reduction in the adjusted tax basis of a non-U.S. holder's common stock, and to the extent the amount of the distribution exceeds a non-U.S. holder's adjusted tax basis in our common stock, the excess will be treated as gain from the disposition of our common stock (the tax treatment of which is discussed below under "—Gain on Disposition of Common Stock").

Dividends paid to a non-U.S. holder generally will be subject to withholding of United States federal income tax at a 30% rate or such lower rate as may be specified by an applicable income tax treaty. However, dividends that are effectively connected with the conduct of a trade or business by the non-U.S. holder within the United States (and, if required by an applicable income tax treaty, are attributable to a United States permanent establishment) are not subject to the withholding tax, provided certain certification and disclosure requirements are satisfied. Instead, such dividends are subject to United States federal income tax on a net income basis in the same manner as if the non-U.S. holder were a United States person as defined under the Code. Any such effectively connected dividends received by a foreign corporation may be subject to an additional "branch profits tax" at a 30% rate or such lower rate as may be specified by an applicable income tax treaty.

A non-U.S. holder who wishes to claim the benefit of an applicable treaty rate and avoid backup withholding, as discussed below, for dividends will be required (a) to provide the applicable withholding agent with a properly executed Internal Revenue Service ("IRS") Form W-8BEN or Form W-8BEN-E (or other applicable form) certifying under penalty of perjury that such holder is not a United States person as defined under the Code and is eligible for treaty benefits or (b) if our common stock is held through certain foreign intermediaries, to satisfy the relevant certification requirements of applicable United States Treasury regulations. Special certification and other requirements apply to certain non-U.S. holders that are pass-through entities rather than corporations or individuals.

A non-U.S. holder eligible for a reduced rate of United States federal withholding tax pursuant to an income tax treaty may obtain a refund of any excess amounts withheld by timely filing an appropriate claim for refund with the IRS.

Gain on Disposition of Common Stock

Subject to the discussion of backup withholding below, any gain realized by a non-U.S. holder on the sale or other disposition of our common stock generally will not be subject to United States federal income tax unless:

- the gain is effectively connected with a trade or business of the non-U.S. holder in the United States (and, if required by an applicable income tax treaty, is attributable to a United States permanent establishment of the non-U.S. holder);
- the non-U.S. holder is an individual who is present in the United States for 183 days or more in the taxable year of that disposition, and certain other conditions are met; or
- we are or have been a "United States real property holding corporation" for United States federal income tax purposes and certain other conditions are met.

A non-U.S. holder described in the first bullet point immediately above will be subject to tax on the gain derived from the sale or other disposition in the same manner as if the non-U.S. holder were a United States person as defined under the Code. In addition, if any non-U.S. holder described in the first bullet point immediately above is a foreign corporation, the gain realized by such non-U.S. holder may be subject to an additional "branch profits tax" at a 30% rate or such lower rate as may be specified by an applicable income tax treaty. An individual non-U.S. holder described in the second bullet point immediately above will be subject to a 30% (or such lower rate as may be specified by an applicable income tax treaty) tax on the gain derived from the sale or other disposition, which gain may be offset by United States source capital losses even though the individual is not considered a resident of the United States.

Generally, a corporation is a "United States real property holding corporation" if the fair market value of its United States real property interests equals or exceeds 50% of the sum of the fair market value of its worldwide real property interests and its other assets used or held for use in a trade or business (all as determined for United States federal income tax purposes). We believe we are not and do not anticipate becoming a "United States real property holding corporation" for United States federal income tax purposes. If, however, we are or become a "United States real property holding corporation," so long as our common stock is regularly traded on an established securities market during the calendar year in which the sale or other disposition occurs, only a non-U.S. holder who holds or held (at any time during the shorter of the five year period preceding the date of disposition or the holder's holding period) more than 5% of our common stock will be subject to United States federal income tax on the sale or other disposition of our common stock.

Federal Estate Tax

Common stock held by an individual non-U.S. holder at the time of death will be included in such holder's gross estate for United States federal estate tax purposes, unless an applicable estate tax treaty provides otherwise.

Information Reporting and Backup Withholding

Distributions paid to a non-U.S. holder and the amount of any tax withheld with respect to such distributions generally will be reported to the IRS. Copies of the information returns reporting such distributions and any withholding may also be made available to the tax authorities in the country in which the non-U.S. holder resides under the provisions of an applicable income tax treaty.

A non-U.S. holder will not be subject to backup withholding on dividends received if such holder certifies under penalty of perjury that it is a non-U.S. holder (and the payor does not have actual knowledge or reason to know that such holder is a United States person as defined under the Code), or such holder otherwise establishes an exemption.

Information reporting and, depending on the circumstances, backup withholding will apply to the proceeds of a sale or other disposition of our common stock made within the United States or conducted through certain United States-related financial intermediaries, unless the beneficial owner certifies under penalty of perjury that it is a non-U.S. holder (and the payor does not have actual knowledge or reason to know that the beneficial owner is a United States person as defined under the Code), or such owner otherwise establishes an exemption.

Backup withholding is not an additional tax and any amounts withheld under the backup withholding rules will be allowed as a refund or a credit against a non-U.S. holder's United States federal income tax liability provided the required information is timely furnished to the IRS.

Additional Withholding Requirements

Under Sections 1471 through 1474 of the Code (such Sections commonly referred to as "FATCA"), a 30% United States federal withholding tax may apply to any dividends paid on our common stock to (1) a "foreign financial institution" (as specifically defined in the Code) which does not provide sufficient documentation, typically on IRS Form W-8BEN-E, evidencing either (a) an exemption from FATCA, or (b) its compliance (or deemed compliance) with FATCA (which may alternatively be in the form of compliance with an intergovernmental agreement with the United States) in a manner which avoids withholding, or (2) a "non- financial foreign entity" (as specifically defined in the Code) which does not provide sufficient documentation, typically on IRS Form W-8BEN-E, evidencing either (a) an exemption from FATCA, or (b) adequate information regarding certain substantial United States beneficial owners of such entity (if any). If a dividend payment is both subject to withholding under FATCA and subject to the withholding tax discussed above under "—Dividends," the withholding under FATCA may be credited against, and therefore reduce, such other withholding tax. You should consult your own tax advisors regarding these requirements and whether they may be relevant to your ownership and disposition of our common stock.

CERTAIN ERISA CONSIDERATIONS

The following is a summary of certain considerations associated with the purchase of our common stock by (i) employee benefit plans that are subject to Title I of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), (ii) plans, individual retirement accounts and other arrangements that are subject to Section 4975 of the Code or provisions under any other federal, state, local, non-U.S. or other laws or regulations that are similar to such provisions of ERISA or the Code (collectively, "Similar Laws"), and (iii) entities which are deemed to hold the assets of any of the foregoing types of plans, accounts or arrangements (each of the foregoing described in clauses (i), (ii), and (iii) being referred to herein as a "Plan").

General fiduciary matters and prohibited transaction issues

ERISA and the Code impose certain duties on persons who are fiduciaries of a Plan subject to Title I of ERISA or Section 4975 of the Code (a "Covered Plan") and prohibit certain transactions involving the assets of a Covered Plan and its fiduciaries or other interested parties. Under ERISA and the Code, any person who exercises any discretionary authority or control over the administration of such a Covered Plan or the management or disposition of the assets of such a Covered Plan, or who renders investment advice for a fee or other compensation to such a Covered Plan, is generally considered to be a fiduciary of the Covered Plan.

Section 406 of ERISA and Section 4975 of the Code prohibit Covered Plans from engaging in specified transactions involving plan assets with persons or entities who are "parties in interest," within the meaning of ERISA, or "disqualified persons," within the meaning of Section 4975 of the Code, unless an exemption is available. A party in interest or disqualified person who engaged in a non-exempt prohibited transaction may be subject to excise taxes and other penalties and liabilities under ERISA and the Code. In addition, the fiduciary of the Covered Plan that engaged in such a non-exempt prohibited transaction may be subject to penalties and liabilities under ERISA and the Code.

In considering an investment in our common stock with a portion of the assets of any Plan, a fiduciary should determine whether the investment is in accordance with the documents and instruments governing the Plan and the applicable provisions of ERISA, the Code or any Similar Law relating to a fiduciary's duty to the Plan, including without limitation, the prudence, diversification, delegation of control and prohibited transaction provisions of ERISA, the Code and any other applicable Similar Laws.

Government plans, foreign plans and certain church plans, while not subject to the fiduciary responsibility provisions of Title I of ERISA or the prohibited transaction provisions of Section 406 of ERISA or Section 4975 of the Code, may nevertheless be subject to Similar Laws. Fiduciaries of such Plans should consult with their counsel before acquiring shares of our common stock.

Representation

Accordingly, by its acceptance of our common stock, each purchaser and subsequent transferee will be deemed to have represented and warranted that either (i) no portion of the assets used by such purchaser or transferee to acquire our common stock constitutes assets of any Plan or (ii) the acquisition of our common stock by such purchaser or transferee will not constitute or result in a non-exempt prohibited transaction under Section 406 of ERISA or Section 4975 of the Code or a similar violation under any applicable Similar Laws.

The foregoing discussion is general in nature and is not intended to be all-inclusive. Due to the complexity of these rules and the penalties that may be imposed upon persons involved in non-exempt prohibited transactions, it is particularly important that fiduciaries or other persons considering purchasing our common stock on behalf of, or with the assets of, any Plan, consult with their counsel regarding the potential applicability of ERISA, Section 4975 of the Code or any Similar Law and whether an exemption would be required. Neither

this discussion nor anything provided in this prospectus is, or is intended to be, investment advice directed at any potential Plan purchasers, or at Plan purchasers generally, and such purchasers of our common stock should consult and rely on their own counsel and advisers as to whether an investment in our common stock is suitable for the Plan. The sale of our common stock to any Plan is in no respect a representation by us, an underwriter or any of our or their affiliates or representatives that such an investment meets all relevant legal requirements with respect to investments by Plans generally or any particular Plan, or that such investment is prudent or appropriate for plans generally or any particular Plan.

UNDERWRITING

Under the terms and subject to the conditions in an underwriting agreement dated the date of this prospectus supplement, the underwriters named below, for whom Goldman Sachs & Co. LLC and RBC Capital Markets, LLC are acting as representatives, have severally agreed to purchase, and we have agreed to sell to them, severally, the number of shares of our common stock indicated below:

Underwriters	Number of Shares
Goldman Sachs & Co. LLC	9,829,939
RBC Capital Markets, LLC	9,829,939
Merrill Lynch, Pierce, Fenner & Smith Incorporated	2,296,103
Morgan Stanley & Co. LLC	2,296,103
Wells Fargo Securities, LLC	1,607,272
PNC Capital Markets LLC	1,974,648
Barclays Capital Inc.	1,607,272
Citizens Capital Markets, Inc.	551,065
The Huntington Investment Company	551,065
MUFG Securities Americas Inc.	551,065
J.P. Morgan Securities LLC	375,642
TD Securities (USA) LLC	375,642
Robert W. Baird & Co. Incorporated	162,478
Boenning & Scattergood, Inc.	162,478
HSBC Securities (USA) Inc.	162,478
Janney Montgomery Scott LLC	162,478
Total	32,495,667

The underwriters and the representatives are collectively referred to as the “underwriters” and the “representatives,” respectively. The underwriters are offering the shares subject to their acceptance of the shares from us and subject to prior sale. The underwriting agreement provides that the obligations of the several underwriters to pay for and accept delivery of the shares offered by this prospectus supplement are subject to the approval of certain legal matters by their counsel and to certain other conditions. The underwriters are obligated to take and pay for all of the shares offered by this prospectus supplement if any such shares are taken. However, the underwriters are not required to take or pay for the shares covered by the underwriters’ option to purchase additional shares described below.

The underwriters initially propose to offer part of the shares directly to the public at the offering price listed on the cover page of this prospectus supplement and part to certain dealers. After the initial offering of the shares, the offering price and other selling terms may from time to time be varied by the representatives.

We have granted to the underwriters an option, exercisable for 30 days from the date of this prospectus supplement, to purchase up to 4,874,350 additional shares of our common stock at the public offering price listed on the cover page of this prospectus supplement, less underwriting discounts. To the extent the option is exercised, each underwriter will become obligated, subject to certain conditions, to purchase about the same percentage of the additional shares as the number listed next to the underwriter’s name in the preceding table bears to the total number of shares listed next to the names of all underwriters in the preceding table.

The following table shows the per share and total public offering price, underwriting discount we will pay to the underwriters in this offering, and proceeds before expenses to us. These amounts are shown assuming both no exercise and full exercise of the underwriters’ option to purchase up to an additional 4,874,350 shares.

	Per Share	Total No Exercise	Total Full Exercise
Public offering price	$ 34.620	$1,124,999,992	$1,293,749,989
Underwriting discount	$ 0.779	$ 25,314,125	$ 29,111,243
Proceeds, before expenses, to us	$ 33.841	$1,099,685,867	$1,264,638,746

The estimated offering expenses payable by us, exclusive of the underwriting discount, are approximately $1.4 million. We have agreed to reimburse the underwriters for expense relating to any required review of this offering by the Financial Industry Regulatory Authority, Inc.

Our common stock is listed on the NYSE under the symbol "WTR."

We and all of our continuing directors (as described in our Definitive Proxy Statement on Schedule 14A filed with the SEC on March 22, 2019), director nominees and officers, through entering into lock-up agreements, have agreed that, without the prior written consent of the representatives on behalf of the underwriters, we and they will not, during the period ending 90 days after the date of this prospectus supplement (the "restricted period"): (i) offer, sell, contract to sell, pledge, grant any option to purchase, make any short sale or otherwise transfer or dispose of, directly or indirectly, our common stock, any options, rights or warrants to purchase our common stock or any securities convertible into or exchangeable for, or substantially similar to, our common stock (collectively, "restricted securities"); (ii) enter into any swap or other agreement that transfers to another, in whole or in part, any of the economic consequences of ownership of the common stock or any such other securities, whether any such transaction described in (i) or (ii) is to be settled by delivery of common stock or such other securities, in cash or otherwise or (iii) publicly disclose the intention to take any of the foregoing actions. In addition, we agreed not to file with the SEC any registration statement relating to any restricted securities, and our continuing directors, director nominees and officers each agreed not to make any demand for, or exercise any right with respect to, the registration of any restricted securities, in each case during the restricted period and without the prior written consent of the representatives on behalf of the underwriters.

The restrictions described in the immediately preceding paragraph do not apply to:

- the sale of the shares to the underwriters in this offering, the sale of the TEUs to the underwriters of the TEU Offering or the sale of the shares of our common stock in the Private Placement;
- the issuance by us of, or the receipt by our continuing directors, director nominees and officers of, restricted securities pursuant to our existing employee equity or equity-based incentive plans, employee stock purchase plans or dividend reinvestment plans, or upon the conversion or exchange of convertible or exchangeable securities outstanding as of the date of this prospectus supplement;
- the filing by us of registration statements relating to securities issuable under our existing employee equity or equity-based plans or employee stock purchase plans;
- the issuance of shares of common stock in connection with certain investments, acquisitions, with joint ventures, commercial relationships or other strategic transactions, provided that the aggregate number of shares issued or issuable pursuant to this clause does not exceed 10% of the number of shares of common stock outstanding immediately after this offering and prior to such issuance;
- in the case of our continuing directors, director nominees and officers, (i) the establishment of a trading plan pursuant to Rule 10b5-1 under the Exchange Act for the transfer of our common stock following expiration of the restricted period, (ii) transfers in accordance with the terms of existing trading plans pursuant to Rule 10b5-1 under the Exchange Act, (iii) certain transfers of shares held as of the date of this prospectus supplement through our existing 401(k) plan pursuant to portfolio balancing

opportunities provided by the terms of such plan, (iv) transfers to us to satisfy certain tax obligations in connection with vesting of restricted stock units, restricted shares, performance share units or phantom shares and (v) certain other transfers to us;

- in the case of our continuing directors, director nominees and officers, transfers to us upon death, disability or termination or employment, in each case, of such person;

- the receipt by us or our subsidiaries of shares (a) in the exercise of outstanding options, warrants, restricted stock units or other equity interests, including transfers deemed to occur upon the "net" or "cashless" exercise of options or (b) for the sole purpose of paying the exercise price of such options, warrants, restricted stock units or other equity interests or for paying taxes (including estimated taxes) due as a result of the exercise of such options, warrants, restricted stock units or other equity interests or as a result of the vesting of shares under restricted stock awards or restricted stock units pursuant to our existing employee benefit plans disclosed herein relating to this public offering, in each case on a "cashless" or "net exercise" basis, provided that any such shares received upon such exercise shall be subject to the terms of the lock-up agreement;

- tenders, sales or other transfers pursuant to a bona fide third-party tender offer, merger, consolidation or other similar transaction made to all holders of restricted securities involving a "change of control" of us (provided that if such transaction is not consummated, our continuing directors', director nominees' and officers' shares shall remain subject to the restrictions set forth in the lock-up agreements);

- the exercise for cash of options to purchase shares disclosed as outstanding herein, provided that any such shares received upon such exercise shall be subject to the terms of the lock-up agreements;

- in the case of our continuing directors, director nominees and officers, the disposition of shares acquired in this offering or in open market transactions after completion of this offering; and

- transfers of shares or other of our securities pursuant to an order of a court or regulatory agency or to comply with any regulations related to ownership by our continuing directors, director nominees and officers of their shares.

The representatives, in their sole discretion, may release the common stock and other securities subject to the lock-up agreements described above in whole or in part at any time.

In order to facilitate the offering of the shares, the underwriters may engage in transactions that stabilize, maintain or otherwise affect the price of the shares. Specifically, the underwriters may sell more shares than they are obligated to purchase under the underwriting agreement, creating a short position. A short sale is covered if the short position is no greater than the number of shares available for purchase by the underwriters under the option to purchase additional shares. The underwriters can close out a covered short sale by exercising the option or purchasing shares of our common stock in the open market. In determining the source of shares to close out a covered short sale, the underwriters will consider, among other things, the open market price of shares of our common stock compared to the price available under the option. The underwriters may also sell shares of our common stock in excess of the option, creating a naked short position. The underwriters must close out any naked short position by purchasing shares of our common stock in the open market. A naked short position is more likely to be created if the underwriters are concerned that there may be downward pressure on the price of the shares in the open market after pricing that could adversely affect investors who purchase in this offering. As an additional means of facilitating this offering, the underwriters may bid for, and purchase, shares of our common stock in the open market to stabilize the price of the shares. These activities may raise or maintain the market price of the shares above independent market levels or prevent or retard a decline in the market price of the shares. The underwriters are not required to engage in these activities and may end any of these activities at any time.

We have agreed to indemnify the underwriters against certain liabilities in connection with this offering,including liabilities under the Securities Act, or to contribute to payments that the underwriters may be required to make in respect of those liabilities.

The underwriters and their respective affiliates are full-service financial institutions engaged in various activities, which may include securities trading, commercial and investment banking, financial advisory, investment management, investment research, principal investment, hedging, financing and brokerage activities. Certain of the underwriters and their respective affiliates have, from time to time, performed, and may in the future perform, various financial advisory and investment banking services for us, for which they received or will receive customary fees and expenses. For example, Goldman Sachs & Co. LLC and RBC Capital Markets, LLC acted as our financial advisers in connection with the Acquisition, for which they are receiving customary fees and expenses. Also in connection with the Acquisition, certain of the underwriters and/or their affiliates have provided committed financing under the Bridge Commitment, pursuant to which they receive customary commitment fees in connection with their respective commitments and, in the event we borrow under the Bridge Facility, would receive certain additional funding and other fees. Certain of the underwriters and/or their affiliates are also lenders and/or agents under the Revolving Credit Facility, which we expect to draw upon to refinance Peoples's revolving credit facility in connection with the Acquisition, and receive customary fees and expenses in connection therewith and would receive proceeds from this offering if we were to temporarily reduce our borrowings under the Revolving Credit Facility as described in "Use of Proceeds." Certain of the underwriters in this offering are also acting as underwriters in our concurrent TEU Offering, and may act as underwriters in the Notes Offering, for which they will receive customary fees and expenses. Certain of the underwriters may also receive fees and expenses in connection with the Private Placement. In addition, in an effort to manage our exposure to interest rate risk associated with the Notes Offering, we have entered into, and in the future, may enter into, financial derivative instruments such as interest rate swap agreements with certain of the underwriters or their respective affiliates.

In addition, in the ordinary course of their various business activities, the underwriters and their respective affiliates may make or hold a broad array of investments and actively trade debt and equity securities (or related derivative securities) and financial instruments (including bank loans) for their own account and for the accounts of their customers and may at any time hold long and short positions in such securities and instruments. Such investment and securities activities may involve our securities and instruments. Certain of the underwriters and/or their affiliates have lending relationships with us and may hedge their credit exposure to us consistent with their customary risk management policies. Typically, the underwriters and their affiliates would hedge such exposure by entering into transactions which consist of either the purchase of credit default swaps or the creation of short positions in our securities or the securities of our affiliates. Any such credit default swaps or short positions could adversely affect future trading prices of the shares offered hereby. The underwriters and their respective affiliates may also make investment recommendations or publish or express independent research views in respect of such securities or instruments and may at any time hold, or recommend to clients that they acquire, long or short positions in such securities and instruments, for which they received or will receive customary fees and expenses.

Selling Restrictions

Canada

The shares may be sold only to purchasers purchasing, or deemed to be purchasing, as principal that are accredited investors, as defined in National Instrument 45-106 Prospectus Exemptions or subsection 73.3(1) of the Securities Act (Ontario), and are permitted clients, as defined in National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations. Any resale of the shares must be made in accordance with an exemption from, or in a transaction not subject to, the prospectus requirements of applicable securities laws.

Securities legislation in certain provinces or territories of Canada may provide a purchaser with remediesfor rescission or damages if this prospectus supplement (including any amendment thereto) contains a misrepresentation, provided that the remedies for rescission or damages are exercised by the purchaser within the time limit prescribed by the securities legislation of the purchaser's province or territory. The purchaser should refer to any applicable provisions of the securities legislation of the purchaser's province or territory for particulars of these rights or consult with a legal advisor.

Pursuant to section 3A.3 (or, in the case of securities issued or guaranteed by the government of a non- Canadian jurisdiction, section 3A.4) of National Instrument 33-105 Underwriting Conflicts (NI 33-105), the underwriters are not required to comply with the disclosure requirements of NI 33-105 regarding underwriter conflicts of interest in connection with this offering.

European Economic Area

In relation to each Member State of the European Economic Area which has implemented the Prospectus Directive (each, a "Relevant Member State") an offer to the public of our common shares may not be made in that Relevant Member State, except that an offer to the public in that Relevant Member State of our common shares may be made at any time under the following exemptions under the Prospectus Directive:

(a) to any legal entity which is a qualified investor as defined in the Prospectus Directive;

(b) to fewer than 150 natural or legal persons (other than qualified investors as defined in the Prospectus Directive), subject to obtaining the prior consent of the underwriters for any such offer; or

(c) in any other circumstances falling within Article 3(2) of the Prospectus Directive, provided that no such offer of shares of our common stock shall result in a requirement for the publication by us or any underwriter of a prospectus pursuant to Article 3 of the Prospectus Directive.

For the purposes of this provision, the expression an "offer to the public" in relation to our common shares in any Relevant Member State means the communication in any form and by any means of sufficient information on the terms of the offer and our common shares to be offered so as to enable an investor to decide to purchase our common shares, as the same may be varied in that Member State by any measure implementing the Prospectus Directive in that Member State, the expression "Prospectus Directive" means Directive 2003/71/ EC (as amended), including by Directive 2010/73/EU, and includes any relevant implementing measure in the Relevant Member State.

This European Economic Area selling restriction is in addition to any other selling restrictions set out below.

United Kingdom

In addition, this document is being distributed only to, and is directed only at, and any offer subsequently made may only be directed at: (i) in the United Kingdom, persons having professional experience in matters relating to investments falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005, as amended (the "Order"), and/or persons falling within Article 49(2)(a) to (d) of the Order; (ii) persons who are outside the United Kingdom; and (iii) any other persons to whom it may otherwise lawfully be distributed (all such persons together being referred to as "relevant persons"). This document must not be acted on or relied on by persons who are not relevant persons. Any investment or investment activity to which this document relates is available only to, and will be engaged in only with, relevant persons.

Australia

No placement document, prospectus, product disclosure statement or other disclosure document has been lodged with the Australian Securities and Investments Commission ("ASIC") in relation to the offering. This prospectus supplement, the accompanying prospectus and any other offering or marketing material relating to the shares or this offering do not constitute a prospectus, product disclosure statement or other disclosure document under the prospectus, product disclosure statement or other disclosure document under the Corporations Act 2001 (Cth) (the "Corporations Act"), and do not purport to include the information required for a prospectus, product disclosure statement or other disclosure document under the Corporations Act.

Any offer in Australia of the shares may only be made to persons (the "Exempt Investors") who are "sophisticated investors" (within the meaning of section 708(8) of the Corporations Act), "professional investors" (within the meaning of section 708(11) of the Corporations Act) or otherwise pursuant to one or more exemptions contained in section 708 of the Corporations Act so that it is lawful to offer the shares without disclosure to investors under Chapter 6D of the Corporations Act.

The shares applied for by Exempt Investors in Australia must not be offered for sale in Australia for a period of 12 months after the date of allotment under the offering, except in circumstances where disclosure to investors under Chapter 6D of the Corporations Act would not be required pursuant to an exemption under section 708 of the Corporations Act or otherwise or where the offer is pursuant to a disclosure document which complies with Chapter 6D of the Corporations Act. Any person acquiring shares must observe such Australian on-sale restrictions.

This prospectus supplement and the accompanying prospectus contain general information only and do not take account of the investment objectives, financial situation or particular needs of any particular person. They do not contain any securities recommendations or financial product advice. Before making an investment decision, investors need to consider whether the information in this prospectus supplement and the accompanying prospectus is appropriate to their needs, objectives and circumstances, and, if necessary, seek expert advice on those matters.

Hong Kong

The shares may not be offered or sold in Hong Kong by means of any document other than (i) in circumstances which do not constitute an offer to the public within the meaning of the Companies Ordinance (Cap. 32, Laws of Hong Kong), or (ii) to "professional investors" within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder, or (iii) in other circumstances which do not result in the document being a "prospectus" within the meaning of the Companies Ordinance (Cap. 32, Laws of Hong Kong) and no advertisement, invitation or document relating to the shares may be issued or may be in the possession of any person for the purpose of issue (in each case whether in Hong Kong or elsewhere), which is directed at, or the contents of which are likely to be accessed or read by, the public in Hong Kong (except if permitted to do so under the laws of Hong Kong) other than with respect to shares which are or are intended to be disposed of only to persons outside Hong Kong or only to "professional investors" within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder.

Japan

The shares have not been and will not be registered under the Financial Instruments and Exchange Act of Japan (Act No. 25 of 1948, as amended) (the "FIEA"). The shares may not be offered or sold, directly or indirectly, in Japan or to or for the benefit of any resident of Japan (including any person resident in Japan or any corporation or other entity organized under the laws of Japan) or to others for reoffering or resale, directly or indirectly, in Japan or to or for the benefit of any resident of Japan, except pursuant to an exemption from the registration requirements of the FIEA and otherwise in compliance with any relevant laws, regulations and ministerial guidelines of Japan.

Korea

Neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the shares or the offering should be construed in any way as our (or any of our affiliates or agents) soliciting investment or offering to sell the shares in the Republic of Korea ("Korea"). We are not making any representation with respect to the eligibility of any recipients of this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the shares or the offering to acquire the shares under the laws of Korea, including, without limitation, the Financial Investment Services and Capital Markets Act (the "FSCMA"), the Foreign Exchange Transaction Act (the "FETA"), and any regulations thereunder. The shares have not been registered with the Financial Services Commission of Korea (the "FSC") in any way pursuant to the FSCMA, and the shares may not be offered, sold or delivered, or offered or sold to any person for reoffering or resale, directly or indirectly, in Korea or to any resident of Korea except pursuant to applicable laws and regulations of Korea. Furthermore, the shares may not be resold to any Korean resident unless such Korean resident as the purchaser of the resold shares complies with all applicable regulatory requirements (including, without limitation, reporting or approval requirements under the FETA and regulations thereunder) relating to the purchase of the resold shares.

Singapore

Neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the shares or the offering has been registered as a prospectus with the Monetary Authority of Singapore. Accordingly, neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the shares or the offering may be circulated or distributed, nor may the shares be offered or sold, or be made the subject of an invitation for subscription or purchase, whether directly or indirectly, to persons in Singapore, other than (a) to an institutional investor under Section 274 of the Securities and Futures Act, Chapter 289 of Singapore (the "SFA"), (b) to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions specified in Section 275 of the SFA or (c) pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA.

Where the shares are subscribed or purchased under Section 275 by a relevant person which is: (i) a corporation (which is not an accredited investor) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or (ii) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary is an accredited investor, shares, debentures and units of shares and debentures of that corporation or the beneficiaries' rights and interest in that trust shall not be transferable for six months after that corporation or that trust has acquired the shares under Section 275 except: (1) to an institutional investor under Section 274 of the SFA or to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions, specified in Section 275 of the SFA; (2) where no consideration is given for the transfer; or (3) by operation of law.

Solely for the purposes of its obligations pursuant to sections 309B(1)(a) and 309B(1)(c) of the Securities and Futures Act (Chapter 289 of Singapore) (the "SFA"), we have determined, and hereby notify all relevant persons (as defined in Section 309A of the SFA) that the shares are "prescribed capital markets products" (as defined in the Securities and Futures (Capital Markets Products) Regulations 2018) and Excluded Investment Products (as defined in MAS Notice SFA 04-N12: Notice on the Sale of Investment Products and MAS Notice FAA-N16: Notice on Recommendations on Investment Products).

Switzerland

The shares may not be publicly offered in Switzerland and will not be listed on the SIX Swiss Exchange ("*SIX*") or on any other exchange or regulated trading facility in Switzerland. This prospectus supplement, the accompanying prospectus and any other offering or marketing material relating to the shares or this offering do not

constitute a prospectus within the meaning of and have been prepared without regard to the disclosure standards for issuance prospectuses under art. 652a or art. 1156 of the Swiss Code of Obligations or the disclosure standards for listing prospectuses under art. 27 ff. of the SIX Listing Rules or the listing rules of any other exchange or regulated trading facility in Switzerland.

Neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the shares or the offering may be publicly distributed or otherwise made publicly available in Switzerland. Neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the offering, the Company or the shares has been or will be filed with or approved by any Swiss regulatory authority. In particular, this prospectus supplement and the accompanying prospectus will not be filed with, and the offer of shares will not be supervised by, the Swiss Financial Market Supervisory Authority, and the offer of shares has not been and will not be authorized under the Swiss Federal Act on Collective Investment Schemes (the "*CISA*"). The investor protection afforded to acquirers of interests in collective investment schemes under the CISA does not extend to acquirers of the shares.

Taiwan

The shares have not been and will not be registered or filed with, or approved by, the Financial Supervisory Commission of Taiwan and/or any other regulatory authority of Taiwan pursuant to relevant securities laws and regulations and may not be sold, issued or offered within Taiwan through a public offering or in circumstances which could constitute an offer within the meaning of the Securities and Exchange Act of Taiwan or relevant laws and regulations that require a registration, filing or approval of the Financial Supervisory Commission of Taiwan and/or other regulatory authority of Taiwan. No person or entity in Taiwan has been authorized to offer or sell the shares in Taiwan.

United Arab Emirates

The shares have not been, and are not being, publicly offered, sold, promoted or advertised in the United Arab Emirates (including the Abu Dhabi Global Market and the Dubai International Financial Centre) other than in compliance with the laws, regulations and rules of the United Arab Emirates, the Abu Dhabi Global Market and the Dubai International Financial Centre governing the issue, offering and sale of securities. Further, this prospectus supplement, the accompanying prospectus and any other offering or marketing material relating to the shares or the offering do not constitute a public offer of securities in the United Arab Emirates (including the Abu Dhabi Global Market and the Dubai International Financial Centre) and are not intended to be a public offer. This prospectus supplement, the accompanying prospectus and any other offering or marketing material relating to the shares or the offering have not been approved by or filed with the Central Bank of the United Arab Emirates, the Securities and Commodities Authority, the Financial Services Regulatory Authority or the Dubai Financial Services Authority.

LEGAL MATTERS

Certain legal matters will be passed upon for us by Simpson Thacher & Bartlett LLP, New York, New York. Ballard Spahr LLP, Philadelphia, Pennsylvania will issue an opinion regarding certain matters of Pennsylvania law, including the validity of the securities offered by the prospectus supplement. Certain legal matters will be passed upon for the underwriters by Cravath, Swaine & Moore LLP, New York, New York.

EXPERTS

The financial statements and management's assessment of the effectiveness of internal control over financial reporting (which is included in Management's Report on Internal Control over Financial Reporting) incorporated in this prospectus supplement by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2018 have been so incorporated in reliance on the report of PricewaterhouseCoopers LLP, an independent registered public accounting firm, given on the authority of said firm as experts in auditing and accounting.

The consolidated financial statements of LDC Funding LLC as of December 31, 2018 and 2017 and for each of the three years in the period ended December 31, 2018, incorporated by reference in this prospectus supplement and in the accompanying prospectus from Aqua America's Current Report on Form 8-K/A filed on April 15, 2019, have been audited by Deloitte & Touche LLP, independent auditors, as stated in their report, which is incorporated by reference herein, and are incorporated in reliance upon the report of such firm given upon their authority as experts in accounting and auditing.

WHERE YOU CAN FIND ADDITIONAL INFORMATION; INCORPORATION OF CERTAIN DOCUMENTS BY REFERENCE

We file annual, quarterly and current reports, proxy statements and other information with the SEC. The SEC maintains a website at *www.sec.gov* that contains periodic and current reports, proxy and information statements, and other information regarding registrants that are filed electronically with the SEC.

These documents are also available, free of charge, through the Investors section of our website, which is located at *http://ir.aquaamerica.com/*. Information contained on our website is not incorporated by reference into this prospectus supplement or the accompanying prospectus and you should not consider information on our website to be part of this prospectus supplement or the accompanying prospectus.

We have filed with the SEC a "shelf" registration statement on Form S-3 under the Securities Act of 1933 relating to the securities that may be offered by this prospectus supplement. This prospectus supplement is a part of that registration statement, but does not contain all of the information in the registration statement. We have omitted certain parts of the registration statement in accordance with rules and regulations of the SEC. Statements made in this prospectus supplement as to the contents of any contract, agreement or other documents are not necessarily complete, and, in each instance, we refer you to a copy of such document filed as an exhibit to the registration statement, of which this prospectus supplement is a part, or otherwise filed with the SEC. For more detail about us and any securities that may be offered by this prospectus supplement, you may examine the registration statement on Form S-3 and the exhibits filed with it at the locations listed in the previous paragraph.

The SEC allows us to "incorporate by reference" into this prospectus supplement and the accompanying prospectus the information we file with them, which means that we can disclose important information to you by referring you to those documents. The information incorporated by reference is considered to be part of this prospectus supplement. When we file information with the SEC in the future, that information will automatically update and supersede this information. We incorporate by reference the documents listed below and any future filings we will make with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of

1934 until we sell all of the securities covered by this prospectus supplement or this offering is terminated; provided, however, that we are not incorporating, in each case, any portions of documents or information furnished or deemed to have been furnished and not filed in accordance with SEC rules:

- Our Annual Report on Form 10-K for the year ended December 31, 2018 filed with the SEC on February 26, 2019;
- The portions of our Definitive Proxy Statement on Schedule 14A filed with the SEC on March 22, 2019, that are incorporated by reference into our Annual Report on Form 10-K for the fiscal year ended December 31, 2018;
- Our Current Reports on Form 8-K filed with the SEC on October 23, 2018, February 19, 2019 (Item 8.01 only) and March 29, 2019, and our Current Report on Form 8-K/A filed with the SEC on April 15, 2019; and
- The description of our common stock set forth in our Registration Statement on Form 8-A, including any amendments or reports filed for the purpose of updating such description.

These documents contain important business and financial information about us that is not included in or delivered with this prospectus supplement. You may request a copy of any or all documents that we incorporate by reference at no cost, by writing or telephoning us at:

Aqua America, Inc.
762 W. Lancaster Avenue
Bryn Mawr, PA 19010-3489
Telephone: 610-527-8000
Attention: Corporate Secretary

We have not, and the underwriters have not, authorized anyone to provide you with any information other than that contained or incorporated by reference in this prospectus supplement, the accompanying prospectus or in any free writing prospectus we may provide to you in connection with this offering. Neither we nor the underwriters take any responsibility for, or provide any assurances as to the reliability of, any additional or different information that others may give you. You should assume that the information contained in this prospectus supplement, the accompanying prospectus and any free writing prospectus we may provide to you in connection with this offering is accurate only as of their respective dates or as of the respective dates specified in such information, as applicable, and the information contained in documents incorporated by reference is accurate only as of the respective dates of those documents or as of the respective dates specified in such information, as applicable, in each case regardless of the time of delivery of this prospectus supplement or the accompanying prospectus or any such free writing prospectus or any sale of our common stock. Our business, financial condition, results of operations and prospects may have changed since those dates.

Any statement contained herein or in a document incorporated or deemed to be incorporated by reference herein shall be deemed to be modified or superseded for purposes of this prospectus supplement to the extent that a statement contained herein, in any other subsequently filed document which also is or is deemed to be incorporated by reference herein or in the accompanying prospectus, modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified and superseded, to constitute a part of this prospectus supplement.

PROSPECTUS

AQUA AMERICA, INC.

Common Stock
Preferred Stock
Common Stock Purchase Contracts
Warrants
Units
Depositary Shares
Debt Securities

Aqua America, Inc. may, from time to time, in one or more offerings, offer and sell common stock, preferred stock, common stock purchase contracts, warrants, units, depositary shares and debt securities. The debt securities and preferred stock may be convertible into or exchangeable or exercisable for other securities. We will provide specific terms of any offering and the offered securities in supplements to this prospectus. The prospectus supplements may also add, update or change information contained in this prospectus.

We may offer and sell these securities to or through underwriters, dealers or agents, directly to purchasers or through a combination of these methods. If an offering of securities involves any underwriters, dealers or agents, then the names of the underwriters, dealers or agents and the terms of the arrangements with such entities will be stated in an accompanying prospectus supplement.

Our common stock is listed on the New York Stock Exchange under the symbol "WTR." We have not yet determined whether any of the other securities that may be offered by this prospectus will be listed on any exchange, inter-dealer quotation system or over-the-counter market. If we decide to seek listing of any such securities upon issuance, an accompanying prospectus supplement will disclose the exchange, quotation system or market on which the securities will be listed.

The prospectus may not be used to sell our securities unless it is accompanied by a prospectus supplement.

Investing in our securities involves risk. Before you invest, you should carefully read and evaluate the risk factors and other information included in this prospectus and any applicable prospectus supplement, including the documents incorporated by reference. See "Risk Factors" beginning on page 8 of this prospectus.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is February 28, 2018.

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ABOUT THIS PROSPECTUS

This document is called a prospectus and is part of a registration statement that we filed with the Securities and Exchange Commission (SEC) using a "shelf" registration process. Under this shelf process, we may, from time to time, in one or more offering, offer and sell common stock, preferred stock, common stock purchase contracts, warrants, units, depositary shares and debt securities. This prospectus provides you with a general description of the securities we may offer. Each time we sell any securities under this prospectus, we will provide a prospectus supplement that will contain specific information about the terms of that offering and the offered securities. That prospectus supplement may include a discussion of any risk factors or other special considerations applicable to those securities. The prospectus supplement also may add, update or change information contained in this prospectus. You should read both this prospectus and the applicable prospectus supplement and the exhibits filed with our registration statement together with the additional information described below under the heading "Where You Can Find More Information" before you decide whether to invest in the securities.

The registration statement (including the exhibits) of which this prospectus is a part contains additional information about us and the securities we may offer by this prospectus. Specifically, we have filed certain legal documents that control the terms of the securities offered by this prospectus as exhibits to the registration statement. We will file certain other legal documents that will control the terms of the securities we may offer by this prospectus as exhibits to the registration statement or to reports we file with the SEC. The registration statement and the reports can be read at the SEC website or at the SEC offices mentioned under the heading "Where You Can Find More Information."

You should rely only upon the information contained in, or incorporated by reference into, this prospectus and the applicable prospectus supplement that contains specific information about the securities we are offering. We have not authorized any other person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should assume that the information appearing in this document is accurate only as of the date on the front cover of this document. Our business, financial condition, results of operations and prospects may have changed since that date.

Except as otherwise provided in this prospectus, unless the context otherwise requires, references in this prospectus to "Aqua America," "we," "us" or "our" refer to Aqua America, Inc. and its direct and indirect subsidiaries. In addition, references to "Aqua Pennsylvania" refer to our wholly-owned subsidiary, Aqua Pennsylvania, Inc., and its subsidiaries.

FORWARD-LOOKING STATEMENTS

Certain statements in this prospectus, or incorporated by reference into this prospectus, are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 and are made based upon, among other things, our current assumptions, expectations, plans, and beliefs concerning future events and their potential effect on us. These forward-looking statements involve risks, uncertainties and other factors, many of which are outside our control, that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. In some cases you can identify forward- looking statements where statements are preceded by, followed by, or include the words "believes," "expects," "anticipates," "plans," "future," "potential," "probably," "predictions," "intends," "will," "continue" or the negative of such terms or similar expressions. Forward-looking statements in this prospectus, or incorporated by reference into this prospectus, include, but are not limited to, statements regarding:

- recovery of capital expenditures and expenses in rates;
- projected capital expenditures and related funding requirements;
- our capability to pursue timely rate increase requests;
- the availability and cost of capital financing;
- developments, trends and consolidation in the water and wastewater utility and infrastructure industries;
- dividend payment projections;
- opportunities for future acquisitions, both within and outside the water and wastewater industry, the success of pending acquisitions and the impact of future acquisitions;
- the capacity of our water supplies, water facilities and wastewater facilities;
- the impact of federal and/or state tax laws or policies and the regulatory treatment of the effects of those laws or policies, including the Tax Cuts and Jobs Act;
- the impact of geographic diversity on our exposure to unusual weather;
- the impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer;
- our authority to carry on our business without unduly burdensome restrictions;
- the continuation of investments in strategic ventures;
- our ability to obtain fair market value for condemned assets;
- the impact of fines and penalties;
- the impact of changes in and compliance with governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- the impact of decisions of governmental and regulatory bodies, including decisions to raise or lower rates;
- the development of new services and technologies by us or our competitors;
- the availability of qualified personnel;
- the condition of our assets;
- the impact of legal proceedings;
- general economic conditions;
- acquisition-related costs and synergies;

- the sale of water and wastewater divisions; and
- the amount of income tax deductions for qualifying utility asset improvements and the Internal Revenue Service's ultimate acceptance of the deduction methodology.

Because forward-looking statements involve risks and uncertainties, there are important factors that could cause actual results to differ materially from those expressed or implied by these forward-looking statements, including but not limited to:

- changes in general economic, business, credit and financial market conditions;
- changes in governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- the profitability of future acquisitions;
- changes to the rules or our assumptions underlying our determination of what qualifies for an income tax deduction for qualifying utility asset improvements;
- the decisions of governmental and regulatory bodies, including decisions on rate increase requests;
- our ability to file rate cases on a timely basis to minimize regulatory lag;
- abnormal weather conditions, including those that result in water use restrictions;
- changes in, or unanticipated, capital requirements;
- changes in our credit rating or the market price of our common stock;
- changes in valuation of strategic ventures;
- our ability to integrate businesses, technologies or services which we may acquire;
- our ability to manage the expansion of our business;
- our ability to treat and supply water or collect and treat wastewater;
- the extent to which we are able to develop and market new and improved services;
- the effect of the loss of major customers;
- our ability to retain the services of key personnel and to hire qualified personnel as we expand;
- labor disputes;
- increasing difficulties in obtaining insurance and increased cost of insurance;
- cost overruns relating to improvements to, or the expansion of, our operations;
- increases in the costs of goods and services;

- civil disturbance or terroristic threats or acts;
- the continuous and reliable operation of our information technology systems, including the impact of cyber security attacks or other cyber-related events;
- changes in accounting pronouncements;
- litigation and claims; and
- changes in environmental conditions, including the effects of climate change.

Given these risks and uncertainties, you should not place undue reliance on any forward-looking statements. You should read this prospectus and the documents that we incorporate by reference into this prospectus completely and with the understanding that our actual future results, performance and achievements may be materially different from what we expect. These forward-looking statements represent assumptions, expectations, plans and beliefs only as of the date of this prospectus. Except for our ongoing obligations to disclose certain information under the federal securities laws, we are not obligated, and assume no obligation, to update these forward-looking statements, even though our situation may change in the future. For further information or other factors which could affect our financial results and such forward-looking statements, see “Risk Factors.” We qualify all of our forward-looking statements by these cautionary statements.

AQUA AMERICA, INC.

Aqua America, Inc. is the holding company for regulated utilities providing water or wastewater services to an estimated three million people in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana, and Virginia. Our largest operating subsidiary is Aqua Pennsylvania, Inc., which accounted for approximately 52% of our operating revenues and approximately 74% of our net income for 2017. As of December 31, 2017, Aqua Pennsylvania provided water or wastewater services to approximately one-half of the total number of people we serve. Aqua Pennsylvania's service territory is located in the suburban areas in counties north and west of the City of Philadelphia and in 27 other counties in Pennsylvania. Our other regulated utility subsidiaries provide similar services in seven other states. In addition, the Company's market-based activities are conducted through Aqua Infrastructure, LLC and Aqua Resources Inc. Aqua Infrastructure provides non- utility raw water supply services for firms in the natural gas drilling industry. Aqua Resources provides water and wastewater service through two operating and maintenance contracts with municipal authorities close to our utility companies' service territory; and offers, through a third party, water and wastewater line repair service and protection solutions to households. In 2017, we completed the sale of business units that are reported within Aqua Resources, which installed and tested devices that prevent the contamination of potable water and repaired water and wastewater systems, and repaired and performed maintenance on water and wastewater systems. Additionally, during 2016, we completed the sale of business units within Aqua Resources, which provided liquid waste hauling and disposal services and inspection, and cleaning and repair of storm and sanitary wastewater lines.

Aqua America, which prior to its name change in 2004 was known as Philadelphia Suburban Corporation, was formed in 1968 as a holding company for its primary subsidiary, Aqua Pennsylvania, formerly known as Philadelphia Suburban Water Company. In the early 1990s, we embarked on a growth through acquisition strategy focused on water and wastewater operations. Our most significant transactions to date have been the merger with Consumers Water Company in 1999, the acquisition of the regulated water and wastewater operations of AquaSource, Inc. in 2003, the acquisition of Heater Utilities, Inc. in 2004, and the acquisition of American Water Works Company, Inc.'s regulated water and wastewater operations in Ohio in 2012. Since the early 1990s, our business strategy has been primarily directed toward the regulated water and wastewater utility industry, where we have more than quadrupled the number of regulated customers we serve, and have extended our regulated operations from southeastern Pennsylvania to include our current regulated utility operations throughout Pennsylvania and in seven other states. During 2010 through 2013, we sold our utility operations in six states, pursuant to a portfolio rationalization strategy to focus our operations in areas where we have critical mass and economic growth potential. Currently, the Company seeks to acquire businesses in the U.S. regulated sector, which includes water and wastewater utilities and other regulated utilities, and to pursue growth ventures in market-based activities, such as infrastructure opportunities that are supplementary and complementary to our regulated businesses.

Our growth in revenues over the past five years is primarily a result of increases in water and wastewater rates and customer growth. The increase in our utility customer base has been due to customers added through acquisitions, partnerships with developers, and organic growth (excluding dispositions) as shown below:

Year	Utility Customer Growth Rate
2017	1.1%
2016	1.6%
2015	1.9%
2014	1.3%
2013	1.3%

In 2017, our customer count increased by 10,584 customers, primarily due to utility systems that we acquired and organic growth. Overall, for the five-year period of 2013 through 2017, our utility customer base, adjusted to exclude customers associated with utility system dispositions, increased at an annual compound rate of 1.4%. During the five-year period ended December 31, 2017, our utility customer base including customers associated with utility system acquisitions and dispositions increased from 968,357 at January 1, 2013 to 982,849 at December 31, 2017. This five-year period includes the impact of the condemnation of our Fort Wayne, IN system in 2014, which resulted in the loss of approximately 13,000 connections.

Our principal executive office is located at 762 W. Lancaster Avenue, Bryn Mawr, Pennsylvania 19010- 3489, and our telephone number is 610-527-8000. Our website may be accessed at www.aquaamerica.com. The references to our website and the SEC's website are intended to be inactive textual references only, and the contents of those websites are not incorporated by reference herein and should not be considered part of this prospectus.

RISK FACTORS

Investing in our securities involves risks. Please see the risk factors described under the section captioned "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2017, as such risk factors may be updated from time to time in filings we make with the SEC subsequent to the date hereof. Before making an investment decision, you should carefully consider these risk factors, together with all other information contained in or incorporated by reference into this prospectus or any applicable prospectus supplement (which includes information contained in certain filings we make with the SEC subsequent to the date hereof as set forth in the section below captioned "Where You Can Find More Information"). Please also refer to the section above captioned "Forward-Looking Statements."

USE OF PROCEEDS

Unless we otherwise specify in the applicable prospectus supplement, we intend to use the net proceeds from the sale of the securities we may offer by this prospectus to fund our capital expenditures, to provide capital for our growth strategy, which includes potential future acquisitions of municipally owned and investor- owned water and wastewater systems, regulated utilities and infrastructure projects, and market-based activities complementary to our regulated business, to fund the integration of any businesses that we acquire into our existing business, and to purchase and maintain plant equipment, as well as for working capital and other general corporate purposes. Our management will have broad discretion in the allocation of net proceeds from the sale of any securities sold by us.

CERTAIN RATIOS

Our ratio of earnings to fixed charges and ratio of earnings to combined fixed charges and preferred stock dividends for the periods indicated below were as follows:

	Year Ended December 31,				
	2017	**2016**	**2015**	**2014**	**2013**
Ratio of earnings to fixed charges	3.90	4.17	4.15	4.05	3.79
Ratio of earnings to combined fixed charges and preferred stock dividends	3.90	4.17	4.15	4.05	3.79

The ratios of earnings to fixed charges and the ratios of earnings to combined fixed charges and preferred stock dividends were computed by dividing our earnings by fixed charges and by combined fixed charges and preferred stock dividends, respectively. For the purpose of these computations, earnings include the sum of income from continuing operations before income taxes and non-controlling interest, and fixed charges, less

capitalized interest. Fixed charges consist of interest on all indebtedness, whether expensed or capitalized, amortization of debt expense, and the estimated interest attributable to rental and lease expense calculated using an assumed interest factor of 33% of rental and lease expense.

DESCRIPTION OF CAPITAL STOCK

As of February 13, 2018 our authorized capital stock was 301,770,819 shares, consisting of:

- 300,000,000 shares of common stock, par value $0.50 per share, of which 177,750,505 shares were outstanding; and
- 1,770,819 shares of preferred stock, par value $1.00 per share, of which no shares were outstanding.

The following summary of certain terms of our common stock and preferred stock is qualified in its entirety by the provisions of our articles of incorporation and bylaws each of which is incorporated by reference as an exhibit to the registration statement of which this prospectus constitutes a part.

Common Stock

This section describes the general terms of our common stock. For more detailed information, you should refer to our articles of incorporation and bylaws, including any amendments thereto, copies of which have been filed with the SEC. These documents are incorporated by reference into this prospectus.

Voting Rights

Holders of our common stock are entitled to one vote for each share held by them at all meetings of the shareholders and are not entitled to cumulate their votes for the election of directors.

Dividend Rights and Limitations

Holders of our common stock may receive dividends when declared by our board of directors. Because we are a holding company, the funds we use to pay any dividends on our common stock are derived predominantly from the dividends that we receive from our subsidiaries and the dividends they receive from their subsidiaries. Therefore, our ability to pay dividends to holders of our common stock depends upon our subsidiaries' earnings, financial condition and ability to pay dividends. Most of our subsidiaries are subject to regulation by state utility commissions and the amounts of their earnings and dividends are affected by the manner in which they are regulated. In addition, they are subject to restrictions on the payment of dividends contained in their various debt agreements. Under our most restrictive debt agreements, the amount available for payment of dividends to us as of December 31, 2017 was approximately $1.4 billion of Aqua Pennsylvania's retained earnings and $143 million of the retained earnings of certain other subsidiaries. Payment of dividends on our common stock is also subject to the preferential rights of the holders of any outstanding preferred stock.

Liquidation Rights

In the event that we liquidate, dissolve or wind-up, the holders of our common stock are entitled to share ratably in all of the assets that remain after we pay our liabilities. This right is subject, however, to the prior distribution rights of any outstanding preferred stock.

Preferred Stock

Our board of directors has the authority, from time to time and without further action by our shareholders, to divide our unissued capital stock into one or more classes and one or more series within any class and to

make determinations of the designation and number of shares of any class or series and determinations of the voting rights, preferences, limitations and special rights, if any, of the shares of any class or series. The rights, preferences, limitations and special rights of different classes of capital stock may differ with respect to dividend rates, amounts payable on liquidation, voting rights, conversion rights, redemption provisions, sinking fund provisions and other matters. The rights, preferences, privileges and restrictions of each series may be fixed by the designations of that series set forth in either a restated version of our articles of incorporation or a certificate of designations relating to that series, which will be filed with the SEC as an exhibit to or incorporated by reference in the registration statement of which this prospectus constitutes a part.

The issuance of preferred stock may be perceived by some as possibly having the effect of delaying, deferring or preventing a change of control of us without further action by our shareholders. The issuance of preferred stock with voting and conversion rights may also adversely affect the voting power of the holders of our common stock. In certain circumstances, an issuance of preferred stock could possibly have the effect of decreasing the market price of our common stock.

Whenever preferred stock is to be sold pursuant to this prospectus, we will file a prospectus supplement relating to that sale which will specify:

- the number of shares in the series of preferred stock;
- the designation for the series of preferred stock by number, letter or title that will distinguish the series from any other series of preferred stock;
- the dividend rate, if any, and whether dividends on that series of preferred stock will be cumulative, noncumulative or partially cumulative;
- the voting rights of that series of preferred stock, if any;
- any conversion provisions applicable to that series of preferred stock;
- any redemption or sinking fund provisions applicable to that series of preferred stock;
- any preemptive rights provisions applicable to that series of preferred stock;
- the liquidation preference per share of that series of preferred stock; and
- the terms of any other preferences or rights, if any, applicable to that series of preferred stock.

Anti-Takeover Provisions

Pennsylvania State Law Provisions

Under Section 1712 of the Pennsylvania Business Corporation Law of 1988, as amended (PBCL), which is applicable to us, directors stand in a fiduciary relation to their corporation and, as such, are required to perform their duties in good faith, in a manner they reasonably believe to be in the best interests of the corporation and with such care, including reasonable inquiry, skill and diligence, as a person of ordinary prudence would use under similar circumstances. Under Section 1715 of the PBCL, in discharging their duties, directors may, in considering the best interests of their corporation, consider various constituencies, including, shareholders, employees, suppliers, customers and creditors of the corporation, and upon communities in which offices or other establishments of the corporation are located. Directors are not required to give prominent consideration to the interests of any particular constituency. Absent a breach of fiduciary duty, a lack of good faith or self-dealing, any act of the board of directors,

a committee thereof or an individual director is presumed to be in the best interests of the corporation. Actions by directors relating to an acquisition or potential acquisition of control of the corporation are not subject to any greater obligation to justify, or higher burden of proof, than is applied to any other acts of directors. The PBCL expressly provides that the fiduciary duty of directors does not require them to (i) redeem or otherwise render inapplicable outstanding rights issued under any shareholder rights plan; (ii) render inapplicable the anti-takeover statutes set forth in Chapter 25 of the PBCL (described below); or (iii) take any action solely because of the effect it may have on a proposed acquisition or the consideration to be received by shareholders in such a transaction. In addition, Section 2513 of the PBCL specifically validates shareholder rights plans, or "poison pills," and the discriminatory dilution provisions contained in such plans.

Chapter 25 of the PBCL contains several anti-takeover statutes applicable to publicly-traded corporations. Corporations may opt-out of such anti-takeover statutes under certain circumstances. We have not opted-out of any of such statutes.

Section 2538 of Subchapter 25D of the PBCL requires certain transactions with an "interested shareholder" to be approved by a majority of disinterested shareholders. "Interested shareholder" is defined broadly to include any shareholder who is a party to the transaction or who is treated differently than other shareholders and affiliates of the interested shareholder.

Subchapter 25E of the PBCL requires a person or group of persons acting in concert which acquires 20% or more of the voting shares of the corporation to offer to purchase the shares of any other shareholder at "fair value." "Fair value" means the value not less than the highest price paid per share by the controlling person or group during the 90-day period prior to the control transaction, plus a control premium. Among other exceptions, Subchapter 25E does not apply to shares acquired directly from the corporation in a transaction exempt from the registration requirements of the Securities Act of 1933, or to a one-step merger.

Subchapter 25F of the PBCL generally establishes a 5-year moratorium on a "business combination" with an "interested shareholder." "Interested shareholder" is defined generally to be any beneficial owner of 20% or more of the corporation's voting stock or an affiliate or associate of the corporation that at any time within the prior five-year period was a beneficial owner of 20% or more of the corporation's voting stock. "Business combination" is defined broadly to include mergers, consolidations, asset sales and certain self-dealing transactions. Certain restrictions apply to business combination following the 5-year period. Among other exceptions, Subchapter 25F will be rendered inapplicable if the board of directors approves the proposed business combination, or approves the interested shareholder's acquisition of 20% of the voting shares, in either case prior to the date on which the shareholder first becomes an interested shareholder.

Subchapter 25G of the PBCL provides that "control shares" lose voting rights unless such rights are restored by the affirmative vote of a majority of (i) the disinterested shares (generally, shares held by persons other than the acquiror, executive officers of the corporation and certain employee stock plans) and (ii) the outstanding voting shares of the corporation. "Control shares" are defined as shares which, upon acquisition, will result in a person or group acquiring for the first time voting control over (a) 20%, (b) 33 1/3% or (c) 50% or more of the outstanding shares, together with shares acquired within 180 days of attaining the applicable threshold and shares purchased with the intention of attaining such threshold. A corporation may redeem control shares if the acquiring person does not request restoration of voting rights as permitted by Subchapter 25G. Among other exceptions, Subchapter 25G does not apply to a merger, consolidation or a share exchange if the corporation is a party to the transaction agreement.

Subchapter 25H of the PBCL provides in certain circumstances for the recovery by the corporation of profits realized from the sale of its stock by a controlling person or group if the sale occurs within 18 months after the controlling person or group became a controlling person or group, and the stock was acquired during such month period or within 24 months before such period. A controlling person or group is a person or group that

has acquired, offered to acquire, or publicly disclosed an intention to acquire 20% or more of the voting shares of the corporation or a person or group that has otherwise publicly disclosed or caused to be disclosed that it may seek to acquire control of the corporation through any means. Among other exceptions, Subchapter 25H does not apply to transactions approved by both the board of directors and the shareholders prior to the acquisition or distribution, as appropriate.

Subchapter 25I of the PBCL mandates severance compensation for eligible employees who are terminated within 24 months after the approval of a control-share acquisition. Eligible employees generally are all employees employed in Pennsylvania for at least two years prior to the control-share approval. Severance equals the weekly compensation of the employee multiplied by the employee's years of service (up to 26 years), less payments made due to the termination.

Subchapter 25J of the PBCL requires the continuation of certain labor contracts relating to business operations owned at the time of a control-share approval.

Articles of Incorporation and Bylaw Provisions

Certain provisions of our articles of incorporation and bylaws may have the effect of discouraging unilateral tender offers or other attempts to take over and acquire our business. These provisions might discourage some potentially interested purchaser from attempting a unilateral takeover bid for us on terms which some shareholders might favor. Our articles of incorporation require that certain fundamental transactions must be approved by the holders of 75% of the outstanding shares of our capital stock entitled to vote on the matter unless at least a majority of the members of the board of directors has approved the transaction, in which case the required shareholder approval will be the minimum approval required by applicable law. The fundamental transactions that are subject to this provision are those transactions that require approval by shareholders under applicable law or the articles of incorporation. These transactions include certain amendments of our articles of incorporation or bylaws, certain sales or other dispositions of our assets, certain issuances of our capital stock, or certain transactions involving our merger, consolidation, division, reorganization, dissolution, liquidation or winding up. Our articles of incorporation and bylaws provide that:

- a special meeting of shareholders may only be called by the chairman, the president, the board of directors or shareholders entitled to cast a majority of the votes which all shareholders are entitled to cast at the particular meeting;

- nominations for election of directors may be made by any shareholder entitled to vote for election of directors if the name of the nominee and certain information relating to the nominee is filed with our corporate secretary not less than 14 days nor more than 50 days before any meeting of shareholders to elect directors; and

- certain advance notice procedures must be met for shareholder proposals to be made at annual meetings of shareholders. These advance notice procedures generally require a notice to be delivered not less than 90 days nor more than 120 days before the anniversary date of the immediately preceding annual meeting of shareholders.

Transfer Agent and Registrar

The transfer agent and registrar for our common stock is Computershare Trust Company, N.A.

DESCRIPTION OF COMMON STOCK PURCHASE CONTRACTS

We may issue stock purchase contracts, representing contracts entitling or obligating holders to purchase from us, and us to sell to the holders, a specified number of shares or amount of common stock at a future date or dates. The price per share of common stock may be fixed at the time each contract is issued or may be determined by reference to a specific formula set forth in the contract. Each common stock purchase contract may be issued separately or as a part of a unit, each consisting of a common stock purchase contract and, as security for the holder's obligation to purchase the common stock under the contract, the following:

- our senior debt securities or subordinated debt securities described under "Description of Debt Securities;"
- debt obligations of third parties, including U.S. Treasury securities;
- any other asset as security described in the applicable prospectus supplement; or
- any combination of the foregoing.

Each common stock purchase contract may require us to make periodic payments to the holder of the unit or vice versa, and such payments may be unsecured or prefunded on some basis discussed in the applicable prospectus supplement. Each common stock purchase contract may require holders to secure their obligations thereunder in a specified manner and, in certain circumstances, we may deliver a newly issued prepaid common stock purchase contract, which is referred to as a "prepaid security," upon release to a holder of any collateral securing such holder's obligations under the original contract.

The applicable prospectus supplement will describe the terms of any common stock purchase contract and, if applicable, prepaid security. The description in the prospectus supplement will not purport to be complete
and will be qualified in its entirety by reference to the contracts, the collateral arrangements and depositary arrangements, if applicable, relating to such contracts and, if applicable, the prepaid securities and the documents pursuant to which such prepaid securities will be issued. The applicable prospectus supplement will also describe the material United States federal income tax considerations applicable to the common stock purchase contracts.

DESCRIPTION OF WARRANTS

General

The following summary of certain provisions of the warrants does not purport to be complete and is subject to, and qualified in its entirety by reference to, the provisions of the warrant agreement that will be filed with the SEC in connection with the offering of such warrants.

We may issue warrants for the purchase of debt securities, preferred stock or common stock. Warrants may be issued independently or together with debt securities, preferred stock or common stock offered by any prospectus supplement and may be attached to or separate from any such offered securities. Each series of warrants will be issued under a separate warrant agreement to be entered into between the Company and a bank or trust company, as warrant agent. The warrant agent will act solely as the Company's agent in connection with the warrants and will not assume any obligation or relationship of agency or trust for or with any holders or beneficial owners of warrants.

Debt Warrants

The prospectus supplement relating to a particular issue of debt warrants will describe the terms of such debt warrants, including the following: (a) the title of such debt warrants; (b) the offering price for such debt warrants, if any; (c) the aggregate number of such debt warrants; (d) the designation and terms of the debt securities purchasable upon exercise of such debt warrants; (e) if applicable, the designation and terms of the debt securities with which such debt warrants are issued and the number of such debt warrants issued with each such debt security; (f) if applicable, the date from and after which such debt warrants and any debt securities issued therewith will be separately transferable; (g) the principal amount of debt securities purchasable upon exercise of a debt warrant and the price at which such principal amount of debt securities may be purchased upon exercise (which price may be payable in cash, securities, or other property); (h) the date on which the right to exercise such debt warrants shall commence and the date on which such right shall expire; (i) if applicable, the minimum or maximum amount of such debt warrants that may be exercised at any one time; (j) whether the debt warrants represented by the debt warrant certificates or debt securities that may be issued upon exercise of the debt warrants will be issued in registered or bearer form; (k) information with respect to book-entry procedures, if any; (1) the currency or currency units in which the offering price, if any, and the exercise price are payable; (m) if applicable, a discussion of material United States federal income tax considerations; (n) the anti-dilution provisions of such debt warrants, if any; (o) the redemption or call provisions, if any, applicable to such debt warrants; (p) any provisions for changes to or adjustments in the exercise price for the debt warrants and (q) any additional terms of such debt warrants, including terms, procedures, and limitations relating to the exchange and exercise of such debt warrants.

Stock Warrants

The prospectus supplement relating to any particular issue of preferred stock warrants or common stock warrants will describe the terms of such warrants, including the following: (a) the title of such warrants; (b) the offering price for such warrants, if any; (c) the aggregate number of such warrants; (d) the designation and terms of the common stock or preferred stock purchasable upon exercise of such warrants; (e) if applicable, the designation and terms of the offered securities with which such warrants are issued and the number of such warrants issued with each such offered security; (f) if applicable, the date from and after which such warrants and any offered securities issued therewith will be separately transferable; (g) the number of shares of common stock or preferred stock purchasable upon exercise of a warrant and the price at which such shares may be purchased upon exercise; (h) the date on which the right to exercise such warrants shall commence and the date on which such right shall expire; (i) if applicable, the minimum or maximum amount of such warrants that may be exercised at any one time; (j) the currency or currency units in which the offering price, if any, and the exercise price are payable, (k) if applicable, a discussion of material United States federal income tax considerations; (l) the anti-dilution provisions of such warrants, if any; (m) the redemption or call provisions, if any, applicable to such warrants; (m) any provisions for changes to or adjustments in the exercise price for the stock warrants and any additional terms of such warrants, including terms, procedures and limitations relating to the exchange and exercise of such warrants.

DESCRIPTION OF UNITS

We may, from time to time, issue units comprised of one or more of the other securities that may be offered under this prospectus, in any combination. Each unit will be issued so that the holder of the unit is also the holder of each security included in the unit. Thus, the holder of a unit will have the rights and obligations of a holder of each included security. The unit agreement under which a unit is issued may provide that the securities included in the unit may not be held or transferred separately at any time, or at any time before a specified date.

The applicable prospectus supplement will describe the terms of any unit. The description in the prospectus supplement will not purport to be complete and will be qualified in its entirety by reference to units, the collateral arrangements and depositary arrangements, if applicable, relating to such units and, if applicable, the prepaid securities and the documents pursuant to which such prepaid securities will be issued. The applicable prospectus supplement will also describe the material United States federal income tax considerations applicable to the units.

DESCRIPTION OF DEPOSITORY SHARES

We may, at our option, offer fractional shares of our preferred stock, rather than whole shares of our preferred stock. In the event we do so, we will issue receipts for depositary shares, each of which will represent a fraction (to be set forth in the prospectus supplement relating to offering of the depositary shares) of a share of the related series of preferred stock.

The shares of our preferred stock represented by depositary shares will be deposited under a deposit agreement between us and a bank or trust company selected by us having its principal office in the United States and that meets certain other requirements. Subject to the terms of the deposit agreement, each owner of a depositary share will be entitled, in proportion to the applicable fraction of a share of preferred stock, represented by the depositary share to all of the rights and preferences of the preferred stock represented by the depositary shares (including dividend, voting, redemption, conversion and liquidation rights).

The above description of depositary shares is only a summary, is not complete and is subject to, and is qualified in its entirety by the description in the applicable prospectus supplement and the provisions of the deposit agreement, which will contain the form of depository receipt. A copy of the deposit agreement will be filed with the SEC as an exhibit to or incorporated by reference in the registration statement of which this prospectus is a part.

DESCRIPTION OF DEBT SECURITIES

Please note that in this section entitled “Description of Debt Securities,” references to “we,” “us,” “ours” or “our” refer only to Aqua America, Inc. and not to its consolidated subsidiaries. Also, in this section, references to “holders” mean those who own debt securities registered in their own names, on the books that we maintain or the trustee maintains for this purpose, and not those who own beneficial interests in debt securities registered in street name or in debt securities issued in book-entry form through one or more depositaries. Owners of beneficial interests in the debt securities should read the section below entitled “Book-Entry Procedures and Settlement.”

General

The debt securities offered by this prospectus will be our unsecured obligations, except as otherwise set forth in an accompanying prospectus supplement, and will be either senior or subordinated debt. We will issue senior debt under a senior debt indenture, and we will issue subordinated debt under a subordinated debt indenture. We sometimes refer to the senior debt indenture and the subordinated debt indenture, individually, as an indenture and, collectively, as the indentures. We have filed forms of the indentures with the SEC as exhibits to the registration statement of which this prospectus forms a part.You can obtain copies of the indentures by following the directions outlined in “Where You Can Find More Information,” or by contacting the applicable indenture trustee.

A form of each debt security, reflecting the particular terms and provisions of a series of offered debt securities, will be filed with the SEC at the time of the offering and incorporated by reference as exhibits to the registration statement of which this prospectus forms a part.

The following briefly summarizes certain material provisions that may be included in the indentures. Other terms, including pricing and related terms, will be disclosed for a particular issuance in an accompanying prospectus supplement. You should read the more detailed provisions of the applicable indenture, including the defined terms, for provisions that may be important to you. You should also read the particular terms of a series of debt securities, which will be described in more detail in an accompanying prospectus supplement. So that you may easily locate the more detailed provisions, the numbers in parentheses below refer to sections in the applicable indenture or, if no indenture is specified, to sections in each of the indentures. Wherever particular sections or defined terms of the applicable indenture are referred to, such sections or defined terms are incorporated into this prospectus by reference, and the statement in this prospectus is qualified by that reference.

The trustee under each indenture will be determined at the time of issuance of debt securities, and the name of the trustee will be provided in an accompanying prospectus supplement.

The indentures provide that our senior or subordinated debt securities may be issued in one or more series, with different terms, in each case as we authorize from time to time. We also have the right to "reopen" a previous issue of a series of debt securities by issuing additional debt securities of such series without the consent of the holders of debt securities of the series being reopened or any other series. Any additional debt securities of the series being reopened will have the same ranking, interest rate, maturity and other terms as the previously issued debt securities of that series. These additional debt securities, together with the previously issued debt securities of that series, will constitute a single series of debt securities under the terms of the applicable indenture.

Types of Debt Securities

We may issue fixed or floating rate debt securities. Fixed rate debt securities will bear interest at a fixed rate described in the prospectus supplement. This type includes zero coupon debt securities, which bear no interest and are often issued at a price lower than the principal amount. United States federal income tax consequences and other special considerations applicable to any debt securities issued at a discount will be described in the applicable prospectus supplement.

Upon the request of the holder of any floating rate debt security, the calculation agent will provide the interest rate then in effect for that debt security, and, if determined, the interest rate that will become effective on the next interest reset date. The calculation agent's determination of any interest rate, and its calculation of the amount of interest for any interest period, will be final and binding in the absence of manifest error.

All percentages resulting from any interest rate calculation relating to a debt security will be rounded upward or downward, as appropriate, to the next higher or lower one hundred-thousandth of a percentage point.

All amounts used in or resulting from any calculation relating to a debt security will be rounded upward or downward, as appropriate, to the nearest cent, in the case of U.S. dollars, or to the nearest corresponding hundredth of a unit, in the case of a currency other than U.S. dollars, with one-half cent or one-half of a corresponding hundredth of a unit or more being rounded upward.

In determining the base rate that applies to a floating rate debt security during a particular interest period, the calculation agent may obtain rate quotes from various banks or dealers active in the relevant market, as described in the prospectus supplement. Those reference banks and dealers may include the calculation agent itself and its affiliates, as well as any underwriter, dealer or agent participating in the distribution of the relevant floating rate debt securities and its affiliates.

Information in the Prospectus Supplement

The prospectus supplement for any offered series of debt securities will describe the following terms, as applicable:

- the title;
- whether the debt is senior or subordinated;
- whether the debt securities are secured or unsecured and, if secured, the collateral securing the debt;
- the total principal amount offered;
- the percentage of the principal amount at which the debt securities will be sold and, if applicable, the method of determining the price;
- the maturity date or dates;
- whether the debt securities are fixed rate debt securities or floating rate debt securities;
- if the debt securities are fixed rate debt securities, the yearly rate at which the debt security will bear interest, if any, and the interest payment dates;
- if the debt security is an original issue discount debtsecurity, the yield to maturity;
- if the debt securities are floating rate debt securities, the interest rate basis; any applicable index currency or maturity, spread or spread multiplier or initial, maximum or minimum rate; the interest reset, determination, calculation and payment dates, and the day count used to calculate interest payments for any period;
- the date or dates from which any interest will accrue, or how such date or dates will be determined, and the interest payment dates and any related record dates;
- if other than in U.S. dollars, the currency or currency unit in which payment will be made;
- the denominations in which the currency or currency unit of the securities will be issuable if other than denominations of $1,000 and integral multiples thereof;
- the terms and conditions on which the debt securities may be redeemed at our option;
- any obligation we may have to redeem, purchase or repay the debt securities at the option of a holder upon the happening of any event and the terms and conditions of redemption, purchase or repayment;
- the names and duties of the trustee and any co-trustees, depositaries, authenticating agents, calculation agents, paying agents, transfer agents or registrars for the debt securities;
- any material provisions of the applicable indenture described in this prospectus that do not apply tothe debt securities;
- a discussion of United States federal income tax, accounting and special considerations, procedures and limitations with respect to the debt securities;

- whether and under what circumstances we will pay additional amounts to holders in respect of any tax assessment or government charge, and, if so, whether we will have the option to redeem the debt securities rather than pay such additional amounts; and

- any other specific terms of the debt securities that are consistent with the provisions of the indenture.

The terms on which a series of debt securities may be convertible into or exchangeable for other of our securities or any other entity will be set forth in the prospectus supplement relating to such series. Such terms will include provisions as to whether conversion or exchange is mandatory, at the option of the holder or at our option. The terms may include provisions pursuant to which the number of other securities to be received by the holders of such series of debt securities may be adjusted.

We will issue the debt securities only in registered form. As currently anticipated, debt securities of a series will trade in book-entry form, and global notes will be issued in physical (paper) form, as described below under "Book-Entry Procedures and Settlement." Unless otherwise provided in the accompanying prospectus supplement, we will issue debt securities denominated in U.S. dollars and only in denominations of $1,000 and integral multiples thereof.

The prospectus supplement relating to offered debt securities denominated in a foreign or composite currency will specify the denomination of the offered debt securities.

The debt securities may be presented for exchange, and debt securities other than a global security may be presented for registration of transfer, at the principal corporate trust office of the trustee named in the applicable prospectus supplement. Holders will not have to pay any service charge for any registration of transfer or exchange of debt securities, but we may require payment of a sum sufficient to cover any tax or other governmental charge payable in connection with such registration of transfer (Section 3.05).

Payment and Paying Agents

Distributions on the debt securities other than those represented by global notes will be made in the designated currency against surrender of the debt securities at the principal corporate trust office of the trustee named in the applicable prospectus supplement. Payment will be made to the registered holder at the close of business on the record date for such payment. Interest payments will be made at the principal corporate trust office of the trustee named in the applicable prospectus supplement, or by a check mailed to the holder at his registered address. Payments in any other manner will be specified in the applicable prospectus supplement.

Calculation Agents

Calculations relating to floating rate debt securities and indexed debt securities will be made by the calculation agent, an institution that we appoint as our agent for this purpose. We may appoint one of our affiliates as calculation agent.We may appoint a different institution to serve as calculation agent from time to time after the original issue date of the debt security without your consent and without notifying you of the change. The initial calculation agent will be identified in the applicable prospectus supplement.

Senior Debt

We may issue senior debt securities under the senior debt indenture. Senior debt will constitute our unsecured and unsubordinated obligations and will rank on a basis equal in priority with all our other unsecured and unsubordinated debt.

Subordinated Debt

We may issue subordinated debt securities under the subordinated debt indenture. Subordinated debt will constitute our unsecured and subordinated obligations and will be junior in right of payment to our senior debt (including senior debt securities), which is defined as "senior indebtedness" in the subordinated debt indenture (Section 16.01).

If we default in the payment of any principal of, or premium, ifany, or interest on any senior debt when it becomes due and payable after any applicable grace period, then, unless and until the default is cured or waived or ceases to exist, we cannot make a payment on account of or redeem or otherwise acquire the subordinated debt securities (Section 16.04).

If there is any insolvency, bankruptcy, liquidation or other similar proceeding relating to us or our property, then all senior debt must be paid in full before any payment may be made to any holders of subordinated debt securities (Section 16.02).

Furthermore, if we default in the payment of the principal of and accrued interest on any subordinated debt securities that is declared due and payable upon an event of default under the subordinated debt indenture, holders of all our senior debt will first be entitled to receive payment in full in cash before holders of such subordinated debt can receive any payments (Section 16.03).

Except as may be otherwise set forth in an accompanying prospectus supplement, senior debt means:

- the principal, premium, if any, and interest in respect of indebtedness for money borrowed and indebtedness evidenced by securities, notes, debentures, bonds or other similar instruments issued, including, as to us, the senior debt securities;
- all capitalized lease obligations;
- all obligations representing the deferred purchase price of property; and
- all deferrals, renewals, extensions and refundings of obligations of the type referred to above (Section 1.01 of Subordinated Indenture).

However, senior debt does not include:

- the subordinated debt securities (Section 16.01 of Subordinated Indenture);
- any indebtedness that by its terms is subordinated to, or ranks in priority on an equal basis with, subordinated debt securities (Section 1.01 of Subordinated Indenture); and
- items of indebtedness (other than capitalized lease obligations) that would not appear as liabilities on a balance sheet prepared in accordance with accounting principles generally accepted in the United States of America.

Covenants

The accompanying prospectus supplement will contain any covenants applicable to the debt securities.

Modification of the Indentures

The indentures will provide that we and the relevant trustee may enter into supplemental indentures to establish the form and terms of any new series of debt securities without obtaining the consent of any holder of debt securities (Section 9.01).

We and the trustee may, with the consent of the holders of at least a majority in aggregate outstanding principal amount of the debt securities of a series, modify the applicable indenture or the rights of the holders of the securities of such series (Section 9.02).

No such modification may, without the consent of each holder of an affected security:

- extend the fixed maturity of any such security;
- reduce the rate or change the time of payment of interest on such security;
- reduce the principal amount of such securities or the premium, if any, on such security;
- change any obligation of ours to pay additional amounts with respect to such security;
- reduce the amount of the principal payable on acceleration of such security if issued originally at a discount;
- adversely affect the right of repayment or repurchase of such security at the option of the holder;
- reduce or postpone any sinking fund or similar provision with respect to such security;
- change the currency or currency unit in which such security is payable or the right of selection thereof;
- impair the right to sue for the enforcement of any payment with respect to such security on or after the maturity of such security;
- reduce the percentage of the aggregate outstanding principal amount of debt securities of the series referred to above whose holders need to consent to the modification or a waiver without the consent of such holders; or
- change any obligation of ours with respect to such security to maintain an office or agency.

Defaults

Except as may be otherwise set forth in an accompanying prospectus supplement, each indenture will provide that events of default regarding any series of debt securities will be:

- our failure to pay for 30 days required interest on any debt security of such series;
- our failure to pay principal or premium, if any, on any debt security of such series when due;
- our failure to make any required scheduled installment payment for 30 days on debt securities of such series;

- our failure to perform for 90 days after notice any other covenant in the relevant indenture otherthan a covenant included in the relevant indenture solely for the benefit of a series of debt securities other than such series; and

- certain events of bankruptcy or insolvency, whether voluntary or not (Section 5.01).

Except as may be otherwise set forth in an accompanying prospectus supplement, if an event of default regarding debt securities of any series issued under the indentures should occur and be continuing, either the trustee or the holders of 25% in the principal amount of outstanding debt securities of such series may declare each debt security of that series due and payable (Section 5.02). We may be required to file annually with the trustee a statement of an officer as to the fulfillment by us of our obligations under the indenture during the preceding year.

No event of default regarding one series of debt securities issued under an indenture is necessarily an event of default regarding any other series of debt securities.

Holders of a majority in aggregate principal amount of the outstanding debt securities of any series will be entitled to control certain actions of the trustee under the indentures and to waive past defaults regarding such series (Sections 5.12 and 5.13). The holders of debt securities generally will not be able to require the trustee to take any action, unless one or more of such holders provides to the trustee reasonable security or indemnity (Section 6.02).

If an event of default occurs and is continuing regarding a series of debt securities, the trustee may use any sums that it holds under the relevant indenture for its own reasonable compensation and expenses incurred prior to paying the holders of debt securities of such series (Section 5.06).

Before any holder of any series of debt securities may institute action for any remedy, except payment on such holder's debt security when due, the holders of not less than 25% in principal amount of the debt securities of that series outstanding must request the trustee to take action. Holders must also offer and give the satisfactory security and indemnity against liabilities incurred by the trustee for taking such action (Section 5.07).

Defeasance

Except as may otherwise be set forth in an accompanying prospectus supplement, after we have deposited with the trustee, cash or government securities, in trust for the benefit of the holders sufficient to pay the principal of, premium, if any, and interest on the debt securities of such series when due, and satisfied certain other conditions, including receipt of an opinion of counsel that holders will not recognize taxable gain or loss for United States federal income tax purposes, then:

- we will be deemed to have paid and satisfied our obligations on all outstanding debt securities of such series, which is known as defeasance and discharge (Section 14.02); or

- we will cease to be under any obligation, other than to pay when due the principal of, premium, if any, and interest on such debt securities, relating to the debt securities of such series, which is known as covenant defeasance (Section 14.03).

When there is a defeasance and discharge, the applicable indenture will no longer govern the debt securities of such series, we will no longer be liable for payments required by the terms of the debt securities of such series and the holders of such debt securities will be entitled only to the deposited funds. When there is a covenant defeasance, however, we will continue to be obligated to make payments when due if the deposited funds are not sufficient.

Governing Law

Unless otherwise stated in the prospectus supplement, the debt securities and the indentures will be governed by Pennsylvania law (Section 1.12).

Concerning the Trustee Under the Indentures

We may have banking and other business relationships with the trustee named in the prospectus supplement, or any subsequent trustee, in the ordinary course of business.

Form, Exchange and Transfer

We will issue debt securities only in registered form; no debt securities will be issued in bearer form (Section 2.03). We will issue each debt security in book-entry form only, unless otherwise specified in the applicable prospectus supplement. We will issue any common stock issuable upon conversion of any debt security being offered in both certificated and book-entry form, unless otherwise specified in the applicable prospectus supplement. Debt securities in book-entry form will be represented by a global security registered in the name of a depositary, which will be the holder of all the debt securities represented by the global security (Section 2.04). Those who own beneficial interests in a global security will do so through participants in the depositary's system, and the rights of these indirect owners will be governed solely by the applicable procedures of the depositary and its participants. Only the depositary will be entitled to transfer or exchange a debt security in global form, since it will be the sole holder of the debt security (Section 3.05). These book-entry securities are described below under "Book-Entry Procedures and Settlement."

If any debt securities are issued in non-global form or cease to be book-entry securities (in the circumstances described in the next section), the following will apply to them:

- The debt securities will be issued in fully registered form in denominations stated in the prospectus supplement. You may exchange debt securities for debt securities of the same series in smaller denominations or combined into fewer debt securities of the same series of larger denominations, as long as the total amount is not changed (Section 3.05).

- You may exchange, transfer, present for payment or exercise debt securities at the office of the relevant trustee or agent indicated in the prospectus supplement (Section 3.05). You may also replace lost, stolen, destroyed or mutilated debt securities at that office. We may appoint another entity to perform these functions or may perform them (Section 3.06).

- You will not be required to pay a service charge to transfer or exchange the debt securities, but you may be required to pay any tax or other governmental charge associated with the transfer or exchange (Sections 3.05 and 3.06). The transfer or exchange, and any replacement, will be made only if our transfer agent is satisfied with your proof of legal ownership. The transfer agent may also require an indemnity before replacing any debt securities (Section 3.06).

- If we have the right to redeem, accelerate or settle any debt securities before their maturity or expiration, and we exercise that right as to less than all those debt securities, we may block the transfer or exchange of those debt securities during the period beginning 15 days before the day we mail the notice of exercise and ending on the day of that mailing, in order to freeze the list of holders to prepare the mailing. We may also refuse to register transfers of or exchange any debt security selected for early settlement, except that we will continue to permit transfers and exchanges of the unsettled portion of any debt security being partially settled (Section 3.05).

- If fewer than all of the debt securities represented by a certificate that are payable or exercisable in part are presented for payment or exercise, a new certificate will be issued for the remaining amount of securities (Section 15.02).

Book-Entry Procedures and Settlement

Most offered debt securities will be book-entry (global) securities. Upon issuance, all book-entry securities will be represented by one or more fully registered global securities, without coupons (Section 3.02). Each global security will be deposited with, or on behalf of, The Depository Trust Company, or DTC, a securities depository, and will be registered in the name of DTC or a nominee of DTC (Section 3.01). DTC will thus be the only registered holder of these debt securities.

Purchasers of debt securities may only hold interests in the global notes through DTC if they are participants in the DTC system. Purchasers may also hold interests through a securities intermediary—banks, brokerage houses and other institutions that maintain securities accounts for customers—that has an account with DTC or its nominee. DTC will maintain accounts showing the security holdings of its participants, and these participants will in turn maintain accounts showing the security holdings of their customers. Some of these customers may themselves be securities intermediaries holding securities for their customers. Thus, each beneficial owner of a book-entry security will hold that debt security indirectly through a hierarchy of intermediaries, with DTC at the top and the beneficial owner's own securities intermediary at the bottom.

The debt securities of each beneficial owner of a book-entry security will be evidenced solely by entries on the books of the beneficial owner's securities intermediary. The actual purchaser of the debt securities will generally not be entitled to have the debt securities represented by the global securities registered in its name and will not be considered the owner under the declaration. In most cases, a beneficial owner will also not be able to obtain a paper certificate evidencing the holder's ownership of debt securities. The book-entry system for holding securities eliminates the need for physical movement of certificates and is the system through which most publicly traded common stock is held in the United States. However, the laws of some jurisdictions require some purchasers of securities to take physical delivery of their securities in definitive form. These laws may impair the ability to transfer book-entry securities.

A beneficial owner of book-entry securities represented by a global security may exchange the securities for definitive (paper) securities only if:

- DTC is unwilling or unable to continue as depositary for such global security and we do not appoint a qualified replacement for DTC within 90 days; or

- We in our sole discretion decide to allow some or all book-entry securities to be exchangeable for definitive securities in registered form (Section 3.05).

Unless we indicate otherwise, any global security that is exchangeable will be exchangeable in whole for definitive securities in registered form, with the same terms and of an equal aggregate principal amount. Definitive securities will be registered in the name or names of the person or persons specified by DTC in a written instruction to the registrar of the securities (Section 3.05). DTC may base its written instruction upon directions that it receives from its participants.

In this prospectus, for book-entry securities, references to actions taken by security holders will mean actions taken by DTC upon instructions from its participants, and references to payments and notices of redemption to security holders will mean payments and notices of redemption to DTC as the registered holder of the securities for distribution to participants in accordance with DTC's procedures.

DTC is a limited purpose trust company organized under the laws of the State of New York, a member of the Federal Reserve System, a clearing corporation within the meaning of the New York Uniform Commercial Code and a clearing agency registered under section 17A of the Securities Exchange Act of 1934. The rules applicable to DTC and its participants are on file with the SEC.

We will not have any responsibility or liability for any aspect of the records relating to, or payments made on account of, beneficial ownership interest in the book-entry securities or for maintaining, supervising or reviewing any records relating to the beneficial ownership interests.

PLAN OF DISTRIBUTION

We may sell any of the securities being offered by this prospectus separately or together:

- through agents;
- to or through underwriters who may act directly or through a syndicate represented by one or more managing underwriters;
- through dealers;
- through a block trade in which the broker or dealer engaged to handle the block trade will attempt to sell the securities as agent, but may position and resell a portion of the block as principal to facilitate the transaction;
- through "at the market" offerings, within the meaning of Rule 415(a)(4) of the Securities Act of 1933, to or through a market maker or into an existing trading market on an exchange or otherwise;
- in exchange for our outstanding indebtedness;
- directly to purchasers, through a specific bidding, auction or other process; or
- through a combination of any of these methods of sale.

If the securities offered under this prospectus are issued in exchange for our outstanding securities, the applicable prospectus supplement will describe the terms of the exchange, and the identity and the terms of sale of the securities offered under this prospectus by the selling security holders.

The distribution of securities may be effected from time to time in one or more transactions at a fixed price or prices that may be changed, at market prices prevailing at the time of sale or prices related to prevailing market prices or at negotiated prices.

Agents designated by us from time to time may solicit offers to purchase the securities. We will name any agent involved in the offer or sale of the securities and set forth any commissions payable by us to an agent in the prospectus supplement for that transaction. Unless otherwise indicated in the prospectus supplement, any agent will be acting on a best efforts basis for the period of its appointment. Any agent may be deemed to be an "underwriter" of the securities as that term is defined in the Securities Act of 1933.

If we utilize an underwriter or underwriters in the sale of securities, we will execute an underwriting agreement with the underwriter or underwriters at the time we reach an agreement for sale. We will set forth in the prospectus supplement the names of the specific managing underwriter or underwriters, as well as any other underwriters, and the terms of the transactions, including compensation of the underwriters and dealers. This compensation may be in the form of discounts, concessions or commissions. Underwriters and others participating in any offering of securities may engage in transactions that stabilize, maintain or otherwise affect the price of securities. We will describe any of these activities in the prospectus supplement.

If a dealer is utilized in the sale of the securities, we or an underwriter will sell securities to the dealer, as principal. The dealer may then resell the securities to the public at varying prices to be determined by the dealer at the time of resale. The prospectus supplement will set forth the name of the dealer and the terms of the transactions.

We may directly solicit offers to purchase the securities, and we may sell directly to institutional investors or others. These persons may be deemed to be underwriters within the meaning of the Securities Act of 1933 with respect to any resale of the securities. The prospectus supplement will describe the terms of any direct sales, including the terms of any bidding or auction process, if utilized.

Agreements we enter into with agents, underwriters and dealers may entitle them to indemnification by us against specified liabilities, including liabilities under the Securities Act of 1933, or to contribution by us to payments they may be required to make in respect of these liabilities. The prospectus supplement will describe the terms and conditions of indemnification or contribution.

Certain of the agents, underwriters and dealers that we sell the securities offered under this prospectus to or through, and certain of their affiliates, engage in transactions with and perform services for us in the ordinary course of business. We may enter into hedging transactions in connection with any particular issue of the securities offered under this prospectus, including forwards, futures, options, interest rate or exchange rate swaps and repurchase or reverse repurchase transactions with, or arranged by, the applicable agent, underwriter or dealer, an affiliate of that agent, underwriter or dealer or an unrelated entity. We, the applicable agent, underwriter or dealer or other parties may receive compensation, trading gain or other benefits in connection with these transactions. We are not required to engage in any of these transactions. If we commence these transactions, we may discontinue them at any time. Counterparties to these hedging activities also may engage in market transactions involving the securities offered under this prospectus.

No securities may be sold under this prospectus without delivery (in paper format, in electronic format, in electronic format on the Internet, or by other means) of the applicable prospectus supplement describing the method and terms of the offering.

LEGAL MATTERS

Unless otherwise indicated in the applicable prospectus supplement, the validity of the securities that may be offered hereby will be passed upon for us by Ballard Spahr LLP, Philadelphia, Pennsylvania. If legal matters in connection with the offering made by this prospectus are passed on by counsel for the underwriters, dealers or agents, if any, that counsel will be named in the applicable prospectus supplement.

EXPERTS

The financial statements and management's assessment of the effectiveness of internal control over financial reporting (which is included in Management's Report on Internal Control over Financial Reporting) incorporated in this Prospectus by reference to the Annual Report on Form 10-K for the year ended December 31, 2017, have been so incorporated in reliance on the report of PricewaterhouseCoopers LLP, an independent registered public accounting firm, given on the authority of said firm as experts in auditing and accounting.

WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the SEC. You may read and copy any document we file at the SEC's Public Reference Room at 100 F Street N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the Public Reference Room. You may also obtain our SEC filings from the SEC's website at www.sec.gov or from our website at http:// ir.aquaamerica.com/.

We have filed with the SEC a "shelf" registration statement on Form S-3 under the Securities Act of 1933 relating to the securities that may be offered by this prospectus. This prospectus is a part of that registration statement, but does not contain all of the information in the registration statement. We have omitted certain parts of the registration statement in accordance with rules and regulations of the SEC. Statements made in this prospectus as to the contents of any contract, agreement or other documents are not necessarily complete, and, in each instance, we refer you to a copy of such document filed as an exhibit to the registration statement, of which this prospectus is a part, or otherwise filed with the SEC. For more detail about us and any securities that may be offered by this prospectus, you may examine the registration statement on Form S-3 and the exhibits filed with it at the locations listed in the previous paragraph.

The SEC allows us to "incorporate by reference" the information we file with them, which means that we can disclose important information to you by referring you to those documents. The information incorporated by reference is considered to be part of this prospectus. When we file information with the SEC in the future, that information will automatically update and supersede this information. We incorporate by reference the documents listed below and any future filings we will make with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934 until we sell all of the securities covered by this prospectus; provided, however, that we are not incorporating, in each case, any documents or information deemed to have been furnished and not filed in accordance with SEC rules:

- Our Annual Report on Form 10-K for the year ended December 31, 2017 filed with the SEC on February 28, 2018; and
- The description of our common stock set forth in our Registration Statement on Form 8-A, including any amendments or reports filed for the purpose of updating such description.

These documents contain important business and financial information about us that is not included in or delivered with this prospectus. You may request a copy of any or all documents that we incorporate by reference at no cost, by writing or telephoning us at:

Aqua America, Inc.
762 W. Lancaster Avenue
Bryn Mawr, PA 19010-3489
Telephone: 610-527-8000
Attention: Corporate Secretary

You should rely only on the information contained in or incorporated by reference in this prospectus and any supplements to this prospectus.We have not authorized anyone to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. You should not assume that the information provided in this prospectus or incorporated by reference in this prospectus is accurate as of any date other than the date on the front of this prospectus or the date of those documents. Our business, financial condition, results of operations and prospects may have changed since those dates.

If you find inconsistencies between the documents, or between the documents and this prospectus or the applicable prospectus supplement, you should rely on the most recent document, prospectus or prospectus supplement.

32,495,667 Shares

AQUA AMERICA, INC.

Common Stock

PROSPECTUS SUPPLEMENT

Joint Bookrunners

Goldman Sachs & Co. LLC | **RBC Capital Markets**
BofA Merrill Lynch | **Morgan Stanley** | **Wells Fargo Securities**

Co-Managers

PNC Capital Markets LLC | **Barclays** | **Citizens Capital Markets** | **Huntington Capital Markets**
MUFG | **J.P. Morgan** | **TD Securities** | **Baird**
Boenning & Scattergood | **Janney Montgomery Scott** | **HSBC**

April 17, 2019

Filed Pursuant to Rule 424(b)(5)
Registration No. 333-223306

Title of Each Class of Securities to be Registered	Amount to be Registered[(1)]	Maximum Offering Price per Unit	Maximum Aggregate Offering Price[(1)]	Amount of Registration Fee[(2)]
6.00% Tangible Equity Units	13,800,000	$50.00	$690,000,000	$83,628

(1) Assumes full exercise of the underwriters' option to purchase up to an additional 1,800,000 6.00% Tangible Equity Units, solely to cover over-allotments, if any.

(2) Calculated in accordance with Rule 457(r) of the Securities Act of 1933, as amended.

Prospectus Supplement
(To Prospectus dated February 28, 2018)

AQUA AMERICA, INC.

12,000,000 6.00% TANGIBLE EQUITY UNITS

We are offering 12,000,000 6.00% tangible equity units, or "Units." Each Unit has a stated amount of $50.00. Each Unit is comprised of (i) a prepaid stock purchase contract issued by us and (ii) a senior amortizing note due April 30, 2022 issued by us. Each amortizing note will have an initial principal amount of $8.62909 and a final installment payment date of April 30, 2022.

Unless earlier redeemed by us or settled earlier at your option or at our option as described herein, on April 30, 2022 (subject to postponement in certain limited circumstances), each purchase contract will automatically settle, and we will deliver a number of shares of our common stock, par value $0.50 per share, per purchase contract based on the applicable market value (as defined herein) of our common stock as set forth below:

- if the applicable market value is greater than the threshold appreciation price, which is approximately $42.41, you will receive 1.1790 shares per purchase contract;
- if the applicable market value is less than or equal to the threshold appreciation price but greater than or equal to the reference price, which is approximately $34.62, you will receive a number of shares per purchase contract having a value, based on the applicable market value, equal to $50.00, divided by the applicable market value; and
- if the applicable market value is less than the reference price, you will receive 1.4442 shares per purchase contract.

At any time prior to the second scheduled trading day immediately preceding April 30, 2022, you may settle your purchase contracts early, and we will deliver 1.1790 shares of our common stock per purchase contract (subject to adjustment). In addition, if a "fundamental change" (as defined herein) occurs and you elect to settle your purchase contracts early in connection with such fundamental change, you will receive a number of shares of our common stock per purchase contract equal to the fundamental change early settlement rate, as described herein. We may elect to settle all, but not less than all, outstanding purchase contracts on or after January 30, 2020 and prior to April 30, 2022 at the "early mandatory settlement rate" (as defined herein). If the closing of the Acquisition (as defined below) has not occurred on or prior to April 22, 2020, or if, prior to such date, the Acquisition Agreement (as defined herein) is terminated, we may elect to redeem all, but not less than all, outstanding purchase contracts at the "redemption amount" (as defined herein), by delivering notice to all holders during the five business day period immediately following the earlier of (x) April 22, 2020 if the closing of the Acquisition has not occurred on or prior to such date and (y) the date on which the Acquisition Agreement is terminated.

The amortizing notes will pay you equal quarterly cash installments of $0.75000 per amortizing note (except for the July 30, 2019 installment payment, which will be $0.80833 per amortizing note), which cash payment in the aggregate will be equivalent to 6.00% per year with respect to each $50.00 stated amount of Units. The amortizing notes will be our general unsecured senior obligations and will rank equally with all of our other existing and future unsecured senior indebtedness from time to time outstanding. If we elect to redeem the purchase contracts or to settle the purchase contracts early, you will have the right to require us to repurchase your amortizing notes. Other than cash payments in lieu of fractional shares or, under certain circumstances, in the event of an acquisition termination redemption, holders of purchase contracts will not receive any cash distributions.

Our common stock is listed on the New York Stock Exchange ("NYSE") under the symbol "WTR." On April 17, 2019, the last reported sale price of our common stock on the NYSE was $34.82 per share. We have applied to list the Units on the NYSE under the symbol "WTRU," subject to satisfaction of its minimum listing standards with respect to the Units. If the Units are approved for listing, we expect trading on the NYSE to begin within 30 calendar days after the Units are first issued. We will not initially apply to list the separate purchase contracts or the separate amortizing notes on any securities exchange or automated inter-dealer quotation system, but we may apply to list such separate purchase contracts and separate amortizing notes in the future as described herein. Prior to this offering, there has been no public market for the Units.

We intend to use the net proceeds from this offering, together with the net proceeds from the other Financing Transactions (as defined herein), to (1) fund the acquisition (the "Acquisition") of all of the issued and outstanding limited liability company membership interests of LDC Funding LLC ("LDC"), the parent of a group of natural gas public utility companies (collectively with LDC, "Peoples"), (2) complete the Company Debt Refinancing (as defined herein) and (3) pay related costs and expenses. This offering is not conditioned upon the consummation of the Acquisition. If the Acquisition is not consummated, we intend to use the net proceeds from this offering, after payment of any cash redemption amount and/or repurchase price (if applicable), for general corporate purposes, which may include the Company Debt Refinancing, the redemption of securities issued in connection with the other Financing Transactions, repurchases of our common stock, debt repayment, capital expenditures and investments. See "Use of Proceeds."

Concurrently with this offering of Units, we have commenced the Common Stock Offering (as defined herein), which is being made by means of a separate prospectus supplement and not by means of this prospectus supplement. This offering is not conditioned upon the completion of the other Financing Transactions, including the Common Stock Offering. This prospectus supplement is not an offer to sell or a solicitation of an offer to buy any securities offered in any of the other Financing Transactions.

Investing in the Units involves risks. See "Risk Factors" on page S-18 of this prospectus supplement, page 6 of the accompanying prospectus and in

the documents we incorporate by reference in this prospectus supplement and the accompanying prospectus.

	Per Unit	Total[(1)]
Public Offering Price	$ 50.00	$600,000,000
Underwriting Discount	$ 1.125	$ 13,500,000
Proceeds, before expenses, to Aqua America	$ 48.875	$586,500,000

(1) Assumes no exercise of the underwriters' option to purchase additional Units, described below.

We have granted the underwriters an option to purchase, within 13 days beginning on, and including, the date of the initial issuance of the Units, up to an additional 1,800,000 Units at the price to public less the underwriting discount solely to cover over-allotments.

Neither the U.S. Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus supplement or the accompanying prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The underwriters expect to deliver the Units to purchasers on or about April 23, 2019.

Joint Bookrunners

RBC Capital Markets **Goldman Sachs & Co. LLC**

BofA Merrill Lynch **Morgan Stanley** **Wells Fargo Securities**

Co-Managers

PNC Capital Markets LLC **Barclays** **Citizens Capital Markets** **Huntington Capital Markets**

MUFG **J.P. Morgan** **TD Securities** **Baird**

Boenning & Scattergood **Janney Montgomery Scott** **HSBC**

April 17, 2019

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ABOUT THIS PROSPECTUS SUPPLEMENT

Unless otherwise specified or the context requires otherwise, references in this prospectus supplement to (1) "Aqua America," the "Company," "we," "us," "our" and similar references refer to Aqua America, Inc. and its subsidiaries prior to the proposed Acquisition, (2) the "combined company" refers to Aqua America and its subsidiaries after completion of the Acquisition (as defined herein) and (3) "this offering" refers to this offering of the Units pursuant to this prospectus supplement and the accompanying prospectus.

This document is in two parts. The first part is this prospectus supplement, which describes the specific terms of this offering of Units and also adds to and updates information contained in the accompanying prospectus and the documents incorporated by reference in the accompanying prospectus. The second part is the accompanying prospectus, which gives more general information about us, some of which does not apply to this offering of Units. To the extent the information in this prospectus supplement is inconsistent with the information in the accompanying prospectus, you should rely on the information in this prospectus supplement.

We have not, and the underwriters have not, authorized anyone to provide you with any information other than that contained or incorporated by reference in this prospectus supplement, the accompanying prospectus or in any free writing prospectus we may provide to you in connection with this offering. Neither we nor the underwriters take any responsibility for, or provide any assurances as to the reliability of, any additional or different information that others may give you. Neither we nor the underwriters are offering to sell the Units or seeking offers to buy the Units in jurisdictions where offers or sales are not permitted. You should assume that the information contained in this prospectus supplement, the accompanying prospectus and any related free writing prospectus is accurate only as of their respective dates or as of the respective dates specified in such information, as applicable, and the information contained in documents incorporated by reference is accurate only as of the respective dates of those documents or as of the respective dates specified in such information, as applicable, in each case regardless of the time of delivery of this prospectus supplement or the accompanying prospectus or any such free writing prospectus or any sale of the Units. Our business, financial condition, results of operations and prospects may have changed since those dates.

The distribution of this prospectus supplement, the accompanying prospectus and any related free writing prospectus and the offering of the Units in certain jurisdictions may be restricted by law. Persons into whose possession this prospectus supplement, the accompanying prospectus and any such free writing prospectus come should inform themselves about and observe any such restrictions. This prospectus supplement, the accompanying prospectus and any such free writing prospectus do not constitute, and may not be used in connection with, an offer or solicitation by anyone in any jurisdiction in which such offer or solicitation is not authorized or in which the person making such offer or solicitation is not qualified to do so or to any person to whom it is unlawful to make such offer or solicitation. See "Underwriting."

BASIS OF PRESENTATION

Unless otherwise specified or the context requires otherwise, the information in this prospectus supplement and the accompanying prospectus, including the documents incorporated by reference herein or therein, (1) does not give effect to any of the Transactions (as defined below), (2) when giving effect to this offering or the Common Stock Offering, assumes that the underwriters for this offering and the underwriters for the Common Stock Offering do not exercise their respective options to purchase additional Units or additional shares of our common stock, respectively, from us and (3) when giving effect to the Acquisition, assumes there are no adjustments to the Default Cash Acquisition Consideration (as defined herein) and that the Cash Acquisition Consideration (as defined herein) will therefore be $4.275 billion.

Although (1) the Acquisition has not yet occurred and, if completed, will not occur until after the closing of this offering, (2) this offering and certain of the other Financing Transactions are not contingent upon the completion of the other Financing Transactions, the Acquisition or the Company Debt Refinancing and (3) the indebtedness or other securities to be incurred or issued in certain of the Financing Transactions may not be incurred or issued, or may be redeemed, repaid, or repurchased, if the Acquisition is not consummated or is not consummated by a specified date, the pro forma and certain of the as adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus gives pro forma effect to the Acquisition, the Company Debt Refinancing and the Financing Transactions as if we had completed all such transactions as of December 31, 2018, in the case of balance sheet data, and as of January 1, 2018, in the case of income statement data, unless otherwise specified. The pro forma financial information included or incorporated by reference in this prospectus supplement does not, unless otherwise stated, give effect to our expected issuance of $150 million of the Debt Financing, because we intend to use that portion of the Debt Financing for general corporate purposes, including working capital and capital needs. See "Use of Proceeds." Moreover, the unaudited pro forma consolidated combined financial information included in our Current Report on Form 8-K/A filed with the U.S. Securities and Exchange Commission (the "SEC") on April 15, 2019, which is incorporated by reference in this prospectus supplement and the accompanying prospectus and may be obtained as described in this prospectus supplement under the heading "Where You Can Find Additional Information; Incorporation of Certain Documents by Reference," and certain pro forma and as adjusted information included in this prospectus supplement, have been calculated on the basis of assumptions made by our management at the time such information was prepared. For example, such unaudited pro forma consolidated combined financial information and other adjusted information reflects assumptions regarding (a) the amount of proceeds we will receive from, and certain pricing and other terms of, the Financing Transactions, (b) the number of securities to be issued in connection with the Financing Transactions and (c) the terms on which the Acquisition and the Company Debt Refinancing will be completed. As a result, purchasers in this offering should not place undue reliance on the pro forma and as adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus because this offering is not contingent upon completion of any of the other transactions reflected in that information.

All references to currency amounts included in this prospectus supplement are in U.S. dollars unless specifically noted otherwise.

FORWARD-LOOKING STATEMENTS

Certain statements in this prospectus supplement, the accompanying prospectus and the documents they incorporate by reference contain, and any free writing prospectus we may provide to you in connection with this offering are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), that are made based upon, among other things, our current assumptions, expectations, plans, and beliefs concerning future events and their potential effect on us. These forward-looking statements involve risks, uncertainties and other factors, many of which are outside our control that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. In some cases you can identify forward-looking statements where statements are preceded by, followed by or include the words "believes," "expects," "anticipates," "plans," "future," "potential," "probably," "predictions," "intends," "will," "continue," "in the event" or the negative of such terms or similar expressions. Such forward-looking statements include, but are not limited to, statements regarding:

- recovery of capital expenditures and expenses in rates;
- projected capital expenditures and related funding requirements;
- our capability to pursue timely rate increase requests;
- the availability and cost of capital financing;
- developments, trends and consolidation in the water and wastewater utility and infrastructure industries;
- dividend payment projections;
- opportunities for future acquisitions, both within and outside the water and wastewater industry, the success of pending acquisitions and the impact of future acquisitions;
- expectations regarding the proposed Acquisition, including statements regarding regulatory approvals for the Acquisition, potential financing transactions related to the Acquisition (including statements regarding the Financing Transactions and the use of proceeds therefrom, including the Company Debt Refinancing), closing of the Acquisition or the impact of the Acquisition on the Company;
- the capacity of our water supplies, water facilities and wastewater facilities;
- the impact of federal and/or state tax policies, including changes in tax laws and policies as a result of the Tax Cuts and Jobs Act of 2017, and the regulatory treatment of the effects of those policies;
- the impact of geographic diversity on our exposure to unusual weather;
- the impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer;
- our authority to carry on our business without unduly burdensome restrictions;
- the continuation of investments in strategic ventures;
- our ability to obtain fair market value for condemned assets;

- the impact of fines and penalties;
- the impact of changes in and compliance with governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- the impact of decisions of governmental and regulatory bodies, including decisions to raise or lower rates and decisions regarding potential acquisitions;
- the development of new services and technologies by us or our competitors;
- the availability of qualified personnel;
- the condition of our assets;
- the impact of legal proceedings;
- general economic conditions;
- acquisition-related costs and synergies;
- the sale of water and wastewater divisions; and
- the amount of income tax deductions for qualifying utility asset improvements and the Internal Revenue Service's ultimate acceptance of the deduction methodology.

Because forward-looking statements involve risks and uncertainties, there are important factors that could cause actual results to differ materially from those expressed or implied by these forward-looking statements, including but not limited to:

- our ability to integrate and otherwise realize all of the anticipated benefits of businesses, technologies or services which we may acquire;
- our ability to manage the expansion of our business, including our ability to manage our expanded operations following the closing of the Acquisition;
- changes in general economic, business, credit and financial market conditions;
- changes in governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- our ability to treat and supply water or collect and treat wastewater;
- Peoples's ability to transport, distribute and store natural gas;
- the profitability of future acquisitions;
- changes to the rules or our assumptions underlying our determination of what qualifies for an income tax deduction for qualifying utility asset improvements;
- conditions to the completion of the Acquisition may not be satisfied or waived on a timely basis, or at all;

- the decisions of governmental and regulatory bodies, including decisions on rate increase requests and decisions regarding potential acquisitions;
- our ability to file rate cases on a timely basis to minimize regulatory lag;
- abnormal weather conditions, including those that result in water use restrictions and seasonality effects;
- changes in, or unanticipated, capital requirements;
- changes in our credit ratings or the market price of our common stock;
- changes in valuation of strategic ventures;
- the extent to which we are able to develop and market new and improved services;
- the effect of the loss of major customers;
- our ability to retain the services of key personnel and to hire qualified personnel as we expand;
- the diversion of our management's time and resources caused by the announcement and pendency of the Acquisition;
- labor disputes;
- increasing difficulties in obtaining insurance and increased cost of insurance;
- cost overruns relating to improvements to, or the expansion of, our operations;
- increases in the costs of goods and services and commodity prices;
- civil disturbance or terroristic threats or acts;
- the continuous and reliable operation of our information technology systems, including the impact of cyber security attacks or other cyber-related events;
- changes in accounting pronouncements;
- litigation and claims;
- changes in environmental conditions, including the effects of climate change;
- restrictions on our subsidiaries' ability to make dividends and other distributions;
- restrictions and limitations that may stem from financing arrangements we enter into or assume in the future, or from the redemptions and repurchases we may undertake if the Acquisition is not consummated;
- dilution to our shareholders related to any financing transactions, including the Financing Transactions; and
- broad discretion of our management to use the net proceeds from this offering if the Acquisition is not consummated.

Given these risks and uncertainties, you should not place undue reliance on any forward-looking statements. You should read this prospectus supplement, the accompanying prospectus and the documents that we incorporate by reference into this prospectus supplement completely and with the understanding that our actual results, performance and achievements may be materially different from what we expect. These forward-looking statements represent assumptions, expectations, plans and beliefs only as of the date of this prospectus supplement, the date of the document containing the applicable statement or the date specified in such statement, as applicable. Except for our ongoing obligations to disclose certain information under the federal securities laws, we are not obligated, and assume no obligation, to update these forward-looking statements, even though our situation may change in the future. For further information or other factors which could affect our financial results and such forward-looking statements, see "Risk Factors." We qualify all of our forward-looking statements by these cautionary statements.

Investing in the Units involves risks. You should review and consider carefully the risks, uncertainties and other factors that affect our business, financial condition and results of operations and the value of the Units and shares of our common stock, including those described in the "Business," "Risk Factors," and "Management's Discussion and Analysis of Financial Condition and Results of Operations" sections and other sections in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018, and our Current Report on Form 8-K/A filed with the SEC on April 15, 2019, which are incorporated by reference in this prospectus supplement, and those described in the "Risk Factors" sections and other sections of this prospectus supplement and the accompanying prospectus. You may obtain copies of these reports and documents as described under "Where You Can Find Additional Information; Incorporation of Certain Documents by Reference" in this prospectus supplement. These risks, uncertainties and other factors could cause you to suffer a loss of all or part of your investment in the Units. Before making an investment decision, you should carefully consider these risks, uncertainties and other factors, as well as other information contained or incorporated by reference in this prospectus supplement and the accompanying prospectus and any related free writing prospectus we may provide to you in connection with this offering. However, additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our business, operations, financial condition and financial results and the value of the Units.

MARKET AND INDUSTRY DATA

This prospectus supplement, the accompanying prospectus and the documents incorporated by reference in this prospectus supplement and the accompanying prospectus include, and any free writing prospectus we may provide to you in connection with this offering may include, market, demographic and industry data and forecasts related to our business and Peoples's business that are based on or derived from sources such as independent industry publications, publicly available information, government data and other information from third parties or that have been compiled or prepared by our or Peoples's management or employees. We do not guarantee the accuracy or completeness of any of this information, and we have not independently verified any of the information provided by third-party sources.

In addition, market, demographic and industry data and forecasts involve estimates, assumptions and other uncertainties and are subject to change based on various factors, including those discussed under the heading "Risk Factors" in this prospectus supplement and under similar headings in the documents that are incorporated by reference in this prospectus supplement and the accompanying prospectus. Accordingly, you should not place undue reliance on any of this information.

SUMMARY INFORMATION

The following summary highlights, and should be read together with, the information contained elsewhere in this prospectus supplement, the accompanying prospectus and the documents incorporated by reference herein and therein. This summary may not contain all of the information that may be important to you, and you should carefully read this entire prospectus supplement, the accompanying prospectus, any free writing prospectus we may provide to you in connection with this offering and the documents incorporated by reference herein and therein before making an investment decision. You may obtain a copy of the documents incorporated by reference by following the instructions in the section titled "Where You Can Find Additional Information; Incorporation of Certain Documents by Reference," in this prospectus supplement. Unless we state otherwise or the context otherwise requires, references appearing in this prospectus supplement to "Aqua America," the "Company," "we," "us" and "our" should be read to refer to Aqua America, Inc. and its subsidiaries.

Aqua America, Inc.

Aqua America, Inc., a Pennsylvania corporation, is the holding company for regulated utilities providing water or wastewater services to an estimated three million people in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana, and Virginia. Our largest operating subsidiary is Aqua Pennsylvania, Inc., which accounted for approximately 53% of our operating revenues and approximately 71% of our regulated segment's income for 2018. As of December 31, 2018, Aqua Pennsylvania provided water or wastewater services to approximately one-half of the total number of people we serve. Aqua Pennsylvania's service territory is located in the suburban areas in counties north and west of the City of Philadelphia and in 27 other counties in Pennsylvania. Our other regulated utility subsidiaries provide similar services in seven other states. In addition, the Company's market-based activities are conducted through Aqua Infrastructure, LLC ("Aqua Infrastructure") and Aqua Resources Inc. ("Aqua Resources"). Aqua Infrastructure provides non-utility raw water supply services for firms in the natural gas drilling industry. Aqua Resources provides water service through operating and maintenance contracts with a municipal authority and another party close to our utility companies' service territory; and offers, through a third-party, water and sewer line protection solutions and repair services to households. In 2017, we completed the sale of two business units that were reported within Aqua Resources, one which installed and tested devices that prevent the contamination of potable water and another that constructed, maintained, and repaired water and wastewater systems. Additionally, during 2016, we completed the sale of business units within Aqua Resources, which provided liquid waste hauling and disposal services and inspection, and cleaning and repair of storm and sanitary wastewater lines.

Aqua America, which prior to its name change in 2004 was known as Philadelphia Suburban Corporation, was formed in 1968 as a holding company for its primary subsidiary, Aqua Pennsylvania, formerly known as Philadelphia Suburban Water Company. In the early 1990s, we embarked on a growth through acquisition strategy focused on water and wastewater operations. Our most significant transactions to date have been the merger with Consumers Water Company in 1999, the acquisition of the regulated water and wastewater operations of AquaSource, Inc. in 2003, the acquisition of Heater Utilities, Inc. in 2004, and the acquisition of American Water Works Company, Inc.'s regulated water and wastewater operations in Ohio in 2012. Since the early 1990s, our business strategy has been primarily directed toward the regulated water and wastewater utility industry, where we have more than quadrupled the number of regulated customers we serve, and have extended our regulated operations from southeastern Pennsylvania to include our current regulated utility operations throughout Pennsylvania and in seven other states. During 2010 through 2013, we sold our utility operations in six states, pursuant to a portfolio rationalization strategy to focus our operations in areas where we have critical mass and economic growth potential. Currently, the Company seeks to acquire businesses in the U.S. regulated sector, which includes water and wastewater utilities and other regulated utilities, and to pursue growth ventures in market-based activities, such as infrastructure opportunities that are supplementary and complementary to our regulated businesses. On October 22, 2018, we entered into a purchase agreement to acquire a group of natural gas public utility companies that we refer to as "Peoples." Peoples serves approximately 740,000 gas utility

customers in western Pennsylvania, West Virginia, and Kentucky. See "—Recent Developments—Proposed Peoples Gas Acquisition" for additional information regarding Peoples and the Acquisition.

Our growth in revenues over the past five years is primarily a result of increases in water and wastewater rates and customer growth. The increase in our utility customer base, as shown below, has been due to customers added through acquisitions, partnerships with developers, and organic growth (excluding dispositions):

Year	Utility Customer Growth Rate
2018	2.3%
2017	1.1%
2016	1.6%
2015	1.9%
2014	1.3%

In 2018, our customer count increased by 22,741 customers, primarily due to utility systems that we acquired and organic growth. Overall, for the five-year period of 2014 through 2018, our utility customer base, adjusted to exclude customers associated with utility system dispositions, increased at an annual compound rate of 1.6%. During the five-year period ended December 31, 2018, our utility customer base, including customers associated with utility system acquisitions and dispositions, increased from 941,008 at January 1, 2014 to 1,005,590 at December 31, 2018. This five-year period includes the impact of the condemnation of our Fort Wayne, Indiana system in 2014, which resulted in the loss of approximately 13,000 connections.

Our principal executive office is located at 762 W. Lancaster Avenue, Bryn Mawr, Pennsylvania 19010-3489, and our telephone number is 610-527-8000. Our website may be accessed at *www.aquaamerica.com*. The reference to our website is intended to be an inactive textual reference only, and the contents of our website is not incorporated by reference herein and should not be considered part of this prospectus supplement.

Our Business Strategy

Since the early 1990s, our business strategy has been primarily directed toward the regulated water and wastewater utility industry, where we have more than quadrupled the number of regulated customers we serve, and have extended our regulated operations from southeastern Pennsylvania to include our current regulated utility operations throughout Pennsylvania and in seven other states. We are focused on operating our businesses in a safe and efficient manner to provide exceptional service to our customers. Our key strategic priorities are as follows:

Pursue High-Quality, Low-Risk Earnings Growth

Growth in our existing water and wastewater utility business comes from both customer growth and increases in water and wastewater rates, driven by utility infrastructure investment. We expect to invest approximately $1.4 billion into our existing water utility infrastructure over the 2019-2021 timeframe including approximately $550 million in 2019. These estimates exclude planned capital expenditures by Peoples and the costs of new mains financed by advances and contributions in aid of construction. Our investment plans are supported by constructive regulatory environments in the jurisdictions in which we operate, and are expected to result in annual rate base growth over the same time period. Our regulators have a track record of setting rates and establishing terms of service that allow our regulated subsidiaries to obtain a fair and reasonable return on capital invested. Further, several of our regulators have put in place programs that incentivize prudent investments in our utility system by providing for reduced regulatory lag. For example, New Jersey allows for an infrastructure rehabilitation surcharge for water utilities, while Pennsylvania, Illinois, Ohio, Indiana and North Carolina allow for the use of an infrastructure rehabilitation surcharge for both water and wastewater utility systems. Aqua Virginia is also piloting an infrastructure rehabilitation surcharge for its water and wastewater utilities to be implemented in 2019, pursuant to the final order issued in Aqua Virginia's 2018 rate case.

In addition to our organic infrastructure investment, we expect to continue to actively explore opportunities to expand our operations through acquisitions of government-owned and regulated water and wastewater systems that provide services in areas near our existing service territories or in new service areas. With approximately 50,000 community water systems in the United States, 81% of which serve less than 3,300 customers, the water industry is the most fragmented of the major utility industries (telephone, natural gas, electric, water and wastewater). In the states where we operate regulated utilities, we believe there are approximately 14,000 community water systems of widely-varying size, with the majority of the population being served by government-owned water systems. Because of the fragmented nature of the water and wastewater utility industries, we believe that there are many potential water and wastewater system acquisition candidates throughout the United States. We believe numerous factors will drive continued consolidation of these systems, including the benefits of economies of scale, the increasing cost and complexity of environmental regulations, the need for substantial capital investment and the need for technological and managerial expertise.

Six of the states in which we operate currently have some form of fair market value legislation. This legislation allows the relevant public utility commission to utilize fair market value to set ratemaking rate base instead of the depreciated original cost of water or wastewater assets for certain qualifying municipal acquisitions. We believe that this legislation is another factor that will encourage consolidation in the water and wastewater industry, providing municipalities with an option for exiting the business if they are dealing with challenges associated with their aging, deteriorating water and wastewater assets, do not have the expertise or technical capabilities to continue to comply with ever increasing environmental regulations or simply want to focus on other community priorities. In 2018, we closed six municipal acquisitions with over 13,700 customers and over $100 million of rate base.

Maintain a Low-Risk Regulated Utility Profile

Our core skill set is operating, maintaining and growing a regulated utility platform. The vast majority of our earnings are derived from regulated utilities, and we intend to maintain our focus on regulated utility platforms. As further discussed in "—Recent Developments—Peoples Gas Acquisition—Strategic Rationale for the Acquisition," the Acquisition is consistent with this strategy. Our focus on regulated utilities has contributed to our historically stable earnings and cash flows, which forms the foundation for our dividend policy and has allowed us to raise dividends 28 times in the last 27 years.

Maintain Our Commitment to a Strong Balance Sheet

Our goal is to maintain a strong balance sheet and liquidity position in addition to solid investment grade credit ratings. We believe maintaining these objectives affords us the financial flexibility necessary to take advantage of significant growth opportunities in our regulated utility businesses.

Our Competitive Strengths

We believe that we are well-positioned to meet our obligations to customers, grow our business and create shareholder value because of the following factors:

Extensive Track Record of Operating Stable Utilities

Our earnings are principally derived from the return on investment we earn on our utility assets. We estimate that, as of December 31, 2018, our rate base was approximately $4.5 billion. We estimate that, as of December 31, 2019, assuming consummation of the Acquisition, our rate base will be approximately $7.2 billion. Of the $7.2 billion expected rate base as of December 31, 2019, we estimate that approximately 70% will be derived from water and wastewater utilities and approximately 30% will be derived from natural gas distribution. We have more than 130 years of service experience and a proven track record of operational efficiency.

Operations in Constructive Regulatory Jurisdictions

We currently have regulated utility operations in eight different states, which have collectively provided constructive regulatory environments for our utility operations, and following the Acquisition will have regulated utility operations in ten different states, which we believe will provide constructive regulatory environments for our expanded utility operations. Two of these ten states have in place rate decoupling mechanisms for water or gas utility businesses, which reduce the dependency of our revenues to the changes in the volume of managed water or natural gas that may result from fluctuations in the weather, gas consumption, water conservation, and other factors. Further, regulators in several of these states have put in place certain programs that incentivize prudent capital investments in our utility system by providing for accelerated recovery of and on capital. The regulatory framework in Pennsylvania, which accounted for approximately 71% of our Regulated segment's income for 2018, is generally considered progressive and is highly rated by Regulatory Research Associates. Pennsylvania's high rating is based on the probable level and quality of the earnings to be realized by the state's utilities as a result of regulatory, legislative and court actions, as well as the utilization of fully forecasted test years, Distribution Systems Improvement Charges and other automatic adjustment clauses that are intended to reduce the gap between the time that a capital project is completed and the recovery of costs in rates. As further discussed in "—Recent Developments —Peoples Gas Acquisition—Strategic Rationale for the Acquisition," the Acquisition would increase our presence in constructive regulatory jurisdictions, particularly in Pennsylvania.

Significant Infrastructure Needs & Core Competency in Infrastructure Investment

According to recent U.S. EPA surveys, there are approximately 50,000 community water systems and approximately 15,000 wastewater systems in the United States, a majority of which are municipally owned, and more than $740 billion will need to be spent to maintain and improve U.S. water and wastewater infrastructure over the next 20 years. We have historically leveraged our expertise in infrastructure improvement and pipeline replacement to improve safety and reliability throughout the states in which we operate. For example, over the last 15 years, our investment in pipe replacement in southeastern Pennsylvania has resulted in a 53% reduction in discolored water-quality-related service orders and a 60% reduction in main breaks. As municipalities face the challenges of replacing deteriorating infrastructure, we provide a viable and valuable solution to communities through our expertise and our economies of scale. In addition, we expect the Acquisition will introduce new infrastructure investment opportunities, as discussed in "—Recent Developments—Peoples Gas Acquisition—Strategic Rationale for the Acquisition."

Consistent History of Dividend Growth. We have paid dividends consecutively for 74 years

In 2018, our Board of Directors raised the quarterly dividend on our common stock by 7%, increasing the effective annual dividend rate to $0.876 per share, beginning with the dividend payment in September 2018. This is the 28th dividend increase in the past 27 years and the 20th consecutive year that we have increased our dividend in excess of 5%.

Experienced Management Team

Our senior management team is highly experienced in the utility industry. The team is supported by a core group of employees in leadership positions with substantial experience in the operation of regulated utility businesses. In addition, as discussed in "—Recent Developments—Peoples Gas Acquisition—Strategic Rationale for the Acquisition," the Peoples's management team has significant experience in the natural gas utility industry. Additionally, the Aqua America CEO serves on the Board of Directors of the National Association of Water Companies.

Recent Developments

Proposed Peoples Gas Acquisition

On October 22, 2018, we entered into a Purchase Agreement (the "Acquisition Agreement") with LDC Parent LLC, a Delaware limited liability company ("Seller"), to acquire all of the issued and outstanding limited liability company membership interests of LDC, the parent of a group of natural gas public utility companies including Peoples Natural Gas Company LLC, a Pennsylvania limited liability company, Peoples Gas Company LLC, a Pennsylvania limited liability company, Peoples Gas WV LLC, a West Virginia limited liability company, Peoples Gas Kentucky LLC, a Kentucky limited liability company, and Delta Natural Gas Co., Inc., a Kentucky corporation, as well as other operating subsidiaries.

The Acquisition, once consummated, will expand our regulated utility business to include natural gas distribution. The cash purchase price for the Acquisition will be an amount equal to $4.275 billion (the "Default Cash Acquisition Consideration"), subject to adjustments for working capital, certain capital expenditures, transaction expenses and closing indebtedness as set forth in the Acquisition Agreement (as so adjusted, the "Cash Acquisition Consideration"). The Company expects to assume, as a result of acquiring Peoples, approximately $1,370 million of Peoples's indebtedness upon the closing of the Acquisition, which would reduce the cash purchase price by approximately $1,370 million pursuant to the foregoing adjustments. See "—Financing Transactions" and "Use of Proceeds" for a discussion of our plans to finance the Cash Acquisition Consideration.

Closing of the Acquisition is subject to customary closing conditions set forth in the Acquisition Agreement, including, among others, (1) the absence of any law or governmental order prohibiting the consummation of the Acquisition, (2) the accuracy of the parties' representations and warranties, subject to customary materiality standards and certain other exceptions, (3) compliance in all material respects of the parties with their applicable covenants under the Acquisition Agreement, subject to certain exceptions, (4) the absence of a "material adverse effect" with respect to LDC and its subsidiaries and (5) receipt of certain regulatory approvals, including from the public utility commission in Pennsylvania and West Virginia. The closing of the Acquisition is not subject to any financing condition. We currently expect the Acquisition will close in mid-2019.

The Acquisition Agreement contains certain termination rights for each of us and Seller. The Acquisition Agreement may be terminated at any time prior to the closing of the Acquisition in the event the Acquisition is not completed by October 22, 2019 (subject to extension, on the terms set forth in the Acquisition Agreement, to April 22, 2020 in order to obtain necessary regulatory approvals) (the "Acquisition Outside Date"). However, neither we nor Seller may terminate the Acquisition Agreement pursuant to the foregoing if our or Seller's respective failure to fulfill any obligation under the Acquisition Agreement was the primary cause of the failure of the closing to occur on or before the Acquisition Outside Date. The Acquisition Agreement may also be terminated at any time prior to the closing of the Acquisition by mutual written consent of us and Seller, and in other customary circumstances. In the event that the Acquisition Agreement is terminated due to certain breaches by us, we would be required to pay a fee of $120 million to the Seller as liquidated damages.

The Acquisition and the Acquisition Agreement are described in more detail in our Current Report on Form 8-K filed with the SEC on October 23, 2018 (the "Acquisition 8-K"), which is incorporated by reference into this prospectus supplement and the accompanying prospectus. The foregoing summary description does not purport to be complete and is qualified in its entirety by reference to the complete text of the Acquisition Agreement, which was filed as Exhibit 2.1 to the Acquisition 8-K.

The Acquisition Agreement has been filed as an exhibit to our public reports filed with the SEC, and has been incorporated by reference into this prospectus supplement and the accompanying prospectus, solely to provide information to current and prospective investors and security holders regarding its terms. The Acquisition Agreement and the description of certain terms of the Acquisition Agreement appearing in this prospectus supplement and some of the documents incorporated by reference in the accompanying prospectus are not intended to provide any other factual information about Aqua America, Peoples, their respective businesses, or the actual or future conduct of their respective businesses or to modify or supplement any factual disclosures about Aqua America or Peoples included in this prospectus supplement, the accompanying prospectus or the documents incorporated by reference therein or Aqua America's other public reports. The Acquisition Agreement and any descriptions thereof should not be relied upon as representations or warranties about Aqua America or Peoples or, other than with respect to the terms of the Acquisition Agreement, as disclosure about Aqua America or Peoples. No one should rely on the representations, warranties and covenants in the Acquisition Agreement or any descriptions thereof as characterizations of the actual state of facts or conditions of Aqua America or Peoples or any of their respective subsidiaries or affiliates. The representations and warranties contained in the Acquisition Agreement are the product of negotiations among the parties thereto and that the parties made to, and solely for the benefit of, each other as of specified dates. The assertions embodied in those representations and warranties are subject to qualifications and limitations agreed to by the respective parties and are also qualified in important part by confidential disclosure schedules delivered in connection with the Acquisition Agreement. In addition, those representations and warranties were made for the purpose of allocating contractual risk between the parties to the Acquisition Agreement instead of establishing these matters as facts, and may be subject to standards of materiality used by the contracting parties that differ from those applicable to investors and security holders. Moreover, information concerning the subject matter of the representations and warranties may change after the dates contemplated by the Acquisition Agreement, which subsequent information may or may not be reflected in this prospectus supplement or the documents incorporated by reference in this prospectus supplement and the accompanying prospectus or in Aqua America's other public reports. The Acquisition Agreement and any such descriptions thereof should not be read alone, but should instead be read in conjunction with the other information regarding Aqua America or Peoples that is contained in, or incorporated by reference into, this prospectus supplement, the accompanying prospectus and the documents incorporated by reference herein and therein.

The consummation of this offering is not conditioned upon the closing of the Acquisition. There can be no assurance that the Acquisition will be consummated on the terms or by the time currently contemplated, or at all, or, if consummated, that the terms of the Acquisition, including the financing thereof and the closing date, will not differ, perhaps substantially, from those currently contemplated or described in this prospectus supplement or the documents incorporated by reference in this prospectus supplement and the accompanying prospectus. The closing of the Acquisition is subject to, among other conditions, the receipt of regulatory approval by the Pennsylvania Public Utility Commission. We filed an application for approval by the Pennsylvania Public Utility Commission, and several entities have intervened in the proceeding. The procedural schedule requires rebuttal testimony to be filed on April 30, 2019. We have initiated settlement discussions with the intervenors and those negotiations are ongoing. Whether through a settlement agreement or through a litigated proceeding, we may be required to agree to certain actions, undertakings, terms, or other measures, including those that may require increased capital or other expenditures by the Company. See "Risk Factors—Risks Related to the Acquisition and the Financing Transactions" in this prospectus supplement, "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018 and "Risk Factors" in our Current Report on Form 8-K/A filed with the SEC on April 15, 2019 (as updated by annual, quarterly and other reports and documents we file with the SEC that are incorporated by reference in this prospectus supplement and the accompanying prospectus).

About Peoples

Headquartered in Pittsburgh, Pennsylvania, Peoples primarily engages in regulated distribution and transportation of natural gas to approximately 740,000 residential, commercial and industrial customers in Pennsylvania, West Virginia and Kentucky. For the year ended December 31, 2018, Peoples's operating revenues amounted to $914 million.

For a discussion of Peoples's business, operations, financial condition and financial results and the specific risks related to Peoples's business, operations, financial condition and financial results, please see the "Peoples's Business," "Risk Factors related to Peoples" and "Management's Discussion and Analysis of Financial Condition and Results of Operations of Peoples" in our Current Report on Form 8-K/A filed with the SEC on April 15, 2019 and incorporated by reference in this prospectus supplement and the accompanying prospectus.

Strategic Rationale for the Acquisition

We believe the Acquisition is a strategically compelling transaction that brings together two high-quality regulated utility companies in regions with constructive regulatory environments and attractive demographics. Consistent with our strategy of growing our regulated utility platform, we expect that the Acquisition will introduce a new platform for regulated growth, creating a leading water and natural gas utility in the United States with scale across the water, wastewater and natural gas distribution sectors. We believe this enhanced growth platform will present opportunities for the Company to grow our rate base through a wider range of infrastructure investment opportunities. In addition, as a larger publicly traded utility, we expect to have better access to capital to fund our infrastructure and capital expenditure needs. We also believe our enhanced scale and better access to the capital markets will support our commitment to strong investment grade credit ratings.

Both Aqua America and Peoples have demonstrated the ability to earn a return on and recover invested capital, with a history of sustained growth in earnings and cash flow. We believe the Acquisition will diversify the Company's cash flow while preserving our low-risk regulated utility profile, resulting in a multi-platform utility with operations spanning ten states.

We expect that the Acquisition will increase our presence in constructive regulatory jurisdictions, particularly Pennsylvania, where the regulatory framework is generally considered progressive and is highly rated by Regulatory Research Associates. Pennsylvania's high rating is based on the probable level and quality of the earnings to be realized by the state's utilities as a result of regulatory, legislative, and court actions, as well as the utilization of fully forecasted test years, Distribution Systems Improvement Charges and other automatic adjustment clauses that are intended to reduce the gap between the time that a capital project is completed and the recovery of costs in rates. The Peoples's management team will bring significant experience investing in and operating critical energy and safety infrastructure; their experience and knowledge is expected to be highly complementary to our core focus of operating our businesses in a safe and efficient manner to provide exceptional service to our customers.

We expect the Acquisition to increase our scale, cash flow diversity and rate base and strengthen our financial foundation, creating an enhanced platform for long-term growth. However, there can be no assurance that the Acquisition will be consummated on the terms or by the time currently contemplated, or at all, or, if consummated, that we will realize the anticipated benefits of the Acquisition. See "Risk Factors—Risks Related to the Acquisition and the Financing Transactions" in this prospectus supplement and "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018 (as updated by annual, quarterly and other reports and documents we file with the SEC that are incorporated by reference in this prospectus supplement and the accompanying prospectus).

Financing Transactions

In addition to the sale of the Units in connection with this offering, we expect to obtain additional financing to (1) fund the Acquisition, (2) complete the redemption of approximately $314 million aggregate principal amount of our privately placed notes (such notes, the "PPNs," and such redemption, the "Company Debt Refinancing") and (3) pay related costs and expenses as described below. In addition, we intend to use $150 million of proceeds of the Debt Financings for general corporate purposes, including working capital and capital needs. For information regarding sources and uses of funds in connection with the Acquisition and the Financing Transactions, see "Use of Proceeds."

Common Stock Offering

Concurrently with this offering, we are offering, by means of a separate prospectus supplement, 32,495,667 shares of our common stock, par value $0.50 per share ("our common stock"), or up to 37,370,017 shares if the underwriters of such offering exercise their option to purchase additional shares of our common stock (the "Common Stock Offering"). The net proceeds from the sale of common stock in the Common Stock Offering will be approximately $1,098.3 million (or approximately $1,263.2 million if the underwriters of such offering exercise their option to purchase additional shares of our common stock in full).

Private Placement

On March 29, 2019, we entered into a Stock Purchase Agreement (the "CPPIB Agreement") with Canada Pension Plan Investment Board ("CPPIB") pursuant to which CPPIB agreed to purchase an aggregate of 21,661,095 newly issued shares of our common stock (the "Private Placement") at the lower of (1) $34.62 per share and (2) the volume weighted average price per share in our public offerings of Common Stock to fund the Acquisition, the Company Debt Refinancing and pay related costs and expenses related thereto.

We expect the Private Placement to close concurrently with the consummation of the Acquisition, subject to certain closing conditions, including the closing of the Acquisition, the completion of additional equity offerings (including this offering and the Common Stock Offering) which raise gross proceeds in an aggregate amount of at least $1,600 million and the execution and delivery of a shareholder's agreement between CPPIB and the Company. The completion of the Private Placement is not conditioned upon the consummation of the Company Debt Refinancing or the Debt Financings.

Pursuant to the CPPIB Agreement, the shares purchased by CPPIB in the Private Placement will be subject to certain transfer restrictions until the earlier of 15 months following the completion of the Private Placement or specified change of control events with respect to the Company, subject to certain exceptions. In addition, subject to ownership thresholds and other customary requirements, CPPIB will have, pursuant to the shareholder's agreement to be entered into in connection with the closing of the Private Placement, (1) the right to appoint a member of our board of directors, (2) certain pre-emptive rights, (3) certain registration rights in respect of the shares purchased by CPPIB in the Private Placement and (4) certain "standstill" obligations with respect to the Company, subject to certain exceptions. Upon closing of the Private Placement, the Company has agreed to reimburse CPPIB for reasonable out-of-pocket diligence expenses of up to $4 million, subject to certain exceptions.

The foregoing description of the Private Placement does not purport to be complete and is qualified in its entirety by reference to the full text of the CPPIB Agreement, which was filed as Exhibit 10.1 to our Current Report on Form 8-K filed with the SEC on March 29, 2019 and incorporated by reference herein.

Debt Financings

We intend to obtain or otherwise incur up to approximately $1,009 million of senior indebtedness in connection with the Acquisition and the Company Debt Refinancing and approximately $150 million of senior indebtedness to be used for general corporate purposes, including working capital and capital needs. We refer to this $1,159 million of senior indebtedness financing as the "Debt Financings". The Debt Financings may include some combination of the following:

- *Notes Offering.* Subsequent to this offering we expect to offer, pursuant to one or more separate prospectus supplements, one or more series of senior unsecured notes (such notes, the "New Notes" and, such offerings, the "Notes Offering").

- *Bridge Facility.* On October 22, 2018, we obtained a commitment (the "Bridge Commitment") from Goldman Sachs Bank USA and Royal Bank of Canada to provide 364-day senior unsecured bridge loans (the "Bridge Facility"), in an aggregate amount of up to $5,100 million, subject to customary conditions set forth in the Bridge Commitment. As of the date of this prospectus supplement, we have terminated approximately $1,633 million of commitments under the Bridge Commitment in connection with, among other things, the replacement of our prior unsecured revolving credit facility, the expected refinancing of Peoples's revolving credit facility using our senior unsecured revolving credit facility (our "Revolving Credit Facility") and the expected assumption of Peoples's private placement notes. The Bridge Commitment may only be drawn upon to fund the Acquisition, the Company Debt Refinancing and related fees and expenses, and will expire upon the earliest to occur of (1) the termination of the Acquisition Agreement prior to the consummation of the Acquisition, (2) the closing of the Acquisition or (3) the Acquisition Outside Date.

In addition, if and to the extent that the Common Stock Offering and/or the Private Placement is not completed, or such offerings are completed for less aggregate net proceeds than anticipated, we currently intend to fund any shortfall through the issuance of additional shares of common stock or equity-linked securities prior to the consummation of the Acquisition. However, if we are unable to issue such shares or equity-linked securities, we would fund any shortfall with additional debt financings, which may include borrowings under the Bridge Facility and/or the Revolving Credit Facility.

In this prospectus supplement, references to the "Financing Transactions" refer to this offering, the Common Stock Offering, the Private Placement and the Debt Financings, and references to the "Transactions" refer to the Financing Transactions, the Acquisition and the Company Debt Refinancing, including the application of the net proceeds from the Financing Transactions to complete such transactions as described herein. In addition, unless otherwise specified or the context requires otherwise, references in this prospectus supplement to the "consummation of the Acquisition" or similar expressions shall be deemed to include the application of the net proceeds from the Financing Transactions to complete such transactions as described herein, including the consummation of the Company Debt Refinancing.

This offering and certain of the other Financing Transactions are not conditioned upon the consummation of any other Financing Transactions, the Acquisition or the Company Debt Refinancing. In addition, the indebtedness or other securities to be incurred or issued in certain of the Financing Transactions may not be incurred or issued, or may be redeemed, repaid, or repurchased, if the Acquisition is not consummated or is not consummated by a specified date. Accordingly, even if the Acquisition, the Company Debt Refinancing or other Financing Transactions do not occur, the Units issued in this offering will remain outstanding, unless, in the event the Acquisition does not occur by April 22, 2020 or is terminated prior to such date, we elect to redeem the outstanding purchase contracts (in which case holders can require us to repurchase their amortizing notes) as described herein. Purchasers of the Units in this offering should not place undue reliance on the pro forma and as adjusted information included and incorporated by reference in this prospectus supplement and the accompanying prospectus because this offering is not contingent upon the completion of any of the other Financing Transactions, the Acquisition or the Company Debt Refinancing, some or all of which are reflected in the adjustments included in that information, and because the actual amount of proceeds from the sale of shares and from any other Financing Transaction, and the actual terms of each of the Transactions, may differ, perhaps substantially, from those reflected in the prospectus supplement.

We cannot assure you that we will complete the Acquisition or any of the other Financing Transactions on the terms contemplated by this prospectus supplement, or at all.

The Offering

The summary below describes the principal terms of the Units, the purchase contracts and the amortizing notes. Certain of the terms and conditions described below are subject to important limitations and exceptions. The "Description of the Units," Description of the Purchase Contracts" and "Description of the Amortizing Notes" sections of this prospectus supplement, together with the "Description of Debt Securities" section of the accompanying prospectus, contain a more detailed description of the terms and conditions of the Units, the purchase contracts and the amortizing notes.

As used in this section, unless the context otherwise requires, references to "Aqua America," the "Company," "we," "us," "our" and similar references refer only to Aqua America, Inc. and not to its consolidated subsidiaries.

The Units

Issuer	Aqua America, Inc., a Pennsylvania corporation
Number of Units Offered	12,000,000 Units
Underwriters' Option	We have granted the underwriters an option to purchase within 13 days beginning on, and including, the date of initial issuance of the Units up to an additional 1,800,000 Units at the public offering price less the underwriting discount. This option may be exercised by the underwriters solely to cover over-allotments, if any.
Stated Amount of Each Unit	$50.00 for each Unit
Components of Each Unit	Each Unit is comprised of two parts: • a prepaid stock purchase contract issued by us (a "purchase contract"); and • a senior amortizing note issued by us (an "amortizing note"). Unless earlier redeemed by us in connection with an acquisition termination redemption or settled earlier at the holder's option or at our option, each purchase contract will, subject to postponement in certain limited circumstances, automatically settle on April 30, 2022 (such date, as so postponed (if applicable), the "mandatory settlement date"). Upon any settlement on the mandatory settlement date, we will deliver not more than 1.4442 shares and not less than 1.1790 shares of our common stock per purchase contract, subject to adjustment, based upon the applicable settlement rate and applicable market value of our common stock, as described below under "Description of the Purchase Contracts—Delivery of Common Stock." Each amortizing note will have an initial principal amount of $8.62909, will bear interest at the rate of 3.00% per annum and will have a final installment payment date of April 30, 2022. On each January 30, April 30, July 30 and October 30, commencing on July 30, 2019, we will pay equal quarterly cash installments of $0.75000 per amortizing note (except for the July 30, 2019 installment payment, which will be $0.80833 per amortizing note), which cash payment in the aggregate per year will be equivalent to 6.00% per year with respect to each $50.00 stated amount of Units.

	Each installment payment will constitute a payment of interest and a partial repayment of principal, allocated as set forth under "Description of the Amortizing Notes—Amortization Schedule." The return to an investor on a Unit will depend upon the return provided by each component. The overall return will consist of the value of the shares of our common stock delivered upon settlement of the purchase contracts and the cash installments paid on the amortizing notes.
Each Unit May Be Separated into Its Components	Each Unit may be separated by a holder into its constituent purchase contract and amortizing note on any business day during the period beginning on, and including, the business day immediately following the date of initial issuance of the Units to, but excluding, the second scheduled trading day immediately preceding April 30, 2022 or, if earlier, the second scheduled trading day immediately preceding any "early mandatory settlement date" or the second scheduled trading day immediately preceding any "acquisition redemption settlement date" and also excluding the business day immediately preceding any installment payment date (*provided*, the right to separate the Units shall resume after such business day). Prior to separation, the purchase contracts and amortizing notes may only be purchased and transferred together as Units. See "Description of the Units—Separating and Recreating Units."
A Unit May Be Recreated from Its Components	If you hold a separate purchase contract and a separate amortizing note, you may combine the two components to recreate a Unit. See "Description of the Units—Separating and Recreating Units."
Listing	We have applied to list the Units on the NYSE under the symbol "WTRU", subject to satisfaction of its minimum listing standards with respect to the Units. However, we cannot assure you that the Units will be approved for listing. If approved for listing, we expect trading on the NYSE to begin within 30 calendar days after the Units are first issued. We will not initially apply to list the separate purchase contracts or the separate amortizing notes on any securities exchange or automated inter-dealer quotation system, but we may apply to list such separate purchase contracts and separate amortizing notes in the future as described under "Description of the Units—Listing of Securities." Prior to this offering, there has been no public market for the Units. Our common stock is listed on the NYSE under the symbol "WTR."
Use of Proceeds	We estimate that the net proceeds from this Units offering, after deducting underwriting discounts and estimated offering expenses, will be approximately $585.8 million (or approximately $673.7 million if the underwriters exercise their option to purchase additional Units in full). We intend to use the net proceeds from this offering, together with the net proceeds from the other Financing Transactions, to (1) fund the Acquisition, (2) complete the Company Debt Refinancing and (3) pay related costs and expenses as described below. See "—Recent Developments—Proposed

	Peoples Gas Acquisition." In addition, we intend to use $150 million of proceeds of the Debt Financings for general corporate purposes, including working capital and capital needs. If for any reason the Acquisition is not consummated, we expect we would use the net proceeds from this offering, after payment of any cash redemption amount and/or repurchase price (if applicable), for general corporate purposes, which may include the Company Debt Refinancing, the redemption of securities issued in connection with the other Financing Transactions, repurchases of our common stock, debt repayment, capital expenditures and investments. See "Use of Proceeds."
Concurrent Common Stock Offering	Concurrently with this offering of Units, we are offering, by means of a separate prospectus supplement, 32,495,667 shares (or up to 37,370,017 shares if the underwriters for that offering exercise their option to purchase additional shares of common stock). The net proceeds from the sale of common stock in the Common Stock Offering will be approximately $1,098.3 million (or approximately $1,263.2 million if the underwriters of such offering exercise their option to purchase additional shares of our common stock in full). This prospectus supplement is not an offer to sell or a solicitation of an offer to buy any securities being offered in the Common Stock Offering. There can be no assurance that the Common Stock Offering will be completed. Neither this offering nor the Common Stock Offering is conditioned upon the consummation of the Acquisition or completion of any other Financing Transactions. See "—Recent Developments—Financing Transactions—Common Stock Offering."
Private Placement	On March 29, 2019, we entered into the CPPIB Agreement pursuant to which CPPIB agreed to purchase an aggregate of 21,661,095 shares of our common stock at the lower of (1) $34.62 per share and (2) the volume weighted average price per share in our public offerings of Common Stock to fund the Acquisition, the Company Debt Refinancing and pay related costs and expenses related thereto. This prospectus supplement is not an offer to sell or a solicitation of an offer to buy any securities being offered in the Private Placement. This offering is not conditioned upon completion of the Private Placement. The completion of the Private Placement is subject to certain closing conditions, including the closing of the Acquisition, the completion of additional equity offerings (including this offering and the Common Stock Offering) which raise gross proceeds in an aggregate amount of at least $1,600 million and the execution and delivery of a shareholders agreement between CPPIB and the Company. See "—Recent Developments —Financing Transactions—Private Placement."
Risk Factors	Investing in our Units involves risks. See "Risk Factors" in this prospectus supplement, the accompanying prospectus and in the documents we incorporate by reference into this prospectus supplement and the accompanying prospectus for a discussion of some of the risks and other factors you should carefully consider before deciding to invest in the Units.
United States Federal Income Tax Consequences	There is no authority directly on point regarding the characterization of the Units or instruments similar to the Units for U.S. federal income tax purposes and therefore the characterization of the Units for these purposes is not entirely free from doubt. We will take the position that each Unit will be treated as an investment unit composed of two separate instruments for U.S.

	federal income tax purposes: (i) a purchase contract to acquire our common stock and (ii) an amortizing note that is our indebtedness. Under this treatment, a holder of Units will be treated as if it held each component of the Units for U.S. federal income tax purposes. By acquiring a Unit, you will agree to treat (i) a Unit as an investment unit composed of two separate instruments in accordance with its form and (ii) the amortizing notes as indebtedness of Aqua America, Inc. for U.S. federal income tax purposes. If, however, the components of a Unit were treated as a single instrument, the U.S. federal income tax consequences could differ from the consequences described herein. Prospective investors should consult their tax advisors regarding the tax treatment of an investment in Units and whether a purchase of a Unit is advisable in light of the investor's particular tax situation and the tax treatment described under "Certain United States Federal Income and Estate Tax Consequences."
Governing Law	The Units, the purchase contract agreement, the purchase contracts, the indenture and the amortizing notes will all be governed by, and construed in accordance with, the laws of the State of New York.
The Purchase Contracts	
Issuer	Aqua America, Inc., a Pennsylvania Corporation
Mandatory Settlement Date	April 30, 2022, subject to postponement in limited circumstances.
Mandatory Settlement	On the mandatory settlement date, unless such purchase contract has been earlier redeemed by us in connection with an acquisition termination redemption or earlier settled at the holder's option or at our option, each purchase contract will automatically settle, and we will deliver a number of shares of our common stock, based on the applicable settlement rate.
Settlement Rate for the Mandatory Settlement Date	The "settlement rate" for each purchase contract will be not more than 1.4442 shares and not less than 1.1790 shares of our common stock (each subject to adjustment as described herein) depending on the applicable market value of our common stock, calculated as follows: • if the applicable market value (as defined below) is greater than the threshold appreciation price (as defined below), you will receive 1.1790 shares of common stock per purchase contract (the "minimum settlement rate"); • if the applicable market value is less than or equal to the threshold appreciation price but greater than or equal to the reference price, you will receive a number of shares of our common stock per purchase contract equal to $50.00, *divided by* the applicable market value; and • if the applicable market value is less than the reference price, you will receive 1.4442 shares of common stock per purchase contract (the "maximum settlement rate").

Each of the maximum settlement rate and the minimum settlement rate is subject to adjustment as described below under "Description of the Purchase Contracts—Adjustments to the Fixed Settlement Rates."

The "applicable market value" means the arithmetic average of the VWAP (as defined below under "Description of the Purchase Contracts—Delivery of Common Stock") per share of our common stock over the settlement period (as defined below)

The "settlement period" means the 20 consecutive trading day period beginning on, and including, the 21st scheduled trading day immediately preceding April 30, 2022.

The "reference price" is calculated by dividing $50.00 by the then applicable maximum settlement rate and is initially approximately equal to $34.62, which is the per share public offering price of our common stock in the Common Stock Offering.

The "threshold appreciation price" is calculated by dividing $50.00 by the then applicable minimum settlement rate. The threshold appreciation price, which is initially approximately $42.41, represents a premium of approximately 22.5% over the reference price.

No fractional shares of our common stock will be issued to holders upon settlement or redemption of purchase contracts. In lieu of fractional shares otherwise issuable, holders will be entitled to receive a cash payment of equivalent value calculated as described herein. Other than cash payments in lieu of fractional shares or, under certain circumstances, in the event of an acquisition termination redemption, holders of purchase contracts will not receive any cash distributions.

The following table illustrates the settlement rate per purchase contract and the value of our common stock issuable upon settlement on the mandatory settlement date, determined using the applicable market value shown, subject to adjustment.

Applicable Market Value of Our Common Stock	Settlement Rate	Value of Common Stock Delivered (Based on the Applicable Market Value Thereof)
Less than the reference price	1.4442 shares of our common stock	Less than $50.00
Less than or equal to the threshold appreciation price but greater than or equal to the reference price	A number of shares of our common stock equal to $50.00 *divided by* the applicable market value	$50.00
Greater than the threshold appreciation price	1.1790 shares of our common stock	Greater than $50.00

Early Settlement at Your Election

At any time prior to 5:00 p.m., New York City time, on the second scheduled trading day immediately preceding April 30, 2022, you may settle any or all of your purchase contracts early, in which case we will deliver a number of shares of our common stock per purchase contract equal to the minimum settlement rate, which is subject to adjustment as described below under "Description of the Purchase Contracts—Adjustments to the Fixed

	Settlement Rates" (unless such early settlement occurs in connection with a fundamental change, in which case the provisions described under "—Early Settlement Upon a Fundamental Change" below will apply). That is, the market value of our common stock on the early settlement date will not affect the early settlement rate. Your right to settle your purchase contracts prior to the second scheduled trading day immediately preceding April 30, 2022 is subject to the delivery of your purchase contracts. Upon early settlement at the holder's election of a purchase contract that is a component of a Unit, the corresponding amortizing note will remain outstanding and beneficially owned by or registered in the name of, as the case may be, the holder who elected to settle the related purchase contract early.
Early Settlement Upon a Fundamental Change	At any time prior to the second scheduled trading day immediately preceding April 30, 2022, if a "fundamental change" (as defined herein) occurs, you may settle any or all of your purchase contracts early. If you elect to settle your purchase contracts early in connection with such fundamental change, you will receive a number of shares of our common stock (and any cash payable for fractional shares) per purchase contract equal to the "fundamental change early settlement rate" as described under "Description of the Purchase Contracts—Early Settlement Upon a Fundamental Change." Upon early settlement at the holder's election in connection with a fundamental change of a purchase contract that is a component of a Unit, the corresponding amortizing note will remain outstanding and beneficially owned by or registered in the name of, as the case may be, the holder who elected to settle the related purchase contract early upon such fundamental change.
Early Mandatory Settlement at Our Election	On or after January 30, 2020, we may elect to settle all, but not less than all, outstanding purchase contracts early at the "early mandatory settlement rate" (as described under "Description of the Purchase Contracts — Early Mandatory Settlement at Our Election") on a date fixed by us upon not less than five business days' notice (the "early mandatory settlement date"). The "early mandatory settlement rate" will be the maximum settlement rate as of the "notice date" (as defined under "Description of the Purchase Contracts—Early Mandatory Settlement at Our Election"), unless the closing price per share of our common stock for at least 20 trading days (whether or not consecutive), including the trading day immediately preceding the notice date in a period of 30 consecutive trading days ending on, and including, the trading day immediately preceding the notice date exceeds 130% of the threshold appreciation price in effect on each such trading day, in which case the "early mandatory settlement rate" will be the minimum settlement rate as of the notice date. If we elect to settle all the purchase contracts early, you will have the right to require us to repurchase your amortizing notes on the repurchase date and at the repurchase price as described under "Description of the Amortizing Notes—Repurchase of Amortizing Notes at the Option of the Holder."

Acquisition Termination Redemption	If the closing of the Acquisition has not occurred on or prior to April 22, 2020, or if, prior to such date, the Acquisition Agreement is terminated, we may elect to redeem all, but not less than all, of the outstanding purchase contracts (an "acquisition termination redemption"), for the applicable redemption amount, as described below under "Description of the Purchase Contracts—Acquisition Termination Redemption," by delivering notice during the five business day period immediately following the earlier of (x) April 22, 2020 if the closing the Acquisition has not occurred on or prior to such date and (y) the date on which the Acquisition Agreement is terminated. If the "acquisition termination stock price" (as defined under "Description of the Purchase Contracts—Acquisition Termination Redemption") is equal to or less than the reference price, the redemption amount will be an amount of cash as described under "Description of the Purchase Contracts—Acquisition Termination Redemption." Otherwise, the redemption amount will be a number of shares of our common stock equal to the acquisition redemption rate, calculated in the manner described under "Description of the Purchase Contracts—Acquisition Termination Redemption;" *provided, however*, that we may elect to pay cash in lieu of delivering any or all of such shares in an amount equal to such number of shares *multiplied by* the redemption market value thereof. The "redemption market value" means the arithmetic average of the VWAPs of our common stock for the 20 consecutive trading day period beginning on, and including, the 21st scheduled trading day immediately preceding the scheduled acquisition redemption settlement date. In the event of an acquisition termination redemption, you will have the right to require us to repurchase your amortizing notes, as described under "Description of the Amortizing Notes—Repurchase of Amortizing Notes at the Option of the Holder."
The Amortizing Notes	
Issuer	Aqua America, Inc., a Pennsylvania corporation
Initial Principal Amount of Each Amortizing Note	$8.62909
Installment Payments	Each installment payment of $0.75000 per amortizing note (except for the July 30, 2019 installment payment, which will be $0.80833 per amortizing note) will be paid in cash and will constitute a partial repayment of principal and a payment of interest, computed at an annual rate of 3.00%. Interest will be calculated on the basis of a 360-day year consisting of twelve 30-day months. Payments will be applied first to the interest due and payable and then to the reduction of the unpaid principal amount, allocated as set forth on the amortization schedule set forth under "Description of the Amortizing Notes—Amortization Schedule."

Installment Payment Dates	Each January 30, April 30, July 30 and October 30, commencing on July 30, 2019, with a final installment payment date of April 30, 2022.
Ranking	The amortizing notes will be our general unsecured senior obligations and will rank equally with all of our other existing and future unsecured senior indebtedness from time to time outstanding. See "Description of the Amortizing Notes—Ranking" in this prospectus supplement. At December 31, 2018, on a pro forma basis after giving effect to the Transactions: • Aqua America would have had approximately $2,096 million of indebtedness outstanding, of which none would have been secured indebtedness; and • our subsidiaries (including LDC and its subsidiaries) would have had a total of approximately $5,856 million of outstanding liabilities, including indebtedness, owed to non-affiliated third parties.
Repurchase of Amortizing Notes at the Option of the Holder	If we elect to settle the purchase contracts early or in the event of an acquisition termination redemption, holders will have the right to require us to repurchase their amortizing notes for cash at the repurchase price as described under "Description of the Amortizing Notes—Repurchase of Amortizing Notes at the Option of the Holder."
Sinking Fund	None.
Trustee	U.S. Bank N.A.

Immediately after the consummation of the Common Stock Offering we will have 210,587,288 shares of common stock (or 215,461,638 shares if the underwriters for the Common Stock Offering exercise their option to purchase additional shares in full) issued and outstanding. The number of shares of common stock to be outstanding immediately after the Common Stock Offering is based on 178,091,621 shares of common stock outstanding as of December 31, 2018, and does not reflect:

- 21,661,095 shares of our common stock issuable upon completion of the Private Placement;
- 17,330,400 shares of our common stock (or 19,929,960 shares of our common stock if the underwriters exercise their option with respect to this offering in full) issuable upon settlement of the purchase contracts, assuming the maximum number of shares issuable upon automatic settlement of such purchase contracts that are components of the Units offered hereby; and
- 18,738,059 shares of our common stock reserved for issuance upon exercise of stock options outstanding, upon vesting of our time based restricted stock units, upon vesting of our performance based restricted stock units or performance share units, as well as additional shares we may issue under our dividend reinvestment program, employee stock purchase plan or 401(k) savings plans.

RISK FACTORS

Investing in the Units involves risks. You should review and carefully consider the risks, uncertainties and other factors described below and all of the information included elsewhere in this prospectus supplement, the accompanying prospectus, any free writing prospectus we may provide to you in connection with this offering and the documents incorporated by reference herein and therein before deciding to invest in the Units. We also urge you to consider carefully the risks, uncertainties and other factors set forth under the headings "Forward-Looking Statements" and "Market and Industry Data." However, additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our business, operations, financial condition and financial results and the value of the Units.

Risks Related to Our Business

For a discussion of specific risks related to our business, operations, financial condition and financial results, including certain risks related to the Acquisition, please see the "Business," Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" sections in our Annual Report on Form 10-K for our fiscal year ended December 31, 2018, as updated by our annual, quarterly and other reports and documents we file with the SEC that are incorporated by reference in this prospectus supplement and the accompanying prospectus. See "Where You Can Find Additional Information; Incorporation of Certain Documents by Reference," in this prospectus supplement. In addition, we provide the following risk factor.

Changes in our earnings may differ from changes in our rate base.

Our business is capital intensive and requires significant capital investments for additions to or replacement of property, plant and equipment. These capital investments create assets that are used and useful in providing regulated utility service, and as a result, increase our rate base, on which we generate earnings through the regulatory process. Changes in our reported earnings, however, may differ from changes in our rate base in a given period due to several factors, including rate case timing and the terms of such rate cases; over-or under-earnings in a given period due to changes in operating costs; the effects of tax rates or tax treatment of capital investments, including the effect of repair tax; capital expenditures that are not eligible for DSIC between rate cases; and acquisitions which have not yet been included in rate base. We anticipate that we may experience periods in which growth in earnings is less than growth in rate base; such differences may be significant and may persist over multiple reporting periods.

Risks Related to Peoples's Business

For a discussion of specific risks related to Peoples's business, please see "Risk Factors related to Peoples" in our Current Report on Form 8-K/A filed on April 15, 2019 and incorporated by reference in this prospectus supplement and the accompanying prospectus. These risks, uncertainties and other factors are not the only ones that Peoples faces. Additional risks, uncertainties and other factors not presently known to us or that we currently deem immaterial may also impair Peoples's business, operations, financial condition and financial results. Any of these risks could, if the Acquisition is consummated, impair the combined company's business, operations, financial condition and financial results or could otherwise adversely impact our investment in Peoples, in which case you may lose all or part of your investment in the Units.

Risks Related to the Acquisition and the Financing Transactions

Aqua America expects to incur significant additional indebtedness in connection with the Acquisition. As a result, it may be more difficult for Aqua America to pay or refinance its debts or take other actions, and Aqua America may need to divert cash to fund debt service payments.

As discussed herein, Aqua America expects to incur significant additional indebtedness to finance the Cash Acquisition Consideration and the Company Debt Refinancing and pay related transaction costs. Additionally, in connection with the Acquisition, Aqua America currently intends to assume approximately $1,370 million of Peoples's indebtedness. Moreover, although Aqua America currently plans to fund a significant portion of the Cash Acquisition Consideration and the Company Debt Refinancing through the sales of its equity securities, if and to the extent that such sales are not completed or are completed for less aggregate net proceeds than anticipated, the amount of indebtedness it will incur to finance the Acquisition, the Company Debt Refinancing and associated transactions costs would increase, perhaps substantially. The increase in Aqua America's debt service obligations resulting from additional indebtedness could have a material adverse effect on the results of operations, financial condition and prospects of the combined company.

Aqua America's increased indebtedness could also:

- make it more difficult and/or costly for Aqua America to pay or refinance its debts as they become due, particularly during adverse economic and industry conditions, because a decrease in revenues or increase in costs could cause cash flow from operations to be insufficient to make scheduled debt service payments;
- limit Aqua America's flexibility to pursue other strategic opportunities or react to changes in its business and the industry sectors in which it operates and, consequently, put Aqua America at a competitive disadvantage to its competitors that have less debt;
- require a substantial portion of Aqua America's available cash to be used for debt service payments, thereby reducing the availability of its cash to fund working capital, capital expenditures, development projects, acquisitions, dividend payments and other general corporate purposes, which could harm Aqua America's prospects for growth and the market price of our common stock, Units and debt securities, among other things;
- result in a downgrade in the credit ratings on Aqua America's indebtedness, which could limit Aqua America's ability to borrow additional funds on favorable terms or at all (including in order to refinance the Bridge Facility (if drawn) and/or its other debt), increase the interest rates under its credit facilities and under any new indebtedness it may incur, and reduce the trading prices of its outstanding debt securities, common stock and Units (see "Summary Information—Recent Developments—Financing Transactions");
- make it more difficult for Aqua America to raise capital to fund working capital, make capital expenditures, pay dividends, pursue strategic initiatives or for other purposes;
- result in higher interest expense, which could be further increased in the event of increases in interest rates on Aqua America's current or future borrowings subject to variable rates of interest; and
- require that additional materially adverse terms, conditions or covenants be placed on Aqua America under its debt instruments, which covenants might include, for example, limitations on additional borrowings and specific restrictions on uses of its assets, as well as prohibitions or limitations on its ability to create liens, pay dividends, receive distributions from its subsidiaries, redeem or repurchase its stock or make investments, any of which could hinder its access to capital markets and limit or delay its ability to carry out its capital expenditure program or otherwise limit its flexibility in the conduct of its business and make it more vulnerable to economic downturns and adverse competitive and industry conditions.

It is possible that the Notes Offering will not be completed or, if completed, will generate less aggregate net proceeds than anticipated, which is a scenario in which we may incur borrowings under the Bridge Facility and/ or incur borrowings under the Revolving Credit Facility. It is also possible that this offering, the Common Stock Offering and the Private Placement will not be completed or, if completed, will generate less aggregate net proceeds than anticipated, in which case we intend to fund any shortfall through the issuance of additional shares of common stock or equity-linked securities prior to the consummation of the Acquisition, but may ultimately fund any shortfall with additional debt financings (which could include borrowings under the Bridge Facility) and/or borrowings under the Revolving Credit Facility. Any such borrowings under the Bridge Facility or the Revolving Credit Facility may cause us to incur significantly higher borrowing costs than the contemplated long-term financing, which would increase the overall cost of the Acquisition and could harm our business, financial condition, results of operations, and cash flows. Any borrowings under the Bridge Facility will mature 364 days after they are incurred. We may not be able to refinance borrowings under the Bridge Facility on favorable terms or at all before their maturity. In addition, the interest rate applicable to borrowings under the Bridge Facility will increase at the end of each three-month period after the borrowing date. Accordingly, we may incur additional interest expense if we are unable to refinance borrowings under the Bridge Facility before the interest rate increases take effect.

The increased indebtedness in connection with the Acquisition could cause us to place more reliance on cash flow from operations to pay principal and interest on debt and to satisfy our other obligations. Based on the current and expected results of operations and financial condition of Aqua America and its subsidiaries and the currently anticipated financing structure for the Acquisition, Aqua America believes that its cash flow from operations, together with the proceeds from borrowings, issuances of equity and debt securities in the capital markets, and equity sales will generate sufficient cash on a consolidated basis to make all of the principal and interest payments when such payments are due under Aqua America's and its current subsidiaries' existing credit facilities, indentures and other instruments governing their outstanding indebtedness, under the indebtedness anticipated to be incurred to fund the Cash Acquisition Consideration and the Company Debt Refinancing and under the indebtedness of Peoples anticipated to be assumed as a result of the Acquisition. However, Aqua America's expectation is based upon numerous estimates and assumptions and is subject to numerous uncertainties. LDC and its subsidiaries will not guarantee any indebtedness of Aqua America or any of its other subsidiaries, nor will any of them have any obligation to provide funds (nor will we have any ability to require them to provide funds), whether in the form of dividends, loans or otherwise, to enable Aqua America to pay dividends on its common stock or to enable Aqua America and its other subsidiaries to make required debt service payments or meet its other cash needs (including those described above under "Summary Information—Recent Developments"). In addition, as described above in "—Aqua America's ability to pay dividends and to meet its debt obligations largely depends on the performance of its subsidiaries and the ability to utilize the cash flows from those subsidiaries," certain of LDC and its subsidiaries may face limitations on their ability to provide funds to Aqua America. As a result, Aqua America may substantially increase its debt services obligations in anticipation of the Acquisition without any assurance that Aqua America will receive any cash from LDC or any of its subsidiaries to assist Aqua America in servicing its indebtedness, paying dividends on its common stock or meetings its other cash needs. Even if the Acquisition is consummated, Aqua America may not have access to the cash or other assets of certain of LDC and its subsidiaries.

In order to maintain its credit ratings, Aqua America may consider it appropriate to reduce the amount of its indebtedness outstanding following the Acquisition. Aqua America may seek to reduce this indebtedness with the proceeds from the issuance of additional shares of common stock and, possibly, other equity-linked securities, cash on hand and proceeds from asset sales, which may dilute the voting rights and economic interests of holders of Aqua America's common stock. However, the ability of Aqua America to raise additional equity financing after completion of the Acquisition will be subject to market conditions and a number of other risks and uncertainties, including whether the results of operations of the combined company meet the expectations of investors and securities analysts. Aqua America may not be able to issue additional shares of its common stock or other equity securities after the Acquisition on terms that it considers acceptable or at all, and Aqua America may not be able to reduce the amount of its outstanding indebtedness after the Acquisition, should it elect to do so, to a level that permits it to maintain its investment grade credit ratings.

The unaudited pro forma consolidated combined financial information and other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus are presented for illustrative purposes only and do not purport to represent what the financial position or results of operations of the combined company would have been had the Transactions been completed on the dates assumed for purposes of that information, nor do they represent the actual financial position or results of operations of the combined company following the Transactions, if consummated.

The unaudited pro forma consolidated combined financial information and other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus are presented for illustrative purposes only, are based on numerous adjustments, assumptions and estimates, are subject to numerous other uncertainties and do not purport to reflect what the combined company's financial position or results of operations would have been had the Transactions been completed as of the dates assumed for purposes of that information, nor do they reflect the financial position or results of operations of the combined company following the Transactions, if consummated. Such unaudited pro forma consolidated combined financial information and certain other adjusted information reflects the assumptions of our management at the time that such information was initially prepared, and therefore does not reflect the amount of proceeds we will receive from, and certain pricing and other terms of, each of the Debt Financings, the Common Stock Offering, the Private Placement and this offering, the number of shares of our common stock sold in the Common Stock Offering and in the Private Placement and the number of Units sold in this offering, and the actual amount of costs and expenses and underwriting discounts we will pay in connection with the Transactions. Therefore, actual amounts, including the actual amount of net proceeds from the respective Financing Transactions, may differ, perhaps substantially, from the assumed amounts set forth in the unaudited pro forma consolidated combined financial information and the other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus.

The unaudited pro forma consolidated combined financial information and other adjusted information has also been prepared on the assumption that the Transactions will be completed on the terms and in accordance with the assumptions set forth in such unaudited pro forma consolidated combined financial information or such adjusted information, as applicable. Any changes relative to these assumptions, including, without limitation, any changes in the assumed types or sizes of the Financing Transactions, the assumed interest on debt we will issue or otherwise incur, the assumed number of shares of common stock or Units we issue, the assumed amount of our Transactions costs, the assumed amounts of net proceeds we receive from the respective Financing Transactions would result in a change relative to such unaudited pro forma consolidated combined financial information or such other adjusted information, which could be material. In addition, none of the Financing Transactions (other than the Private Placement) will be contingent upon completion of any of the other Financing Transactions, and it is possible that one or more of the Financing Transactions will not be completed. Likewise, because certain of the Financing Transactions are not contingent upon completion of the Acquisition, it is possible that this offering and certain of the other Financing Transactions may be completed even if the Acquisition is not consummated, in which case we may be required to redeem or otherwise repay certain indebtedness or debt securities we may issue in the Debt Financings, and we may elect to redeem all of the purchase contracts (if issued), in which case holders of Units would have the right to require us to repurchase their outstanding amortizing notes. It is also possible that this offering, the Common Stock Offering, the Private Placement and the Notes Offering, if completed, will not generate the anticipated amount of net proceeds, in which case we may draw upon the Bridge Commitment and/ or incur borrowings under our Revolving Credit Facility and/or issue additional shares of common stock or equity-linked securities. In any event, our and Peoples's actual financial positions and results of operations prior to the Acquisition and those of the combined company following the Acquisition, if consummated, may not be consistent with, or evident from, the unaudited pro forma consolidated combined financial information or other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus.

For purposes of the unaudited pro forma consolidated combined financial information, the Cash Acquisition Consideration has been preliminarily allocated to the identifiable assets acquired and liabilities assumed based on limited information presently available to estimate fair values. The Cash Acquisition Consideration will be

allocated among the relative fair values of the identifiable assets acquired and liabilities assumed based on their estimated fair values as of the date of the Acquisition. The relative fair values of the assets acquired and liabilities assumed are estimates, which are subject to change pending further review. The actual amounts recorded at the completion of the Acquisition, if completed, may differ materially from the information presented in the unaudited pro forma consolidated combined financial information.

Although the unaudited pro forma consolidated combined financial information and other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus include sensitivity analyses that are intended to assist you in quantifying the impact of changes in certain of the assumptions used in preparing such information, those sensitivity analyses reflect the pro forma impact of only a limited number of those assumptions and therefore do not allow you to quantify the impact of changes in certain other assumptions made in calculating this information. Changes in such other assumptions may have a material impact on such information. Likewise, the sensitivity analyses we have provided do not necessarily address the impact of all possible changes in the assumptions contemplated by such analyses. We do not intend to provide you with updated unaudited pro forma consolidated combined financial information or other adjusted information that reflects the actual size and terms of the Financing Transactions (other than to disclose the actual size and pricing terms of this offering and the Common Stock Offering in one or more free writing prospectuses) prior to the time you will be required to make a decision whether or not to invest in this offering.

As a result of the foregoing, investors should not place undue reliance on unaudited pro forma consolidated combined financial information and other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus.

We may not complete the Acquisition. If we incur indebtedness or issue debt securities to finance a portion of the Acquisition, and we do not complete the Acquisition on or before a specified date or if other specified events occur, we may be required to redeem or repay any such indebtedness or debt securities. We may not have the financial resources necessary to effect such redemption or repayment. It is possible that our failure to complete Acquisition may have a material adverse effect on our financial condition and the market price of the Units and our common stock.

The Acquisition is subject to a number of customary closing conditions. See "Summary Information—Recent Developments—Proposed Peoples Gas Acquisition." Satisfaction of many of these conditions is beyond our control. If these conditions are not satisfied or waived, the Acquisition will not be completed. As a result, the Acquisition may not close as scheduled or at all. Among other conditions, the closing of the Acquisition is subject to the receipt of regulatory approval by the Pennsylvania Public Utility Commission. Whether through a settlement agreement or through a litigated proceeding, we may be required to agree to certain actions, undertakings, terms, or other measures, including those that may require increased capital or other expenditures by the Company. Any additional items we agree to in order to resolve this matter may have an adverse effect on our business, financial condition or results of operations. The closing of this offering is not conditioned on, and is expected to be consummated before, the closing of the Acquisition. Accordingly, if you decide to purchase Units in this offering, you should be willing to do so whether or not we complete the Acquisition.

We expect to incur a substantial amount of additional indebtedness as part of the Financing Transactions. See "Summary Information—Recent Developments—Financing Transactions" and "Use of Proceeds." To the extent we incur indebtedness or issue debt securities as part of the Financing Transactions and we do not complete the Acquisition by a specified date or if certain other specified events, such as termination of the Acquisition Agreement, occur, we expect that we will be required to redeem or repay some or all of such indebtedness and debt securities and that the redemption or repayment price will include a premium.

We will not be required to deposit the proceeds from the Financing Transactions into an escrow account pending completion of the Acquisition or to grant any security interest or other lien on those proceeds to secure

any required repayment or redemption of any Financing Transactions. If we are required to redeem or repay any indebtedness or debt securities issued in the Financing Transactions under the circumstances described above, our ability to pay the redemption or repayment price may be limited by our financial resources at the time and the terms of our debt instruments or other instruments and agreements and it is possible that we will not have sufficient financial resources available to satisfy our obligation to effect such redemption or repayment. Any failure to pay the mandatory redemption or repayment price of any Financing Transactions as and when required could have a material adverse effect on our business, results of operations and financial condition and the market price of our securities, including the Units, our common stock, or any indebtedness incurred or other securities issued as part of the Financing Transactions. If the Acquisition is not completed by April 22, 2020 or the Acquisition Agreement is terminated prior to such date, we will have the option, but not the obligation, to redeem all, but not less than all, of the outstanding purchase contracts. If we elect to redeem the purchase contracts, holders will have the right to require us to repurchase their amortizing notes. It is possible that our failure to complete the Acquisition, or the expenditure of our funds to redeem or repay any securities issued or borrowings incurred in the other Financing Transactions, may have a material adverse effect on the market price of the Units and our common stock.

Risks Related to the Units, the Separate Purchase Contracts, the Separate Amortizing Notes and our Common Stock

If the closing of the Acquisition has not occurred on or prior to April 22, 2020, or if, prior to such date, the Acquisition Agreement is terminated, we may redeem the purchase contracts, in which case holders of Units would have the right to require us to repurchase the amortizing notes, for an amount of cash and/or a number of shares of our common stock (depending on the price of our common stock at the time of redemption) with a value that may not adequately compensate you for any lost option value.

The Acquisition may not be consummated. See "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018 and "—Risks Related to the Acquisition and the Financing Transactions" herein. If the closing of the Acquisition has not occurred on or prior to April 22, 2020, or if, prior to such date, the Acquisition Agreement is terminated, we may elect to redeem all, but not less than all, of the outstanding purchase contracts by delivering notice during the five business day period immediately following the earlier of (x) the April 22, 2020 if the closing of the Acquisition has not occurred on prior to such date and (y) the date on which the Acquisition Agreement is terminated. We will pay or deliver, as the case may be, a redemption amount to be determined based on the price of our common stock at that time in cash or in shares of our common stock in accordance with the terms of the purchase contracts (as described under "Description of the Purchase Contracts—Acquisition Termination Redemption"). If we elect to redeem the purchase contracts, the holders thereof would have the right to require us to repurchase the amortizing notes at the relevant repurchase price set forth under "Description of the Amortizing Notes—Repurchase of Amortizing Notes at the Option of the Holder." The redemption amount that you receive upon an acquisition termination redemption may not adequately compensate you for any lost option value of the purchase contracts. In addition, if the Acquisition is not consummated, the net proceeds from this offering and of the Common Stock Offering, if completed, will not be used to consummate the Acquisition. Instead, we intend to use the net proceeds from this offering and the Common Stock Offering, after payment of any cash redemption amount and/or repurchase price (if applicable), for general corporate purposes, which may include the Company Debt Refinancing, the redemption of securities issued in connection with the other Financing Transactions, repurchases of our common stock, debt repayment, capital expenditures and investments.

Upon redemption of the purchase contracts included in Units or separate purchase contracts upon an acquisition termination redemption, our common stock may incur immediate net tangible book value dilution on a per share basis. In addition, if the purchase contracts are redeemed for cash and the holders thereof require us to repurchase the amortizing notes, we would experience reduced liquidity, which could limit our flexibility in the conduct of our business and make us more vulnerable to economic downturns and adverse competitive and industry conditions.

You will bear the risk that the market value of our common stock may decline.

The purchase contracts, pursuant to which we will deliver to you shares of our common stock, are components of the Units. The number of shares of common stock that you will receive upon settlement of a purchase contract on the mandatory settlement date (subject to earlier settlement or redemption), whether as a component of a Unit or a separate purchase contract, will depend upon the applicable market value, which is equal to the arithmetic average of the VWAP per share of our common stock on each of the 20 consecutive trading day period beginning on, and including, the 21st scheduled trading day immediately preceding April 30, 2022. There can be no assurance that the market value of the common stock received by you will be greater than or equal to the reference price of approximately $34.62. If the applicable market value of our common stock is less than the reference price, then the market value of the common stock issued to you on the mandatory settlement date (assuming that the market value is the same as the applicable market value of the common stock) will be less than the effective price per share paid by you for such common stock on the date of issuance of the Units. Furthermore, because we will in no event deliver more than 1.4442 shares (subject to adjustment as described herein) upon settlement of a purchase contract, the market value of the common stock delivered to you upon any early settlement may be less than the effective price per share paid to you for such common stock on the date of the issuance of the Units. Therefore, you assume the entire risk that the market value of our common stock may decline before the mandatory settlement date, early settlement date, fundamental change early settlement date, acquisition redemption settlement date or early mandatory settlement date, as applicable. Any decline in the market value of our common stock may be substantial.

The opportunity for equity appreciation provided by an investment in the Units is less than that provided by a direct investment in our common stock.

The aggregate market value of our common stock delivered to you upon settlement of a purchase contract on the mandatory settlement date generally will exceed the $50.00 stated amount of each Unit only if the applicable market value of our common stock exceeds the threshold appreciation price. Therefore, during the period prior to the mandatory settlement date, an investment in a Unit affords less opportunity for equity appreciation than a direct investment in our common stock. If the applicable market value exceeds the reference price but is less than the threshold appreciation price, you will realize no equity appreciation on our common stock above the reference price. Furthermore, if the applicable market value exceeds the threshold appreciation price, you would receive only a portion of the appreciation in the market value of the shares of our common stock you would have received had you purchased shares of common stock with $50.00 at the public offering price in the Common Stock Offering. See “Description of the Purchase Contracts—Delivery of Common Stock” for a table showing the number of shares of common stock that you would receive at various applicable market values.

We may not be able to settle or redeem your purchase contracts and deliver shares of our common stock, or make payments on the amortizing notes or repurchase the amortizing notes, in the event that we file for bankruptcy.

Pursuant to the terms of the purchase contract agreement, your purchase contracts will automatically accelerate upon the occurrence of specified events of bankruptcy, insolvency or reorganization with respect to us.

A bankruptcy court may prevent us from delivering our common stock to you in settlement or redemption of your purchase contracts. In such circumstances or if for any other reason the accelerated purchase contracts are not settled by the delivery of common stock, your resulting claim for damages against us following such acceleration will rank pari passu with the claims of holders of our common stock in the relevant bankruptcy proceeding. As such, to the extent we fail to deliver common stock to you upon such an acceleration, you will only be able to recover damages to the extent holders of our common stock receive any recovery. See “Description of the Purchase Contracts—Consequences of Bankruptcy.”

In addition, with respect to the amortizing notes, bankruptcy law and bankruptcy-related court orders generally prohibit the payment of pre-bankruptcy debt by a company that has commenced a bankruptcy case while the case is pending. If we become a debtor in a bankruptcy case, so long as the case was pending, you would likely not receive timely installment payments under, or, if you exercised your right to require repurchase following an acquisition termination redemption or early mandatory settlement, receive any repurchase price on, the amortizing notes.

The Units are not protected by restrictive covenants.

Neither the purchase contracts nor the indenture contains any financial or operating covenants or restrictions on the payments of dividends, the incurrence of indebtedness or the issuance or repurchase of securities by us or any of our subsidiaries. Neither the purchase contracts nor the indenture contains any covenants or other provisions to afford protection to holders of the purchase contracts or the amortizing notes in the event of a fundamental change involving Aqua America, Inc. except, with respect to the purchase contracts, to the extent described under "Description of the Units—Early Settlement Upon a Fundamental Change."

The amortizing notes will be subject to the prior claims of any secured creditors, and if a default occurs, we may not have sufficient funds to fulfill our obligations under the amortizing notes.

The amortizing notes are unsecured obligations, ranking equally with our other senior unsecured indebtedness and effectively junior to any existing and future secured indebtedness we may incur. The indenture that will govern the amortizing notes will not restrict our or our subsidiaries' ability to incur additional debt (including secured debt) and, if we do incur additional secured debt, our assets securing any such indebtedness will be subject to prior claims by our secured creditors. In the event of the bankruptcy, insolvency, liquidation, reorganization, dissolution or other winding up of the Company, our assets that secure debt will be available to pay obligations on the amortizing notes only after all debt secured by those assets has been repaid in full. Holders of the amortizing notes will participate in any remaining assets ratably with all of the Company's other unsecured and unsubordinated creditors, including trade creditors If there are not sufficient assets remaining to pay all creditors, then all or a portion of the amortizing notes then outstanding would remain unpaid. Additionally, if any portion of the amount payable on the amortizing notes upon acceleration is considered by a court to be unearned interest, the court could disallow recovery of any such portion. As of December 31, 2018, on a pro forma basis after giving effect to the Transactions, the Company would have had no secured indebtedness.

The amortizing notes are structurally subordinated to the liabilities of our subsidiaries, which will include the liabilities of Peoples and its subsidiaries if the Acquisition is consummated.

The amortizing notes are our obligations exclusively and not of any of our subsidiaries. Therefore, the amortizing notes will be structurally subordinated to all existing and future indebtedness and other liabilities of our subsidiaries (including, upon consummation of the Acquisition, indebtedness and other liabilities of LDC and its subsidiaries that we assume in connection with the Acquisition). Any right of the Company to receive assets of any of its subsidiaries upon the liquidation or reorganization thereof, and the consequent right of the holders of the amortizing notes to receive the proceeds of those assets, will be effectively subordinated to the claims of that subsidiary's creditors, except to the extent that the Company is itself recognized as a creditor of such subsidiary. If the Company is recognized as a creditor of such subsidiary, its claims would still be subordinate in right of payment to any security interest in the assets of that subsidiary and any indebtedness of that subsidiary senior to that held by the Company. At December 31, 2018, on a pro forma basis after giving effect to the Transactions, (i) Aqua America, Inc. would have had approximately $2,096 million of indebtedness outstanding, of which none would have been secured indebtedness and (ii) our subsidiaries (including LDC and its subsidiaries) would have had a total of approximately $5,856 million of outstanding liabilities, including indebtedness, owed to non-affiliated third parties.

Aqua America's ability to pay dividends and to meet its debt obligations largely depends on the performance of its subsidiaries and the ability to utilize the cash flows from those subsidiaries.

Aqua America is a holding company substantially all of whose assets are owned by its subsidiaries and substantially all of whose operations are conducted through its subsidiaries. Aqua America's ability to pay dividends and meet its debt and other obligations depends almost entirely on cash flows from its subsidiaries and, in the short term, its ability to raise capital from external sources. In the long term, cash flows from its subsidiaries depend on their ability to generate operating cash flows in excess of their own expenditures, common and preferred stock dividends (if any), and debt or other obligations. Its subsidiaries are separate and distinct legal entities that are not obligated to pay dividends or make loans or distributions to Aqua America (whether to enable Aqua America to pay dividends on its common stock, to pay principal and interest on its debt, to settle, repurchase or redeem its debt (including the amortizing notes) or other securities (including the purchase contracts), or to satisfy its other obligations). In addition, notwithstanding its controlling interest in such subsidiaries, many of them are limited in their ability to pay dividends or make loans or distributions to Aqua America, including, without limitation, as a result of legislation, regulation, court order, contractual restrictions and other restrictions or in times of financial distress. Likewise, certain of LDC and its subsidiaries face similar restrictions that, if the Acquisition is consummated, will limit their ability to pay dividends or make loans or distributions to Aqua America. As a result, the Company may not be able to cause its subsidiaries (including, following the Acquisition, LDC and its subsidiaries) and other entities to distribute funds or provide loans sufficient to enable it to pay dividends and meet its debt and other obligations.

The trading prices for the Units, the purchase contracts and the amortizing notes will be directly affected by the trading prices for our common stock, the general level of interest rates and our credit quality, each of which is impossible to predict.

It is impossible to predict whether the prices of our common stock, interest rates or our credit quality will rise or fall. The market price for our common stock has historically experienced, and may continue to experience, volatility, which could materially reduce our stock price and cause the market price of the Units to decline. In addition, the sale or issuance of substantial amounts of our common stock, or the perception that such sales or issuances could occur, could adversely affect the market price of our common stock and/or the Units. Shares of our common stock will be issuable upon settlement or redemption of the purchase contracts and the number of shares may be substantial. The settlement rates for the purchase contracts will be subject to certain anti-dilution adjustments that could increase, potentially significantly, the number of shares of our common stock issuable upon such settlement. Similarly, although CPPIB is currently subject to restrictions on resale, if the Private Placement is completed, a significant portion of our common stock will be available for resale into the market by a small number of investors following the expiration of such restrictions. The issuance or sale of shares, or the perception that such issuances or sales could occur, could adversely affect the market price of our common stock, even if our business is doing well. Any of the foregoing may also impair our ability to raise additional capital through the sale of our equity securities.

The market price of our common stock may be influenced by many factors, some of which are beyond our control, including the factors discussed above under "Forward-Looking Statements" and "Market and Industry Data" or elsewhere in this Risk Factors section and the following:

- actual or anticipated fluctuations in our operating results or our competitors' or peers' operating results;
- actions by applicable regulatory authorities, including the Pennsylvania Public Utility Commission;
- announcements by us, our competitors or our partners of significant contracts, acquisitions, divestitures or strategic investments;
- our growth rate and our competitors' or peers' growth rates;

- the financial markets and general economic conditions;
- changes in stock market analyst recommendations regarding us, our competitors, our peers or the energy infrastructure, gas and electricity services industries generally, or lack of analyst coverage of our common stock;
- sales of our common stock by our executive officers, directors and significant shareholders or sales of substantial amounts of our common stock or securities convertible into or exchangeable for our common stock;
- changes in the amount of our common stock dividends per share, the common stock dividends per share paid by our competitors and interest rates; and
- changes in tax laws and regulations.

The market for our common stock likely will influence, and be influenced by, any market that develops for the Units or the separate purchase contracts. For example, investors' anticipation of the distribution into the market of the additional shares of common stock issuable upon settlement of the purchase contracts could depress the price of our common stock and increase the volatility of the common stock price, which could in turn depress the price of the Units or the separate purchase contracts. The price of our common stock also could be affected by possible sales of such common stock by investors who view the Units as a more attractive means of equity participation in us and by hedging or arbitrage trading activity that is likely to develop involving the Units, separate purchase contracts and the common stock. Such hedging or arbitrage activity could, in turn, affect the trading prices of the Units, the separate purchase contracts and the common stock.

In addition, in general, as market interest rates rise, notes (such as the amortizing notes) bearing interest at a fixed rate generally decline in value because the premium, if any, over market interest rates will decline. Consequently, if you purchase Units and market interest rates increase, the market value of the amortizing notes forming a portion of the Units may decline. We cannot predict the future level of market interest rates.

Regulatory actions and other events may adversely affect the trading price and liquidity of the Units.

We expect that many investors in, and potential purchasers of, the Units will employ, or seek to employ, an equity-linked arbitrage strategy with respect to the Units. Investors would typically implement such a strategy by selling short the common stock underlying the Units and dynamically adjusting their short position while continuing to hold the Units. Investors may also implement this type of strategy by entering into swaps on our common stock in lieu of or in addition to short selling the common stock. As a result, any specific rules regulating equity swaps or short selling of securities or other governmental action that interferes with the ability of market participants to effect short sales or equity swaps with respect to our common stock would adversely affect the ability of investors in, or potential purchasers of, the Units to conduct the arbitrage strategy that we believe they will employ, or seek to employ, with respect to the Units. This could, in turn, adversely affect the trading price and liquidity of the Units.

The SEC and other regulatory and self-regulatory authorities have implemented various rules and taken certain actions, and may in the future adopt additional rules and take other actions, that may impact those engaging in short selling activity involving equity securities (including our common stock). Such rules and actions include Rule 201 of SEC Regulation SHO, the adoption by the Financial Industry Regulatory Authority, Inc. and the national securities exchanges of a "Limit Up-Limit Down" program, the imposition of market-wide circuit breakers that halt trading of securities for certain periods following specific market declines, and the implementation of certain regulatory reforms required by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. Any governmental or regulatory action that restricts the ability of investors in, or potential

purchasers of, the Units to effect short sales of our common stock, borrow our common stock or enter into swaps on our common stock could adversely affect the trading price and the liquidity of the Units.

In addition, if investors and potential purchasers seeking to employ an equity-linked arbitrage strategy are unable to borrow or enter into swaps on our common stock, in each case, on commercially reasonable terms, the trading price and liquidity of the Units may be adversely affected.

You may receive shares of common stock upon settlement or redemption of the purchase contracts that are lower in value than the price of the common stock just prior to the mandatory settlement date or acquisition redemption settlement date, as the case may be.

Because the applicable market value of the common stock is determined over (i) the 20 consecutive trading day period beginning on, and including, the 21st scheduled trading day immediately preceding April 30, 2022, in the case of settlement on the mandatory settlement date, or (ii) the five business day period ending on, and including, the trading day immediately preceding April 22, 2020 (or, if prior to such date, the Acquisition Agreement is terminated, the five business day period immediately following such date of termination), in the case of an acquisition termination redemption, the number of shares of common stock delivered for each purchase contract may, on the mandatory settlement date or the acquisition redemption settlement date, as the case may be, be greater than or less than the number of shares that would have been delivered based on the closing price (or VWAP) per share of the common stock on the last trading day in the related 20 or five trading day period. In addition, you will bear the risk of fluctuations in the market price of the shares of common stock deliverable upon settlement of the purchase contracts between the end of such period and the date such shares are delivered.

If you elect to settle your purchase contracts early, you may not receive the same return on your investment as purchasers whose purchase contracts are settled on the mandatory settlement date.

Holders of the Units or separate purchase contracts have the option to settle their purchase contracts early at any time beginning on, and including, the business day immediately following the date of initial issuance of the Units until the second scheduled trading day immediately preceding April 30, 2022. However, if you settle your purchase contracts prior to the second scheduled trading day immediately preceding April 30, 2022, you will receive for each purchase contract a number of shares of common stock equal to the minimum settlement rate, regardless of the current market value of our common stock, unless you elect to settle your purchase contracts early in connection with a fundamental change, in which case you will be entitled to settle your purchase contracts at the fundamental change early settlement rate, which may be greater than the minimum settlement rate. In either case, you may not receive the same return on your investment as purchasers whose purchase contracts are settled on the mandatory settlement date.

Upon issuance of the shares of common stock in the Common Stock Offering and the Private Placement and the issuance of the Units, our common stock will incur immediate dilution.

Upon the issuance of the shares of common stock in the Common Stock Offering and the Private Placement and the issuance of the Units, holders of our common stock will incur immediate and substantial net tangible book value dilution on a per share basis.

We expect that we will need to raise additional capital, and raising additional funds by issuing additional equity securities or with additional debt financing may cause dilution to shareholders or restrict our operations.

If and to the extent that any of the Common Stock Offering or the Private Placement is not completed, or such offerings are completed for less aggregate net proceeds than anticipated, we currently intend to fund any shortfall through the issuance of additional shares of common stock or equity-linked securities prior to the consummation of the Acquisition. However, if we are unable to issue such shares or equity-linked securities,

we would fund any shortfall with additional Debt Financings, which may include borrowings under the Bridge Facility and/or the Revolving Credit Facility. In addition, we expect that we will need to raise additional capital in the future in order to, among other things, repay indebtedness and fund our operations and future acquisitions, which we may do through equity and equity-linked securities offerings or additional debt financings, as well as borrowings under our credit facilities. Additional issuances of equity securities, including shares of our common stock, or debt or other securities that are convertible into or exchangeable for, or that represent the right to receive, common stock, including the Units, could dilute the economic and other rights and interests of holders of shares of our common stock and cause the market price of our common stock and/or the Units to decline. Subject to certain exceptions, such issuances may be made without any action or approval by our shareholders.

Any new debt financing we enter into may involve covenants that restrict our operations more than our current outstanding debt and credit facilities. These restrictive covenants could include limitations on additional borrowings, and specific restrictions on the use of our assets, as well as prohibitions or limitations on our ability to create liens, pay dividends, receive distributions from our subsidiaries, redeem or repurchase our stock or make investments. These covenants could hinder our access to capital markets and limit or delay our ability to carry out our capital expenditure program.

The fundamental change early settlement rate or the amount of cash and/or number of shares of our common stock paid or delivered, as the case may be, upon an acquisition termination redemption, may not adequately compensate you.

If a "fundamental change" occurs and you elect to exercise your fundamental change early settlement right, you will be entitled to settle your purchase contracts at the fundamental change early settlement rate. In addition, in connection with any acquisition termination redemption, upon redemption of the purchase contracts, you will be paid an amount of cash equal to the redemption amount (or, in certain circumstances, a number of shares of our common stock or any combination of cash and shares of our common stock). Although the fundamental change early settlement rate or the redemption amount, as the case may be, is designed to compensate you for the lost option value of your purchase contracts as a result of the early settlement of the purchase contracts, this feature may not adequately compensate you for such loss. In addition, if the stock price in the fundamental change is greater than $100.00 per share (subject to adjustment), this feature of the purchase contracts will not compensate you for any additional loss suffered in connection with a fundamental change. See "Description of the Purchase Contracts—Early Settlement Upon a Fundamental Change" and "Description of the Purchase Contracts—Acquisition Termination Redemption."

Our obligation to settle the purchase contracts at the fundamental change early settlement rate or to redeem the purchase contracts pursuant to an acquisition termination redemption could be considered a penalty, in which case the enforceability thereof would be subject to general principles of reasonableness of economic remedies.

The minimum settlement rate and maximum settlement rate of the purchase contracts may not be adjusted for all dilutive events and any adjustment may not be adequate compensation for lost value.

The minimum settlement rate and maximum settlement rate of the purchase contracts are subject to adjustment for certain events, including, but not limited to, certain dividends on our common stock, the issuance of certain rights, options or warrants to holders of our common stock, subdivisions or combinations of our common stock, certain distributions of assets, debt securities, capital stock or cash to holders of our common stock and certain tender offers or exchange offers, as described under "Description of the Purchase Contracts—Adjustments to the Fixed Settlement Rates" in this prospectus supplement. The minimum settlement rate, maximum settlement rate, reference price and threshold appreciation price will not be adjusted for other events that may adversely affect the trading price of the purchase contracts or the Units and the market price of our common stock, such as employee stock options grants, offerings of our common stock for cash (including pursuant to the Common Stock Offering), certain exchanges of our common stock for our other securities or in

connection with acquisitions and other transactions. The terms of the Units and the separate purchase contracts do not restrict our ability to engage in these activities, and events may occur that are adverse to the interests of the holders of the purchase contracts or the Units and their value, but that do not result in an adjustment to the minimum settlement rate, maximum settlement rate, reference price and threshold appreciation price, or that result in an adjustment that is not adequate compensation for lost value.

Until the purchase contracts are settled with, or redeemed for, common stock, you will not be entitled to any rights with respect to our common stock, but you will be subject to all changes made with respect to our common stock.

Until the date on which you are treated as the record holder of common stock on account of a redemption or settlement of the purchase contracts for or with, as the case may be, common stock, you will not be entitled to any rights with respect to our common stock, including voting rights and rights to receive any dividends or other distributions on our common stock, but you will be subject to all changes affecting the common stock. You will be treated as the record holder of any shares of our common stock issuable upon settlement or redemption of the purchase contracts only as follows:

- in the case of (x) settlement of purchase contracts on the mandatory settlement date or (y) an acquisition termination redemption if the acquisition termination stock price is greater than the reference price and we elect to pay cash in lieu of delivering a portion of any shares of common stock that would otherwise be included in the redemption amount, as of 5:00 p.m., New York City time, on the last trading day of the 20 consecutive trading day period during which the applicable market value or redemption market value, as the case may be, is determined;

- in the case of settlement of purchase contracts in connection with any early settlement at the holder's option, as of 5:00 p.m., New York City time, on the early settlement date;

- in the case of settlement of purchase contracts following exercise of a holder's fundamental change early settlement right, as of 5:00 p.m., New York City time, on the fundamental change early settlement date;

- in the case of settlement of purchase contracts following exercise by us of our early mandatory settlement right, as of 5:00 p.m., New York City time, on the notice date; and

- in the case of an acquisition termination redemption where we elect (or are deemed to have elected) to settle the redemption amount solely by delivering shares of common stock, as of 5:00 p.m., New York City time, on the date of the acquisition redemption notice.

For example, in the event that an amendment is proposed to our amended and restated articles of incorporation or amended and restated bylaws requiring stockholder approval and the record date for determining the stockholders of record entitled to vote on the amendment occurs prior to the date specified above on which you are treated as the record holder of the shares of our common stock, you will not be entitled to vote on the amendment, although you will nevertheless be subject to any changes in the powers, preferences or special rights of our common stock once you become a stockholder.

Some significant restructuring transactions may not constitute fundamental changes, in which case we would not be obligated to early settle the purchase contracts, and you will not have the right to require repurchase of your amortizing notes upon a fundamental change.

Upon the occurrence of specified fundamental changes, you will have the right to require us to settle the purchase contracts. You will not have the right to require repurchase of your amortizing notes upon a fundamental change, however. Additionally, the definition of "fundamental change" herein is limited to specified corporate

events and may not include other events that might adversely affect our financial condition or the value of the purchase contracts. For example, events such as leveraged recapitalizations, refinancings, restructurings or acquisitions initiated by us may not constitute a fundamental change requiring us to settle the purchase contracts at the applicable fundamental change early settlement rate. In the event of any such events, the holders of the purchase contracts would not have the right to require us to settle the purchase contracts at the applicable fundamental change early settlement rate, even though each of these transactions could increase the amount of our indebtedness, or otherwise adversely affect our capital structure or any credit ratings, thereby adversely affecting the trading price of the purchase contracts and/or the amortizing notes.

We may not have the ability to raise the funds necessary to repurchase the amortizing notes following the exercise of our early mandatory settlement right or in connection with an acquisition termination redemption, and our debt outstanding at that time may contain limitations on our ability to repurchase the amortizing notes.

If we elect to exercise our early mandatory settlement right or effect an acquisition termination redemption, holders of the amortizing notes will have the right to require us to repurchase the amortizing notes on the repurchase date at the repurchase price described under "Description of the Amortizing Notes—Repurchase of Amortizing Notes at the Option of the Holder." However, we may not have enough available cash or be able to obtain financing at the time we are required to make repurchases of amortizing notes surrendered for repurchase. In addition, our ability to pay the relevant repurchase price for the amortizing notes may be limited by agreements governing our current and future indebtedness. Our failure to repurchase amortizing notes at a time when the repurchase is required by the indenture would constitute a default under the indenture. A default under the indenture could also lead to a default under agreements governing our indebtedness outstanding at that time. If the repayment of the related indebtedness were to be accelerated after any applicable notice or grace periods, we may not have sufficient funds to repay the indebtedness and the repurchase price for the amortizing notes.

The secondary market for the Units, the purchase contracts and the amortizing notes may be illiquid.

We have applied to list the Units on the NYSE under the symbol "WTRU", subject to satisfaction of its minimum listing standards with respect to the Units. However, we cannot assure you that the Units will be approved for listing. If the Units are approved for listing, we expect that the Units will begin trading on the NYSE within 30 calendar days after the Units are first issued. In addition, the underwriters have advised us that they intend to make a market in the Units, but the underwriters are not obligated to do so. However, listing on the NYSE does not guarantee that a trading market will develop, and the underwriters may discontinue market making at any time in their sole discretion without prior notice to Unit holders. Accordingly we cannot assure you that a liquid trading market will develop for the Units (or, if developed, that a liquid trading market will be maintained), that you will be able to sell Units at a particular time or that the prices you receive when you sell will be favorable.

Beginning on the business day immediately succeeding the date of initial issuance of the Units, purchasers of Units will be able to separate each Unit into a purchase contract and an amortizing note. We are unable to predict how the separate purchase contracts or the separate amortizing notes will trade in the secondary market, or whether that market will be liquid or illiquid. We will not initially apply to list the separate purchase contracts or the separate amortizing notes on any securities exchange or automated inter-dealer quotation system, but we may apply to list such separate purchase contracts and separate amortizing notes in the future as described herein. If (i) a sufficient number of Units are separated into separate purchase contracts and separate amortizing notes and traded separately such that applicable listing requirements are met and (ii) a sufficient number of holders of such separate purchase contracts and separate amortizing notes request that we list such separate purchase contracts and separate amortizing notes, we may endeavor to list such separate purchase contracts and separate amortizing notes on an exchange of our choosing (which may or may not be the NYSE) subject to applicable listing requirements. However, even if we do so apply to list such separate purchase contracts or separate amortizing notes, we cannot assure you that such securities will be approved for listing.

The purchase contract agreement will not be qualified under the Trust Indenture Act, and the obligations of the purchase contract agent are limited.

The purchase contract agreement between us and the purchase contract agent will not be qualified as an indenture under the Trust Indenture Act of 1939, and the purchase contract agent will not be required to qualify as a trustee under the Trust Indenture Act. Thus, you will not have the benefit of the protection of the Trust Indenture Act with respect to the purchase contract agreement or the purchase contract agent. The amortizing notes constituting a part of the Units will be issued pursuant to an indenture, which has been qualified under the Trust Indenture Act. Accordingly, if you hold Units, you will have the benefit of the protections of the Trust Indenture Act only to the extent applicable to the amortizing notes. The protections generally afforded the holder of a security issued under an indenture that has been qualified under the Trust Indenture Act include:

- disqualification of the indenture trustee for "conflicting interests," as defined under the Trust Indenture Act;
- provisions preventing a trustee that is also a creditor of the issuer from improving its own credit position at the expense of the security holders immediately prior to or after a default under such indenture; and
- the requirement that the indenture trustee deliver reports at least annually with respect to certain matters concerning the indenture trustee and the securities.

The U.S. federal income tax consequences relating to the Units are uncertain.

The Units are complex financial instruments and no statutory, judicial or administrative authority directly addresses all aspects of the treatment of the Units or instruments similar to the Units for U.S. federal income tax purposes, and no assurance can be given that the Internal Revenue Service ("IRS") will agree with the tax consequences described herein. As a result, the U.S. federal income tax consequences of the purchase, ownership and disposition of the Units are unclear. We have not sought any rulings concerning the treatment of the Units, and the tax consequences described herein are not binding on the IRS or the courts, either of which could disagree with the explanations or conclusions contained in this summary. Accordingly, you should consult your tax advisor regarding the consequences to you of the possible recharacterization of the components of a Unit as a single instrument. See "Certain United States Federal Income and Estate Tax Consequences."

You may be subject to tax upon an adjustment to the settlement rate of the purchase contracts even though you do not receive a corresponding cash distribution.

You might be treated as receiving a constructive distribution from us if (i) the fixed settlement rates are adjusted and as a result of such adjustment your proportionate interest in our assets or earnings and profits is increased and (ii) the adjustment is not made pursuant to a bona fide, reasonable anti-dilution formula. An adjustment in the fixed settlement rates would not be considered made pursuant to such a formula if the adjustment were made to compensate you for taxable distributions with respect to our common stock (for example, if we increase the cash dividend on our common stock). Certain of the possible settlement rate adjustments (including, without limitation, adjustments in respect of taxable dividends to holders of our common stock and as discussed in "Description of the Purchase Contracts—Early Settlement Upon a Fundamental Change") may not qualify as being pursuant to a bona fide reasonable adjustment formula. Thus, under certain circumstances, an increase in the fixed settlement rates might give rise to a constructive distribution to you even though you would not receive any cash related thereto. In addition, in certain situations, you might be treated as receiving a constructive distribution if we fail to adjust the fixed settlement rates. Any constructive distribution will be taxable as a dividend, return of capital, or capital gain in accordance with the earnings and profits rules described below in "Certain United States Federal Income and Estate Tax Consequences—U.S. Holders—Common Stock Acquired under a Purchase Contract—Distributions" and "Certain United States Federal Income and Estate Tax Consequences—Non-U.S. Holders—U.S. Federal Income Tax." If you are a "non-U.S. holder"

(as defined in "Certain United States Federal Income and Estate Tax Consequences—Non-U.S. Holders"), a deemed dividend may be subject to U.S. federal withholding tax (currently at a 30% rate, or such lower rate as may be specified by an applicable income tax treaty), which may be withheld from shares of common stock or sales proceeds subsequently paid or credited to you. It is possible that U.S. withholding tax on deemed dividends would be withheld from any interest or other amounts paid to a non-U.S. holder. See "Certain United States Federal Income and Estate Tax Consequences—Non-U.S. Holders—U.S. Federal Withholding Tax."

Any adverse rating action with respect to the Units may cause their trading price to fall.

We do not intend to seek a rating on the Units. However, if a rating service were to rate the Units and if such rating service were to lower its rating on the Units below the rating initially assigned to the Units or otherwise announces its intention to put the Units on credit watch, the trading price of the Units could decline.

Anti-takeover provisions in our organizational documents and under Pennsylvania law might discourage, delay or prevent changes in control of our company and may result in an entrenchment of management and diminish the value of our common stock.

Certain provisions of our articles of incorporation and bylaws could have the effect of delaying, deterring or preventing another party from acquiring or seeking to acquire control of us. These provisions are intended to discourage certain types of coercive takeover practices and inadequate takeover bids and to encourage anyone seeking to acquire control of us to negotiate first with our board of directors. However, these provisions could also delay, deter or prevent a change of control or other takeover of our company that our shareholders might consider to be in their best interests, including transactions that might result in a premium being paid over the market prices of our common stock and Units, and may also limit the prices that investors are willing to pay in the future for our common stock and Units. These provisions may also have the effect of preventing changes in our management.

For example, our articles of incorporation and bylaws include anti-takeover provisions that:

- authorize our board of directors, without a vote or other action by our shareholders, to cause the issuance of preferred stock in one or more series and, with respect to each series, to fix the number of shares constituting that series and to establish the rights, preferences, privileges and restrictions of that series, which may include, among other things, dividend and liquidation rights and preferences, rights to convert such shares into common stock, voting rights and other rights which may adversely affect the voting or other rights and the economic interests of holders of our common stock and Units;

- require that certain fundamental transactions must be approved by the holders of 75% of the outstanding shares of our capital stock entitled to vote on the matter unless at least a majority of the members of the board of directors has approved the transaction, in which case the required shareholder approval will be the minimum approval required by applicable law;

- establish advance notice requirements and procedures for shareholders to submit nominations of candidates for election to our board of directors and to propose other business to be brought before a shareholders meeting;

- provide that vacancies in our board of directors, including vacancies created by the removal of any director, or any increase in the number of directors may be filled by a majority of the directors then in office or by the sole remaining director;

- provide that no shareholder may cumulate votes in the election of directors, which means that the holders of a majority of our outstanding shares of common stock can elect all directors standing for election by our common shareholders;

- require that any action to be taken by our shareholders must be taken either (1) at a duly called annual or special meeting of shareholders or (2) by the unanimous written consent of all of our shareholders;

- require action by shareholders entitled to cast a majority of the votes which all shareholders are entitled to cast at the particular meeting in order for our shareholders to call a special meeting of shareholders; and

- provide that a state court located within Montgomery County, Pennsylvania (or, in the event such court lacks jurisdiction over such action or proceeding, the United States District Court for the Eastern District of Pennsylvania) will be the exclusive forum for the adjudication of certain disputes, including derivative actions.

In addition, anti-takeover provisions in Pennsylvania law could make it more difficult for a third party to acquire control of us including, but not limited to, provisions relating to (1) control share acquisitions, (2) disgorgement of profits by certain controlling persons, (3) business combination transactions with interested shareholders, and (4) the rights of shareholders to demand fair value for their stock following a control transaction. Pennsylvania law permits corporations to opt-out of these anti-takeover provisions, but we have not done so. Such provisions could have the effect of deterring takeovers or delaying changes in control or management of us. Additionally, such provisions could limit the price that some investors might be willing to pay in the future for shares of our common stock.

In addition, other debt financings may include certain terms that may have anti-takeover effects.

This offering is not conditioned upon the completion of the Acquisition. If the Acquisition is not consummated, we will have broad discretion on the use of the net proceeds of this offering.

This offering is not conditioned upon the completion of the Acquisition. Accordingly, your purchase of Units in this offering may be an investment in Aqua America on a stand-alone basis without any of the assets of Peoples or anticipated benefits of the Acquisition. We will have broad discretion to use the net proceeds of this offering if the Acquisition does not occur. If the Acquisition does not occur, we expect to use the net proceeds from this offering, after payment of any cash redemption amount and/or repurchase price (if applicable), for general corporate purposes, which may include the Company Debt Refinancing, the redemption of securities issued in connection with the other Financing Transactions, repurchases of our common stock, debt repayment, capital expenditures and investments. See “Use of Proceeds.”

We may be unable to, or may choose not to, continue to pay dividends on our common stock at current or planned rates or at all.

Any future payments of cash dividends, and the amount of any cash dividends we pay, on our common stock will depend on, among other things, our financial condition, capital requirements and results of operations, and the ability of our subsidiaries to distribute cash to us, as well as other factors that our board of directors may consider relevant. If we were to reduce the amount of cash dividends per share payable on our common stock, fail to increase the amount of those cash dividends per share in the future or cease paying those cash dividends altogether, it would likely have an adverse impact on the market price of our common stock and the Units. In addition, under Pennsylvania law, our board of directors (or an authorized committee thereof) may not declare and pay dividends on shares of our common stock if, after giving effect to the dividend (1) we would be unable to pay our debts as they become due in the ordinary course of business, or (2) our total assets would be less than the sum of our total liabilities plus the amount that would be needed, if we were to be dissolved as of the date for measuring the dividend, to satisfy the preferential rights upon dissolution of shareholders whose preferential rights are superior to those receiving the dividend.

USE OF PROCEEDS

We estimate that the net proceeds to us from this offering, after deducting underwriting discounts and estimated offering expenses, will be approximately $585.8 million (or approximately $673.7 million if the underwriters exercise their option to purchase additional Units in full).

We intend to use the net proceeds from this offering, together with net proceeds from the Common Stock Offering, the Private Placement and the Debt Financings, to (1) fund the Acquisition, (2) complete the redemption of approximately $314 million aggregate principal amount of the PPNs and (3) pay related costs and expenses as described below. In addition to the $1,009 million aggregate principal amount of Debt Financings we intend to incur to fund the Acquisition, complete the Company Debt Refinancing and pay related costs and expenses, we expect to incur $150 million aggregate principal amount of Debt Financings, the net proceeds of which we intend to use for general corporate purposes, including working capital and capital needs.

This offering and certain of the other Financing Transactions are not conditioned upon the consummation of any other Financing Transactions, the Acquisition or the Company Debt Refinancing. In addition, the indebtedness or other securities to be incurred or issued in certain of the Financing Transactions may not be incurred or issued, or may be redeemed, repaid, or repurchased, if the Acquisition is not consummated or is not consummated by a specified date. Even if the Acquisition, the Company Debt Refinancing and/or other Financing Transactions do not occur, the Units issued in this offering will remain outstanding (unless we elect to redeem the Units in the event the Acquisition does not occur by April 22, 2020 or the Acquisition Agreement is terminated prior to such date). If for any reason the Acquisition is not consummated, we expect we would use the net proceeds for this offering, after payment of any cash redemption amount and/or repurchase price (if applicable), for general corporate purposes, which may include the Company Debt Refinancing, the redemption of securities issued in connection with the other Financing Transactions, repurchases of our common stock, debt repayment, capital expenditures and investments. Pending application of the net proceeds of this offering for the foregoing purposes, the net proceeds may be invested temporarily in investment-grade securities or similar instruments, or be used to temporarily reduce borrowings under the Revolving Credit Facility.

The following table outlines the estimated sources and uses of funds for the Acquisition, the Company Debt Refinancing and the related costs and expenses. The actual net proceeds from the Financing Transactions and the costs and expenses related to the Transactions will likely vary from the estimates reflected in the following table. See "Summary Information–Recent Developments—Financing Transactions."

The following table does not reflect the sale of any shares or Units that may be sold to the underwriters of this offering or of the Common Stock Offering upon exercise of their respective options to purchase additional shares and Units. To the extent the underwriters exercise such options, we expect that the net proceeds from such sales will be used to fund a portion of the purchase price of the Acquisition, which would reduce, by a corresponding amount, the amount of the debt financings we expect to incur to fund a portion of the purchase price of the Acquisition.

Sources of Funds[1]		**Uses of Funds**	
	(in millions)		
Units offered hereby	$ 600	Cash Acquisition Consideration[2]	$ 2,905
Common Stock Offering	1,125	Company Debt Refinancing[3]	314
Private Placement	750	Transactions costs and expenses, including	
Debt Financings[4]	1,009	discounts and financing fees	265
Assumption of Peoples's existing debt	1,370	Assumption of Peoples's existing debt	1,370
Total sources of funds	$ 4,854	**Total uses of funds**	$ 4,854

(1) All amounts are estimated proceeds before underwriting discounts and offering expenses. If and to the extent that any of this offering, the Common Stock Offering or the Private Placement is not completed, or if the aggregate net proceeds from this offering, the Common Stock Offering and the Private Placement are less than the aggregate amount set forth in this table, we intend to fund any shortfall by issuing additional shares of common stock or equity-linked securities prior to the consummation of the Acquisition. However, if we are unable to issue such shares or equity-linked securities, we would fund any shortfall with additional debt financings, which may include borrowings under the Bridge Facility and/or the Revolving Credit Facility.

(2) Assumes the only adjustment to the Default Cash Acquisition Consideration is a reduction of $1,370 million based upon the assumption by the Company of $1,370 million aggregate principal amount of Peoples's indebtedness upon closing of the Acquisition. To the extent we assume less than $1,370 million aggregate principal amount of Peoples's existing indebtedness, we may issue additional shares of common stock, equity-linked securities and/or New Notes and/or incur borrowings under the Bridge Facility and/or the Revolving Credit Facility.

(3) In connection with the Acquisition and the Financing Transactions, we expect to redeem approximately $314 million in aggregate principal amount of our PPNs prior to the closing of the Acquisition. Estimated premiums payable in connection with the Company Debt Refinancing are included in "Transaction costs and expenses, including discounts and financing fees" above. The PPNs we intend to redeem in the Company Debt Refinancing have maturities ranging from 2019-2037 and interest rates ranging from 3.57-5.83%.

(4) In addition to the $1,009 million aggregate principal amount of Debt Financings we intend to incur to fund the Acquisition, complete the Company Debt Refinancing and pay related costs and expenses, we expect to incur $150 million aggregate principal amount of Debt Financings, the net proceeds of which we intend to use for general corporate purposes, including working capital and capital needs.

CAPITALIZATION

The following table sets forth our consolidated cash and cash equivalents and capitalization as of December 31, 2018:

- on an actual basis;
- on an as adjusted basis to give effect to this offering;
- on an as further adjusted basis to give effect to this offering and the Common Stock Offering; and
- on a pro forma basis to give effect to the Transactions, including this offering, the Common Stock Offering, the Acquisition, the Company Debt Refinancing, the Private Placement and the Debt Financings.

The following table does not reflect the sale of any Units that may be sold to the underwriters of this offering upon exercise of their option to purchase additional Units or the sale of any shares of common stock that may be sold to the underwriters of the Common Stock Offering upon exercise of their option to purchase additional shares in the Common Stock Offering. If such underwriters exercise their respective options to purchase additional Units and/or shares, we expect that the proceeds from such sales will be used to fund a portion of the purchase price of the Acquisition, which would reduce, by a corresponding amount, the amount of the Debt Financings we expect to incur to fund a portion of the purchase price of the Acquisition.

The completion of this offering is not conditioned upon the consummation of any of the other Transactions, including the Acquisition. Accordingly, investors should not place undue reliance on the as further adjusted and pro forma information included in this prospectus supplement because this offering is not conditioned upon the consummation of any of the other transactions reflected in such information. In addition, even if the Transactions are completed, actual amounts may vary from such information depending on several factors, including potential changes in our financing plans as a result of market conditions or the timing of the consummation of the Acquisition.

The following data are qualified in their entirety by our financial statements and related notes and other information incorporated by reference in this prospectus supplement and the accompanying prospectus. This table should be read in conjunction with “Summary Information–Recent Developments—Proposed Peoples Gas Acquisition,” “Risk Factors,” “Use of Proceeds,” and our pro forma and consolidated financial statements and related notes incorporated by reference in this prospectus supplement and the accompanying prospectus, and the other information contained in the documents incorporated by reference in this prospectus supplement and the accompanying prospectus.

(dollars in thousands)	Actual	As Adjusted for this Offering	As Further Adjusted for this Offering and the Common Stock Offering	Pro Forma for the Transactions
Cash and cash equivalents[1]	$ 3,627	$ 589,401	$ 1,687,741	$ 209,100
Debt:				
Long-term debt of subsidiaries[2]	$ 1,604,233	$ 1,604,233	$ 1,604,233	$ 1,604,233
Revolving Credit Facility[3]	370,000	370,000	370,000	370,000
Privately placed notes[4]	589,427	589,427	589,427	275,927
Debt Financings[5]	—	—	—	1,159,000
Assumed People's indebtedness[6]	—	—	—	1,329,227
Amortizing notes that are components of the Units[7]	—	103,549	103,549	103,549
Total debt	$ 2,563,660	$ 2,667,209	$ 2,667,209	$ 4,841,936
Equity:				
Preferred stock, $1.00 par value (1,770,819 shares authorized, none issued)	—	—	—	—
Common stock, $0.50 par value (300,000,000 shares authorized; 181,151,827 issued, actual and as adjusted; 213,647,494 issued, as further adjusted and 235,308,589 issued, pro forma)[8]	90,576	90,576	106,824	117,654
Capital in excess of par value[8][9]	820,378	1,305,106	2,387,198	3,104,807
Retained earnings[10]	1,174,245	1,174,245	1,174,245	1,130,168
Treasury stock, at cost (3,060,206 shares)	(75,835)	(75,835)	(75,835)	(75,835)
Total stockholders' equity	$ 2,009,364	$ 2,494,092	$ 3,592,432	$ 4,276,794
Total capitalization	$ 4,573,024	$ 5,161,301	$ 6,259,641	$ 9,118,730

(1) As adjusted amount reflects the impact of the net proceeds of $585.8 million from this offering. As further adjusted amount additionally reflects the impact of the net proceeds of $1,098.3 million from the Common Stock Offering. The pro forma amount additionally reflects Peoples's cash balance of $13.7 million as of December 31, 2018, the estimated net proceeds from the Private Placement of $728.4 million and the estimated net proceeds of the Debt Financings of $1,149.4 million, less the estimated cash purchase price of Peoples of $2,945.8 million (see Note 6), the estimated amount of the Company Debt Refinancing of approximately $314 million (see Note 4) and additional estimated acquisition-related payments for expenses of $110.3 million. Cash and cash equivalents may increase or decrease depending on, among other things, actual costs and expenses incurred in connection with the Transactions.

(2) Such amounts do not include subsidiary debt that is reflected in "Privately placed notes" or in "Assumed Peoples's indebtedness".

(3) In December 2018, we entered into a five-year $550 million unsecured Revolving Credit Facility, which replaced our prior unsecured revolving credit facility. Subject to customary conditions, we may request that the lenders under the Revolving Credit Facility provide an incremental unsecured revolving credit facility of up to $450 million upon the closing of the Acquisition. As described below in note 6, at the closing of the Acquisition, we expect to borrow $270 million under the Revolving Credit Facility in order to repay $270 million under the Peoples's revolving credit facility that is expected to be assumed at the closing of the Acquisition and terminated).

(4) In connection with the Acquisition and the Financing Transactions, we expect to redeem approximately $314 million in aggregate principal amount of our PPNs, of which $150.9 million in aggregate principal amount is indebtedness of our subsidiaries, prior to the closing of the Acquisition.

(5) The pro forma amount of $1,159 million represents the assumed aggregate principal amount of the Debt Financings, including the $150 million aggregate principal amount we intend to use for general corporate purposes. If we do not consummate the Common Stock Offering or the Private Placement, or if such offerings are completed for less aggregate net proceeds than anticipated, we may issue additional shares of common stock or equity-linked securities prior to the consummation of the Acquisition. However, if we are unable to issue such shares or equity-linked securities, we would fund any shortfall with additional debt financings, which may include borrowings under the Bridge Facility and/or the Revolving Credit Facility.
We expect the terms of one or more series of New Notes issued in the Debt Financings will include a special mandatory redemption provision requiring us to redeem such New Notes if the Acquisition is not consummated by a specified date. If the Acquisition is not consummated, we do not expect to incur any borrowings under the Bridge Facility.

(6) The pro forma amount reflects approximately $1,329 million aggregate principal amount of Peoples's existing indebtedness expected to be assumed in connection with the Acquisition as of December 31, 2018. We expect the amount of such assumed debt will be $1,370 million as of the closing of the Acquisition. Of the $1,370 million of expected assumed Peoples's indebtedness at closing, $270 million is expected to be borrowings under the Peoples's revolving credit facility which is expected to be repaid at the closing of the Acquisition with borrowings under the Revolving Credit Facility and terminated.

(7) Each Unit will include an amortizing note. Approximately 17.3% of the stated amount of the Units, $103.5 million, is represented by the amortizing notes. If the Acquisition does not occur by April 22, 2020 or if the Acquisition Agreement is terminated prior to such date, we may elect to redeem all, but not less than all, of the outstanding purchase contracts in accordance with the terms thereof, in which case holders of Units would have the right to require us to repurchase their outstanding amortizing notes at the relevant repurchase price. See "Description of the Amortizing Notes—Repurchase of Amortizing Notes at the Option of the Holder."

(8) As further adjusted and pro forma share numbers and amounts ($16.2 million with respect to "Common stock" and $1,082.1 million with respect to "Capital in excess of par value") with respect to the Common Stock Offering reflect related underwriting discounts and estimated offering expenses.

The pro forma share number and amount also reflects the expected issuance of 21,661,095 shares of our common stock in the Private Placement at an offering price of $34.62 per share (an incremental $10.8 million with respect to "Common stock" and an incremental $717.6 million with respect to "Capital in excess of par value") and reflects placement agent fees and other estimated issuance costs. In addition to other closing conditions, the completion of the Private Placement is conditioned upon the completion of at least $1.6 billion in common stock and equity-linked securities offerings and the consummation of the Acquisition.

If and to the extent that any of this offering, the Common Stock Offering or the Private Placement is not completed, or if the aggregate net proceeds from such offerings is less than anticipated, we currently intend to issue additional shares of common stock or equity-linked securities prior to the consummation of the Acquisition. However, if we are unable to issue such shares or equity-linked securities, we would fund any shortfall with additional debt financings, which may include borrowings under the Bridge Facility and/or the Revolving Credit Facility.

Share numbers and amounts do not reflect shares of our common stock issuable upon settlement of the purchase contracts, shares of our common stock reserved for issuance upon exercise of stock options outstanding, shares of our common stock reserved for issuance upon vesting of our time based restricted stock units (including reinvested dividends), shares of our common stock reserved for issuance upon the vesting of our performance based restricted stock units or performance share units or additional shares we may issue under our dividend reinvestment program, employee stock purchase plan or 401(k) savings plans.

(9) Each Unit will include a purchase contract. We will account for the purchase contracts that are components of the Units as equity and will record the initial fair value of these purchase contracts, net of the related underwriting discounts and estimated offering expenses allocated to the purchase contracts, as capital in excess of par value, $484.7 million. The exact amount we record as capital in excess of par value will not be determined until our determination of the final offering expenses. See footnote (7) above. If the offering is completed but the Acquisition is not consummated, we may redeem all, but not less than all, of the outstanding purchase contracts by issuing a redemption notice during the five business day period immediately following the earlier of (x) the April 22, 2020 if the closing of the Acquisition has not occurred on or prior to such date and (y) the date on which the Acquisition Agreement is terminated. We will pay a redemption price to be determined based on our common stock price at the time in cash or in shares of our common stock in accordance with the terms of the purchase contracts. If we elect to redeem the purchase contracts, we may be required by the holders thereof to repurchase the amortizing notes at the repurchase price set forth in the amortizing notes as described under "Description of the Amortizing Notes—Repurchase of Amortizing Notes at the Option of the Holder."

(10) The pro forma amount, a reduction of $44.1 million, reflects the payment of additional Acquisition-related expenses and the write-off of unamortized debt issuance costs.

LISTING OF OUR COMMON STOCK AND THE UNITS AND DIVIDENDS

Our common stock is listed on the NYSE under the symbol "WTR." As of March 31, 2019, there were (i) 178,369,078 shares of our common stock outstanding and (ii) options to acquire 1,112,210 shares of our common stock outstanding.

On April 17, 2019, the last reported sale price of our common stock on the NYSE was $34.82. As of December 31, 2018, there were approximately 23,476 holders of record of our common stock.

We have applied to list the Units on the NYSE under the symbol "WTRU", subject to satisfaction of its minimum listing standards with respect to the Units. We will not initially apply to list the separate purchase contracts or the separate amortizing notes on any securities exchange or automated inter-dealer quotation system, but we may apply to list such separate purchase contracts and separate amortizing notes in the future as described herein. Prior to this offering, there has been no public market for the Units.

We have historically paid quarterly dividends on our common stock; however, the declaration, amount, timing and payment of any future dividends are subject to the determination and approval of our board of directors based on then-current or anticipated future conditions including our results of operations, capital requirements, financial condition, legal requirements or other factors deemed relevant by our board of directors. See "Risk Factors—Risks Related to the Units, the Separate Purchase Contracts, the Separate Amortizing Notes and our Common Stock—We may be unable to, or may choose not to, continue to pay dividends on our common stock at current or planned rates or at all."

DESCRIPTION OF THE UNITS

We are offering 12,000,000 Units (or 13,800,000 Units if the underwriters exercise their option to purchase additional Units in full), each with a stated amount of $50.00. Each Unit is comprised of a prepaid stock purchase contract (a "purchase contract") issued by us and a senior amortizing note issued by us. The following summary of the terms of the Units, the summary of the terms of the purchase contracts set forth under the caption "Description of the Purchase Contracts" and the summary of the terms of the amortizing notes set forth under the caption "Description of the Amortizing Notes" in this prospectus supplement and under the caption "Description of Debt Securities" in the accompanying prospectus contain a description of certain terms of the Units and their components but are not complete and are subject to, and qualified in their entirety by reference to, the related contracts. We refer you to:

- the purchase contract agreement (the "purchase contract agreement"), to be dated the date of first issuance of the Units, to be entered into among us, U.S. Bank N.A., as purchase contract agent (the "purchase contract agent") and attorney-in-fact for the holders of purchase contracts from time to time, and U.S. Bank N.A., as trustee (the "trustee") under the indenture described below, pursuant to which the purchase contracts and Units will be issued; and

- the indenture between us, as issuer, and the trustee, and a related supplemental indenture, between us, as issuer, and U.S. Bank N.A., as trustee, each to be dated the date of first issuance of the Units, under which the amortizing notes will be issued.

The form of indenture has been filed as an exhibit to the registration statement of which this prospectus supplement forms a part, and a supplemental indenture related to a change in governing law to New York law, among other matters, and a supplemental indenture for the amortizing notes and the purchase contract agreement will be filed as exhibits to a current report on Form 8-K and incorporated by reference as exhibits to that registration statement. Whenever particular sections or defined terms are referred to, such sections or defined terms are incorporated herein by reference.

As used in this section, unless the context otherwise requires, references to "Aqua America," "we," "us" or "our" refer to Aqua America, Inc. and do not include any of its existing or future subsidiaries.

Components of the Units

Each Unit offered is comprised of:

- a prepaid stock purchase contract issued by us pursuant to which we will deliver to the holder, not later than 5:00 p.m., New York City time, on April 30, 2022 (subject to postponement in certain limited circumstances, the "mandatory settlement date"), unless earlier redeemed or settled, a number of shares of our common stock, par value $0.50 per share (the "common stock"), per purchase contract equal to the settlement rate described below under "Description of the Purchase Contracts—Delivery of Common Stock;" and

- a senior amortizing note issued by us with an initial principal amount of $8.62909 that pays equal quarterly installments of $0.75000 per amortizing note (except for the July 30, 2019 installment payment, which will be $0.80833 per amortizing note), which cash payment in the aggregate will be equivalent to 6.00% per year with respect to the $50.00 stated amount per Unit.

Unless previously settled at your option as described in "Description of the Purchase Contracts—Early Settlement" or "Description of the Purchase Contracts —Early Settlement Upon a Fundamental Change," settled at our option as described in "Description of the Purchase Contracts—Early Mandatory Settlement at Our Election" or redeemed at our option as described in "Description of the Purchase Contracts—Acquisition

Termination Redemption," we will deliver to you not more than 1.4442 shares and not less than 1.1790 shares of our common stock on the mandatory settlement date, based upon the applicable "settlement rate" (as defined under "Description of the Purchase Contracts—Delivery of Common Stock"), which is subject to adjustment as described herein, and the "applicable market value" (as defined under "Description of the Purchase Contracts—Delivery of Common Stock") of our common stock, as described below under "Description of the Purchase Contracts—Delivery of Common Stock."

Each amortizing note will have an initial principal amount of $8.62909. On each January 30, April 30, July 30 and October 30, commencing on July 30, 2019, we will pay equal cash installments of $0.75000 on each amortizing note (except for the July 30, 2019 installment payment, which will be $0.80833 per amortizing note). Each installment payment will constitute a payment of interest (at a rate of 3.00% per annum) and a partial repayment of principal on the amortizing note, allocated as set forth on the amortization schedule set forth under "Description of the Amortizing Notes—Amortization Schedule."

The stated amount of each Unit must be allocated between the amortizing note and the purchase contract based upon their relative fair market values. We have determined that the fair market value of each amortizing note is $8.62909 and the fair market value of each purchase contract is $41.37091, as set forth in the purchase contract agreement. Each holder agrees to such allocation and this position will be binding upon each holder (but not on the Internal Revenue Service).

Separating and Recreating Units

Upon the conditions and under the circumstances described below, a holder of a Unit will have the right to separate a Unit into its component parts, and a holder of a separate purchase contract and a separate amortizing note will have the right to combine the two components to recreate a Unit.

Separating Units

At initial issuance, the purchase contracts and amortizing notes may be purchased and transferred only as Units and will trade under the CUSIP number for the Units.

On any business day during the period beginning on, and including, the business day immediately following the date of initial issuance of the Units to, but excluding, the second scheduled trading day immediately preceding April 30, 2022 or, if earlier, the second scheduled trading day immediately preceding any "early mandatory settlement date" (as defined under "Description of the Purchase Contracts") or the second scheduled trading day immediately preceding any "acquisition redemption settlement date" (as defined under "Description of the Purchase Contracts") and also excluding the business day immediately preceding any installment payment date (*provided*, the right to separate the Units shall resume after such business day), you will have the right to separate your Unit into its constituent purchase contract and amortizing note (which we refer to as a "separate purchase contract" and a "separate amortizing note," respectively, and which will thereafter trade under their respective CUSIP numbers), in which case that Unit will cease to exist. If you beneficially own a Unit, you may separate it into its component purchase contract and component amortizing note by delivering written instructions to the broker or other direct or indirect participant through which you hold an interest in your Unit (your "participant") to notify The Depository Trust Company ("DTC") through DTC's Deposit/Withdrawal at Custodian ("DWAC") system of your desire to separate the Unit. Holders who elect to separate a Unit into its constituent purchase contract and amortizing note shall be responsible for any fees or expenses payable in connection with such separation.

"Business day" means any day other than a Saturday, Sunday or any day on which banking institutions in New York, New York are authorized or obligated by applicable law or executive order to close or be closed.

Separate purchase contracts and separate amortizing notes will be transferable independently from each other.

Recreating Units

On any business day during the period beginning on, and including, the business day immediately following the date of initial issuance of the Units to, but excluding, the second scheduled trading day immediately preceding April 30, 2022 or, if earlier, the second scheduled trading day immediately preceding any early mandatory settlement date or the second scheduled trading day immediately preceding any acquisition redemption settlement date and also excluding the business day immediately preceding any installment payment date (*provided*, the right to recreate the Units shall resume after such business day), you may recreate a Unit from your separate purchase contract and separate amortizing note. If you beneficially own a separate purchase contract and a separate amortizing note, you may recreate a Unit by delivering written instruction to your participant to notify DTC through DTC's DWAC system of your desire to recreate the Unit. Holders who elect to recreate Units shall be responsible for any fees or expenses payable in connection with such recreation.

Global Securities

Your Unit, purchase contract and amortizing note will be represented by global securities registered in the name of a nominee of DTC. You will not be entitled to receive definitive physical certificates for your Units, purchase contracts or amortizing notes, except under the limited circumstances described under "Book-Entry Procedures and Settlement." Beneficial interests in a Unit and, after separation, the separate purchase contract and separate amortizing note will be represented through book-entry accounts of, and transfers will be effected through, direct or indirect participants in DTC.

Deemed Actions by Holders by Acceptance

Each holder of Units or separate purchase contracts, by acceptance of such securities, will be deemed to have:

- irrevocably authorized and directed the purchase contract agent to execute, deliver and perform on its behalf the purchase contract agreement, and appointed the purchase contract agent as its attorney-in-fact for any and all such purposes;
- in the case of a purchase contract that is a component of a Unit, or that is evidenced by a separate purchase contract, irrevocably authorized and directed the purchase contract agent to execute, deliver and hold on its behalf the separate purchase contract or the component purchase contract evidencing such purchase contract, and appointed the purchase contract agent as its attorney-in-fact for any and all such purposes;
- consented to, and agreed to be bound by, the terms and provisions of the purchase contract agreement; and
- represented that either (i) no portion of the assets used to acquire or hold the Units, common stock issuable on upon settlement of the purchase contracts or amortizing notes constitutes assets of any (a) employee benefit plans that are subject to Title I of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), (b) plan, individual retirement account or other arrangement that is subject to Section 4975 of the Internal Revenue Code of 1986, as amended (the "Code") or provisions under any other U.S. or non-U.S. federal, state, local or other laws or regulations that are similar to such provisions of ERISA or the Code (collectively, "Similar Laws"), or (c) entity which is deemed to hold the assets of any of the foregoing types of plans, accounts or arrangements described in clauses (a) and (b) (each of the foregoing described in clause (a), (b) and (c) referred to as a "Plan") or (ii) (1) the acquisition and holding of the Units, common stock issuable upon settlement of the purchase contracts or amortizing notes and any of its constituent parts will not constitute or result in a non-exempt prohibited transaction under Section 406 of ERISA or Section 4975 of the Code or a similar violation under any applicable Similar Laws and (2) neither Aqua America, the underwriters or any of their respective affiliates is, or is undertaking to be, a fiduciary with respect to the Plan in connection

with the Plan's acquisition, holding or disposition of the Units, common stock issuable upon settlement of the purchase contracts or amortizing notes, as applicable;

- in the case of a holder of a Unit, agreed, for all purposes, including U.S. federal income tax purposes, to treat:
  - a Unit as an investment unit composed of two separate instruments, in accordance with its form;
  - the amortizing notes as indebtedness of ours; and
  - the allocation of the $50.00 stated amount per Unit between the purchase contract and the amortizing note so that such holder's initial tax basis in each purchase contract will be $41.37091 and such holder's initial tax basis in each amortizing note will be $8.62909.

Listing of Securities

We have applied to list the Units on the NYSE under the symbol "WTRU," subject to satisfaction of its minimum listing standards with respect to the Units. However, we can give no assurance that the Units will be so listed. If the Units are approved for listing, we expect that the Units will begin trading on the NYSE within 30 calendar days after the Units are first issued. In addition, the underwriters have advised us that they intend to make a market in the Units, but the underwriters are not obligated to do so. However, listing on the NYSE does not guarantee that a trading market will develop, and the underwriters may discontinue market making at any time in their sole discretion without notice. Accordingly, we cannot assure you that a liquid trading market will develop for the Units (or, if developed, that a liquid trading market will be maintained), that you will be able to sell Units at a particular time or that the prices you receive when you sell will be favorable.

We will not initially apply to list the separate purchase contracts or the separate amortizing notes on any securities exchange or automated inter-dealer quotation system. If (i) a sufficient number of Units are separated into separate purchase contracts and separate amortizing notes and traded separately such that applicable listing requirements are met and (ii) a sufficient number of holders of such separate purchase contracts and separate amortizing notes request that we list such separate purchase contracts and separate amortizing notes, we may endeavor to list such separate purchase contracts and separate amortizing notes on an exchange of our choosing (which may or may not be the NYSE) subject to applicable listing requirements.

Our common stock is listed on the NYSE under the symbol "WTR." We have applied to have the shares of our common stock deliverable upon settlement of all purchase contracts approved for listing on the NYSE.

Title

We, the purchase contract agent and the trustee will treat the registered owner, which we expect at initial issuance to be a nominee of DTC, of any Unit or separate purchase contract or separate amortizing note as the absolute owner of the Unit or separate purchase contract or separate amortizing note for the purpose of settling the related purchase contract or making payments on the separate amortizing note and for all other purposes.

Accounting for the Units

We expect to record the issuance of the purchase contract portion of the Units as additional paid-in-capital, net of issuance costs of the purchase contracts, in our financial statements. We also expect to record the amortizing notes portion of the Units as long-term debt and to record the issuance costs of the amortizing notes as an adjustment to the carrying amount of the amortizing notes. The amortization of the amortizing notes will be

calculated using the effective interest method over the life of the amortizing notes. We will allocate the proceeds from the issuance of the Units to the purchase contracts and amortizing notes based on the relative fair values of the respective components, determined as of the date of issuance of the Units. We have determined that the allocation of the purchase price of each Unit as between the amortizing note and the purchase contract will be $8.62909 for the amortizing note and $41.37091 for the purchase contract, as set forth in the purchase contract agreement.

Based on the expected structure of the Units, Aqua America expects the purchase contracts to meet equity classification, which has been reflected as such in the unaudited pro forma consolidated combined balance sheet presented in "Unaudited Pro Forma Consolidated Combined Financial Information" included or incorporated by reference in this prospectus supplement. The classification of the Units will be subject to detailed assessment once finalized and a different conclusion may result in a material impact on the information presented in "Unaudited Pro Forma Consolidated Combined Financial Information" included or incorporated by reference in this prospectus supplement.

Based on U.S. GAAP, we do not expect the purchase contract component of the Units to be revalued under fair value accounting principles.

Our earnings per share calculations will reflect the shares issuable upon settlement of the purchase contracts portion of the Units. Our basic earnings per share will include the minimum shares issuable under the purchase contract for each period and our diluted earnings per share will include any incremental shares that would be issuable assuming a settlement of the purchase contract at the end of each accounting period, if dilutive.

Replacement of Unit Certificates

In the event that physical certificates evidencing the Units have been issued, any mutilated Unit certificate will be replaced by us at the expense of the holder upon surrender of the certificate to the purchase contract agent. Unit certificates that become destroyed, lost or stolen will be replaced by us at the expense of the holder upon delivery to us and the purchase contract agent of evidence of their destruction, loss or theft satisfactory to us and the purchase contract agent. In the case of a destroyed, lost or stolen Unit certificate, an indemnity satisfactory to us and the purchase contract agent may be required at the expense of the holder of the Units before a replacement will be issued.

Notwithstanding the foregoing, we will not be obligated to replace any Unit certificates on or after the second scheduled trading day immediately preceding April 30, 2022 or the second scheduled trading day immediately preceding any early mandatory settlement date or the second scheduled trading day immediately preceding any acquisition redemption settlement date. In those circumstances, the purchase contract agreement will provide that, in lieu of the delivery of a replacement Unit certificate, the purchase contract agent, upon delivery of the evidence and indemnity described above, will deliver or arrange for delivery of the shares of common stock issuable (and/or, in the case of an acquisition redemption settlement date, make the required cash payment, if any) pursuant to the purchase contracts included in the Units evidenced by the Unit certificate.

Miscellaneous

The purchase contract agreement will provide that we will pay all fees and expenses related to the offering of the Units and the enforcement by the purchase contract agent of the rights of the holders of the Units or the separate purchase contracts or separate amortizing notes, other than expenses (including legal fees) of the underwriters.

Should you elect to separate or recreate Units, you will be responsible for any fees or expenses payable in connection with that separation or recreation, and we will have no liability therefor.

DESCRIPTION OF THE PURCHASE CONTRACTS

The purchase contracts will be issued pursuant to the terms and provisions of the purchase contract agreement. The following summary of the terms of the purchase contracts contains a description of certain terms of the purchase contracts, but is not complete and is subject to, and is qualified in its entirety by reference to, all of the provisions of the purchase contract agreement, including the definitions of specified terms in the purchase contract agreement. We refer you to the purchase contract agreement which will be filed as an exhibit to a current report on Form 8-K and incorporated by reference as an exhibit to the registration statement of which this prospectus supplement forms a part. See "Where You Can Find More Information."

Each purchase contract will initially form a part of a Unit. Each Unit may be separated by a holder into its constituent purchase contract and amortizing note on any business day during the period beginning on, and including, the business day immediately following the date of initial issuance of the Units to, but excluding, the second scheduled trading day immediately preceding April 30, 2022 or, if earlier, the second scheduled trading day immediately preceding any "early mandatory settlement date" or the second scheduled trading day immediately preceding any "acquisition redemption settlement date," and also excluding the business day immediately preceding any installment payment date (*provided*, the right to separate the Units shall resume after such business day). Following such separation, purchase contracts may be transferred separately from amortizing notes.

As used in this section, unless the context otherwise requires, references to:

- "Aqua America," "we," "us" or "our" refer to Aqua America, Inc. and do not include any of its existing or future subsidiaries;
- "close of business" refer to 5:00 p.m., New York City time; and
- "open of business" refer to 9:00 a.m., New York City time.

Delivery of Common Stock

Unless previously redeemed or settled early at your or our option, for each purchase contract we will deliver to you on April 30, 2022 (subject to postponement in certain limited circumstances described below, the "mandatory settlement date") a number of shares of our common stock. The number of shares of our common stock issuable upon settlement of each purchase contract (the "settlement rate") will be determined as follows:

- if the "applicable market value" (as defined below) of our common stock is greater than the "threshold appreciation price" (as defined below), then you will receive 1.1790 shares of common stock for each purchase contract (the "minimum settlement rate");
- if the applicable market value of our common stock is less than or equal to the threshold appreciation price but greater than or equal to the "reference price" (as defined below), then you will receive a number of shares of common stock for each purchase contract equal to the Unit stated amount of $50.00, *divided by* the applicable market value; and
- if the applicable market value of our common stock is less than the reference price, then you will receive 1.4442 shares of common stock for each purchase contract (the "maximum settlement rate").

The maximum settlement rate and the minimum settlement rate are each subject to adjustment as described under "—Adjustments to the Fixed Settlement Rates" below. Each of the minimum settlement rate and the maximum settlement rate is referred to as a "fixed settlement rate."

The reference price is calculated by dividing $50.00 by the then applicable maximum settlement rate and initially is approximately equal to $34.62, which is the per share public offering price of our common stock in the concurrent common stock offering.

The threshold appreciation price is calculated by dividing $50.00 by the then applicable minimum settlement rate. The threshold appreciation price, which is initially approximately $42.41, represents a premium of approximately 22.5% over the reference price.

"Applicable market value" means the arithmetic average of the VWAP per share of our common stock over the settlement period.

"Settlement period" means the 20 consecutive trading day period beginning on, and including, the 21st scheduled trading day immediately preceding April 30, 2022.

"VWAP" per share of our common stock on any trading day means the per share volume-weighted average price as displayed under the heading "Bloomberg VWAP" on Bloomberg (or any successor service) page "WTR <Equity> AQR" (or its equivalent successor if such page is not available) in respect of the period from the scheduled open until the scheduled close of trading of the primary trading session on such trading day; or, if such price is not available, the market value per share of our common stock on such trading day as determined, using a volume-weighted average method, by a nationally recognized independent investment banking firm retained by us for this purpose. For the avoidance of doubt, "VWAP" will be determined without regard to after hours trading or any other trading outside of the regular trading session trading hours.

"Trading day" means a day on which:

- there is no "market disruption event" (as defined below); and
- trading in our common stock (or other security for which a VWAP must be determined) generally occurs on the relevant stock exchange (as defined below);

provided, that if our common stock (or such other security) is not so listed or traded, "trading day" means a "business day."

"Relevant stock exchange" means the NYSE or, if our common stock (or other security for which a VWAP or closing price must be determined) is not then listed on the NYSE, on the principal other U.S. national or regional securities exchange on which our common stock (or such other security) is then listed or, if our common stock (or such other security) is not then listed on a U.S. national or regional securities exchange, on the principal other market on which our common stock (or such other security) is then listed or admitted for trading.

"Scheduled trading day" means a day that is scheduled to be a trading day on the relevant stock exchange. If our common stock (or other such security) is not listed or admitted for trading on a relevant stock exchange, "scheduled trading day" means a "business day."

"Market disruption event" means:

- a failure by the relevant stock exchange to open for trading during its regular trading session; or
- the occurrence or existence on the relevant stock exchange prior to 1:00 p.m., New York City time, on any scheduled trading day for our common stock (or such other security) for more than one half-hour period in the aggregate during regular trading hours of any suspension or limitation imposed on trading (by reason of movements in price exceeding limits permitted by the relevant stock exchange or otherwise) in our common stock (or such other security) or in any options contracts or futures contracts relating to our common stock (or such other security).

On the mandatory settlement date, our common stock will be issued and delivered to you or your designee, upon:

- surrender of certificates representing the purchase contracts, if such purchase contracts are held in certificated form; and
- payment by you of any transfer or similar taxes payable in connection with the issuance of our common stock to any person other than you.

As long as the purchase contracts are evidenced by one or more global purchase contract certificates deposited with DTC, procedures for settlement will be governed by DTC's applicable procedures.

If one or more of the 20 consecutive scheduled trading days in the settlement period is not a trading day, the mandatory settlement date will be postponed until the second scheduled trading day immediately following the last trading day of the settlement period.

Prior to the close of business on the last trading day of the settlement period, the shares of common stock underlying each purchase contract will not be outstanding, and the holder of such purchase contract will not have any voting rights, rights to dividends or other distributions or other rights of a holder of our common stock by virtue of holding such purchase contract. The person in whose name any shares of our common stock shall be issuable upon settlement of the purchase contract on the mandatory settlement date will be treated as the holder of record of such shares as of the close of business on the last trading day of the settlement period.

We will pay any documentary, stamp or similar issue or transfer tax due on the issue of any shares of our common stock upon settlement or redemption of the purchase contracts, unless the tax is due because the holder requests any shares to be issued in a name other than the holder's name, in which case the holder will be obligated to pay that tax.

Hypothetical Settlement Values

For illustrative purposes only, the following table shows the number of shares of common stock issuable upon settlement of a purchase contract at assumed applicable market values. The table assumes that there will be no adjustments to the fixed settlement rates described under "—Adjustments to the Fixed Settlement Rates" below and that the purchase contracts have not been redeemed as described under "—Acquisition Termination Redemption" below or settled early at the option of holders or at our option as described under "—Early Settlement," "—Early Settlement Upon a Fundamental Change" or "—Early Mandatory Settlement at Our Election" below. The actual applicable market value may differ from those set forth in the table below. Based on a reference price of approximately $34.62 and a threshold appreciation price of approximately $42.41, a holder of a Unit or a separate purchase contract, as applicable, would receive on the mandatory settlement date the number of shares of common stock for each Unit or separate purchase contract set forth below:

Assumed Applicable Market Value	Number of Shares of Common Stock to be Received on the Mandatory Settlement Date	Assumed Settlement Value (Calculated as Applicable Market Value multiplied by the Number of Shares of Common Stock to be received on the Mandatory Settlement Date)
$ 10.00	1.4442	$ 14.44
$ 15.00	1.4442	$ 21.66
$ 20.00	1.4442	$ 28.88
$ 25.00	1.4442	$ 36.11
$ 30.00	1.4442	$ 43.33
$ 32.00	1.4442	$ 46.21
$ 34.62	1.4442	$ 50.00
$ 37.00	1.3514	$ 50.00
$ 39.00	1.2821	$ 50.00
$ 41.00	1.2195	$ 50.00
$ 42.41	1.1790	$ 50.00
$ 45.00	1.1790	$ 53.06
$ 47.00	1.1790	$ 55.41
$ 50.00	1.1790	$ 58.95
$ 60.00	1.1790	$ 70.74
$ 70.00	1.1790	$ 82.53
$ 80.00	1.1790	$ 94.32
$ 90.00	1.1790	$106.11
$100.00	1.1790	$117.90

As the above table illustrates, if, on the mandatory settlement date, the applicable market value is greater than the threshold appreciation price, we would be obligated to deliver 1.1790 shares of common stock for each purchase contract. As a result, if the applicable market value exceeds the threshold appreciation price, you will receive only a portion of the appreciation in the market value of the shares of our common stock you would have received had you purchased $50.00 worth of shares of common stock at the public offering price in the concurrent common stock offering.

If, on the mandatory settlement date, the applicable market value is less than or equal to the threshold appreciation price but greater than or equal to the reference price of approximately $34.62, we would be obligated to deliver a number of shares of our common stock on the mandatory settlement date equal to $50.00, *divided by* the applicable market value. As a result, we would retain all appreciation in the market value of our common stock underlying each purchase contract between the reference price and the threshold appreciation price.

If, on the mandatory settlement date, the applicable market value is less than the reference price of approximately $34.62, we would be obligated to deliver upon settlement of the purchase contract 1.4442 shares of common stock for each purchase contract, regardless of the market price of our common stock. As a result, the holder would realize the entire loss on the decline in market value of the common stock underlying each purchase contract since the date of the pricing of Units.

Because the applicable market value of the common stock is determined over the settlement period, the number of shares of common stock delivered for each purchase contract may be greater than or less than the number that would have been delivered based on the closing price (or VWAP) per share of the common stock on the last trading day in the settlement period. In addition, you will bear the risk of fluctuations in the market price

of the shares of common stock deliverable upon settlement of the purchase contracts between the last trading day in the settlement period and the date such shares are delivered.

Early Settlement

Prior to the close of business on the second scheduled trading day immediately preceding April 30, 2022, you, as a holder of Units or a holder of separate purchase contracts, may elect to settle your purchase contracts early, in whole or in part, and receive a number of shares of common stock per purchase contract equal to the "early settlement rate" (and any cash payable for fractional shares). The early settlement rate is equal to the minimum settlement rate in effect on the early settlement date unless you elect to settle your purchase contracts early in connection with a fundamental change, in which case you will receive upon settlement of your purchase contracts a number of shares of our common stock based on the "fundamental change early settlement rate" as described under "— Early Settlement Upon a Fundamental Change."

Your right to receive common stock (and any cash payable for fractional shares) upon early settlement of a purchase contract is subject to:

- delivery of a written and signed notice of election (an "early settlement notice") to the purchase contract agent electing early settlement of such purchase contract;
- if the Unit that includes such purchase contract or such purchase contract is held in certificated form, surrendering the certificates representing the purchase contract, or if held in global form, surrendering in accordance with DTC's applicable procedures; and
- payment by you of any transfer or similar taxes payable in connection with the issuance of our common stock to any person other than you.

As long as the purchase contracts or the Units are evidenced by one or more global certificates deposited with DTC, procedures for early settlement will be governed by DTC's applicable procedures.

Upon surrender of the Unit or the separate purchase contract and payment of any applicable transfer or similar taxes due because of any issue of such shares in a name of a person other than the holder, you will receive the applicable number of shares of common stock (and any cash payable for fractional shares) due upon early settlement on the second business day following the "early settlement date" (as defined below).

If you comply with the requirements for effecting early settlement of your purchase contracts earlier than the close of business on any business day, then that day will be considered the "early settlement date." If you comply with such requirements at or after the close of business on any business day or at any time on a day that is not a business day, then the next succeeding business day will be considered the "early settlement date." Prior to the close of business on the early settlement date, the shares of common stock underlying each purchase contract will not be outstanding, and the holder of such purchase contract will not have any voting rights, rights to dividends or other distributions or other rights of a holder of our common stock by virtue of holding such purchase contract. The person in whose name any shares of our common stock shall be issuable upon such early settlement of the purchase contract will be treated as the holder of record of such shares as of the close of business on the relevant early settlement date.

Upon early settlement at the holder's election of the purchase contract component of a Unit, the amortizing note underlying such Unit will remain outstanding and be beneficially owned by or registered in the name of, as the case may be, the holder who elected to settle the related purchase contract early and will no longer constitute a part of the Unit.

Early Settlement Upon a Fundamental Change

If a "fundamental change" occurs and you elect to settle your purchase contracts early in connection with such fundamental change, you will receive per purchase contract a number of shares of our common stock (and any cash payable for fractional shares) (or, if a reorganization event has occurred, cash, securities or other property, as applicable) equal to the "fundamental change early settlement rate," as described below. An early settlement will be deemed for these purposes to be "in connection with" such fundamental change if you deliver your early settlement notice to the purchase contract agent, and otherwise satisfy the requirements for effecting early settlement of your purchase contracts, during the period beginning on, and including, the effective date of the fundamental change and ending at the close of business on the 35th business day thereafter (or, if earlier, the second scheduled trading day immediately preceding April 30, 2022) (the "fundamental change early settlement period"). We refer to this right as the "fundamental change early settlement right."

A holder's right to common stock (and any cash payable for fractional shares) (or, if a reorganization event has occurred, cash, securities or other property, as applicable) upon early settlement in connection with a fundamental change is subject to compliance with the conditions described under "—Early Settlement."

Upon surrender of the Unit or the separate purchase contract and payment of any applicable transfer or similar taxes due because of any issue of such shares in a name of a person other than the holder, you will receive the applicable number of shares of common stock (and any cash payable for fractional shares) (or, if a reorganization event has occurred, cash, securities or other property, as applicable) issuable as a result of your exercise of the fundamental change early settlement right on the second business day following the "fundamental change early settlement date" (as defined below).

If you comply with the requirements for effecting early settlement of your purchase contracts in connection with a fundamental change prior to the close of business on any business day during the fundamental change early settlement period, then that day will be considered the "fundamental change early settlement date." If you comply with such requirements at or after the close of business on any business day during the fundamental change early settlement period or at any time on a day during the fundamental change early settlement period that is not a business day, then the next succeeding business day will be considered the "fundamental change early settlement date."

We will provide the purchase contract agent, the trustee and the holders of Units and separate purchase contracts with a notice of a fundamental change within five business days after its effective date and issue a press release announcing such effective date. The notice will also set forth, among other things:

- the applicable fundamental change early settlement rate;
- if not common stock, the kind and amount of cash, securities and other property receivable by the holder upon settlement; and
- the deadline by which each holder's fundamental change early settlement right must be exercised.

A "fundamental change" will be deemed to have occurred upon the occurrence of any of the following:

- any "person" or "group" within the meaning of Section 13(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), other than us, any of our subsidiaries and any of our and their employee benefit plans, files a Schedule TO or any other schedule, form or report under the Exchange Act disclosing that such person or group has become the direct or indirect "beneficial owner" (as defined in Rule 13d-3 under the Exchange Act) of our common stock representing more than 50% of the voting power of our common stock;

- the consummation of (A) any recapitalization, reclassification or change of our common stock (other than changes resulting from a subdivision or combination) as a result of which our common stock would be converted into, or exchanged for, stock, other securities, other property or assets; (B) any share exchange, consolidation or merger of us pursuant to which our common stock will be converted into cash, securities or other property or assets; or (C) any sale, lease or other transfer in one transaction or a series of transactions of all or substantially all of the consolidated assets of us and our subsidiaries, taken as a whole, to any person or persons other than one of our wholly owned subsidiaries;

- our stockholders approve any plan or proposal for the liquidation or dissolution of us; or

- our common stock (or other common stock receivable upon settlement of your purchase contracts, if applicable) ceases to be listed or quoted on any of the NYSE, the NASDAQ Global Select Market or the NASDAQ Global Market (or any of their respective successors).

A transaction or transactions described in clauses (1) or (2) above will not constitute a fundamental change, however, if (a) at least 90% of the consideration received or to be received by our common stockholders (excluding cash payments for fractional shares and cash payments made in respect of dissenters' appraisal rights) in connection with such transaction or transactions consists of shares of common stock that are listed or quoted on any of the NYSE, the NASDAQ Global Select Market or the NASDAQ Global Market (or any of their respective successors), or will be so listed or quoted when issued or exchanged in connection with such transaction or transactions, and (b) as a result of such transaction or transactions such consideration becomes the consideration receivable upon settlement of your purchase contracts, if applicable, excluding cash payments for fractional shares.

If any transaction in which our common stock is replaced by the securities of another entity occurs, following completion of any related fundamental change early settlement period (or, in the case of a transaction that would have been a fundamental change but for the immediately preceding paragraph, following the effective date of such transaction), references to us in the definition of "fundamental change" above shall instead be references to such other entity.

The "fundamental change early settlement rate" will be determined by us by reference to the table below, based on the date on which the fundamental change occurs or becomes effective (the "effective date") and the "stock price" in the fundamental change, which will be:

- in the case of a fundamental change described in clause (2) of the definition of "fundamental change" in which all holders of shares of our common stock receive only cash in the fundamental change, the stock price will be the cash amount paid per share of our common stock; and

- in all other cases, the stock price will be the arithmetic average of the VWAPs of our common stock over the five consecutive trading day period ending on, and including, the trading day immediately preceding the effective date.

The stock prices set forth in the column headings of the table below will be adjusted as of any date on which the fixed settlement rates are adjusted. The adjusted stock prices will equal the stock prices applicable immediately prior to such adjustment, multiplied by a fraction, the numerator of which is the maximum settlement rate immediately prior to the adjustment giving rise to the stock price adjustment and the denominator of which is the maximum settlement rate as so adjusted. The fundamental change early settlement rates per purchase contract in the table below will be adjusted in the same manner and at the same time as the fixed settlement rates as set forth under "—Adjustments to the Fixed Settlement Rates."

The following table sets forth the fundamental change early settlement rate per purchase contract for each stock price and effective date set forth below:

	Stock Price												
Effective Date	**$ 10.00**	**$ 17.50**	**$ 25.00**	**$ 30.00**	**$ 34.62**	**$ 37.50**	**$ 40.00**	**$ 42.41**	**$ 45.00**	**$ 50.00**	**$ 60.00**	**$ 75.00**	**$100.00**
April 23, 2019	1.1093	1.2275	1.2513	1.2383	1.2837	1.1947	1.1785	1.1641	1.1508	1.1340	1.1290	1.1382	1.1483
July 30, 2019	1.1358	1.2458	1.2667	1.2520	1.2882	1.2043	1.1865	1.1706	1.1561	1.1380	1.1332	1.1418	1.1510
October 30, 2019	1.1610	1.2630	1.2814	1.2652	1.2928	1.2135	1.1940	1.1766	1.1608	1.1415	1.1371	1.1451	1.1535
January 30, 2019	1.1867	1.2805	1.2964	1.2790	1.2979	1.2229	1.2016	1.1824	1.1652	1.1449	1.1411	1.1485	1.1560
April 30, 2020	1.2130	1.2982	1.3119	1.2933	1.3036	1.2327	1.2091	1.1881	1.1693	1.1481	1.1452	1.1518	1.1585
July 30, 2020	1.2399	1.3161	1.3277	1.3081	1.3096	1.2425	1.2164	1.1932	1.1727	1.1510	1.1493	1.1552	1.1611
October 30, 2020	1.2673	1.3343	1.3439	1.3238	1.3175	1.2527	1.2237	1.1978	1.1755	1.1538	1.1535	1.1586	1.1636
January 30, 2021	1.2953	1.3525	1.3605	1.3403	1.3382	1.2633	1.2306	1.2015	1.1773	1.1566	1.1577	1.1619	1.1662
April 30, 2021	1.3239	1.3710	1.3776	1.3581	1.3591	1.2746	1.2371	1.2041	1.1779	1.1599	1.1619	1.1653	1.1687
July 30, 2021	1.3531	1.3894	1.3951	1.3773	1.3802	1.2867	1.2427	1.2044	1.1769	1.1639	1.1662	1.1687	1.1713
October 30, 2021	1.3829	1.4079	1.4127	1.3987	1.4014	1.3005	1.2466	1.2013	1.1745	1.1687	1.1704	1.1721	1.1739
January 30, 2022	1.4132	1.4262	1.4297	1.4224	1.4227	1.3178	1.2470	1.1925	1.1736	1.1739	1.1747	1.1756	1.1764
April 30, 2022	1.4442	1.4442	1.4442	1.4442	1.4442	1.3333	1.2500	1.1790	1.1790	1.1790	1.1790	1.1790	1.1790

The exact stock price and effective date may not be set forth in the table above, in which case:

- if the applicable stock price is between two stock prices in the table or the applicable effective date is between two effective dates in the table, the fundamental change early settlement rate will be determined by straight line interpolation between the fundamental change early settlement rates set forth for the higher and lower stock prices and the earlier and later effective dates, as applicable, based on a 365-or 366-day year, as applicable;

- if the applicable stock price is greater than $100.00 per share (subject to adjustment in the same manner and at the same time as the stock prices set forth in the column headings of the table above), then the fundamental change early settlement rate will be the minimum settlement rate; or

- if the applicable stock price is less than $10.00 per share (subject to adjustment in the same manner and at the same time as the stock prices set forth in the column headings of the table above, the "minimum stock price"), the fundamental change early settlement rate will be determined as if the stock price equaled the minimum stock price, and using straight line interpolation, as described in the first bullet of this paragraph, if the effective date is between two effective dates in the table.

The maximum number of shares of our common stock deliverable under a purchase contract is 1.4442, subject to adjustment in the same manner and at the same time as the fixed settlement rates as set forth under "—Adjustments to the Fixed Settlement Rates."

Our obligation to settle the purchase contracts at the fundamental change early settlement rate could be considered a penalty, in which case the enforceability thereof would be subject to general principles of reasonableness of economic remedies.

We will deliver the shares of our common stock (and any cash payable for fractional shares) (or, if a reorganization event has occurred, cash, securities or other property, as applicable) payable as a result of your exercise of the fundamental change early settlement right on the second business day following the fundamental change early settlement date.

Prior to the close of business on the fundamental change early settlement date, the shares of common stock or other securities, if applicable, underlying each purchase contract will not be outstanding, and the holder of such purchase contract will not have any voting rights, rights to dividends or other distributions or other rights of a holder of our common stock or such other securities by virtue of holding such purchase contract. The person in whose name any shares of our common stock or such other securities shall be deliverable following exercise of a holder's fundamental change early settlement right will be treated as the holder of record of such shares or such other securities as of the close of business on the fundamental change early settlement date.

Upon early settlement at the holder's election upon a fundamental change of the purchase contract component of a Unit, the amortizing note underlying such Unit will remain outstanding and will be beneficially owned by or registered in the name of, as the case may be, the holder who elected to settle the related purchase contract early upon the fundamental change and will no longer constitute a part of the Unit.

If you do not elect to exercise your fundamental change early settlement right, your purchase contracts will remain outstanding and will be subject to normal settlement on any subsequent early settlement date, any subsequent fundamental change early settlement date, any subsequent early mandatory settlement date or the mandatory settlement date or redemption on any subsequent acquisition redemption settlement date, as the case may be.

For the avoidance of doubt, each of the calculation methodologies and adjustments described above also shall apply if the fundamental change repurchase rate is being used as the acquisition redemption rate as described below under "—Acquisition Termination Redemption."

Early Mandatory Settlement at Our Election

We have the right to settle the purchase contracts on or after January 30, 2020, in whole but not in part, on a date fixed by us as described below at the "early mandatory settlement rate" described below. We refer to this right as our "early mandatory settlement right."

The "early mandatory settlement rate" will be the maximum settlement rate as of the date (the "notice date") of the early mandatory settlement notice (as defined below) unless the closing price (as defined below) per share of our common stock for at least 20 trading days (whether or not consecutive), including the trading day immediately preceding the notice date in a period of 30 consecutive trading days ending on, and including, the trading day immediately preceding the notice date exceeds 130% of the threshold appreciation price in effect on each such trading day, in which case the "early mandatory settlement rate" will be the minimum settlement rate as of the notice date.

The "closing price" per share of our common stock (or any other security) on any day means:

- the closing sale price per share (or if no closing sale price is reported, the average of the bid and ask prices or, if more than one in either case, the average of the average bid and the average ask prices) on that date as reported in composite transactions for the relevant stock exchange;
- if our common stock (or any other security) is not listed for trading on a relevant stock exchange on the relevant date, the last quoted bid price for our common stock (or such other security) in the over-the-counter market on the relevant date as reported by OTC Markets Group Inc. or a similar organization; and
- if our common stock (or any other security) is not so quoted, the average of the mid-point of the last bid and ask prices for our common stock (or such other security) on the relevant date from each of at least three nationally recognized independent investment banking firms selected by us for this purpose.

In the event we elect to settle the purchase contracts early, holders of the amortizing notes (whether as components of Units or separate amortizing notes) will have the right to require us to repurchase some or all of their amortizing notes on the repurchase date and at the repurchase price, as described under "Description of the Amortizing Notes—Repurchase of Amortizing Notes at the Option of the Holder." If we exercise our early mandatory settlement right and the holder of any Unit does not require us to repurchase the amortizing note that is a component of such Unit, such amortizing note will remain outstanding and will be beneficially owned by or registered in the name of, as the case may be, such holder. If we exercise our early mandatory settlement right and the holder of any Unit requires us to repurchase the amortizing note that is a component of such Unit

but the related repurchase date falls after the early mandatory settlement date, such amortizing note will remain outstanding (pending such repurchase date) and will be beneficially owned by or registered in the name of, as the case may be, such holder.

If we elect to exercise our early mandatory settlement right, we will provide the purchase contract agent and the holders of Units, separate purchase contracts and separate amortizing notes with a notice of our election (the "early mandatory settlement notice") and issue a press release announcing our election. The early mandatory settlement notice will specify, among other things:

- the early mandatory settlement rate;
- the date on which we will deliver shares of our common stock (and any cash payable for fractional shares) following exercise of our early mandatory settlement right (the "early mandatory settlement date"), which will be on or after January 30, 2020 and at least five but not more than 20 business days following the notice date;
- that holders of Units and separate amortizing notes will have the right to require us to repurchase their amortizing notes that are a component of the Units or their separate amortizing notes, as the case may be (subject to certain exceptions described under "Description of the Amortizing Notes—Repurchase of Amortizing Notes at the Option of the Holder");
- if applicable, the "repurchase price" and "repurchase date" (each as defined below under "Description of the Amortizing Notes—Repurchase of Amortizing Notes at the Option of the Holder");
- if applicable, the last date on which holders of amortizing notes may exercise their repurchase right; and
- if applicable, the procedures that holders of amortizing notes must follow to require us to repurchase their amortizing notes.

We will deliver the shares of our common stock (and any cash payable for fractional shares) to you on the early mandatory settlement date.

Prior to the close of business on the notice date, the shares of common stock underlying each purchase contract will not be outstanding, and the holder of such purchase contract will not have any voting rights, rights to dividends or other distributions or other rights of a holder of our common stock by virtue of holding such purchase contract. The person in whose name any shares of our common stock shall be issuable following exercise of our early mandatory settlement right will be treated as the holder of record of such shares as of the close of business on the notice date.

Acquisition Termination Redemption

If the closing of the Acquisition has not occurred on or prior to April 22, 2020, or if, prior to such date, the Purchase Agreement is terminated, we may elect to redeem all, but not less than all, of the outstanding purchase contracts on the terms described below (an "acquisition termination redemption"), by delivering notice during the five business day period immediately following the earlier of (x) April 22, 2020 if the closing of the Acquisition has not occurred on or prior to such date and (y) the date on which the Purchase Agreement is terminated (such notice, the "acquisition redemption notice") to the purchase contract agent, the trustee and all holders of Units, separate purchase contracts or separate amortizing notes and will issue a press release announcing any such election.

In the event of an acquisition termination redemption, you will have the right to require us to repurchase your amortizing notes (whether as components of Units or separate amortizing notes) on the repurchase date and at the repurchase price, as described under "Description of the Amortizing Notes—Repurchase of Amortizing Notes at the Option of the Holder." If we exercise our right to cause an acquisition termination redemption and the holder of any Unit or separate amortizing note does not require us to repurchase such amortizing note, such amortizing note will remain outstanding and be beneficially owned by or registered in the name of, as the case may be, such holder. If we exercise our right to cause an acquisition termination redemption and the holder of any Unit requires us to repurchase the amortizing note that is a component of such Unit but the related repurchase date falls after the acquisition termination settlement date, such amortizing note will remain outstanding (pending such repurchase date) and will be beneficially owned by or registered in the name of, as the case may be, such holder.

As further described below, redemptions of purchase contracts pursuant to an acquisition termination redemption will be settled in cash if the relevant acquisition termination stock price is equal to or less than the reference price. If the relevant acquisition termination stock price is greater than the reference price, redemptions of purchase contracts pursuant to an acquisition termination redemption will be settled in shares of our common stock, with the amount of such common stock to be determined by reference to the table set forth above in "—Early Settlement Upon a Fundamental Change"; provided that, in such case, we may elect to pay cash in lieu of delivering any or all of such number of shares of our common stock, all as further described below.

The acquisition redemption notice will specify, among other things:

- the "acquisition termination stock price" (as defined below);
- the "scheduled acquisition redemption settlement date" (as defined below);
- if the "redemption amount" (as defined below) is determined pursuant to the first bullet point in the definition thereof, the redemption amount;
- if the redemption amount is determined pursuant to the second bullet point in the definition thereof, the acquisition redemption rate, and, if applicable, the number of shares of our common stock that would otherwise be included in the applicable redemption amount that will be replaced with cash;
- that holders of Units and separate amortizing notes will have the right to require us to repurchase their amortizing notes that are a component of the Units or their separate amortizing notes, as the case may be, as described under "Description of the Amortizing Notes—Repurchase of Amortizing Notes at the Option of the Holder";
- if applicable, the "repurchase price" and "repurchase date," each as defined below under "Description of the Amortizing Notes—Repurchase of Amortizing Notes at the Option of the Holder";
- if applicable, the last date on which holders of amortizing notes may exercise their repurchase right; and
- if applicable, the procedures that holders of amortizing notes must follow to require us to repurchase their amortizing notes.

If we do not specify a number of shares of common stock that will be replaced with cash in the acquisition redemption notice, we will be deemed to have elected to settle the redemption amount solely in shares of common stock.

In the event of an acquisition termination redemption, we will deliver the applicable redemption amount on the acquisition redemption settlement date. "Redemption amount" per purchase contract means:

- if the acquisition termination stock price is equal to or less than the reference price, an amount of cash equal to (x) $50.00 less (y) the applicable repurchase price for the amortizing notes; or

- if the acquisition termination stock price is greater than the reference price, a number of shares of our common stock (the "acquisition redemption rate") equal to the number of shares of our common stock determined by reference to the table set forth above in "—Early Settlement Upon a Fundamental Change" (with references to "stock price" deemed to refer to the "acquisition termination stock price," references to "fundamental change early settlement rate" deemed to refer to the "acquisition redemption rate," and references to "effective date" deemed to refer to the date of the related acquisition redemption notice); *provided* that we may elect to pay cash in lieu of delivering any or all of the shares of our common stock in an amount equal to such number of shares *multiplied by* the redemption market value; *provided further* that, if we so elect to pay cash, we will specify in the acquisition redemption notice the number of shares of our common stock that will be replaced with cash.

"Acquisition termination stock price" means the arithmetic average of the VWAPs of our common stock over the five consecutive trading day period ending on, and including, the trading day immediately preceding the date we provide the acquisition redemption notice.

"Redemption market value" means the arithmetic average of the VWAPs of our common stock for the 20 consecutive trading day period beginning on, and including, the 21st scheduled trading day immediately preceding the scheduled acquisition redemption settlement date.

"Acquisition redemption settlement date" means:

- if (x) the acquisition termination stock price is greater than the reference price and (y) we elect to pay cash in lieu of delivering any or all of the shares of our common stock that would otherwise be included in the redemption amount, the second business day following the last trading day of the 20 consecutive trading day period used to determine the redemption market value; or

- otherwise, the scheduled acquisition redemption settlement date specified in the acquisition redemption notice.

"Scheduled acquisition redemption settlement date" means:

- if (x) the acquisition termination stock price is greater than the reference price and (y) we elect to pay cash in lieu of delivering any or all of the shares of our common stock that would otherwise be included in the redemption amount, a date that is at least 30 and no more than 60 calendar days after the date of the acquisition redemption notice; or

- otherwise, a date that is at least 5 and no more than 30 calendar days after the date of the acquisition redemption notice.

The person in whose name any shares of our common stock shall be issuable will be treated as the holder of record of such shares as of the close of business on:

- the date of the acquisition redemption notice, if we have elected (or are deemed to have elected) to settle the redemption amount solely in shares of our common stock, or

- the last trading day in the 20 consecutive trading day period used to determine the redemption market value, if the acquisition termination stock price is greater than the reference price and we have elected

to pay cash in lieu of delivering any of the shares of our common stock that would otherwise be included in the redemption amount.

Prior to such time, the shares of common stock underlying each purchase contract will not be outstanding, and the holder of such purchase contract will not have any voting rights, rights to dividends or other distributions or other rights of a holder of our common stock by virtue of holding such purchase contract, but, for the avoidance of doubt, the anti-dilution adjustments provided herein under "—Adjustments to the Fixed Settlement Rates" below will continue to apply to the purchase contracts prior to such time.

Adjustments to the Fixed Settlement Rates

The fixed settlement rates will be adjusted as described below, except that we will not make any adjustments to the fixed settlement rates if holders of the purchase contracts participate (other than in the case of (x) a share split or share combination or (y) a tender or exchange offer), at the same time and upon the same terms as holders of our common stock and solely as a result of holding the purchase contracts, in any of the transactions described below without having to settle their purchase contracts as if they held a number of shares of our common stock equal to the maximum settlement rate, *multiplied by* the number of purchase contracts held by such holders.

(a) If we issue common stock to all or substantially all of the holders of our common stock as a dividend or other distribution, or if we effect a share split or share combination, then each fixed settlement rate will be adjusted based on the following formula:

$$SR_1 = SR_0 \times \frac{OS_1}{OS_0}$$

where,

SR_0 = the fixed settlement rate in effect immediately prior to the close of business on the record date (as defined below) for such dividend or distribution or immediately prior to the open of business on the effective date (as defined below) for such share split or share combination, as the case may be;

SR_1 = the fixed settlement rate in effect immediately after the close of business on such record date or immediately after the open of business on such effective date, as the case may be;

OS_0 = the number of shares of our common stock outstanding immediately prior to the close of business on such record date or immediately prior to the open of business on such effective date, as the case may be (in either case, prior to giving effect to such event); and

OS_1 = the number of shares of our common stock that would be outstanding immediately after, and solely as a result of, such dividend, distribution, share split or share combination.

Any adjustment made pursuant to this clause (a) will become effective immediately after the close of business on the record date for such dividend or distribution, or immediately after the open of business on the effective date for such share subdivision or share combination, as the case may be. If any dividend or distribution described in this clause (a) is declared but not so paid or made, each fixed settlement rate will be readjusted, effective as of the date our board of directors (or a committee thereof) publicly announces its decision not to make such dividend or distribution, to such fixed settlement rate that would be in effect if such dividend or distribution had not been declared. For the purposes of this clause (a), the number of shares of common stock outstanding immediately prior to the close of business on the record date for such dividend or distribution or the open of business on the effective date for such share subdivision or share combination, as applicable, will not include shares held in treasury but will include any shares issuable in respect of any scrip certificates issued in

lieu of fractions of shares of common stock. We will not pay any such dividend or make any such distribution on shares of common stock held in treasury.

"Record date" means, when used with respect to any dividend, distribution or other transaction or event in which the holders of our common stock (or other applicable security) have the right to receive any cash, securities or other property or in which our common stock (or other applicable security) is exchanged for or converted into any combination of cash, securities or other property, the date fixed for determination of holders of our common stock (or other applicable security) entitled to receive such cash, securities or other property (whether such date is fixed by our board of directors or a committee thereof, or by statute, contract or otherwise).

"Effective date" means the first date on which the shares of our common stock trade on the relevant stock exchange, regular way, reflecting the relevant share split or share combination, as applicable.

(b) If we issue to all or substantially all holders of our common stock rights, options or warrants (other than rights issued pursuant to a stockholder rights plan) entitling them, for a period of up to 45 calendar days from the date of issuance of such rights, options or warrants, to subscribe for or purchase our shares of common stock at a price per share less than the average of the closing prices (as defined under "—Early Mandatory Settlement at Our Election) per share of our common stock for the 10 consecutive trading day (as defined below) period ending on, and including, the trading day immediately preceding the date of announcement for such distribution per share of our common stock, then each fixed settlement rate will be adjusted based on the following formula:

$$SR_1 = SR_0 \times \frac{(OS_0 + X)}{(OS_0 + Y)}$$

where,

SR_0 = the fixed settlement rate in effect immediately prior to the close of business on the record date for such issuance;

SR_1 = the fixed settlement rate in effect immediately after the close of business on such record date;

OS_0 = the number of shares of our common stock outstanding immediately prior to the close of business on such record date;

X = the total number of shares of our common stock issuable pursuant to such rights, options or warrants; and

Y = the total number of shares of our common stock equal to the aggregate price payable to exercise such rights, options or warrants, *divided by* the average of the closing prices per share of our common stock for the 10 consecutive trading day period ending on, and including, the trading day immediately preceding the date of announcement for such distribution.

Any adjustment made pursuant to this clause (b) will be made successively whenever any such rights, options or warrants are issued and will become effective immediately after the close of business on the record date for such issuance. In the event that such rights, options or warrants described in this clause (b) are not so issued, each fixed settlement rate will be readjusted, effective as of the date our board of directors (or a committee thereof) publicly announces its decision not to issue such rights, options or warrants, to such fixed settlement rate that would then be in effect if such issuance had not been declared. To the extent that such rights, options or warrants are not exercised prior to their expiration or shares of our common stock are otherwise not delivered pursuant to such rights, options or warrants upon the exercise of such rights, options or warrants, each fixed

settlement rate will be readjusted, effective as of the date of such expiration or the date it is determined such shares will not be delivered, as the case may be, to such fixed settlement rate that would then be in effect had the adjustment made upon the issuance of such rights, options or warrants been made on the basis of the delivery of only the number of shares of our common stock actually delivered.

In determining whether any rights, options or warrants entitle the holders thereof to subscribe for or purchase shares of our common stock at less than the average of the closing prices per share of our common stock for the 10 consecutive trading day period ending on, and including, the trading day immediately preceding the date of announcement for such distribution, and in determining the aggregate price payable to exercise such rights, options or warrants, there will be taken into account any consideration received by us for such rights, options or warrants and any amount payable on exercise or conversion thereof, the value of such consideration, if other than cash, to be determined by our board of directors, or a committee thereof.

For the purposes of this clause (b), the number of shares of common stock at the time outstanding will not include shares held in treasury but will include any shares issuable in respect of any scrip certificates issued in lieu of fractions of shares of common stock. We will not issue any such rights, options or warrants in respect of shares of common stock held in treasury.

(c) (1) If we distribute to all or substantially all holders of our common stock shares of our capital stock (other than our common stock), evidences of our indebtedness, assets or rights, options or warrants to acquire our capital stock, indebtedness or assets, excluding:

- any dividend or distribution (including share splits or share combinations) as to which an adjustment was effected pursuant to clause (a) above;
- any rights, options or warrants as to which an adjustment was effected pursuant to clause (b) above;
- except as otherwise described below, rights issued pursuant to any stockholder rights plan of ours then in effect;
- any dividend or distribution described in clause (d) below;
- distributions of exchange property in a transaction described in "—Recapitalizations, Reclassifications and Changes of Our Common Stock;" and
- any spin-off (as defined below) to which the provisions set forth below in clause (c)(2) shall apply;

then each fixed settlement rate will be adjusted based on the following formula:

$$SR_1 = SR_0 \times \frac{SP_0}{(SP_0 - FMV)}$$

where,

SR_0 = the fixed settlement rate in effect immediately prior to the close of business on the record date for such dividend or distribution;

SR_1 = the fixed settlement rate in effect immediately after the close of business on such record date;

SP_0 = the average of the closing prices per share of our common stock for the 10 consecutive trading day period ending on, and including, the trading day immediately preceding the ex-date for such dividend or distribution; and

FMV = the fair market value (as determined by our board of directors or a committee thereof) on the ex-date for such dividend or distribution, of the shares of our capital stock, evidences of our indebtedness, assets or rights, options or warrants so distributed, expressed as an amount per share of common stock.

Notwithstanding the foregoing, if FMV (as defined above) is equal to or greater than SP_0 (as defined above) or if the difference between SP_0 and FMV is less than $1.00, in lieu of the foregoing adjustment, provision shall be made for each holder of a Unit or separate purchase contract to receive, for each Unit or separate purchase contract, at the same time and upon the same terms as holders of our common stock, the kind and amount of our capital stock, evidences of our indebtedness, assets or rights, options or warrants that such holder would have received if such holder owned a number of shares of our common stock equal to the maximum settlement rate in effect on the record date for the dividend or distribution.

Any adjustment made pursuant to this clause (c)(1) will become effective immediately after the close of business on the record date for such dividend or distribution. In the event that such dividend or distribution is not so made, each fixed settlement rate will be readjusted, effective as of the date our board of directors (or a committee thereof) publicly announces its decision not to make such dividend or distribution, to such fixed settlement rate that would then be in effect if such dividend or distribution had not been declared. We will not make any such distribution on shares of common stock held in treasury.

"Ex-date," when used with respect to any issuance or distribution, means the first date on which shares of our common stock (or other applicable security) trade on the applicable exchange or in the applicable market, regular way, without the right to receive such issuance, dividend or distribution in question from us or, if applicable, from the seller of our common stock (or other applicable security) on such exchange or market (in the form of due bills or otherwise) as determined by such exchange or market.

(c)(2) In the event that we make a dividend or distribution to all or substantially all holders of our common stock consisting of capital stock of, or similar equity interests in, or relating to, a subsidiary or other business unit of ours that, upon issuance, will be traded on a U.S. national securities exchange (herein referred to as a "spin-off"), each fixed settlement rate will be adjusted based on the following formula:

$$SR_1 = SR_0 \quad x \frac{(FMV_0 + MP_0)}{MP_0}$$

where,

SR_0 = the fixed settlement rate in effect immediately prior to the open of business on the ex-date for the spin-off;

SR_1 = the fixed settlement rate in effect immediately after the open of business on the ex-date for the spin-off;

FMV_0 = the average of the closing prices (as defined above, as if references to "common stock" therein were references to such capital stock or similar equity interest distributed to the holders of our common stock) per share of the capital stock or similar equity interests so distributed applicable to one share of our common stock for the 10 consecutive trading day period commencing on, and including, the ex-date date for the spin-off (the "valuation period"); and

MP_0 = the average of the closing prices per share of our common stock for the valuation period.

Any adjustment made pursuant to this clause (c)(2) will become effective immediately after the close of business on the last trading day of the valuation period but will be given effect as of immediately after the open

of business on the ex-date of the spin-off. Because we will make the adjustment to each fixed settlement rate with retroactive effect, we will delay any settlement of a Unit or separate purchase contract where any date for determining the number of shares of our common stock issuable to a holder occurs during the valuation period until the second business day after the last date for determining the number of shares of our common stock issuable to such holder with respect to such settlement occurs. In the event that such dividend or distribution described in this clause (c)(2) is not so made, each fixed settlement rate will be readjusted, effective as of the date our board of directors (or a committee thereof) publicly announces its decision not to pay such dividend or distribution, to such fixed settlement rate that would then be in effect if such distribution had not been declared. We will not make any such dividend or distribution on shares of common stock held in treasury.

(d) If we make a dividend or distribution consisting exclusively of cash to all or substantially all holders of our common stock, excluding:

- any regular quarterly dividend that does not exceed $0.219 per share of common stock (the "dividend threshold amount");
- any cash that is distributed in, and will constitute exchange property as a result of, a reorganization event (as defined below) in exchange for shares of our common stock; and
- any dividend or distribution in connection with our liquidation, dissolution or winding up);

then each fixed settlement rate will be adjusted based on the following formula:

$$SR_1 = SR_0 \times \frac{(SP_0 - T)}{(SP_0 - C)}$$

where,

SR_0 = the fixed settlement rate in effect immediately prior to the close of business on the record date for such dividend or distribution;

SR_1 = the fixed settlement rate in effect immediately after the close of business on the record date for such dividend or distribution;

SP_0 = the average of the closing prices per share of our common stock over the 10 consecutive trading day period ending on, and including, the trading day immediately preceding the ex-date for such dividend or distribution;

T = the dividend threshold amount; *provided* that if the dividend or distribution is not a regular quarterly cash dividend, the dividend threshold amount will be deemed to be zero; and

C = the amount in cash per share we distribute to holders of our common stock.

The dividend threshold amount is subject to adjustment on an inversely proportional basis whenever the fixed settlement rates are adjusted (by multiplying the dividend threshold amount by a fraction, the numerator of which will be the minimum settlement rate in effect immediately prior to the adjustment and the denominator of which will be the minimum settlement rate as adjusted), but no adjustment will be made to the dividend threshold amount for any adjustment made to the fixed settlement rates pursuant to this clause (d).

If C (as defined above) is equal to or greater than SP_0 (as defined above) or if the difference between SP_0 and C is less than $1.00, in lieu of the foregoing adjustment, provision shall be made for each holder of a Unit

or separate purchase contract to receive, for each Unit or separate purchase contract, at the same time and upon the same terms as holders of our common stock, the amount of cash that such holder would have received if such holder owned a number of shares of our common stock equal to the maximum settlement rate on the record date for such cash dividend or distribution.

Any adjustment made pursuant to this clause (d) will become effective immediately after the close of business on the record date for such dividend or distribution. In the event that any dividend or distribution described in this clause (d) is not so made, each fixed settlement rate will be readjusted, effective as of the date our board of directors (or a committee thereof) publicly announces its decision not to pay such dividend or distribution, to such fixed settlement rate which would then be in effect if such dividend or distribution had not been declared. We will not make any such dividend or distribution on shares of common stock held in treasury.

(e) If we or any of our subsidiaries successfully complete a tender or exchange offer for our common stock where the cash and the value of any other consideration included in the payment per share of our common stock validly tendered or exchanged exceeds the average of the closing prices per share of our common stock for the 10 consecutive trading day period (the "averaging period") commencing on, and including, the trading day next succeeding the last date on which tenders or exchanges may be made pursuant to such tender offer or exchange offer (the "expiration date"), then each fixed settlement rate will be adjusted based on the following formula:

$$SR_1 = SR_0 \quad x \frac{(AC + (SP \times OS_1))}{(SP \times OS_0)}$$

where,

SR_0 = the fixed settlement rate in effect immediately prior to the close of business on the expiration date;

SR_1 = the fixed settlement rate in effect immediately after the close of business on the expiration date;

AC = the aggregate value of all cash and the fair market value (as determined by our board of directors, or a committee thereof) on the expiration date of any other consideration paid or payable for shares of common stock acquired pursuant to such tender offer or exchange offer;

OS_1 = the number of shares of our common stock outstanding immediately after the expiration date, after giving effect to the purchase of all shares accepted for purchase or exchange in such tender or exchange offer;

OS_0 = the number of shares of our common stock outstanding immediately prior to the expiration date, prior to giving effect to the purchase of any shares accepted for purchase or exchange in such tender or exchange offer; and

SP = the average of the closing prices per share of our common stock over the averaging period.

Any adjustment made pursuant to this clause (e) will become effective immediately after the close of business on the expiration date. Because we will make the adjustment to each fixed settlement rate with retroactive effect, we will delay any settlement of a Unit or separate purchase contract where any date for determining the number of shares of our common stock issuable to a holder occurs during the averaging period until the second business day after the last date for determining the number of shares of our common stock issuable to such holder with respect to such settlement occurs. In the event that we are, or one of our subsidiaries is, obligated to purchase shares of our common stock pursuant to any such tender or exchange offer, but we are, or such subsidiary is, permanently prevented by applicable law from effecting any such purchases, or all such

purchases are rescinded, then each fixed settlement rate will be readjusted to be such fixed settlement rate that would then be in effect if such tender or exchange offer had not been made.

To the extent that we have a rights plan in effect with respect to our common stock on any date for determining the number of shares of our common stock issuable to a holder, you will receive, in addition to our common stock, the rights under the rights plan, unless, prior to such determination date, the rights have separated from our common stock, in which case each fixed settlement rate will be adjusted at the time of separation as if we made a distribution to all holders of our common stock as described in clause (c)(1) above, subject to readjustment in the event of the expiration, termination or redemption of such rights.

For purposes of this "—Adjustments to the Fixed Settlement Rates" section, "trading day" means a day on which:

- trading in our common stock (or other security for which a closing sale price must be determined) generally occurs on the relevant stock exchange, or, if our common stock (or such other security) is not then listed on a relevant stock exchange, on the principal other market on which our common stock (or such other security) is then listed or admitted for trading; and
- a closing price per share for our common stock (or closing sale price for such other security) is available on such securities exchange or market.

If our common stock (or such other security) is not so listed or traded, "trading day" means a "business day."

In addition, subject to applicable law and the applicable listing standards of the NYSE (or any other securities exchange where our common stock is listed) and in accordance with the provisions of the purchase contract agreement, we may make such increases in each fixed settlement rate as we determine to be in our best interests or we deem advisable. We may also (but are not required to) increase each fixed settlement rate in order to avoid or diminish any income tax to holders of our common stock resulting from any dividend or distribution of shares of our common stock (or issuance of rights, options or warrants to acquire shares of our common stock) or from any event treated as such for income tax purposes or for any other reason. We may only make such a discretionary adjustment if we make the same proportionate adjustment to each fixed settlement rate.

You might be treated as receiving a constructive distribution from us if (i) the fixed settlement rates are adjusted and as a result of such adjustment your proportionate interest in our assets or earnings and profits is increased and (ii) the adjustment is not made pursuant to a bona fide, reasonable anti-dilution formula. An adjustment in the fixed settlement rates would not be considered made pursuant to such a formula if the adjustment were made to compensate you for taxable distributions with respect to our common stock (for example, if we increase the cash dividend on our common stock). Certain of the possible settlement rate adjustments (including, without limitation, adjustments in respect of taxable dividends to holders of our common stock and as discussed in "Description of the Purchase Contracts—Early Settlement Upon a Fundamental Change") may not qualify as being pursuant to a bona fide reasonable adjustment formula. Thus, under certain circumstances, an increase in the fixed settlement rates might give rise to a constructive distribution to you even though you would not receive any cash related thereto. In addition, in certain situations, you might be treated as receiving a constructive distribution if we fail to adjust the fixed settlement rates. Any constructive distribution will be taxable as a dividend, return of capital, or capital gain in accordance with the earnings and profits rules described below in "Certain United States Federal Income and Estate Tax Consequences—U.S. Holders—Common Stock Acquired under a Purchase Contract—Distributions" and "Certain United States Federal Income and Estate Tax Consequences—Non-U.S. Holders—U.S. Federal Income Tax." If you are a "non-U.S. holder" (as defined in "Certain United States Federal Income and Estate Tax Consequences—Non-U.S. Holders"), a deemed dividend may be subject to U.S. federal withholding tax (currently at a 30% rate, or such lower rate as

may be specified by an applicable income tax treaty), which may be withheld from shares of common stock or sales proceeds subsequently paid or credited to you. It is possible that U.S. withholding tax on deemed dividends would be withheld from any interest or other amounts paid to a non-U.S. holder. See "Certain United States Federal Income and Estate Tax Consequences—Non-U.S. Holders—U.S. Federal Withholding Tax."

Adjustments to each fixed settlement rate will be calculated to the nearest 1/10,000th of a share. No adjustment in the fixed settlement rates will be required unless the adjustment would require an increase or decrease of at least one percent. If any adjustment is not required to be made because it would not change the fixed settlement rates by at least one percent, then the adjustment will be carried forward and taken into account in any subsequent adjustment; *provided* that, on any date for determining the number of shares of our common stock issuable to a holder (including any date for determining the amount of cash payable in connection with an acquisition termination redemption), adjustments to the fixed settlement rates will be made with respect to any such adjustment carried forward and which has not been taken into account before such determination date.

The fixed settlement rates will only be adjusted as set forth above and will not be adjusted:

- upon the issuance of any common stock pursuant to any present or future plan providing for the reinvestment of dividends or interest payable on our securities and the investment of additional optional amounts in common stock under any plan;
- upon the issuance of any common stock or rights, options or warrants to purchase those shares pursuant to any present or future employee, director or consultant benefit plan or program of or assumed by us or any of our subsidiaries;
- upon the repurchase of any shares of our common stock pursuant to an open market share repurchase program or other buy-back transaction, including structured or derivative transactions, that is not a tender offer or exchange offer of the nature described in clause (e) above;
- for the sale or issuance of shares of our common stock, or securities convertible into or exercisable for shares of our common stock, for cash, including at a price per share less than the fair market value thereof or otherwise or in an acquisition, except as described in one of clauses (a) through (e) above;
- for a third-party tender offer;
- upon the issuance of any common stock pursuant to any option, warrant, right or exercisable, exchangeable or convertible security outstanding as of the date the Units were first issued;
- solely for a change in, or elimination of, the par value of our common stock; or
- for accrued and unpaid interest, if any.

Whenever the fixed settlement rates are adjusted, we will deliver to the purchase contract agent a certificate setting forth in reasonable detail the method by which the adjustment to each fixed settlement rate was determined and setting forth each adjusted fixed settlement rate. In addition, we will, within five business days of any event requiring such adjustment, provide or cause to be provided written notice of the adjustment to the holders of the Units and separate purchase contracts and describe in reasonable detail the method by which each fixed settlement rate was adjusted.

We will adjust the fundamental change early settlement rates and acquisition redemption rates at the time we adjust the fixed settlement rates. For the avoidance of doubt, if we make an adjustment to the fixed settlement rates, it will result in a corresponding adjustment to the early settlement rate and the early mandatory settlement

rate. For the further avoidance of doubt, if we make an adjustment to the fixed settlement rates, no separate inversely proportionate adjustment will be made either to (i) the threshold appreciation price because it is equal to $50.00 divided by the minimum settlement rate as adjusted in the manner described herein (rounded to the nearest $0.0001) or (ii) the reference price because it is equal to $50.00 divided by the maximum settlement rate as adjusted in the manner described herein (rounded to the nearest $0.0001).

Whenever the terms of the purchase contracts require us to calculate closing prices, VWAPs or any other prices or amounts over a span of multiple days (including, without limitation, the applicable market value, the redemption market value, the "stock price" or the "acquisition termination stock price"), we will make appropriate adjustments, if any, to each to account for any adjustment to the fixed settlement rates if the related record date, ex-date, effective date or expiration date occurs during the period in which the closing prices, the VWAPs or such other prices or amounts are to be calculated.

Recapitalizations, Reclassifications and Changes of our Common Stock

In the event of:

- any consolidation or merger of us with or into another person (other than a merger or consolidation in which we are the continuing or surviving corporation and in which the shares of our common stock outstanding immediately prior to the merger or consolidation are not exchanged for cash, securities or other property of us or another person);
- any direct or indirect sale, lease, assignment, transfer or conveyance of all or substantially all of our consolidated property or assets;
- any reclassification of our common stock into securities, including securities other than our common stock (other than changes in par value or resulting from a subdivision or combination); or
- any statutory exchange of our securities with another person (other than in connection with a merger or acquisition);

in each case, as a result of which our common stock would be converted into, or exchanged for, securities, cash or other property (each, a "reorganization event"), each purchase contract outstanding immediately prior to such reorganization event will, without the consent of the holders of the purchase contracts, become a contract to purchase the kind of securities, cash and/or other property that a holder of common stock would have been entitled to receive in connection with such reorganization event (such securities, cash and other property, the "exchange property" with each unit of exchange property being the kind and amount of exchange property that a holder of one share of our common stock would have received in such reorganization event) and, prior to or at the effective time of such reorganization event, we or the successor or purchasing person, as the case may be, shall execute with the purchase contract agent and the trustee a supplemental agreement pursuant to the purchase contract agreement and the purchase contracts to provide for such change in the right to settle the purchase contracts.

For purposes of the foregoing, the type and amount of exchange property in the case of any reorganization event that causes our common stock to be converted into, or exchanged for, the right to receive more than a single type of consideration (determined based in part upon any form of shareholder election) will be deemed to be the weighted average of the types and amounts of consideration actually received by the holders of our common stock.

The number of units of exchange property we will deliver for each purchase contract settled or redeemed (if we elect not to deliver solely cash in respect of such redemption) following the effective date of such reorganization event will be equal to the number of shares of our common stock we would otherwise be required to deliver as determined by the fixed settlement rates then in effect on the applicable settlement date, or such

other settlement rates or redemption rates as provided herein (without interest thereon and without any right to dividends or distributions thereon which have a record date prior to the close of business such purchase contracts are actually settled). Each fixed settlement rate will be determined using the applicable market value of a unit of exchange property, and such value will be determined, on any date of determination, with respect to:

- in the case of any publicly traded securities that comprise all or part of the exchange property, based on the VWAP of such securities on such date;
- in the case of any cash that comprises all or part of the exchange property, based on the amount of such cash; and
- in the case of any other property that comprises all or part of the exchange property, based on the value of such property on such date, as determined by a nationally recognized independent investment banking firm retained by us for this purpose.

In addition, if the exchange property in respect of any reorganization event includes, in whole or in part, securities of another entity, we shall amend the terms of the purchase contract agreement and the purchase contracts, without the consent of holders thereof, to: (x) provide for anti-dilution and other adjustments that shall be as nearly equivalent as practicable, as determined by the officer executing such amendment, to the adjustments described above under the heading "— Adjustments to the Fixed Settlement Rates"; and (y) otherwise modify the terms of the purchase contract agreement and the purchase contracts to reflect the substitution of the applicable exchange property for our common stock (or other exchange property then underlying the purchase contracts). In establishing such anti-dilution and other adjustments referenced in the immediately preceding sentence, such officer shall act in a commercially reasonable manner and in good faith.

In connection with any adjustment to the fixed settlement rates described above, we will also adjust the dividend threshold amount based on the number of shares of common stock comprising the exchange property and (if applicable) the value of any non-stock consideration comprising the exchange property. If the exchange property is comprised solely of non-stock consideration, the dividend threshold amount will be zero.

Fractional Shares

No fractional shares of our common stock will be issued to holders upon settlement or redemption of the purchase contracts. In lieu of fractional shares otherwise issuable, holders will be entitled to receive an amount in cash equal to the fraction of a share of our common stock, calculated on an aggregate basis in respect of the purchase contracts being settled or redeemed (provided that, so long as the Units are in global form, we may elect to aggregate Units for purposes of these calculations on any basis permitted by the applicable procedures of DTC), *multiplied by* the VWAP of our common stock on the trading day immediately preceding the mandatory settlement date, early settlement date, fundamental change early settlement date, early mandatory settlement date or acquisition redemption settlement date, as the case may be.

Legal Holidays

In any case where the mandatory settlement date, early settlement date, fundamental change early settlement date, early mandatory settlement date or acquisition redemption settlement date, as the case may be, shall not be a business day, notwithstanding any term to the contrary in the purchase contract agreement or purchase contract, the settlement or redemption of the purchase contracts shall not be effected on such date, but instead shall be effected on the next succeeding business day with the same force and effect as if made on such settlement date, and no interest or other amounts shall accrue or be payable by us or to any holder in respect of such delay.

Consequences of Bankruptcy

Pursuant to the terms of the purchase contract agreement, the mandatory settlement date for each purchase contract, whether held separately or as part of a Unit, will automatically accelerate upon the occurrence of specified events of bankruptcy, insolvency or reorganization with respect to us. Pursuant to the terms of the purchase contract agreement, upon acceleration, holders will be entitled under the terms of the purchase contracts to receive a number of shares of our common stock per purchase contract equal to the maximum settlement rate in effect immediately prior to such acceleration (regardless of the market value of our common stock at that time). If for any reason the accelerated purchase contracts are not settled by the delivery of our common stock (for example, a bankruptcy court may prevent us from delivering our common stock in settlement of the accelerated purchase contracts), a holder may have a damage claim against us for the value of the common stock that we would have otherwise been required to deliver upon settlement of the purchase contracts. We expect that any such damage claim that holders have against us following such acceleration would rank equally with the claims of holders of our common stock in the relevant bankruptcy proceeding. As such, to the extent we fail to deliver common stock to you upon such an acceleration, you will only be able to recover damages to the extent holders of our common stock receive any recovery.

Modification

The purchase contract agreement will contain provisions permitting us, the purchase contract agent and the trustee to modify the purchase contract agreement or the purchase contracts without the consent of the holders of purchase contracts (whether held separately or as a component of Units) for any of the following purposes:

- to evidence the succession of another person to us, and the assumption by any such successor of the covenants and obligations of ours in the purchase contract agreement and the units and separate purchase contracts, if any;
- to add to the covenants for the benefit of holders of purchase contracts or to surrender any of our rights or powers under the agreement;
- to evidence and provide for the acceptance of appointment of a successor purchase contract agent;
- upon the occurrence of a reorganization event, solely: (i) to provide that each purchase contract will become a contract to purchase exchange property; and (ii) to effect the related changes to the terms of the purchase contracts, in each case, as required by the applicable provisions of the purchase contract agreement;
- to conform the provisions of the purchase contract agreement to the “Description of the Purchase Contracts” and “Description of the Units” sections in the preliminary prospectus supplement, as supplemented by the related pricing term sheet;
- to cure any ambiguity or manifest error, to correct or supplement any provisions that may be inconsistent; and
- to make any other provisions with respect to such matters or questions, so long as such action does not adversely affect the interest of the holders.

The purchase contract agreement will contain provisions permitting us, the purchase contract agent and the trustee, with the consent of the holders of not less than a majority of the purchase contracts at the time outstanding, to modify the terms of the purchase contracts or the purchase contract agreement. However, no

such modification may, without the consent of the holder of each outstanding purchase contract affected by the modification,

- reduce the number of shares of common stock deliverable upon settlement of the purchase contract (except to the extent expressly provided in the anti-dilution adjustments);
- change the mandatory settlement date, or adversely modify the right to settle purchase contracts early or the fundamental change early settlement right;
- reduce the redemption amount or adversely modify the right of any holder to receive such amount if we elect to redeem the purchase contract in connection with an acquisition termination redemption;
- impair the right to institute suit for the enforcement of the purchase contracts; or
- reduce the above-stated percentage of outstanding purchase contracts the consent of the holders of which is required for the modification or amendment of the provisions of the purchase contracts or the purchase contract agreement.

In executing any supplement, modification or amendment to the purchase contract agreement, the purchase contract agent and trustee shall be provided an officer's certificate and an opinion of counsel stating that the execution of such supplemental agreement is authorized or permitted by the purchase contract agreement, and that any and all conditions precedent to the execution and delivery of such supplemental agreement have been satisfied.

Consolidation, Merger, Conveyance, Transfer or Lease

The purchase contract agreement will provide that Aqua America will not consolidate or merge with or into any other entity, or sell, transfer, lease or otherwise convey its properties and assets as an entirety or substantially as an entirety to any entity, unless:

- (i) it is the continuing entity (in the case of a merger), or (ii) the successor entity formed by such consolidation or into which it is merged or which acquires by sale, transfer, lease or other conveyance of its properties and assets, as an entirety or substantially as an entirety, is a corporation organized and existing under the laws of the United States of America or any State thereof or the District of Columbia, and expressly assumes, by a supplement to the purchase contract agreement, all our obligations under the purchase contract agreement; and
- immediately after giving effect to the transaction, no event of default, and no event which after notice or lapse of time or both would become an event of default under the purchase contract agreement or the purchase contracts, has or will have occurred and be continuing.

Although there is a limited body of case law interpreting the phrase "substantially as an entirety," there is no precise established definition of the phrase under applicable law. Accordingly, in certain circumstances there may be a degree of uncertainty as to whether a particular transaction would involve a disposition of our properties and assets "substantially as an entirety." As a result, it may be unclear as to whether the foregoing restrictions on mergers, consolidations, sales, conveyances, transfers, leases and other dispositions would apply to a particular transaction as described above absent a decision by a court of competent jurisdiction.

Reservation of Common Stock

We will at all times reserve and keep available out of our authorized and unissued common stock, solely for issuance upon settlement or redemption of the purchase contracts, the number of shares of common stock that would be issuable upon the settlement of all purchase contracts then outstanding, assuming settlement at the maximum settlement rate.

Governing Law

The purchase contract agreement, the Units, the purchase contracts and any claim, controversy or dispute arising under or related to the purchase contract agreement, the Units or the purchase contracts will be governed by, and construed in accordance with, the laws of the State of New York.

Waiver of Jury Trial

The purchase contract agreement will provide that we, the purchase contract agent and the trustee will waive its respective rights to trial by jury in any action or proceeding arising out of or related to the purchase contracts, the purchase contract agreement or the transactions contemplated thereby, to the maximum extent permitted by law.

Information Concerning the Purchase Contract Agent

U.S. Bank N.A.will be the purchase contract agent. The purchase contract agent will act as the agent for the holders of Units and separate purchase contracts from time to time but shall have no fiduciary relationship to the holder of the Units or any other party. The purchase contract agreement will not obligate the purchase contract agent to exercise any discretionary actions in connection with a default under the terms of the purchase contracts or the purchase contract agreement.

The purchase contract agreement will contain provisions limiting the liability of the purchase contract agent. The purchase contract agreement will contain provisions under which the purchase contract agent may resign or be replaced. This resignation or replacement would be effective upon the acceptance of appointment by a successor purchase contract agent.

We maintain banking relationships in the ordinary course of business with the purchase contract agent and its affiliates.

Calculations in Respect of Purchase Contracts

We will be responsible for making all calculations called for under the Units and any separate purchase contracts. The purchase contract agent will have no obligation to make, review or verify any such calculations. All such calculations made by us will be made in good faith and, absent manifest error, will be final and binding on the purchase contract agent and the holders of the Units and any separate purchase contracts. We will provide a schedule of such calculations to the purchase contract agent and the purchase contract agent will be entitled to conclusively rely upon the accuracy of such calculations without independent verification.

DESCRIPTION OF THE AMORTIZING NOTES

The amortizing notes will be issued by us pursuant to an indenture, as amended, between us, as issuer, and U.S. Bank N.A., as trustee, and a related supplemental indenture, each to be dated the date of first issuance of the Units, between us and the trustee, under which the amortizing notes will be issued (collectively referred to herein as the "indenture").

The following summary of the terms of the amortizing notes taken together with the description under "Description of Debt Securities" in the accompanying prospectus contains a description of certain terms of the amortizing notes but is not complete and is subject to, and is qualified in its entirety by reference to, all of the provisions of the indenture, including the definitions in the indenture of certain terms. We refer you to the form of indenture, which has been filed as an exhibit to the registration statement of which this prospectus supplement forms a part, and a supplemental indenture related to a change in governing law to New York law, among other matters, and a supplemental indenture related to the amortizing notes, each of which will be filed as an exhibit to a current report on Form 8-K in connection with this offering and incorporated by reference as an exhibit to that registration statement. See "Where You Can Find More Information."

As used in this section, unless the context otherwise requires, references to "Aqua America," "we," "us" or "our" refer to Aqua America, Inc. and do not include any of its existing or future subsidiaries.

General

The amortizing notes will be issued as a separate series of senior debt securities under the indenture. The amortizing notes will be issued by us in an aggregate initial principal amount of $103,549,080 (or $119,081,442 if the underwriters exercise their option to purchase additional Units in full). The final installment payment date will be April 30, 2022. We may not redeem the amortizing notes, and no sinking fund is provided for the amortizing notes.

Each amortizing note will initially form a part of a Unit. Each Unit may be separated by a holder into its constituent purchase contract and amortizing note on any business day during the period beginning on, and including, the business day immediately following the date of initial issuance of the Units to, but excluding, the second scheduled trading day immediately preceding April 30, 2022 or, if earlier, the second scheduled trading day immediately preceding any "early mandatory settlement date" or the second scheduled trading day immediately preceding any "acquisition redemption settlement date" and also excluding the business day immediately preceding any installment payment date (*provided*, the right to separate the Units shall resume after such business day). Following such separation, amortizing notes may be transferred separately from purchasing contracts.

Amortizing notes may only be issued in certificated form in exchange for a global security under the circumstances described under "Book-Entry Procedures and Settlement." In the event that amortizing notes are issued in certificated form, such amortizing notes may be transferred or exchanged at the offices described below.

Payments on amortizing notes issued as a global security will be made to DTC, or a successor depositary. In the event amortizing notes are issued in certificated form, installment payments will be made, at the corporate trust office of the trustee. Installment payments on certificated amortizing notes may be made at our option by check mailed to the address of the persons entitled thereto. See "Book-Entry Procedures and Settlement."

The amortizing notes will not be guaranteed by any of our subsidiaries.

There are no covenants or provisions in the indenture that would afford the holders of the amortizing notes protection in the event of a highly leveraged transaction, reorganization, restructuring, merger or similar

transaction involving us that may adversely affect such holders, except to the extent set forth under "—Consolidation, Merger, Conveyance, Transfer or Lease."

The indenture does not limit the aggregate principal amount of indebtedness that may be issued thereunder and provides that debt securities may be issued thereunder from time to time in one or more series.

Ranking

The amortizing notes will be our general unsecured senior obligations and will rank equally in right of payment with all of our other existing and future unsecured senior indebtedness and guarantees and will be structurally subordinated to the indebtedness and other liabilities of our subsidiaries, including, upon consummation of the Acquisition, indebtedness and other liabilities of LDC and its subsidiaries that we assume in connection with the Acquisition. The amortizing notes will rank senior to all of our existing and future indebtedness, if any, that is subordinated to the amortizing notes. The amortizing notes will be effectively subordinated to any of our secured indebtedness to the extent of the collateral securing that indebtedness.

The amortizing notes are our obligations exclusively, and are not the obligations of any of our subsidiaries. We conduct our operations primarily through our subsidiaries and substantially all of our consolidated assets are held by our subsidiaries and, therefore, we depend on the cash flow of our subsidiaries to meet our obligations, including our obligations under the amortizing notes. Many of our subsidiaries are limited in their ability to pay dividends or make loans or distributions to us, including, without limitation, as a result of legislation, regulation, court order, contractual restrictions and other restrictions or in times of financial distress. Likewise, certain of LDC and its subsidiaries face similar restrictions that, if the Acquisition is consummated, will limit their ability to pay dividends or make loans or distributions to us. As a result, we may not be able to cause such subsidiaries and other entities to distribute funds or provide loans sufficient to enable us to meet our debt and other obligations, including obligations under the amortizing notes. See "Risk Factors—Risks Related to the Units, the Separate Purchase Contracts, the Separate Amortizing Notes and our Common Stock—Aqua America's ability to pay dividends and to meet its debt obligations largely depends on the performance of its subsidiaries and the ability to utilize the cash flows from those subsidiaries."

At December 31, 2018, on a pro forma basis after giving effect to the Transactions, (i) Aqua America, Inc. would have had approximately $2,096 million of indebtedness outstanding, of which none would have been secured indebtedness and (ii) our subsidiaries (including LDC and its subsidiaries) would have had a total of approximately $5,856 million of outstanding liabilities, including indebtedness, owed to non-affiliated third parties.

Installment Payments

Each amortizing note will have an initial principal amount of $8.62909. On each January 30, April 30, July 30 and October 30, commencing on July 30, 2019 (each, an "installment payment date"), we will pay, in cash, equal quarterly installments of $0.75000 on each amortizing note (except for the July 30, 2019 installment payment, which will be $0.80833 per amortizing note). Each installment payment will constitute a payment of interest (at a rate of 3.00% per annum) and a partial repayment of principal on the amortizing note, allocated as set forth on the amortization schedule set forth under "—Amortization Schedule."

Installments will be paid to the person in whose name an amortizing note is registered as of 5:00 p.m., New York City time, on January 15, April 15, July 15 and October 15, as applicable.

Each installment payment for any period will be computed on the basis of a 360-day year of twelve 30-day months. The installment payable for any period shorter or longer than a full installment payment period will be computed on the basis of the actual number of days elapsed per 30-day month. In the event that any date on which

an installment is payable is not a business day, then payment of the installment on such date will be made on the next succeeding day that is a business day, and without any interest or other payment in respect of any such delay.

Amortization Schedule

The total installments of principal of and interest on the amortizing notes for each installment payment date are set forth below:

Installment Payment Date	Amount of Principal	Amount of Interest
July 30, 2019	$ 0.73858	$ 0.06975
October 30, 2019	$ 0.69082	$ 0.05918
January 30, 2020	$ 0.69600	$ 0.05400
April 30, 2020	$ 0.70122	$ 0.04878
July 30, 2020	$ 0.70648	$ 0.04352
October 30, 2020	$ 0.71178	$ 0.03822
January 30, 2021	$ 0.71712	$ 0.03288
April 30, 2021	$ 0.72250	$ 0.02750
July 30, 2021	$ 0.72792	$ 0.02208
October 30, 2021	$ 0.73337	$ 0.01663
January 30, 2022	$ 0.73888	$ 0.01112
April 30, 2022	$ 0.74442	$ 0.00558

Repurchase of Amortizing Notes at the Option of the Holder

If we elect to exercise our early mandatory settlement right with respect to, or cause an acquisition termination redemption of, the purchase contracts, then holders of the amortizing notes (whether as components of Units or separate amortizing notes) will have the right (the "repurchase right") to require us to repurchase some or all of their amortizing notes for cash at the repurchase price per amortizing note to be repurchased on the repurchase date, as described below. Holders may not require us to repurchase a portion of an amortizing note. Holders will not have the right to require us to repurchase any or all of such holder's amortizing notes in connection with any early settlement of such holder's purchase contracts at the holder's option, as described above under "Description of the Purchase Contracts—Early Settlement" and "Description of the Purchase Contracts—Early Settlement Upon a Fundamental Change."

The "repurchase date" will be a date specified by us in the early mandatory settlement notice, or acquisition redemption notice, as the case may be, which will be at least 20 but not more than 35 business days following the date of our early mandatory settlement notice as described under "Description of the Purchase Contracts—Early Mandatory Settlement at Our Election" or the date of the acquisition redemption notice as described under "Description of the Purchase Contracts—Acquisition Termination Redemption," as the case may be (and which may or may not fall on the early mandatory settlement date or acquisition redemption settlement date, as the case may be).

The "repurchase price" per amortizing note to be repurchased will be equal to the principal amount of such amortizing note as of the repurchase date, plus accrued and unpaid interest on such principal amount from, and including, the immediately preceding installment payment date to, but not including, the repurchase date, calculated at an annual rate of 3.00%; *provided* that, if the repurchase date falls after a regular record date for any installment payment and on or prior to the immediately succeeding installment payment date, the installment payment payable on such installment payment date will be paid on such installment payment date to the holder as of such regular record date and will not be included in the repurchase price per amortizing note.

To exercise your repurchase right, you must deliver, on or before 5:00 p.m., New York City time, on the business day immediately preceding the repurchase date, the amortizing notes to be repurchased (or the Units, if the early mandatory settlement date or acquisition redemption settlement date, as the case may be, occurs on or after the repurchase date and you have not separated your Units into their constituent components), together with a duly completed written repurchase notice in the form entitled "Form of Repurchase Notice" on the reverse side of the amortizing notes (a "repurchase notice"), in each case, in accordance with appropriate DTC procedures, unless you hold certificated amortizing notes (or Units), in which case you must deliver the amortizing notes to be repurchased (or Units), duly endorsed for transfer, together with a repurchase notice, to the paying agent. Your repurchase notice must state:

- if certificated amortizing notes (or Units) have been issued, the certificate numbers of the amortizing notes (or Units), or if not certificated, your repurchase notice must comply with appropriate DTC procedures;
- the number of amortizing notes to be repurchased; and
- that the amortizing notes are to be repurchased by us pursuant to the applicable provisions of the amortizing notes and the indenture.

You may withdraw any repurchase notice (in whole or in part) by a written, irrevocable notice of withdrawal delivered (in the case of an amortizing note in global form, in accordance with the appropriate DTC procedures) on or before 5:00 p.m., New York City time, on the business day immediately preceding the repurchase date. The notice of withdrawal must state:

- if certificated amortizing notes (or Units) have been issued, the certificate numbers of the withdrawn amortizing notes (or Units), or if not certificated, your notice must comply with appropriate DTC procedures;
- the number of the withdrawn amortizing notes; and
- the number of amortizing notes, if any, that remain subject to the repurchase notice.

We will be required to repurchase the amortizing notes on the repurchase date. You will receive payment of the repurchase price on the later of (i) the repurchase date and (ii) the time of book-entry transfer or the delivery of the amortizing notes. If the trustee holds money sufficient to pay the repurchase price of the amortizing notes to be purchased on the repurchase date, then:

- such amortizing notes will cease to be outstanding and interest will cease to accrue (whether or not book-entry transfer of the amortizing notes is made or whether or not the amortizing notes are delivered to the trustee); and
- all other rights of the holder will terminate (other than the right to receive the repurchase price and, if the repurchase date falls between a regular record date and the corresponding installment payment date, the related installment payment).

Upon repurchase of the amortizing note component of a Unit prior to the related acquisition redemption settlement date, if applicable, the purchase contract component of such Unit will remain outstanding (pending such acquisition redemption settlement date) and beneficially owned by or registered in the name of, as the case may be, the holder who elected repurchase of the related amortizing note and will no longer constitute a part of the Unit.

In connection with any repurchase offer pursuant to an early mandatory settlement notice or acquisition redemption notice, we will, if required, comply with the provisions of the tender offer rules under the Exchange Act that may then be applicable.

No amortizing notes may be repurchased at the option of holders if the principal amount thereof has been accelerated, and such acceleration has not been rescinded, on or prior to the repurchase date (except in the case of an acceleration resulting from a default by us of the payment of the repurchase price with respect to such amortizing notes).

Events of Default

Each of the following will be an "event of default" under the indenture with respect to the amortizing notes:

- default in the payment of any installment payment on any amortizing notes as and when the same shall become due and payable and continuance of such failure for a period of 30 days;
- default in the payment of the repurchase price of any amortizing notes when the same shall become due and payable;
- our failure to give notice of a fundamental change as described under "Description of the Purchase Contracts—Early Settlement Upon a Fundamental Change" when due and continuance of such failure for a period of five business days;
- our failure to perform for 90 days after notice any other covenant in the amortizing notes or the indenture; and
- certain events of bankruptcy or insolvency of Aqua America, whether voluntary or not.

Discharge and Defeasance of Indenture

The defeasance provisions described in the accompanying prospectus under "Description of Debt Securities—Defeasance" will be applicable to the amortizing notes; *provided* that (i) the coin or currency unit to be deposited with the trustee under such provisions shall be U.S. dollars, (ii) references therein to "principal" shall be deemed to refer to "the portion of all future scheduled installment payments constituting the payment of principal in respect of the amortizing notes and the portion of the repurchase price constituting the principal amount of the amortizing notes" and (iii) references therein to "interest" shall be deemed to refer to "the portion of all future scheduled installment payments constituting the payment of interest in respect of the amortizing notes and the portion of the repurchase price constituting the accrued but unpaid interest on the amortizing notes."

Consolidation, Merger, Conveyance, Transfer or Lease

The indenture will provide that Aqua America will not consolidate or merge with or into any other entity, or sell, transfer, lease or otherwise convey its properties and assets as an entirety or substantially as an entirety to any entity, unless:

- (i) it is the continuing entity (in the case of a merger), or (ii) the successor entity formed by such consolidation or into which it is merged or which acquires by sale, transfer, lease or other conveyance of its properties and assets, as an entirety or substantially as an entirety, is a corporation organized and existing under the laws of the United States of America or any State thereof or the District of Columbia,

and expressly assumes, by supplemental indenture, the due and punctual payment of the installment payments on all the debt securities and the performance of all of the covenants under the indenture; and

- immediately after giving effect to the transaction, no event of default, and no event which after notice or lapse of time or both would become an event of default under the indenture, has or will have occurred and be continuing.

Although there is a limited body of case law interpreting the phrase "substantially as an entirety," there is no precise established definition of the phrase under applicable law. Accordingly, in certain circumstances there may be a degree of uncertainty as to whether a particular transaction would involve a disposition of our properties and assets "substantially as an entirety." As a result, it may be unclear as to whether the foregoing restrictions on mergers, consolidations, sales, conveyances, transfers, leases and other dispositions would apply to a particular transaction as described above absent a decision by a court of competent jurisdiction.

Modifications and Amendments

We and the trustee may amend or supplement the indenture or the amortizing notes without consent of the holders to:

- cure any ambiguity, omission, defect or inconsistency in the indenture;
- provide for the assumption by a successor corporation as set forth in "—Consolidation, Merger, Conveyance, Transfer or Lease;
- comply with any requirements of the SEC in connection with the qualification of the indenture under the Trust Indenture Act;
- to evidence and provide for the acceptance of appointment with respect to the amortizing notes by a successor trustee in accordance with the indenture, and add or change any of the provisions of the indenture as shall be necessary to provide for or facilitate the administration of the trusts under the indenture by more than one trustee;
- secure the notes;
- add guarantees with respect to the notes;
- add covenants or events of default for the benefit of the holders or surrender any right or power conferred upon us;
- make any change that does not adversely affect the rights of any holder in any material respect; and
- conform the provisions of the indenture or the amortizing notes to any provision of the "Description of the Amortizing Notes" section in the preliminary prospectus supplement for this Units offering, as supplemented by the related pricing term sheet.

In addition, notwithstanding anything to the contrary in the section of the accompanying prospectus entitled "Description of Debt Securities—Modification of the Indentures," we may not make any modification or amendment to the indenture or the amortizing notes without the consent of each holder affected thereby if that modification or amendment will:

- change any installment payment date or reduce the amount owed on any installment payment date; or
- reduce the repurchase price or amend or modify in any manner adverse to the holders of the amortizing notes our obligation to make such payment.

For purposes of the amortizing notes, the reference in the accompanying prospectus under the section entitled "Description of Debt Securities—Modification of the Indentures" to "the principal of," "premium" or "interest" will be deemed to be replaced by a reference to "the repurchase price, if applicable, of or any installment payment."

Governing Law

The indenture and the amortizing notes shall be governed by and construed in accordance with the laws of the State of New York.

Waiver of Jury Trial

The indenture will provide that we and the trustee will waive our respective rights to trial by jury in any action or proceeding arising out of or related to the amortizing notes, the indenture or the transactions contemplated thereby, to the maximum extent permitted by law.

CERTAIN UNITED STATES FEDERAL INCOME AND ESTATE TAX CONSIDERATIONS

The following summary describes certain U.S. federal income tax and estate consequences for holders as of the date of this prospectus supplement, of the purchase, ownership and disposition of Units, amortizing notes, and the purchase contracts that are or may be the components of a Unit and shares of our common stock acquired under a purchase contract.

This summary deals only with Units, amortizing notes, purchase contracts, and common stock held as capital assets by a holder who purchases the Units upon original issuance at their initial offering price, as indicated on the cover of this prospectus supplement. This summary does not constitute a detailed description of the U.S. federal income tax considerations applicable to you if you are subject to special treatment under the U.S. federal income tax laws, including if you are:

- a dealer in securities or currencies;
- a trader in securities that has elected the mark-to-market method of tax accounting for your securities;
- a regulated investment company;
- a real estate investment trust;
- a tax-exempt organization;
- an insurance company;
- a person holding the Units, amortizing notes, purchase contracts, or common stock as part of a hedging, integrated, conversion or constructive sale transaction or a straddle;
- a financial institution;
- a person liable for alternative minimum tax;
- a partnership or other pass-through entity for United States federal income tax purposes;
- a “U.S. holder” (as defined below) whose “functional currency” is not the U.S. dollar;
- a “controlled foreign corporation”;
- a “passive foreign investment company”;
- a foreign pension fund;
- a person who owns or is deemed to own 10% or more of our stock (by vote or value);
- a person required to accelerate the recognition of any item of gross income with respect to our common shares as a result of such income being recognized on an applicable financial statement; or
- a U.S. expatriate.

If a partnership (or other entity treated as a partnership for United States federal income tax purposes) holds the Units, amortizing notes, purchase contracts, or common stock, the tax treatment of a partner will generally depend upon the status of the partner and the activities of the partnership. If you are a partner of a partnership holding the Units, amortizing notes, purchase contracts, or common stock, you should consult your tax advisor.

The discussion below is based upon the provisions of the Internal Revenue Code of 1986, as amended (the "Code"), and regulations, rulings and judicial decisions thereunder as of the date hereof. Those authorities may be changed, perhaps retroactively, so as to result in U.S. federal income and estate tax consequences different from those discussed below.

This summary does not address all aspects of U.S. federal income and estate taxes and does not address the Medicare tax on net investment income or the effects of any state, local or non-United States tax laws that may be relevant to holders in light of their personal circumstances. **If you are considering the purchase, ownership or disposition of the Units, amortizing notes, purchase contracts or common stock, you should consult your own tax advisors concerning the U.S. federal income and estate tax consequences to you in light of your particular situation as well as any consequences arising under the laws of any other taxing jurisdiction.**

Characterization of Units and Amortizing Notes

There is no authority directly addressing the characterization of the Units or instruments similar to the Units for U.S. federal income tax purposes and therefore the characterization of the Units for these purposes is not entirely free from doubt. We will take the position that each Unit will be treated as an investment unit composed of two separate instruments for U.S. federal income tax purposes: (i) a prepaid purchase contract to acquire our common stock and (ii) an amortizing note that is our indebtedness. Under this treatment, a holder of Units will be treated as if it held each component of the Units for U.S. federal income tax purposes. By acquiring a Unit, you will agree to treat (i) a Unit as an investment unit composed of two separate instruments in accordance with its form and (ii) the amortizing notes as indebtedness of Aqua America, Inc. for U.S. federal income tax purposes. If, however, the components of a Unit were treated as a single instrument, the U.S. federal income tax consequences could differ from the consequences described below. Specifically, if you are a "U.S. holder" (as defined below under "U.S. Holders") you could be required to recognize the entire amount of each installment payment on the amortizing notes, rather than merely the portion of such payment denominated as interest, as income. In addition, if you are a "non-U.S. holder" (as defined below under "Non-U.S. Holders"), payments of principal and interest made to you on the amortizing notes could be subject to U.S. withholding tax. Even if the components of a Unit are respected as separate instruments for U.S. federal income tax purposes, (i) the amortizing notes could be recharacterized as equity for U.S. federal income tax purposes, in which case payments of interest to non-U.S. holders on the amortizing notes could potentially be subject to U.S. withholding tax and (ii) the purchase contracts could be treated as our stock on the date of issuance, in which case the tax consequences of the purchase, ownership and disposition thereof would be substantially the same as the tax consequences described herein, except that a holder's holding period for the common stock received under a purchase contract would include the period during which the U.S. holder held the purchase contract.

The Units are complex financial instruments and no statutory, judicial or administrative authority directly addresses all aspects of the treatment of the Units or instruments similar to the Units for U.S. federal income tax purposes, and no assurance can be given that the Internal Revenue Service ("IRS") will agree with the tax consequences described herein. As a result, the U.S. federal income tax consequences of the purchase, ownership and disposition of the Units are unclear. We have not sought any rulings concerning the treatment of the Units, and the tax consequences described herein are not binding on the IRS or the courts, either of which could disagree with the explanations or conclusions contained in this summary. Accordingly, you should consult your tax advisor regarding the consequences to you of the possible recharacterization of the components of a Unit as a single instrument. Unless stated otherwise, the remainder of this discussion assumes the characterization of the Units as two separate instruments.

Allocation of Purchase Price

Your acquisition of a Unit will be treated as an acquisition of the amortizing note and the purchase contract constituting the Unit and, by purchasing the Unit, you will be deemed to have agreed to such treatment. In addition, we and you, by your acceptance of a beneficial ownership interest in the amortizing notes, agree to treat the notes as indebtedness of Aqua America, Inc. for all U.S. federal income tax purposes. The remainder of this discussion assumes that a holder of a Unit will be treated as owning the amortizing note and the purchase contract.

The purchase price of each Unit will be allocated between the amortizing note and the purchase contract in proportion to their respective fair market values at the time of purchase. Such allocation will establish your initial tax basis in the amortizing note and the purchase contract. We will report the initial fair market value of each amortizing note as $8.62909 and the initial fair market value of the purchase contract as $41.37091. This allocation is binding on you (but not on the IRS), unless you explicitly disclose a contrary position on a statement attached to your timely filed U.S. Federal income tax return. The remainder of this discussion assumes that this allocation of the purchase price will be respected for U.S. Federal income tax purposes.

U.S. Holders

The following is a summary of certain U.S. federal incomes tax consequences that will apply to you if you are a U.S. holder of Units, amortizing notes, purchase contracts or common stock.

As used herein, the term "U.S. holder" means a beneficial owner of Units, amortizing notes, purchase contracts or common stock that, for U.S. federal income tax purposes, is:

- an individual citizen or resident of the United States;
- a corporation (or other entity treated as a corporation for U.S. federal income tax purposes) created or organized in or under the laws of the United States, any state thereof or the District of Columbia;
- an estate the income of which is subject to U.S. federal income taxation regardless of its source; or
- a trust if it (1) is subject to the primary supervision of a court within the United States and one or more United States persons have the authority to control all substantial decisions of the trust or (2) has a valid election in effect under applicable U.S. Treasury regulations to be treated as a United States person.

Units

Separation and Recreation of the Units.

A U.S. holder will not recognize gain or loss by (i) separating a Unit into its components or (ii) recreating a Unit as both procedures are described under "Description of the Units—Separating and Recreating Units."

Sale, Exchange or Other Taxable Disposition of Units

Upon a sale, exchange or other taxable disposition of Units, you will be treated as having sold, exchanged or disposed of both the purchase contracts and the amortizing notes that constitute such Units and you will calculate gain or loss on the purchase contracts separately from the gain or loss on the amortizing notes in proportion to their relative fair market values at the time of the disposition. It is thus possible that you could recognize a capital gain on one component of a Unit but a capital loss on the other component of the Unit. You generally will have gain or loss equal to the difference between (i) the portion of your proceeds allocable to the purchase contract and the amortizing notes and (ii) your respective adjusted tax bases in the purchase contract and the amortizing notes. For purposes of determining gain or loss, your proceeds will not include any amount

attributable to accrued and unpaid interest, which amount will be treated as ordinary interest income to the extent not previously included in income. Such gain or loss generally will be capital gain or loss. Capital gains of individuals derived in respect of assets held for more than one year are subject to tax at preferential rates. The deductibility of capital losses is subject to limitations.

Amortizing Notes

Payments of Interest and Principal on Amortizing Notes

Stated interest on an amortizing note will be includible in your gross income as ordinary interest income at the time it is paid or at the time it accrues in accordance with your method of tax accounting, and payments on the notes other than stated interest will reduce your basis with respect to such amortizing note. It is expected, and this discussion assumes, that the amortizing notes will not be issued with more than a *de minimis* amount of original issue discount ("OID"). In general, however, if the amortizing notes are issued with more than *de minimis* OID, a U.S. holder will be required to include OID in gross income, as ordinary income, under a "constant-yield method" before the receipt of cash attributable to such income, regardless of the U.S. holder's regular method of accounting for U.S. federal income tax purposes. Payments on the amortizing notes other than stated interest (including the portion of each installment payment that is not treated as interest) will reduce a U.S. holder's basis with respect to the amortizing notes.

Sale, Exchange or Other Taxable Disposition of Amortizing Notes

Upon a sale, exchange or other taxable disposition of amortizing notes, you will generally have gain or loss equal to the difference between (i) the amount realized and (ii) your adjusted tax basis in the amortizing note. For purposes of determining gain or loss, your proceeds will not include any amount attributable to accrued and unpaid interest, which amount will be treated as ordinary interest income to the extent not previously included in income. Such gain or loss generally will be capital gain or loss. Capital gains of individuals derived in respect of assets held for more than one year are subject to tax at preferential rates. The deductibility of capital losses is subject to limitations.

Repurchase of Amortizing Notes

If you elect to have us repurchase your notes in connection with an early mandatory settlement or acquisition termination redemption, you will recognize gain or loss in an amount equal to the difference between the amount realized on the repurchase of your amortizing notes and your adjusted tax basis in the amortizing notes. For purposes of determining gain or loss, your amount realized will not include any amount attributable to accrued and unpaid interest, which amount will be treated as ordinary interest income to the extent not previously included in income. Such gain or loss generally will be capital gain or loss. Long-term capital gains of a non-corporate U.S. holder are generally eligible for reduced rates of taxation. The deductibility of capital losses is subject to limitations.

Purchase Contracts

Acquisition Termination Redemption

In the event of a acquisition termination redemption, we may elect to pay cash in lieu of delivering any or all of the shares of common stock due in settlement of the purchase contracts (unless the "acquisition termination stock price" is equal to or less than the reference price, in which case the outstanding purchase contracts will be redeemed solely for cash, the treatment of which is discussed above under "—Sale, Exchange or Other Disposition of Units"). If a U.S. holder receives cash and common stock in settlement of a purchase contract, the tax treatment of the settlement is not entirely certain. A U.S. holder should consult its own tax advisor regarding the consequences of a combination settlement.

Although no authority directly addresses a combination settlement, we intend to take the position that (i) the cash received in respect of a purchase contract should be treated as proceeds from the sale of a portion of the purchase contract and taxed in the manner described above under "—Sale, Exchange or Other Disposition of Units" and (ii) the common stock consideration should be treated as received on settlement of the other portion of the purchase contract and therefore generally not be taxable to a U.S. holder.

In that case, the U.S. holder's adjusted tax basis in the purchase contract would generally be allocated pro rata between the common stock received and the portion of the purchase contract that is treated as sold for cash based on the fair market value of our common stock and the cash. The holding period for our common stock received (including any fractional share deemed received) will commence on the day after the date of receipt.

Alternatively, it is possible that an acquisition termination redemption resulting in combination settlement could result in a U.S. holder recognizing gain, but not loss, equal to the excess of the fair market value of the common stock and cash received over the U.S. holder's adjusted tax basis in the purchase contract. In no event would the gain recognized exceed the amount of cash received. Any gain would be long-term capital gain if, at the time of settlement the purchase contract has been held for more than one year. In this case, (i) a U.S. holder's tax basis in the common stock received generally would equal its tax basis in the purchase contract that was settled, reduced by the amount of any cash received, and increased by the amount of gain, if any, recognized; (ii) the U.S. holder's holding period for common stock received would include the period during which it held the purchase contract; and (iii) a U.S. holder that is a "significant holder" would be subject to certain recordkeeping and information reporting requirements with respect to the settlement.

Acquisition of Common Stock under a Purchase Contract

Except as may occur pursuant to an acquisition termination redemption (as discussed above under "Description of the Purchase Contracts—Acquisition Termination Redemption"), the purchase contracts are expected to physically settle. You generally will not recognize gain or loss on the purchase of common stock under a purchase contract, except with respect to any cash paid in lieu of a fractional share of common stock. Your aggregate initial tax basis in the common stock acquired under a purchase contract should equal your tax basis in the purchase contract less any such tax basis allocable to the fractional share. The holding period for common stock received under a purchase contract will commence on the day after the common stock is acquired.

Constructive Distributions and Dividends

You might be treated as receiving a constructive distribution from us if (i) the fixed settlement rates are adjusted and as a result of such adjustment your proportionate interest in our assets or earnings and profits is increased and (ii) the adjustment is not made pursuant to a bona fide, reasonable anti-dilution formula. An adjustment in the fixed settlement rates would not be considered made pursuant to such a formula if the adjustment were made to compensate you for taxable distributions with respect to our common stock (for example, if we increase the cash dividend on our common stock). Certain of the possible settlement rate adjustments (including, without limitation, adjustments in respect of taxable dividends to holders of our common stock and as discussed in "Description of the Purchase Contracts—Early Settlement Upon a Fundamental Change") may not qualify as being pursuant to a bona fide reasonable adjustment formula. Thus, under certain circumstances, an increase in the fixed settlement rates might give rise to a constructive distribution to you even though you would not receive any cash related thereto. In addition, in certain situations, you might be treated as receiving a constructive distribution if we fail to adjust the fixed settlement rates. Any constructive distribution will be taxable as a dividend, return of capital, or capital gain in accordance with the earnings and profits rules described below.

Sale, Exchange or Other Taxable Disposition of Purchase Contracts

Except as described above under "—Acquisition of Common Stock under a Purchase Contract", upon a sale, exchange, or other taxable disposition of a purchase contract, you will recognize capital gain or loss in an

amount equal to the difference between the amount realized and your adjusted tax basis in the purchase contract. Such gain or loss generally will be capital gain or loss. Long-term capital gains of a non-corporate U.S. holder are generally eligible for reduced rates of taxation. The deductibility of capital losses is subject to limitations.

Common Stock Acquired under a Purchase Contract

Distributions

Any distribution on our common stock (other than certain pro rata distributions of common shares) paid out of our current or accumulated earnings and profits (as determined for U.S. federal income tax purposes) will constitute a dividend and will be includible in income by you when received. Non-corporate U.S. Holders that received dividends on our common stock are eligible for a reduced rate of taxation of certain requirements are satisfied. Any such dividend will be eligible for the dividends-received deduction if you are an otherwise qualifying corporate holder that meets the holding period and other requirements for the dividends-received deduction. Any distributions on our common stock in excess of our current and accumulated earnings and profits will first be applied to reduce your tax basis in the common stock, and any amount in excess of your tax basis will be treated as gain from the sale or exchange of your common stock, as described immediately below.

Sale, Exchange or Other Taxable Disposition of Common Stock

Upon a sale, exchange, or other taxable disposition of our common stock, you will recognize capital gain or loss in an amount equal to the difference between the amount realized and your adjusted tax basis in the common stock. Such gain or loss generally will be capital gain or loss. Long-term capital gains of a non-corporate U.S. holder are generally eligible for reduced rates of taxation. The deductibility of capital losses is subject to limitations.

Information Reporting and Backup Withholding

In general, information reporting requirements may apply to payments on the amortizing notes, the purchase contracts and common stock made to you and to the proceeds of the sale or other disposition of such instruments, unless you are an exempt recipient. Backup withholding may apply to such payments if you fail to provide a taxpayer identification number, a certification of exempt status, or fail to report in full dividend and interest income.

Backup withholding is not an additional tax and any amounts withheld under the backup withholding rules will be allowed as a refund or a credit against your United States federal income tax liability provided the required information is timely furnished to the Internal Revenue Service.

Non-U.S. Holders

The following discussion applies only to non-U.S. holders. As used herein, a "non-U.S. holder" means a beneficial owner of Units, amortizing notes, purchase contracts or common stock that is neither a U.S. holder nor a partnership. As discussed above under "—Characterization of Units and Amortizing Notes", this discussion assumes that a Unit is treated as two separate instruments and that the amortizing notes are treated as indebtedness of Aqua America, Inc. for U.S. federal income tax purposes. Different tax consequences would apply if the Unit was treated as a single instrument.

U.S. Federal Withholding Tax

A 30% U.S. federal withholding tax will not apply to any payment to you of principal or interest on the amortizing notes, provided that you meet the following requirements of the portfolio interest exemption:

- interest paid on the notes is not effectively connected with your conduct of a trade or business in the United States;

- you do not actually (or constructively) own 10% or more of the total combined voting power of all classes of our voting stock within the meaning of the Code and the Treasury regulations;
- you are not a controlled foreign corporation that is related to us through stock ownership;
- you are not a bank whose receipt of interest on the amortizing notes is described in section 881(c)(3)(A) of the Code; and

(a) you provide your name and address on an IRS Form W-8BEN or W-8BEN-E (or other applicable form), and certify, under penalties of perjury, that you are not a United States person, or (b) if you hold your Units or amortizing notes through certain foreign intermediaries, you satisfy the certification requirements of applicable U.S. Treasury regulations. Special certification requirements apply to certain non-U.S. holders that are pass-through entities rather than individuals.

If you cannot satisfy the requirements described above, payments of interest made to you will be subject to the 30% U.S. federal withholding tax, unless you provide a properly executed:

- IRS Form W-8BEN or W-8BEN-E (or other applicable form) claiming an exemption from, or reduction in the rate of, withholding under the benefit of an applicable tax treaty; or
- IRS Form W-8ECI (or other applicable form) stating that interest paid on the amortizing notes is not subject to withholding tax because it is effectively connected with your conduct of a trade or business in the United States.

Except as described below in "—Foreign Investment in Real Property Tax Act" , the 30% U.S. federal withholding tax will generally not apply to any gain that you realize on the sale, exchange, or other disposition of the Units, amortizing notes, purchase contracts or common stock acquired under the purchase contract.

We will generally withhold tax at a 30% rate on dividends paid on common stock acquired under a purchase contract and any constructive dividends resulting from certain adjustments, or failure to make adjustments, to the settlement rate of the purchase contracts (see "—U.S. Holders—Settlement of the Purchase Contracts—Constructive Distributions and Dividends") or such lower rate as may be specified by an applicable income tax treaty. Any applicable withholding taxes imposed in connection with a constructive distribution may be withheld from payments made on the applicable Units or purchase contract. If any withholding taxes are paid on behalf of a Non-U.S. Holder, those withholding taxes may be set off against subsequent payments on the applicable Units or purchase contracts (including any payments, including Common Stock, received upon the settlement of the purchase contracts). However, dividends that are effectively connected with the conduct of a trade or business by the non-U.S. holder within the United States and, where a tax treaty applies, are attributable to a U.S. permanent establishment of the non-U.S. holder, are not subject to the withholding tax, provided the relevant certification requirements are satisfied, but instead are subject to U.S. federal income tax, as described below.

A non-U.S. holder of a Unit, common stock or a purchase contract who wishes to claim the benefit of an applicable treaty rate for dividends or constructive dividends will be required to provide an IRS Form W-8BEN or W-8BEN-E (or other applicable form) claiming an exemption from, or reduction in the rate of, withholding under the benefit of an applicable tax treaty. A non-U.S. holder eligible for a reduced rate of U.S. withholding tax on payments pursuant to an income tax treaty may obtain a refund of any excess amounts withheld by timely filing an appropriate claim for refund with the IRS.

U.S. Federal Income Tax

If you are engaged in a trade or business in the United States and interest on the amortizing notes or dividends on our common stock (or constructive dividends on the purchase contracts) are effectively connected

with the conduct of that trade or business (and, where a tax treaty applies, are attributable to a U.S. permanent establishment of the non-U.S. holder), you will be subject to U.S. federal income tax on the interest or dividends on a net income basis (although exempt from the 30% withholding tax), in the same manner as if you were a United States person as defined under the Code. Certain certification and disclosure requirements must be complied with in order for effectively connected income to be exempt from withholding. In addition, if you are a foreign corporation, you may be subject to a branch profits tax equal to 30% (or lower applicable treaty rate) of your earnings and profits for the taxable year, subject to adjustments, that are effectively connected with the conduct by you of a trade or business in the United States. For this purpose, interest on the amortizing notes or dividends on our common stock and constructive dividends on the purchase contracts will be included in earnings and profits.

Upon a disposition of Units, you will be treated as having sold, exchanged or disposed of both the purchase contracts and the amortizing notes that constitute such Units. Any gain realized on the disposition of an amortizing note, purchase contract or share of common stock generally will not be subject to U.S. federal income tax unless:

- that gain or income is effectively connected with the conduct of a trade or business by you in the United States (and, if required by an applicable income tax treaty, is attributable to a United States permanent establishment of the non-U.S. holder); or
- you are an individual who is present in the United States for 183 days or more in the taxable year of that disposition, and certain other conditions are met; or
- in the case of a purchase contract or our common stock, we are or have been a "United States real property holding corporation" for U.S. federal income tax purposes (see the discussion below under "—Foreign Investment in Real Property Tax Act").

An individual non-U.S. holder described in the first bullet above will be subject to tax on the net gain derived from the sale under regular graduated U.S. federal income tax rates. If a non-U.S. holder that is a foreign corporation falls under the first bullet above, it will be subject to tax on its gain under regular graduated U.S. federal income tax rates and, in addition, may be subject to the branch profits tax equal to 30% of its effectively connected earnings and profits or at such lower rate as may be specified by an applicable income tax treaty. An individual non-U.S. holder described in the second bullet point immediately above will be subject to a 30% (or such lower rate as may be specified by an applicable income tax treaty) tax on the gain derived from the sale or other disposition, which gain may be offset by United States source capital losses even though the individual is not considered a resident of the United States.

Foreign Investment in Real Property Tax Act

Generally, a corporation is a "United States real property holding corporation" if the fair market value of its United States real property interests equals or exceeds 50% of the sum of the fair market value of its worldwide real property interests and its other assets used or held for use in a trade or business (all as determined for United States federal income tax purposes). We believe we are not and do not anticipate becoming a "United States real property holding corporation" for United States federal income tax purposes. If, however, we are or become a "United States real property holding corporation," so long as our common stock is regularly traded on an established securities market during the calendar year in which the sale or other disposition occurs, only a non-U.S. holder who holds or held (at any time during the shorter of the five year period preceding the date of disposition or the holder's holding period) more than 5% of our common stock will be subject to United States federal income tax on the sale or other disposition of our common stock.

U.S. Federal Estate Tax

Your estate will not be subject to U.S. federal estate tax on the amortizing notes beneficially owned by you at the time of your death, provided that any payments made to you on the amortizing notes would be eligible for exemption from the 30% withholding tax under the portfolio interest exemption described above under "—U.S. Federal Withholding Tax" without regard to the certification requirement described in the fourth bullet point regarding portfolio interest.

Common stock acquired under a purchase contract and owned by you at the time of your death will be subject to U.S. federal estate tax unless an applicable estate tax treaty provides otherwise. The purchase contract owned by you at the time of your death may be subject to U.S. federal estate tax unless an applicable estate tax treaty provides otherwise.

Information Reporting and Backup Withholding

The amount of the interest and dividends (including deemed dividends) paid to you and the tax withheld with respect to such interest and dividends, regardless of whether withholding was required, must be reported annually to the IRS and to you. Copies of the information returns reporting the amount of such interest and dividends and the amount of withholding may also be made available to the tax authority in the country in which you reside under the provisions of an applicable income tax treaty.

In general, no backup withholding will be required regarding payments on amortizing notes or common stock that we make to you, provided that we do not have actual knowledge or reason to know that you are a United States person and you have complied with the certification procedures described above under "—U.S. Federal Withholding Tax."

Information reporting and, depending on the circumstances, backup withholding will apply to the proceeds of a sale or other disposition of our common stock made within the United States or conducted through certain United States-related financial intermediaries, unless the beneficial owner certifies under penalty of perjury that it is a non-U.S. holder, provided that we do not have actual knowledge or reason to know that the beneficial owner is a United States person and the beneficial owner has complied with the certification procedures described above under "—U.S. Federal Withholding Tax" or otherwise establishes an exemption.

Additional Withholding Requirements

Under Sections 1471 through 1474 of the Code (such Sections commonly referred to as "FATCA"), a 30% United States federal withholding tax may apply to any dividends and interest paid on our Units, amortizing notes, purchase contracts or common stock, as applicable, to (i) a "foreign financial institution" (as specifically defined in the Code) which does not provide sufficient documentation, typically on IRS Form W-8BEN or W-8BEN-E, evidencing either (x) an exemption from FATCA, or (y) its compliance (or deemed compliance) with FATCA (which may alternatively be in the form of compliance with an intergovernmental agreement with the United States) in a manner which avoids withholding, or (ii) a "non-financial foreign entity" (as specifically defined in the Code) which does not provide sufficient documentation, typically on IRS Form W-8BEN or W-8BEN-E, evidencing either (x) an exemption from FATCA, or (y) adequate information regarding certain substantial United States beneficial owners of such entity (if any). If a dividend or payment, as applicable, is both subject to withholding under FATCA and subject to the withholding tax discussed above under "—U.S. Federal Withholding Tax," the withholding under FATCA may be credited against, and therefore reduce, such other withholding tax. You should consult your own tax advisors regarding these requirements and whether they may be relevant to your ownership and disposition of our Units, amortizing notes, purchase contracts and common stock.

CERTAIN ERISA CONSIDERATIONS

The following is a summary of certain considerations associated with the purchase and holding of the Units, the common stock issuable upon settlement of the purchase contracts and the amortizing notes by (i) employee benefit plans that are subject to Title I of the Employee Retirement Income Security Act of 1974, as amended ("ERISA"), (ii) plans, individual retirement accounts and other arrangements that are subject to Section 4975 of the Code or provisions under any other federal, state, local, non-U.S. or other laws or regulations that are similar to such provisions of ERISA or the Code (collectively, "Similar Laws"), and (iii) entities which are deemed to hold the assets of any of the foregoing types of plans, accounts or arrangements (each of the foregoing described in clauses (i), (ii), and (iii) being referred to herein as a "Plan").

General fiduciary matters

ERISA and the Code impose certain duties on persons who are fiduciaries of a Plan subject to Title I of ERISA or Section 4975 of the Code (a "Covered Plan") and prohibit certain transactions involving the assets of a Covered Plan and its fiduciaries or other interested parties. Under ERISA and the Code, any person who exercises any discretionary authority or control over the administration of such a Covered Plan or the management or disposition of the assets of such a Covered Plan, or who renders investment advice for a fee or other compensation to such a Covered Plan, is generally considered to be a fiduciary of the Covered Plan.

In considering an investment in the Units, the common stock issuable upon settlement of the purchase contracts and/or amortizing notes of a portion of the assets of any Plan, a fiduciary should determine whether the investment is in accordance with the documents and instruments governing the Plan and the applicable provisions of ERISA, the Code or any Similar Law relating to a fiduciary's duties to the Plan including, without limitation, the prudence, diversification, delegation of control and prohibited transaction provisions of ERISA, the Code and any other applicable Similar Laws.

Prohibited transaction issues

Section 406 of ERISA and Section 4975 of the Code prohibit Covered Plans from engaging in specified transactions involving plan assets with persons or entities who are "parties in interest," within the meaning of ERISA, or "disqualified persons," within the meaning of Section 4975 of the Code, unless an exemption is available. A party in interest or disqualified person who engaged in a non-exempt prohibited transaction may be subject to excise taxes and other penalties and liabilities under ERISA and the Code. In addition, the fiduciary of the Covered Plan that engaged in such a non-exempt prohibited transaction may be subject to penalties and liabilities under ERISA and the Code.

The acquisition, holding and/or disposition of the Units, the common stock issuable upon settlement of the purchase contracts or the amortizing notes by a Covered Plan with respect to which we or an underwriter or any of our or their respective affiliates is considered a party in interest or a disqualified person may constitute or result in a direct or indirect prohibited transaction under Section 406 of ERISA and/or Section 4975 of the Code, unless the investment is acquired and is held in accordance with an applicable statutory, class or individual prohibited transaction exemption. In this regard, the U.S. Department of Labor has issued prohibited transaction class exemptions (each, a "PTCE") that may apply to the acquisition and holding of the Units, the common stock issuable upon settlement of the purchase contracts or the amortizing notes. These class exemptions include, without limitation, PTCE 84-14 respecting transactions determined by independent qualified professional asset managers, PTCE 90-1 respecting insurance company pooled separate accounts, PTCE 91-38 respecting bank collective investment funds, PTCE 95-60 respecting life insurance company general accounts and PTCE 96-23 respecting transactions determined by in-house asset managers. In addition, the statutory exemption under Section 408(b)(17) of ERISA and Section 4975(d)(20) of the Code provides relief from certain prohibited transaction provisions of Section 406 of ERISA and Section 4975 of the Code for certain transactions between a Covered Plan and a person who is a party in interest or disqualified person solely as a result of providing services to such Covered Plan or a relationship to such a service provider, provided that neither the person transacting

with the Covered Plan nor any of its affiliates has or exercises any discretionary authority or control or renders any investment advice with respect to the assets of the Covered Plan involved in the transaction and provided, further, that the Covered Plan pays no more than, and receives no less than, adequate consideration in connection with the transaction. Each of the above-noted exemptions contains conditions and limitations on its application. Fiduciaries of Covered Plans considering acquiring holding the Units, the common stock issuable upon settlement of the purchase contracts or the amortizing notes in reliance on these or any other exemption should carefully review the exemption in consultation with counsel to assure it is applicable. There can be no assurance that all of the conditions of any of the foregoing exemptions or any other exemption will be satisfied.

Government plans, foreign plans and certain church plans, while not subject to the fiduciary responsibility provisions of Title I of ERISA or the prohibited transaction provisions of Section 406 of ERISA or Section 4975 of the Code, may nevertheless be subject to Similar Laws. Fiduciaries of such Plans should consult with their counsel before acquiring the Units, common stock issuable upon settlement of the purchase contracts, amortizing notes or any interest therein.

Because of the foregoing, neither the Units or their constituent parts may not be purchased or held by any person investing assets of any Plan, unless such purchase and holding will not constitute or result in a non-exempt prohibited transaction under ERISA or Section 4975 of the Code or a similar violation of any applicable Similar Laws.

Representation

Accordingly, by its acceptance of the Units, common stock issued upon settlement of the purchase contracts or amortizing notes, each purchaser and subsequent transferee will be deemed to have represented and warranted that either (i) no portion of the assets used by such purchaser or transferee to acquire or hold the Units, the common stock upon settlement of the purchase contracts or amortizing notes, or any interest therein constitutes assets of any Plan or (ii) (1) the acquisition, holding and disposition of the Units, common stock issuable upon settlement of the purchase contracts or amortizing notes by such purchaser or transferee will not constitute or result in a non-exempt prohibited transaction under Section 406 of ERISA or Section 4975 of the Code or a similar violation under any applicable Similar Laws and (2) acknowledge and agree that neither the issuer, underwriters or any of their respective affiliates is, or is undertaking to be, a fiduciary with respect to any Plan in connection with the Plan's acquisition, holding or disposition of the Units, common stock issuable upon settlement of the purchase contracts or amortizing notes, as applicable.

The foregoing discussion is general in nature and is not intended to be all-inclusive. Due to the complexity of these rules and the penalties that may be imposed upon persons involved in non-exempt prohibited transactions, it is particularly important that fiduciaries or other persons considering purchasing or holding the Units, common stock issuable upon settlement of the purchase contracts or amortizing notes on behalf of, or with the assets of, any Plan, consult with their counsel regarding the potential applicability of ERISA, Section 4975 of the Code or any Similar Law and whether an exemption would be required. Neither this discussion nor anything provided in this prospectus supplement is, or is intended to be, investment advice directed at any potential Plan purchasers, or at Plan purchasers generally, and such purchasers of the Units or any of its constituent parts should consult and rely on their own counsel and advisers as to whether such an investment is suitable for the Plan. The sale of any of the Units, common stock issuable upon settlement of the purchase contracts or amortizing notes to any Plan is in no respect a representation by us, an Underwriter or any of our or their affiliates or representatives that such an investment meets all relevant legal requirements with respect to investments by Plans generally or any particular Plan, or that such investment is prudent or appropriate for plans generally or any particular Plan.

BOOK-ENTRY PROCEDURES AND SETTLEMENT

The Units, the separate purchase contracts and the separate amortizing notes will initially be issued under a book-entry system in the form of global securities. We will register the global securities in the name of The Depository Trust Company, New York, New York, or DTC, or its nominee and will deposit the global securities with that depositary.

Following the issuance of a global security in registered form, the depositary will credit the accounts of its participants with the Units, the separate purchase contracts and the separate amortizing notes, as the case may be, upon our instructions. Only persons who hold directly or indirectly through financial institutions that are participants in the depositary can hold beneficial interests in the global securities. Because the laws of some jurisdictions require certain types of purchasers to take physical delivery of such securities in definitive form, you may encounter difficulties in your ability to own, transfer or pledge beneficial interests in a global security.

So long as the depositary or its nominee is the registered owner of a global security, we, the trustee and the purchase contract agent will treat the depositary as the sole owner or holder of the Units, the separate purchase contracts and the separate amortizing notes, as the case may be. Therefore, except as set forth below, you will not be entitled to have Units, separate purchase contracts or separate amortizing notes registered in your name or to receive physical delivery of certificates representing the Units, the separate purchase contracts or the separate amortizing notes. Accordingly, you will have to rely on the procedures of the depositary and the participant in the depositary through whom you hold your beneficial interest in order to exercise any rights of a holder under the indenture or the purchase contract agreement, as the case may be. We understand that under existing practices, the depositary would act upon the instructions of a participant or authorize that participant to take any action that a holder is entitled to take.

As long as the separate amortizing notes are represented by the global securities, we will pay installments on those separate amortizing notes to or as directed by DTC as the registered holder of the global securities. Payments to DTC will be in immediately available funds by wire transfer. DTC will credit the relevant accounts of their participants on the applicable date. Neither we nor the trustee will be responsible for making any payments to participants or customers of participants or for maintaining any records relating to the holdings of participants and their customers, and you will have to rely on the procedures of the depositary and its participants.

Settlement

Secondary market trading between DTC participants will occur in the ordinary way in accordance with DTC rules and will be settled in immediately available funds using DTC's Same-Day Funds Settlement System.

Definitive Securities and Paying Agents

Book-entry securities represented by a global security will be exchanged for definitive (paper) securities only if:

- the depositary is at any time unwilling or unable to continue as depositary for such security or ceases to be a clearing agency registered under the Exchange Act, and a successor depositary registered as a clearing agency under the Exchange Act is not appointed by us within 90 days; or

- an Event of Default with respect to the amortizing notes, or any failure on the part of us to observe or perform any covenant or agreement in the purchase contracts, has occurred and is continuing and a beneficial owner requests that its amortizing notes and/or purchase contracts, as the case may be, be issued in physical, certificated form.

The global security will be exchangeable in whole for definitive securities in registered form, with the same terms and of an equal aggregate principal amount. Definitive Units, separate purchase contracts or separate amortizing notes, as the case may be, will be registered in the name or names of the person or persons specified by the depositary in a written instruction to the registrar of the securities. The depositary may base its written instruction upon directions it receives from its participants.

If any of the events described above occurs, then the beneficial owners will be notified through the chain of intermediaries that definitive securities are available and notice will be published as described below under "—Notices." Beneficial owners of book-entry Units, separate purchase contracts or separate amortizing notes, as the case may be, will then be entitled (1) to receive physical delivery in certificated form of definitive Units, separate purchase contracts or separate amortizing notes, as the case may be, equal in aggregate amount of Units, separate purchase contracts or separate amortizing notes, as the case may be, to their beneficial interest and (2) to have the definitive securities registered in their names. Thereafter, the holders of the definitive Units, separate purchase contracts and separate amortizing notes, as the case may be, will be recognized as the "holders" of the Units, separate amortizing notes and separate purchase contracts for purposes of the purchase contract agreement and indenture, respectively.

Each of the purchase contract agreement and indenture provides for the replacement of a mutilated, lost, stolen or destroyed definitive security, so long as the applicant furnishes to us and the trustee such security or indemnity and such evidence of ownership as we and it may require.

In the event definitive separate amortizing notes are issued, the holders thereof will be able to receive installment payments at the office of our paying agent. The final installment payment of a definitive separate amortizing note may be made only against surrender of the separate amortizing note to one of our paying agents. We also have the option of making installment payments by mailing checks to the registered holders of the separate certificated amortizing notes.

In the event definitive Units, separate purchase contracts or separate amortizing notes are issued, the holders thereof will be able to transfer their securities, in whole or in part, by surrendering such securities for registration of transfer at the office specified in the purchase contract agreement or the indenture, as applicable. A form of such instrument of transfer will be obtainable at the relevant office. Upon surrender, we will execute, and the purchase contract agent and the trustee will authenticate and deliver, new Units, separate purchase contracts or separate amortizing notes, as the case may be, to the designated transferee in the amount being transferred, and a new security for any amount not being transferred will be issued to the transferor. Such new securities will be delivered free of charge at the relevant office, as requested by the owner of such new Units, separate purchase contracts or separate amortizing notes. We will not charge any fee for the registration of transfer or exchange, except that we may require the payment of a sum sufficient to cover any applicable tax or other governmental charge payable in connection with the transfer.

Notices

So long as the global securities are held on behalf of DTC or any other clearing system, notices to holders of securities represented by a beneficial interest in the global securities may be given by delivery of the relevant notice to DTC or the alternative clearing system, as the case may be. So long as the amortizing notes are in the form of global securities, any notice will be deemed to have been given on the date given to DTC or the alternative clearing system, as the case may be.

UNDERWRITING

Under the terms and subject to the conditions in an underwriting agreement dated the date of this prospectus supplement, the underwriters named below, for whom RBC Capital Markets, LLC and Goldman Sachs & Co. LLC are acting as representatives, have severally agreed to purchase, and we have agreed to sell to them, severally, the number of Units indicated below:

Underwriters	Number of Units
RBC Capital Markets, LLC	3,630,000
Goldman Sachs & Co. LLC	3,630,000
Merrill Lynch, Pierce, Fenner & Smith Incorporated	847,905
Morgan Stanley & Co. LLC	847,905
Wells Fargo Securities, LLC	593,533
PNC Capital Markets LLC	729,198
Barclays Capital Inc.	593,533
Citizens Capital Markets, Inc.	203,497
The Huntington Investment Company	203,497
MUFG Securities Americas Inc.	203,497
J.P. Morgan Securities LLC	138,717
TD Securities (USA) LLC	138,717
Robert W. Baird & Co. Incorporated	60,000
Boenning & Scattergood, Inc.	60,000
HSBC Securities (USA) Inc.	60,000
Janney Montgomery Scott LLC	60,001
Total	12,000,000

The underwriters and the representatives are collectively referred to as the "underwriters" and the "representatives," respectively. The underwriters are offering the Units subject to their acceptance of the Units from us and subject to prior sale. The underwriting agreement provides that the obligations of the several underwriters to pay for and accept delivery of the Units offered by this prospectus supplement are subject to the approval of certain legal matters by their counsel and to certain other conditions. The underwriters are obligated to take and pay for all of the Units offered by this prospectus supplement if any such Units are taken. However, the underwriters are not required to take or pay for the Units covered by the underwriters' option to purchase additional Units described below.

The underwriters initially propose to offer part of the Units directly to the public at the offering price listed on the cover page of this prospectus supplement and part to certain dealers. After the initial offering of the Units, the offering price and other selling terms may from time to time be varied by the representatives.

We have granted to the underwriters an option, exercisable for 13 days beginning on, and including, the date of the initial issuance of the Units, to purchase up to 1,800,000 additional Units at the public offering price listed on the cover page of this prospectus supplement, less the underwriting discount solely to cover over-allotments. To the extent the option is exercised, each underwriter will become obligated, subject to certain conditions, to purchase about the same percentage of the additional Units as the number listed next to the underwriter's name in the preceding table bears to the total number of Units listed next to the names of all underwriters in the preceding table.

The following table shows the per Unit and total public offering price, underwriting discount we will pay to the underwriters in this offering and proceeds before expenses to us. These amounts are shown assuming both no exercise and full exercise of the underwriters' option to purchase up to an additional 1,800,000 Units.

	Per Unit	Total	
		No Exercise	Full Exercise
Public offering price	$ 50.00	$ 600,000,000	$ 690,000,000
Underwriting discount	$ 1.125	$ 13,500,000	$ 15,525,000
Proceeds, before expenses, to us	$ 48.875	$ 586,500,000	$ 674,475,000

The estimated offering expenses payable by us, exclusive of the underwriting discount, are approximately $750,000. We have agreed to reimburse the underwriters for expense relating to any required review of this offering by the Financial Industry Regulatory Authority, Inc.

The Units are a new issue of securities with no established trading market. We have applied to list the Units on the NYSE under the symbol "WTRU," subject to satisfaction of its minimum listing standards with respect to the Units. If the Units are approved for listing, we expect trading on the NYSE to begin within 30 calendar days after the Units are first issued.

We and all of our continuing directors (as described in our Definitive Proxy Statement on Schedule 14A filed with the SEC on March 22, 2019), director nominees and officers, through entering into lock-up agreements, have agreed that, without the prior written consent of the representatives on behalf of the underwriters, we and they will not, during the period ending 90 days after the date of this prospectus supplement (the "restricted period"): (i) offer, sell, contract to sell, pledge, grant any option to purchase, make any short sale or otherwise transfer or dispose of, directly or indirectly, our common stock, any options, rights or warrants to purchase our common stock or any securities convertible into or exchangeable for, or substantially similar to, our common stock (collectively, "restricted securities"); (ii) enter into any swap or other agreement that transfers to another, in whole or in part, any of the economic consequences of ownership of the common stock or any such other securities, whether any such transaction described in (i) or (ii) is to be settled by delivery of common stock or such other securities, in cash or otherwise or (iii) publicly disclose the intention to take any of the foregoing actions. In addition, we agreed not to file with the SEC any registration statement relating to any restricted securities, and our continuing directors, director nominees and officers each agreed not to make any demand for, or exercise any right with respect to, the registration of any restricted securities, in each case during the restricted period and without the prior written consent of the representatives on behalf of the underwriters.

The restrictions described in the immediately preceding paragraph do not apply to:

- the Units to be sold in this offering and any shares of common stock issued pursuant to the terms of the purchase contracts;
- the sale of the shares of common stock to the underwriters in the Common Stock Offering or the sale of the shares of our common stock to CPPIB in the Private Placement;
- the issuance by us of, or the receipt by our continuing directors, director nominees and officers of, restricted securities pursuant to our existing employee equity or equity-based incentive plans, employee stock purchase plans or dividend reinvestment plans, or upon the conversion or exchange of convertible or exchangeable securities outstanding as of the date of this prospectus supplement;
- the filing by us of registration statements relating to securities issuable under our existing employee equity or equity-based plans or employee stock purchase plans;
- the issuance of shares of common stock in connection with certain investments, acquisitions, with joint ventures, commercial relationships or other strategic transactions, provided that the aggregate number of shares issued or issuable pursuant to this clause does not exceed 10% of the number of shares of common stock outstanding immediately after this offering and prior to such issuance;

- in the case of our continuing directors, director nominees and officers, (i) the establishment of a trading plan pursuant to Rule 10b5-1 under the Exchange Act for the transfer of our common stock following expiration of the restricted period, (ii) transfers in accordance with the terms of existing trading plans pursuant to Rule 10b5-1 under the Exchange Act, (iii) certain transfers of shares held as of the date of this prospectus supplement through our existing 401(k) plan pursuant to portfolio balancing opportunities provided by the terms of such plan, (iv) transfers to us to satisfy certain tax obligations in connection with vesting of restricted stock units, restricted shares, performance share units or phantom shares and (v) certain other transfers to us;

- in the case of our continuing directors, director nominees and officers, transfers to us upon death, disability or termination or employment, in each case, of such person;

- the receipt by us or our subsidiaries of shares (a) in the exercise of outstanding options, warrants, restricted stock units or other equity interests, including transfers deemed to occur upon the "net" or "cashless" exercise of options or (b) for the sole purpose of paying the exercise price of such options, warrants, restricted stock units or other equity interests or for paying taxes (including estimated taxes) due as a result of the exercise of such options, warrants, restricted stock units or other equity interests or as a result of the vesting of shares under restricted stock awards or restricted stock units pursuant to our existing employee benefit plans disclosed herein relating to this public offering, in each case on a "cashless" or "net exercise" basis, provided that any such shares received upon such exercise shall be subject to the terms of the lock-up agreement;

- tenders, sales or other transfers pursuant to a bona fide third-party tender offer, merger, consolidation or other similar transaction made to all holders of restricted securities involving a "change of control" of us (provided that if such transaction is not consummated, our continuing directors', director nominees' and officers' shares shall remain subject to the restrictions set forth in the lock-up agreements);

- the exercise for cash of options to purchase shares disclosed as outstanding herein, provided that any such shares received upon such exercise shall be subject to the terms of the lock-up agreements;

- in the case of our continuing directors, director nominees and officers, the disposition of shares acquired in this offering or in open market transactions after completion of this offering; and

- transfers of shares or other of our securities pursuant to an order of a court or regulatory agency or to comply with any regulations related to ownership by our continuing directors, director nominees and officers of their shares.

The representatives, in their sole discretion, may release the common stock and other securities subject to the lock-up agreements described above in whole or in part at any time.

In order to facilitate the offering of the Units, the underwriters may engage in transactions that stabilize, maintain or otherwise affect the price of the Units. Specifically, the underwriters may sell more Units than they are obligated to purchase under the underwriting agreement, creating a short position. A short sale is covered if the short position is no greater than the number of Units available for purchase by the underwriters under the option to purchase additional Units. The underwriters can close out a covered short sale by exercising the option or purchasing Units in the open market. In determining the source of Units to close out a covered short sale, the underwriters will consider, among other things, the open market price of Units compared to the price available under the option. The underwriters may also sell Units in excess of the option, creating a naked short position. The underwriters must close out any naked short position by purchasing Units in the open market. A naked short position is more likely to be created if the underwriters are concerned that there may be downward pressure on the price of the Units in the open market after pricing that could adversely affect investors who purchase in this offering. As an additional means of facilitating this offering, the underwriters may bid for, and purchase, Units

in the open market to stabilize the price of the Units. These activities may raise or maintain the market price of the Units above independent market levels or prevent or retard a decline in the market price of the Units. The underwriters are not required to engage in these activities and may end any of these activities at any time.

We have agreed to indemnify the underwriters against certain liabilities in connection with this offering, including liabilities under the Securities Act, or to contribute to payments that the underwriters may be required to make in respect of those liabilities.

The underwriters and their respective affiliates are full-service financial institutions engaged in various activities, which may include securities trading, commercial and investment banking, financial advisory, investment management, investment research, principal investment, hedging, financing and brokerage activities. Certain of the underwriters and their respective affiliates have, from time to time, performed, and may in the future perform, various financial advisory and investment banking services for us, for which they received or will receive customary fees and expenses. For example, Goldman Sachs & Co. LLC and RBC Capital Markets, LLC acted as our financial advisers in connection with the Acquisition, for which they are receiving customary fees and expenses. Also in connection with the Acquisition, certain of the underwriters and/or their affiliates have provided committed financing under the Bridge Commitment pursuant to which they receive customary commitment fees in connection with their respective commitments and, in the event we borrow under the Bridge Facility, would receive certain additional funding and other fees. Certain of the underwriters and/or their affiliates are also lenders and/or agents under the Revolving Credit Facility, which we expect to draw upon to refinance Peoples's revolving credit facility in connection with the Acquisition, and receive customary fees and expenses in connection therewith and would receive proceeds from this offering if we were to temporarily reduce our borrowings under the Revolving Credit Facility as described in "Use of Proceeds." Certain of the underwriters in this offering are also acting as underwriters in our concurrent Common Stock Offering, and may act as underwriters in the Notes Offering, for which they will receive customary fees and expenses. Certain of the underwriters may also receive fees and expenses in connection with the Private Placement. In addition, in an effort to manage our exposure to interest rate risk associated with the Notes Offering, we have entered into, and in the future, may enter into, financial derivative instruments such as interest rate swap agreements with certain of the underwriters or their respective affiliates.

In addition, in the ordinary course of their various business activities, the underwriters and their respective affiliates may make or hold a broad array of investments and actively trade debt and equity securities (or related derivative securities) and financial instruments (including bank loans) for their own account and for the accounts of their customers and may at any time hold long and short positions in such securities and instruments. Such investment and securities activities may involve our securities and instruments. Certain of the underwriters and/or their affiliates have lending relationships with us and may hedge their credit exposure to us consistent with their customary risk management policies. Typically, the underwriters and their affiliates would hedge such exposure by entering into transactions which consist of either the purchase of credit default swaps or the creation of short positions in our securities or the securities of our affiliates. Any such credit default swaps or short positions could adversely affect future trading prices of the Units offered hereby. The underwriters and their respective affiliates may also make investment recommendations or publish or express independent research views in respect of such securities or instruments and may at any time hold, or recommend to clients that they acquire, long or short positions in such securities and instruments, for which they received or will receive customary fees and expenses.

Selling Restrictions

Canada

The Units may be sold only to purchasers purchasing, or deemed to be purchasing, as principal that are accredited investors, as defined in National Instrument 45-106 Prospectus Exemptions or subsection 73.3(1) of the Securities Act (Ontario), and are permitted clients, as defined in National Instrument 31-103 Registration

Requirements, Exemptions and Ongoing Registrant Obligations. Any resale of the Units must be made in accordance with an exemption from, or in a transaction not subject to, the prospectus requirements of applicable securities laws.

Securities legislation in certain provinces or territories of Canada may provide a purchaser with remedies for rescission or damages if this prospectus supplement (including any amendment thereto) contains a misrepresentation, provided that the remedies for rescission or damages are exercised by the purchaser within the time limit prescribed by the securities legislation of the purchaser's province or territory. The purchaser should refer to any applicable provisions of the securities legislation of the purchaser's province or territory for particulars of these rights or consult with a legal advisor.

Pursuant to section 3A.3 (or, in the case of securities issued or guaranteed by the government of a non-Canadian jurisdiction, section 3A.4) of National Instrument 33-105 Underwriting Conflicts (NI 33-105), the underwriters are not required to comply with the disclosure requirements of NI 33-105 regarding underwriter conflicts of interest in connection with this offering.

European Economic Area

The Units are not intended to be offered, sold or otherwise made available to and should not be offered, sold or otherwise made available to any retail investor in the European Economic Area (the "EEA"). For these purposes, a retail investor means a person who is one (or more) of: (i) a retail client as defined in point (11) of Article 4(1) of Directive 2014/65/EU (as amended, "MiFID II"); or (ii) a customer within the meaning of Directive 2002/92/EC (as amended, the "Insurance Mediation Directive"), where that customer would not qualify as a professional client as defined in point (10) of Article 4(1) of MiFID II; or (iii) not a qualified investor as defined in Directive 2003/71/EC (and amendments thereto, including by Directive 2010/73/EU, the "Prospectus Directive"). Consequently no key information document required by Regulation (EU) No 1286/2014 (as amended, the "PRIIPs Regulation") for offering or selling the Units or otherwise making them available to retail investors in the EEA has been prepared and therefore offering or selling the Units or otherwise making them available to any retail investor in the EEA may be unlawful under the PRIIPs Regulation. This prospectus supplement and the accompanying prospectus have been prepared on the basis that any offer of Units in any Member State of the EEA will be made pursuant to an exemption under the Prospectus Directive from the requirement to publish a prospectus for offers of Units. This prospectus supplement and the accompanying prospectus are not a prospectus for the purposes of the Prospectus Directive.

United Kingdom

In addition, this document is being distributed only to, and is directed only at, and any offer subsequently made may only be directed at: (i) in the United Kingdom, persons having professional experience in matters relating to investments falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005, as amended (the "Order"), and/or persons falling within Article 49(2)(a) to (d) of the Order; (ii) persons who are outside the United Kingdom; and (iii) any other persons to whom it may otherwise lawfully be distributed (all such persons together being referred to as "relevant persons"). This document must not be acted on or relied on by persons who are not relevant persons. Any investment or investment activity to which this document relates is available only to, and will be engaged in only with, relevant persons.

Australia

No placement document, prospectus, product disclosure statement or other disclosure document has been lodged with the Australian Securities and Investments Commission ("ASIC") in relation to the offering. This prospectus supplement, the accompanying prospectus and any other offering or marketing material relating to the Units or this offering do not constitute a prospectus, product disclosure statement or other disclosure document

under the prospectus, product disclosure statement or other disclosure document under the Corporations Act 2001 (Cth) (the "Corporations Act"), and do not purport to include the information required for a prospectus, product disclosure statement or other disclosure document under the Corporations Act.

Any offer in Australia of the Units may only be made to persons (the "Exempt Investors") who are "sophisticated investors" (within the meaning of section 708(8) of the Corporations Act), "professional investors" (within the meaning of section 708(11) of the Corporations Act) or otherwise pursuant to one or more exemptions contained in section 708 of the Corporations Act so that it is lawful to offer the Units without disclosure to investors under Chapter 6D of the Corporations Act.

The Units applied for by Exempt Investors in Australia must not be offered for sale in Australia for a period of 12 months after the date of allotment under the offering, except in circumstances where disclosure to investors under Chapter 6D of the Corporations Act would not be required pursuant to an exemption under section 708 of the Corporations Act or otherwise or where the offer is pursuant to a disclosure document which complies with Chapter 6D of the Corporations Act. Any person acquiring Units must observe such Australian on-sale restrictions.

This prospectus supplement and the accompanying prospectus contain general information only and do not take account of the investment objectives, financial situation or particular needs of any particular person. They do not contain any securities recommendations or financial product advice. Before making an investment decision, investors need to consider whether the information in this prospectus supplement and the accompanying prospectus is appropriate to their needs, objectives and circumstances, and, if necessary, seek expert advice on those matters.

Hong Kong

The Units may not be offered or sold in Hong Kong by means of any document other than (i) in circumstances which do not constitute an offer to the public within the meaning of the Companies Ordinance (Cap. 32, Laws of Hong Kong), or (ii) to "professional investors" within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder, or (iii) in other circumstances which do not result in the document being a "prospectus" within the meaning of the Companies Ordinance (Cap. 32, Laws of Hong Kong) and no advertisement, invitation or document relating to the Units may be issued or may be in the possession of any person for the purpose of issue (in each case whether in Hong Kong or elsewhere), which is directed at, or the contents of which are likely to be accessed or read by, the public in Hong Kong (except if permitted to do so under the laws of Hong Kong) other than with respect to Units which are or are intended to be disposed of only to persons outside Hong Kong or only to "professional investors" within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder.

Japan

The Units have not been and will not be registered under the Financial Instruments and Exchange Act of Japan (Act No. 25 of 1948, as amended) (the "FIEA"). The Units may not be offered or sold, directly or indirectly, in Japan or to or for the benefit of any resident of Japan (including any person resident in Japan or any corporation or other entity organized under the laws of Japan) or to others for reoffering or resale, directly or indirectly, in Japan or to or for the benefit of any resident of Japan, except pursuant to an exemption from the registration requirements of the FIEA and otherwise in compliance with any relevant laws, regulations and ministerial guidelines of Japan.

Korea

Neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the Units or the offering should be construed in any way as our (or any of our affiliates or agents) soliciting investment or offering to sell the Units in the Republic of Korea ("Korea"). We are not

making any representation with respect to the eligibility of any recipients of this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the Units or the offering to acquire the Units under the laws of Korea, including, without limitation, the Financial Investment Services and Capital Markets Act (the "FSCMA"), the Foreign Exchange Transaction Act (the "FETA"), and any regulations thereunder. The Units have not been registered with the Financial Services Commission of Korea (the "FSC") in any way pursuant to the FSCMA, and the Units may not be offered, sold or delivered, or offered or sold to any person for reoffering or resale, directly or indirectly, in Korea or to any resident of Korea except pursuant to applicable laws and regulations of Korea. Furthermore, the Units may not be resold to any Korean resident unless such Korean resident as the purchaser of the resold Units complies with all applicable regulatory requirements (including, without limitation, reporting or approval requirements under the FETA and regulations thereunder) relating to the purchase of the resold Units.

Singapore

Neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the Units or the offering has been registered as a prospectus with the Monetary Authority of Singapore. Accordingly, neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the Units or the offering may be circulated or distributed, nor may the Units be offered or sold, or be made the subject of an invitation for subscription or purchase, whether directly or indirectly, to persons in Singapore, other than (a) to an institutional investor under Section 274 of the Securities and Futures Act, Chapter 289 of Singapore (the "SFA"), (b) to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions specified in Section 275 of the SFA or (c) pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA.

Where the Units are subscribed or purchased under Section 275 by a relevant person which is: (i) a corporation (which is not an accredited investor) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or (ii) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary is an accredited investor, shares, debentures and units of shares and debentures of that corporation or the beneficiaries' rights and interest in that trust shall not be transferable for six months after that corporation or that trust has acquired the Units under Section 275 except: (1) to an institutional investor under Section 274 of the SFA or to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions, specified in Section 275 of the SFA; (2) where no consideration is given for the transfer; or (3) by operation of law.

Solely for the purposes of its obligations pursuant to sections 309B(1)(a) and 309B(1)(c) of the Securities and Futures Act (Chapter 289 of Singapore) (the "SFA"), we have determined, and hereby notify all relevant persons (as defined in Section 309A of the SFA) that the Units are "prescribed capital markets products" (as defined in the Securities and Futures (Capital Markets Products) Regulations 2018) and Excluded Investment Products (as defined in MAS Notice SFA 04-N12: Notice on the Sale of Investment Products and MAS Notice FAA-N16: Notice on Recommendations on Investment Products).

Switzerland

The Units may not be publicly offered in Switzerland and will not be listed on the SIX Swiss Exchange ("*SIX*") or on any other exchange or regulated trading facility in Switzerland. This prospectus supplement, the accompanying prospectus and any other offering or marketing material relating to the Units or this offering do not constitute a prospectus within the meaning of and have been prepared without regard to the disclosure standards for issuance prospectuses under art. 652a or art. 1156 of the Swiss Code of Obligations or the disclosure standards for listing prospectuses under art. 27 ff. of the SIX Listing Rules or the listing rules of any other exchange or regulated trading facility in Switzerland.

Neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the Units or the offering may be publicly distributed or otherwise made publicly available in Switzerland. Neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the offering, the Company or the Units has been or will be filed with or approved by any Swiss regulatory authority. In particular, this prospectus supplement and the accompanying prospectus will not be filed with, and the offer of Units will not be supervised by, the Swiss Financial Market Supervisory Authority, and the offer of Units has not been and will not be authorized under the Swiss Federal Act on Collective Investment Schemes (the "*CISA*"). The investor protection afforded to acquirers of interests in collective investment schemes under the CISA does not extend to acquirers of the Units.

Taiwan

The Units have not been and will not be registered or filed with, or approved by, the Financial Supervisory Commission of Taiwan and/or any other regulatory authority of Taiwan pursuant to relevant securities laws and regulations and may not be sold, issued or offered within Taiwan through a public offering or in circumstances which could constitute an offer within the meaning of the Securities and Exchange Act of Taiwan or relevant laws and regulations that require a registration, filing or approval of the Financial Supervisory Commission of Taiwan and/or other regulatory authority of Taiwan. No person or entity in Taiwan has been authorized to offer or sell the Units in Taiwan.

United Arab Emirates

The Units have not been, and are not being, publicly offered, sold, promoted or advertised in the United Arab Emirates (including the Abu Dhabi Global Market and the Dubai International Financial Centre) other than in compliance with the laws, regulations and rules of the United Arab Emirates, the Abu Dhabi Global Market and the Dubai International Financial Centre governing the issue, offering and sale of securities. Further, this prospectus supplement, the accompanying prospectus and any other offering or marketing material relating to the Units or the offering do not constitute a public offer of securities in the United Arab Emirates (including the Abu Dhabi Global Market and the Dubai International Financial Centre) and are not intended to be a public offer. This prospectus supplement, the accompanying prospectus and any other offering or marketing material relating to the Units or the offering have not been approved by or filed with the Central Bank of the United Arab Emirates, the Securities and Commodities Authority, the Financial Services Regulatory Authority or the Dubai Financial Services Authority.

LEGAL MATTERS

Certain legal matters will be passed upon for us by Simpson Thacher & Bartlett LLP, New York, New York. Ballard Spahr LLP, Philadelphia, Pennsylvania will issue an opinion regarding certain matters of Pennsylvania law, including the validity of the securities offered by the prospectus supplement. Certain legal matters will be passed upon for the underwriters by Cravath, Swaine & Moore LLP, New York, New York.

EXPERTS

The financial statements and management's assessment of the effectiveness of internal control over financial reporting (which is included in Management's Report on Internal Control over Financial Reporting) incorporated in this prospectus supplement by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2018 have been so incorporated in reliance on the report of PricewaterhouseCoopers LLP, an independent registered public accounting firm, given on the authority of said firm as experts in auditing and accounting.

The consolidated financial statements of LDC, Funding LLC as of December 31, 2018 and 2017 and for each of the three years in the period ended December 31, 2018, incorporated by reference in this prospectus supplement and in the accompanying prospectus from Aqua America's Current Report on Form 8-K/A filed on April 15, 2019, have been audited by Deloitte & Touche LLP, independent auditors, as stated in their report, which is incorporated by reference herein, and are incorporated in reliance upon the report of such firm given upon their authority as experts in accounting and auditing.

WHERE YOU CAN FIND ADDITIONAL INFORMATION; INCORPORATION OF CERTAIN DOCUMENTS BY REFERENCE

We file annual, quarterly and current reports, proxy statements and other information with the SEC. The SEC maintains a website at *www.sec.gov* that contains periodic and current reports, proxy and information statements, and other information regarding registrants that are filed electronically with the SEC.

These documents are also available, free of charge, through the Investors section of our website, which is located at *http://ir.aquaamerica.com/*. Information contained on our website is not incorporated by reference into this prospectus supplement or the accompanying prospectus and you should not consider information on our website to be part of this prospectus supplement or the accompanying prospectus.

We have filed with the SEC a "shelf" registration statement on Form S-3 under the Securities Act of 1933 relating to the securities that may be offered by this prospectus supplement. This prospectus supplement is a part of that registration statement, but does not contain all of the information in the registration statement. We have omitted certain parts of the registration statement in accordance with rules and regulations of the SEC. Statements made in this prospectus supplement as to the contents of any contract, agreement or other documents are not necessarily complete, and, in each instance, we refer you to a copy of such document filed as an exhibit to the registration statement, of which this prospectus supplement is a part, or otherwise filed with the SEC. For more detail about us and any securities that may be offered by this prospectus supplement, you may examine the registration statement on Form S-3 and the exhibits filed with it at the locations listed in the previous paragraph.

The SEC allows us to "incorporate by reference" into this prospectus supplement and the accompanying prospectus the information we file with them, which means that we can disclose important information to you by referring you to those documents. The information incorporated by reference is considered to be part of this prospectus supplement. When we file information with the SEC in the future, that information will automatically update and supersede this information. We incorporate by reference the documents listed below and any future filings we will make with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934 until we sell all of the securities covered by this prospectus supplement or this offering is terminated;

provided, however, that we are not incorporating, in each case, any portions of documents or information furnished or deemed to have been furnished and not filed in accordance with SEC rules:

- Our Annual Report on Form 10-K for the year ended December 31, 2018 filed with the SEC on February 26, 2019;
- The portions of our Definitive Proxy Statement on Schedule 14A filed with the SEC on March 22, 2019, that are incorporated by reference into our Annual Report on Form 10-K for the fiscal year ended December 31, 2018;
- Our Current Reports on Form 8-K filed with the SEC on October 23, 2018, February 19, 2019 (Item 8.01 only), and March 29, 2019, and our Current Report on Form 8-K/A filed with the SEC on April 15, 2019; and
- The description of our common stock set forth in our Registration Statement on Form 8-A, including any amendments or reports filed for the purpose of updating such description.

These documents contain important business and financial information about us that is not included in or delivered with this prospectus supplement. You may request a copy of any or all documents that we incorporate by reference at no cost, by writing or telephoning us at:

Aqua America, Inc.
762 W. Lancaster Avenue
Bryn Mawr, PA 19010-3489
Telephone: 610-527-8000
Attention: Corporate Secretary

We have not, and the underwriters have not, authorized anyone to provide you with any information other than that contained or incorporated by reference in this prospectus supplement, the accompanying prospectus or in any free writing prospectus we may provide to you in connection with this offering. Neither we nor the underwriters take any responsibility for, or provide any assurances as to the reliability of, any additional or different information that others may give you. You should assume that the information contained in this prospectus supplement, the accompanying prospectus and any free writing prospectus we may provide to you in connection with this offering is accurate only as of their respective dates or as of the respective dates specified in such information, as applicable, and the information contained in documents incorporated by reference is accurate only as of the respective dates of those documents or as of the respective dates specified in such information, as applicable, in each case regardless of the time of delivery of this prospectus supplement or the accompanying prospectus or any such free writing prospectus or any sale of our common stock. Our business, financial condition, results of operations and prospects may have changed since those dates.

Any statement contained herein or in a document incorporated or deemed to be incorporated by reference herein shall be deemed to be modified or superseded for purposes of this prospectus supplement to the extent that a statement contained herein, in any other subsequently filed document which also is or is deemed to be incorporated by reference herein or in the accompanying prospectus, modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified and superseded, to constitute a part of this prospectus supplement.

PROSPECTUS

AQUA AMERICA, INC.

Common Stock
Preferred Stock
Common Stock Purchase Contracts
Warrants
Units
Depositary Shares
Debt Securities

Aqua America, Inc. may, from time to time, in one or more offerings, offer and sell common stock, preferred stock, common stock purchase contracts, warrants, units, depositary shares and debt securities. The debt securities and preferred stock may be convertible into or exchangeable or exercisable for other securities. We will provide specific terms of any offering and the offered securities in supplements to this prospectus. The prospectus supplements may also add, update or change information contained in this prospectus.

We may offer and sell these securities to or through underwriters, dealers or agents, directly to purchasers or through a combination of these methods. If an offering of securities involves any underwriters, dealers or agents, then the names of the underwriters, dealers or agents and the terms of the arrangements with such entities will be stated in an accompanying prospectus supplement.

Our common stock is listed on the New York Stock Exchange under the symbol "WTR." We have not yet determined whether any of the other securities that may be offered by this prospectus will be listed on any exchange, inter-dealer quotation system or over-the-counter market. If we decide to seek listing of any such securities upon issuance, an accompanying prospectus supplement will disclose the exchange, quotation system or market on which the securities will be listed.

The prospectus may not be used to sell our securities unless it is accompanied by a prospectus supplement.

Investing in our securities involves risk. Before you invest, you should carefully read and evaluate the risk factors and other information included in this prospectus and any applicable prospectus supplement, including the documents incorporated by reference. See "Risk Factors" beginning on page 8 of this prospectus.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is February 28, 2018.

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ABOUT THIS PROSPECTUS

This document is called a prospectus and is part of a registration statement that we filed with the Securities and Exchange Commission (SEC) using a "shelf" registration process. Under this shelf process, we may, from time to time, in one or more offering, offer and sell common stock, preferred stock, common stock purchase contracts, warrants, units, depositary shares and debt securities. This prospectus provides you with a general description of the securities we may offer. Each time we sell any securities under this prospectus, we will provide a prospectus supplement that will contain specific information about the terms of that offering and the offered securities. That prospectus supplement may include a discussion of any risk factors or other special considerations applicable to those securities. The prospectus supplement also may add, update or change information contained in this prospectus. You should read both this prospectus and the applicable prospectus supplement and the exhibits filed with our registration statement together with the additional information described below under the heading "Where You Can Find More Information" before you decide whether to invest in the securities.

The registration statement (including the exhibits) of which this prospectus is a part contains additional information about us and the securities we may offer by this prospectus. Specifically, we have filed certain legal documents that control the terms of the securities offered by this prospectus as exhibits to the registration statement. We will file certain other legal documents that will control the terms of the securities we may offer by this prospectus as exhibits to the registration statement or to reports we file with the SEC. The registration statement and the reports can be read at the SEC website or at the SEC offices mentioned under the heading "Where You Can Find More Information."

You should rely only upon the information contained in, or incorporated by reference into, this prospectus and the applicable prospectus supplement that contains specific information about the securities we are offering. We have not authorized any other person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should assume that the information appearing in this document is accurate only as of the date on the front cover of this document. Our business, financial condition, results of operations and prospects may have changed since that date.

Except as otherwise provided in this prospectus, unless the context otherwise requires, references in this prospectus to "Aqua America," "we," "us" or "our" refer to Aqua America, Inc. and its direct and indirect subsidiaries. In addition, references to "Aqua Pennsylvania" refer to our wholly-owned subsidiary, Aqua Pennsylvania, Inc., and its subsidiaries.

FORWARD-LOOKING STATEMENTS

Certain statements in this prospectus, or incorporated by reference into this prospectus, are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 and are made based upon, among other things, our current assumptions, expectations, plans, and beliefs concerning future events and their potential effect on us. These forward-looking statements involve risks, uncertainties and other factors, many of which are outside our control, that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. In some cases you can identify forward- looking statements where statements are preceded by, followed by, or include the words "believes," "expects," "anticipates," "plans," "future," "potential," "probably," "predictions," "intends," "will," "continue" or the negative of such terms or similar expressions. Forward-looking statements in this prospectus, or incorporated by reference into this prospectus, include, but are not limited to, statements regarding:

- recovery of capital expenditures and expenses in rates;
- projected capital expenditures and related funding requirements;
- our capability to pursue timely rate increase requests;
- the availability and cost of capital financing;
- developments, trends and consolidation in the water and wastewater utility and infrastructure industries;
- dividend payment projections;
- opportunities for future acquisitions, both within and outside the water and wastewater industry, the success of pending acquisitions and the impact of future acquisitions;
- the capacity of our water supplies, water facilities and wastewater facilities;
- the impact of federal and/or state tax laws or policies and the regulatory treatment of the effects of those laws or policies, including the Tax Cuts and Jobs Act;
- the impact of geographic diversity on our exposure to unusual weather;
- the impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer;
- our authority to carry on our business without unduly burdensome restrictions;
- the continuation of investments in strategic ventures;
- our ability to obtain fair market value for condemned assets;
- the impact of fines and penalties;
- the impact of changes in and compliance with governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- the impact of decisions of governmental and regulatory bodies, including decisions to raise or lower rates;
- the development of new services and technologies by us or our competitors;
- the availability of qualified personnel;
- the condition of our assets;
- the impact of legal proceedings;
- general economic conditions;
- acquisition-related costs and synergies;

- the sale of water and wastewater divisions; and
- the amount of income tax deductions for qualifying utility asset improvements and the Internal Revenue Service's ultimate acceptance of the deduction methodology.

Because forward-looking statements involve risks and uncertainties, there are important factors that could cause actual results to differ materially from those expressed or implied by these forward-looking statements, including but not limited to:

- changes in general economic, business, credit and financial market conditions;
- changes in governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- the profitability of future acquisitions;
- changes to the rules or our assumptions underlying our determination of what qualifies for an income tax deduction for qualifying utility asset improvements;
- the decisions of governmental and regulatory bodies, including decisions on rate increase requests;
- our ability to file rate cases on a timely basis to minimize regulatory lag;
- abnormal weather conditions, including those that result in water use restrictions;
- changes in, or unanticipated, capital requirements;
- changes in our credit rating or the market price of our common stock;
- changes in valuation of strategic ventures;
- our ability to integrate businesses, technologies or services which we may acquire;
- our ability to manage the expansion of our business;
- our ability to treat and supply water or collect and treat wastewater;
- the extent to which we are able to develop and market new and improved services;
- the effect of the loss of major customers;
- our ability to retain the services of key personnel and to hire qualified personnel as we expand;
- labor disputes;
- increasing difficulties in obtaining insurance and increased cost of insurance;
- cost overruns relating to improvements to, or the expansion of, our operations;
- increases in the costs of goods and services;

- civil disturbance or terroristic threats or acts;
- the continuous and reliable operation of our information technology systems, including the impact of cyber security attacks or other cyber-related events;
- changes in accounting pronouncements;
- litigation and claims; and
- changes in environmental conditions, including the effects of climate change.

Given these risks and uncertainties, you should not place undue reliance on any forward-looking statements. You should read this prospectus and the documents that we incorporate by reference into this prospectus completely and with the understanding that our actual future results, performance and achievements may be materially different from what we expect. These forward-looking statements represent assumptions, expectations, plans and beliefs only as of the date of this prospectus. Except for our ongoing obligations to disclose certain information under the federal securities laws, we are not obligated, and assume no obligation, to update these forward-looking statements, even though our situation may change in the future. For further information or other factors which could affect our financial results and such forward-looking statements, see “Risk Factors.” We qualify all of our forward-looking statements by these cautionary statements.

AQUA AMERICA, INC.

Aqua America, Inc. is the holding company for regulated utilities providing water or wastewater services to an estimated three million people in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana, and Virginia. Our largest operating subsidiary is Aqua Pennsylvania, Inc., which accounted for approximately 52% of our operating revenues and approximately 74% of our net income for 2017. As of December 31, 2017, Aqua Pennsylvania provided water or wastewater services to approximately one-half of the total number of people we serve. Aqua Pennsylvania's service territory is located in the suburban areas in counties north and west of the City of Philadelphia and in 27 other counties in Pennsylvania. Our other regulated utility subsidiaries provide similar services in seven other states. In addition, the Company's market-based activities are conducted through Aqua Infrastructure, LLC and Aqua Resources Inc. Aqua Infrastructure provides non- utility raw water supply services for firms in the natural gas drilling industry. Aqua Resources provides water and wastewater service through two operating and maintenance contracts with municipal authorities close to our utility companies' service territory; and offers, through a third party, water and wastewater line repair service and protection solutions to households. In 2017, we completed the sale of business units that are reported within Aqua Resources, which installed and tested devices that prevent the contamination of potable water and repaired water and wastewater systems, and repaired and performed maintenance on water and wastewater systems. Additionally, during 2016, we completed the sale of business units within Aqua Resources, which provided liquid waste hauling and disposal services and inspection, and cleaning and repair of storm and sanitary wastewater lines.

Aqua America, which prior to its name change in 2004 was known as Philadelphia Suburban Corporation, was formed in 1968 as a holding company for its primary subsidiary, Aqua Pennsylvania, formerly known as Philadelphia Suburban Water Company. In the early 1990s, we embarked on a growth through acquisition strategy focused on water and wastewater operations. Our most significant transactions to date have been the merger with Consumers Water Company in 1999, the acquisition of the regulated water and wastewater operations of AquaSource, Inc. in 2003, the acquisition of Heater Utilities, Inc. in 2004, and the acquisition of American Water Works Company, Inc.'s regulated water and wastewater operations in Ohio in 2012. Since the early 1990s, our business strategy has been primarily directed toward the regulated water and wastewater utility industry, where we have more than quadrupled the number of regulated customers we serve, and have extended our regulated operations from southeastern Pennsylvania to include our current regulated utility operations throughout Pennsylvania and in seven other states. During 2010 through 2013, we sold our utility operations in six states, pursuant to a portfolio rationalization strategy to focus our operations in areas where we have critical mass and economic growth potential. Currently, the Company seeks to acquire businesses in the U.S. regulated sector, which includes water and wastewater utilities and other regulated utilities, and to pursue growth ventures in market-based activities, such as infrastructure opportunities that are supplementary and complementary to our regulated businesses.

Our growth in revenues over the past five years is primarily a result of increases in water and wastewater rates and customer growth. The increase in our utility customer base has been due to customers added through acquisitions, partnerships with developers, and organic growth (excluding dispositions) as shown below:

Year	Utility Customer Growth Rate
2017	1.1%
2016	1.6%
2015	1.9%
2014	1.3%
2013	1.3%

In 2017, our customer count increased by 10,584 customers, primarily due to utility systems that we acquired and organic growth. Overall, for the five-year period of 2013 through 2017, our utility customer base, adjusted to exclude customers associated with utility system dispositions, increased at an annual compound rate of 1.4%. During the five-year period ended December 31, 2017, our utility customer base including customers associated with utility system acquisitions and dispositions increased from 968,357 at January 1, 2013 to 982,849 at December 31, 2017. This five-year period includes the impact of the condemnation of our Fort Wayne, IN system in 2014, which resulted in the loss of approximately 13,000 connections.

Our principal executive office is located at 762 W. Lancaster Avenue, Bryn Mawr, Pennsylvania 19010- 3489, and our telephone number is 610-527-8000. Our website may be accessed at www.aquaamerica.com. The references to our website and the SEC's website are intended to be inactive textual references only, and the contents of those websites are not incorporated by reference herein and should not be considered part of this prospectus.

RISK FACTORS

Investing in our securities involves risks. Please see the risk factors described under the section captioned "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2017, as such risk factors may be updated from time to time in filings we make with the SEC subsequent to the date hereof. Before making an investment decision, you should carefully consider these risk factors, together with all other information contained in or incorporated by reference into this prospectus or any applicable prospectus supplement (which includes information contained in certain filings we make with the SEC subsequent to the date hereof as set forth in the section below captioned "Where You Can Find More Information"). Please also refer to the section above captioned "Forward-Looking Statements."

USE OF PROCEEDS

Unless we otherwise specify in the applicable prospectus supplement, we intend to use the net proceeds from the sale of the securities we may offer by this prospectus to fund our capital expenditures, to provide capital for our growth strategy, which includes potential future acquisitions of municipally owned and investor- owned water and wastewater systems, regulated utilities and infrastructure projects, and market-based activities complementary to our regulated business, to fund the integration of any businesses that we acquire into our existing business, and to purchase and maintain plant equipment, as well as for working capital and other general corporate purposes. Our management will have broad discretion in the allocation of net proceeds from the sale of any securities sold by us.

CERTAIN RATIOS

Our ratio of earnings to fixed charges and ratio of earnings to combined fixed charges and preferred stock dividends for the periods indicated below were as follows:

	Year Ended December 31,				
	2017	**2016**	**2015**	**2014**	**2013**
Ratio of earnings to fixed charges	3.90	4.17	4.15	4.05	3.79
Ratio of earnings to combined fixed charges and preferred stock dividends	3.90	4.17	4.15	4.05	3.79

The ratios of earnings to fixed charges and the ratios of earnings to combined fixed charges and preferred stock dividends were computed by dividing our earnings by fixed charges and by combined fixed charges and preferred stock dividends, respectively. For the purpose of these computations, earnings include the sum of income from continuing operations before income taxes and non-controlling interest, and fixed charges, less

capitalized interest. Fixed charges consist of interest on all indebtedness, whether expensed or capitalized, amortization of debt expense, and the estimated interest attributable to rental and lease expense calculated using an assumed interest factor of 33% of rental and lease expense.

DESCRIPTION OF CAPITAL STOCK

As of February 13, 2018 our authorized capital stock was 301,770,819 shares, consisting of:

- 300,000,000 shares of common stock, par value $0.50 per share, of which 177,750,505 shares were outstanding; and
- 1,770,819 shares of preferred stock, par value $1.00 per share, of which no shares were outstanding.

The following summary of certain terms of our common stock and preferred stock is qualified in its entirety by the provisions of our articles of incorporation and bylaws each of which is incorporated by reference as an exhibit to the registration statement of which this prospectus constitutes a part.

Common Stock

This section describes the general terms of our common stock. For more detailed information, you should refer to our articles of incorporation and bylaws, including any amendments thereto, copies of which have been filed with the SEC. These documents are incorporated by reference into this prospectus.

Voting Rights

Holders of our common stock are entitled to one vote for each share held by them at all meetings of the shareholders and are not entitled to cumulate their votes for the election of directors.

Dividend Rights and Limitations

Holders of our common stock may receive dividends when declared by our board of directors. Because we are a holding company, the funds we use to pay any dividends on our common stock are derived predominantly from the dividends that we receive from our subsidiaries and the dividends they receive from their subsidiaries. Therefore, our ability to pay dividends to holders of our common stock depends upon our subsidiaries' earnings, financial condition and ability to pay dividends. Most of our subsidiaries are subject to regulation by state utility commissions and the amounts of their earnings and dividends are affected by the manner in which they are regulated. In addition, they are subject to restrictions on the payment of dividends contained in their various debt agreements. Under our most restrictive debt agreements, the amount available for payment of dividends to us as of December 31, 2017 was approximately $1.4 billion of Aqua Pennsylvania's retained earnings and $143 million of the retained earnings of certain other subsidiaries. Payment of dividends on our common stock is also subject to the preferential rights of the holders of any outstanding preferred stock.

Liquidation Rights

In the event that we liquidate, dissolve or wind-up, the holders of our common stock are entitled to share ratably in all of the assets that remain after we pay our liabilities. This right is subject, however, to the prior distribution rights of any outstanding preferred stock.

Preferred Stock

Our board of directors has the authority, from time to time and without further action by our shareholders, to divide our unissued capital stock into one or more classes and one or more series within any class and to

make determinations of the designation and number of shares of any class or series and determinations of the voting rights, preferences, limitations and special rights, if any, of the shares of any class or series. The rights, preferences, limitations and special rights of different classes of capital stock may differ with respect to dividend rates, amounts payable on liquidation, voting rights, conversion rights, redemption provisions, sinking fund provisions and other matters. The rights, preferences, privileges and restrictions of each series may be fixed by the designations of that series set forth in either a restated version of our articles of incorporation or a certificate of designations relating to that series, which will be filed with the SEC as an exhibit to or incorporated by reference in the registration statement of which this prospectus constitutes a part.

The issuance of preferred stock may be perceived by some as possibly having the effect of delaying, deferring or preventing a change of control of us without further action by our shareholders. The issuance of preferred stock with voting and conversion rights may also adversely affect the voting power of the holders of our common stock. In certain circumstances, an issuance of preferred stock could possibly have the effect of decreasing the market price of our common stock.

Whenever preferred stock is to be sold pursuant to this prospectus, we will file a prospectus supplement relating to that sale which will specify:

- the number of shares in the series of preferred stock;
- the designation for the series of preferred stock by number, letter or title that will distinguish the series from any other series of preferred stock;
- the dividend rate, if any, and whether dividends on that series of preferred stock will be cumulative, noncumulative or partially cumulative;
- the voting rights of that series of preferred stock, if any;
- any conversion provisions applicable to that series of preferred stock;
- any redemption or sinking fund provisions applicable to that series of preferred stock;
- any preemptive rights provisions applicable to that series of preferred stock;
- the liquidation preference per share of that series of preferred stock; and
- the terms of any other preferences or rights, if any, applicable to that series of preferred stock.

Anti-Takeover Provisions

Pennsylvania State Law Provisions

Under Section 1712 of the Pennsylvania Business Corporation Law of 1988, as amended (PBCL), which is applicable to us, directors stand in a fiduciary relation to their corporation and, as such, are required to perform their duties in good faith, in a manner they reasonably believe to be in the best interests of the corporation and with such care, including reasonable inquiry, skill and diligence, as a person of ordinary prudence would use under similar circumstances. Under Section 1715 of the PBCL, in discharging their duties, directors may, in considering the best interests of their corporation, consider various constituencies, including, shareholders, employees, suppliers, customers and creditors of the corporation, and upon communities in which offices or other establishments of the corporation are located. Directors are not required to give prominent consideration to the interests of any particular constituency. Absent a breach of fiduciary duty, a lack of good faith or self-dealing, any act of the board of directors,

a committee thereof or an individual director is presumed to be in the best interests of the corporation. Actions by directors relating to an acquisition or potential acquisition of control of the corporation are not subject to any greater obligation to justify, or higher burden of proof, than is applied to any other acts of directors. The PBCL expressly provides that the fiduciary duty of directors does not require them to (i) redeem or otherwise render inapplicable outstanding rights issued under any shareholder rights plan; (ii) render inapplicable the anti-takeover statutes set forth in Chapter 25 of the PBCL (described below); or (iii) take any action solely because of the effect it may have on a proposed acquisition or the consideration to be received by shareholders in such a transaction. In addition, Section 2513 of the PBCL specifically validates shareholder rights plans, or "poison pills," and the discriminatory dilution provisions contained in such plans.

Chapter 25 of the PBCL contains several anti-takeover statutes applicable to publicly-traded corporations. Corporations may opt-out of such anti-takeover statutes under certain circumstances. We have not opted-out of any of such statutes.

Section 2538 of Subchapter 25D of the PBCL requires certain transactions with an "interested shareholder" to be approved by a majority of disinterested shareholders. "Interested shareholder" is defined broadly to include any shareholder who is a party to the transaction or who is treated differently than other shareholders and affiliates of the interested shareholder.

Subchapter 25E of the PBCL requires a person or group of persons acting in concert which acquires 20% or more of the voting shares of the corporation to offer to purchase the shares of any other shareholder at "fair value." "Fair value" means the value not less than the highest price paid per share by the controlling person or group during the 90-day period prior to the control transaction, plus a control premium. Among other exceptions, Subchapter 25E does not apply to shares acquired directly from the corporation in a transaction exempt from the registration requirements of the Securities Act of 1933, or to a one-step merger.

Subchapter 25F of the PBCL generally establishes a 5-year moratorium on a "business combination" with an "interested shareholder." "Interested shareholder" is defined generally to be any beneficial owner of 20% or more of the corporation's voting stock or an affiliate or associate of the corporation that at any time within the prior five-year period was a beneficial owner of 20% or more of the corporation's voting stock. "Business combination" is defined broadly to include mergers, consolidations, asset sales and certain self-dealing transactions. Certain restrictions apply to business combination following the 5-year period. Among other exceptions, Subchapter 25F will be rendered inapplicable if the board of directors approves the proposed business combination, or approves the interested shareholder's acquisition of 20% of the voting shares, in either case prior to the date on which the shareholder first becomes an interested shareholder.

Subchapter 25G of the PBCL provides that "control shares" lose voting rights unless such rights are restored by the affirmative vote of a majority of (i) the disinterested shares (generally, shares held by persons other than the acquiror, executive officers of the corporation and certain employee stock plans) and (ii) the outstanding voting shares of the corporation. "Control shares" are defined as shares which, upon acquisition, will result in a person or group acquiring for the first time voting control over (a) 20%, (b) 33 1/3% or (c) 50% or more of the outstanding shares, together with shares acquired within 180 days of attaining the applicable threshold and shares purchased with the intention of attaining such threshold. A corporation may redeem control shares if the acquiring person does not request restoration of voting rights as permitted by Subchapter 25G. Among other exceptions, Subchapter 25G does not apply to a merger, consolidation or a share exchange if the corporation is a party to the transaction agreement.

Subchapter 25H of the PBCL provides in certain circumstances for the recovery by the corporation of profits realized from the sale of its stock by a controlling person or group if the sale occurs within 18 months after the controlling person or group became a controlling person or group, and the stock was acquired during such month period or within 24 months before such period. A controlling person or group is a person or group that

has acquired, offered to acquire, or publicly disclosed an intention to acquire 20% or more of the voting shares of the corporation or a person or group that has otherwise publicly disclosed or caused to be disclosed that it may seek to acquire control of the corporation through any means. Among other exceptions, Subchapter 25H does not apply to transactions approved by both the board of directors and the shareholders prior to the acquisition or distribution, as appropriate.

Subchapter 25I of the PBCL mandates severance compensation for eligible employees who are terminated within 24 months after the approval of a control-share acquisition. Eligible employees generally are all employees employed in Pennsylvania for at least two years prior to the control-share approval. Severance equals the weekly compensation of the employee multiplied by the employee's years of service (up to 26 years), less payments made due to the termination.

Subchapter 25J of the PBCL requires the continuation of certain labor contracts relating to business operations owned at the time of a control-share approval.

Articles of Incorporation and Bylaw Provisions

Certain provisions of our articles of incorporation and bylaws may have the effect of discouraging unilateral tender offers or other attempts to take over and acquire our business. These provisions might discourage some potentially interested purchaser from attempting a unilateral takeover bid for us on terms which some shareholders might favor. Our articles of incorporation require that certain fundamental transactions must be approved by the holders of 75% of the outstanding shares of our capital stock entitled to vote on the matter unless at least a majority of the members of the board of directors has approved the transaction, in which case the required shareholder approval will be the minimum approval required by applicable law. The fundamental transactions that are subject to this provision are those transactions that require approval by shareholders under applicable law or the articles of incorporation. These transactions include certain amendments of our articles of incorporation or bylaws, certain sales or other dispositions of our assets, certain issuances of our capital stock, or certain transactions involving our merger, consolidation, division, reorganization, dissolution, liquidation or winding up. Our articles of incorporation and bylaws provide that:

- a special meeting of shareholders may only be called by the chairman, the president, the board of directors or shareholders entitled to cast a majority of the votes which all shareholders are entitled to cast at the particular meeting;
- nominations for election of directors may be made by any shareholder entitled to vote for election of directors if the name of the nominee and certain information relating to the nominee is filed with our corporate secretary not less than 14 days nor more than 50 days before any meeting of shareholders to elect directors; and
- certain advance notice procedures must be met for shareholder proposals to be made at annual meetings of shareholders. These advance notice procedures generally require a notice to be delivered not less than 90 days nor more than 120 days before the anniversary date of the immediately preceding annual meeting of shareholders.

Transfer Agent and Registrar

The transfer agent and registrar for our common stock is Computershare Trust Company, N.A.

DESCRIPTION OF COMMON STOCK PURCHASE CONTRACTS

We may issue stock purchase contracts, representing contracts entitling or obligating holders to purchase from us, and us to sell to the holders, a specified number of shares or amount of common stock at a future date or dates. The price per share of common stock may be fixed at the time each contract is issued or may be determined by reference to a specific formula set forth in the contract. Each common stock purchase contract may be issued separately or as a part of a unit, each consisting of a common stock purchase contract and, as security for the holder's obligation to purchase the common stock under the contract, the following:

- our senior debt securities or subordinated debt securities described under "Description of Debt Securities;"
- debt obligations of third parties, including U.S. Treasury securities;
- any other asset as security described in the applicable prospectus supplement; or
- any combination of the foregoing.

Each common stock purchase contract may require us to make periodic payments to the holder of the unit or vice versa, and such payments may be unsecured or prefunded on some basis discussed in the applicable prospectus supplement. Each common stock purchase contract may require holders to secure their obligations thereunder in a specified manner and, in certain circumstances, we may deliver a newly issued prepaid common stock purchase contract, which is referred to as a "prepaid security," upon release to a holder of any collateral securing such holder's obligations under the original contract.

The applicable prospectus supplement will describe the terms of any common stock purchase contract and, if applicable, prepaid security. The description in the prospectus supplement will not purport to be complete
and will be qualified in its entirety by reference to the contracts, the collateral arrangements and depositary arrangements, if applicable, relating to such contracts and, if applicable, the prepaid securities and the documents pursuant to which such prepaid securities will be issued. The applicable prospectus supplement will also describe the material United States federal income tax considerations applicable to the common stock purchase contracts.

DESCRIPTION OF WARRANTS

General

The following summary of certain provisions of the warrants does not purport to be complete and is subject to, and qualified in its entirety by reference to, the provisions of the warrant agreement that will be filed with the SEC in connection with the offering of such warrants.

We may issue warrants for the purchase of debt securities, preferred stock or common stock. Warrants may be issued independently or together with debt securities, preferred stock or common stock offered by any prospectus supplement and may be attached to or separate from any such offered securities. Each series of warrants will be issued under a separate warrant agreement to be entered into between the Company and a bank or trust company, as warrant agent. The warrant agent will act solely as the Company's agent in connection with the warrants and will not assume any obligation or relationship of agency or trust for or with any holders or beneficial owners of warrants.

Debt Warrants

The prospectus supplement relating to a particular issue of debt warrants will describe the terms of such debt warrants, including the following: (a) the title of such debt warrants; (b) the offering price for such debt warrants, if any; (c) the aggregate number of such debt warrants; (d) the designation and terms of the debt securities purchasable upon exercise of such debt warrants; (e) if applicable, the designation and terms of the debt securities with which such debt warrants are issued and the number of such debt warrants issued with each such debt security; (f) if applicable, the date from and after which such debt warrants and any debt securities issued therewith will be separately transferable; (g) the principal amount of debt securities purchasable upon exercise of a debt warrant and the price at which such principal amount of debt securities may be purchased upon exercise (which price may be payable in cash, securities, or other property); (h) the date on which the right to exercise such debt warrants shall commence and the date on which such right shall expire; (i) if applicable, the minimum or maximum amount of such debt warrants that may be exercised at any one time; (j) whether the debt warrants represented by the debt warrant certificates or debt securities that may be issued upon exercise of the debt warrants will be issued in registered or bearer form; (k) information with respect to book-entry procedures, if any; (1) the currency or currency units in which the offering price, if any, and the exercise price are payable; (m) if applicable, a discussion of material United States federal income tax considerations; (n) the anti-dilution provisions of such debt warrants, if any; (o) the redemption or call provisions, if any, applicable to such debt warrants; (p) any provisions for changes to or adjustments in the exercise price for the debt warrants and (q) any additional terms of such debt warrants, including terms, procedures, and limitations relating to the exchange and exercise of such debt warrants.

Stock Warrants

The prospectus supplement relating to any particular issue of preferred stock warrants or common stock warrants will describe the terms of such warrants, including the following: (a) the title of such warrants; (b) the offering price for such warrants, if any; (c) the aggregate number of such warrants; (d) the designation and terms of the common stock or preferred stock purchasable upon exercise of such warrants; (e) if applicable, the designation and terms of the offered securities with which such warrants are issued and the number of such warrants issued with each such offered security; (f) if applicable, the date from and after which such warrants and any offered securities issued therewith will be separately transferable; (g) the number of shares of common stock or preferred stock purchasable upon exercise of a warrant and the price at which such shares may be purchased upon exercise; (h) the date on which the right to exercise such warrants shall commence and the date on which such right shall expire; (i) if applicable, the minimum or maximum amount of such warrants that may be exercised at any one time; (j) the currency or currency units in which the offering price, if any, and the exercise price are payable, (k) if applicable, a discussion of material United States federal income tax considerations; (l) the anti-dilution provisions of such warrants, if any; (m) the redemption or call provisions, if any, applicable to such warrants; (m) any provisions for changes to or adjustments in the exercise price for the stock warrants and any additional terms of such warrants, including terms, procedures and limitations relating to the exchange and exercise of such warrants.

DESCRIPTION OF UNITS

We may, from time to time, issue units comprised of one or more of the other securities that may be offered under this prospectus, in any combination. Each unit will be issued so that the holder of the unit is also the holder of each security included in the unit. Thus, the holder of a unit will have the rights and obligations of a holder of each included security. The unit agreement under which a unit is issued may provide that the securities included in the unit may not be held or transferred separately at any time, or at any time before a specified date.

The applicable prospectus supplement will describe the terms of any unit. The description in the prospectus supplement will not purport to be complete and will be qualified in its entirety by reference to units, the collateral arrangements and depositary arrangements, if applicable, relating to such units and, if applicable, the prepaid securities and the documents pursuant to which such prepaid securities will be issued. The applicable prospectus supplement will also describe the material United States federal income tax considerations applicable to the units.

DESCRIPTION OF DEPOSITORY SHARES

We may, at our option, offer fractional shares of our preferred stock, rather than whole shares of our preferred stock. In the event we do so, we will issue receipts for depositary shares, each of which will represent a fraction (to be set forth in the prospectus supplement relating to offering of the depositary shares) of a share of the related series of preferred stock.

The shares of our preferred stock represented by depositary shares will be deposited under a deposit agreement between us and a bank or trust company selected by us having its principal office in the United States and that meets certain other requirements. Subject to the terms of the deposit agreement, each owner of a depositary share will be entitled, in proportion to the applicable fraction of a share of preferred stock, represented by the depositary share to all of the rights and preferences of the preferred stock represented by the depositary shares (including dividend, voting, redemption, conversion and liquidation rights).

The above description of depositary shares is only a summary, is not complete and is subject to, and is qualified in its entirety by the description in the applicable prospectus supplement and the provisions of the deposit agreement, which will contain the form of depository receipt. A copy of the deposit agreement will be filed with the SEC as an exhibit to or incorporated by reference in the registration statement of which this prospectus is a part.

DESCRIPTION OF DEBT SECURITIES

Please note that in this section entitled “Description of Debt Securities,” references to “we,” “us,” “ours” or “our” refer only to Aqua America, Inc. and not to its consolidated subsidiaries. Also, in this section, references to “holders” mean those who own debt securities registered in their own names, on the books that we maintain or the trustee maintains for this purpose, and not those who own beneficial interests in debt securities registered in street name or in debt securities issued in book-entry form through one or more depositaries. Owners of beneficial interests in the debt securities should read the section below entitled “Book-Entry Procedures and Settlement.”

General

The debt securities offered by this prospectus will be our unsecured obligations, except as otherwise set forth in an accompanying prospectus supplement, and will be either senior or subordinated debt. We will issue senior debt under a senior debt indenture, and we will issue subordinated debt under a subordinated debt indenture. We sometimes refer to the senior debt indenture and the subordinated debt indenture, individually, as an indenture and, collectively, as the indentures. We have filed forms of the indentures with the SEC as exhibits to the registration statement of which this prospectus forms a part.You can obtain copies of the indentures by following the directions outlined in “Where You Can Find More Information,” or by contacting the applicable indenture trustee.

A form of each debt security, reflecting the particular terms and provisions of a series of offered debt securities, will be filed with the SEC at the time of the offering and incorporated by reference as exhibits to the registration statement of which this prospectus forms a part.

The following briefly summarizes certain material provisions that may be included in the indentures. Other terms, including pricing and related terms, will be disclosed for a particular issuance in an accompanying prospectus supplement. You should read the more detailed provisions of the applicable indenture, including the defined terms, for provisions that may be important to you. You should also read the particular terms of a series of debt securities, which will be described in more detail in an accompanying prospectus supplement. So that you may easily locate the more detailed provisions, the numbers in parentheses below refer to sections in the applicable indenture or, if no indenture is specified, to sections in each of the indentures. Wherever particular sections or defined terms of the applicable indenture are referred to, such sections or defined terms are incorporated into this prospectus by reference, and the statement in this prospectus is qualified by that reference.

The trustee under each indenture will be determined at the time of issuance of debt securities, and the name of the trustee will be provided in an accompanying prospectus supplement.

The indentures provide that our senior or subordinated debt securities may be issued in one or more series, with different terms, in each case as we authorize from time to time. We also have the right to "reopen" a previous issue of a series of debt securities by issuing additional debt securities of such series without the consent of the holders of debt securities of the series being reopened or any other series. Any additional debt securities of the series being reopened will have the same ranking, interest rate, maturity and other terms as the previously issued debt securities of that series. These additional debt securities, together with the previously issued debt securities of that series, will constitute a single series of debt securities under the terms of the applicable indenture.

Types of Debt Securities

We may issue fixed or floating rate debt securities. Fixed rate debt securities will bear interest at a fixed rate described in the prospectus supplement. This type includes zero coupon debt securities, which bear no interest and are often issued at a price lower than the principal amount. United States federal income tax consequences and other special considerations applicable to any debt securities issued at a discount will be described in the applicable prospectus supplement.

Upon the request of the holder of any floating rate debt security, the calculation agent will provide the interest rate then in effect for that debt security, and, if determined, the interest rate that will become effective on the next interest reset date. The calculation agent's determination of any interest rate, and its calculation of the amount of interest for any interest period, will be final and binding in the absence of manifest error.

All percentages resulting from any interest rate calculation relating to a debt security will be rounded upward or downward, as appropriate, to the next higher or lower one hundred-thousandth of a percentage point.

All amounts used in or resulting from any calculation relating to a debt security will be rounded upward or downward, as appropriate, to the nearest cent, in the case of U.S. dollars, or to the nearest corresponding hundredth of a unit, in the case of a currency other than U.S. dollars, with one-half cent or one-half of a corresponding hundredth of a unit or more being rounded upward.

In determining the base rate that applies to a floating rate debt security during a particular interest period, the calculation agent may obtain rate quotes from various banks or dealers active in the relevant market, as described in the prospectus supplement. Those reference banks and dealers may include the calculation agent itself and its affiliates, as well as any underwriter, dealer or agent participating in the distribution of the relevant floating rate debt securities and its affiliates.

Information in the Prospectus Supplement

The prospectus supplement for any offered series of debt securities will describe the following terms, as applicable:

- the title;
- whether the debt is senior or subordinated;
- whether the debt securities are secured or unsecured and, if secured, the collateral securing the debt;
- the total principal amount offered;
- the percentage of the principal amount at which the debt securities will be sold and, if applicable, the method of determining the price;
- the maturity date or dates;
- whether the debt securities are fixed rate debt securities or floating rate debt securities;
- if the debt securities are fixed rate debt securities, the yearly rate at which the debt security will bear interest, if any, and the interest payment dates;
- if the debt security is an original issue discount debtsecurity, the yield to maturity;
- if the debt securities are floating rate debt securities, the interest rate basis; any applicable index currency or maturity, spread or spread multiplier or initial, maximum or minimum rate; the interest reset, determination, calculation and payment dates, and the day count used to calculate interest payments for any period;
- the date or dates from which any interest will accrue, or how such date or dates will be determined, and the interest payment dates and any related record dates;
- if other than in U.S. dollars, the currency or currency unit in which payment will be made;
- the denominations in which the currency or currency unit of the securities will be issuable if other than denominations of $1,000 and integral multiples thereof;
- the terms and conditions on which the debt securities may be redeemed at our option;
- any obligation we may have to redeem, purchase or repay the debt securities at the option of a holder upon the happening of any event and the terms and conditions of redemption, purchase or repayment;
- the names and duties of the trustee and any co-trustees, depositaries, authenticating agents, calculation agents, paying agents, transfer agents or registrars for the debt securities;
- any material provisions of the applicable indenture described in this prospectus that do not apply tothe debt securities;
- a discussion of United States federal income tax, accounting and special considerations, procedures and limitations with respect to the debt securities;

- whether and under what circumstances we will pay additional amounts to holders in respect of any tax assessment or government charge, and, if so, whether we will have the option to redeem the debt securities rather than pay such additional amounts; and

- any other specific terms of the debt securities that are consistent with the provisions of the indenture.

The terms on which a series of debt securities may be convertible into or exchangeable for other of our securities or any other entity will be set forth in the prospectus supplement relating to such series. Such terms will include provisions as to whether conversion or exchange is mandatory, at the option of the holder or at our option. The terms may include provisions pursuant to which the number of other securities to be received by the holders of such series of debt securities may be adjusted.

We will issue the debt securities only in registered form. As currently anticipated, debt securities of a series will trade in book-entry form, and global notes will be issued in physical (paper) form, as described below under "Book-Entry Procedures and Settlement." Unless otherwise provided in the accompanying prospectus supplement, we will issue debt securities denominated in U.S. dollars and only in denominations of $1,000 and integral multiples thereof.

The prospectus supplement relating to offered debt securities denominated in a foreign or composite currency will specify the denomination of the offered debt securities.

The debt securities may be presented for exchange, and debt securities other than a global security may be presented for registration of transfer, at the principal corporate trust office of the trustee named in the applicable prospectus supplement. Holders will not have to pay any service charge for any registration of transfer or exchange of debt securities, but we may require payment of a sum sufficient to cover any tax or other governmental charge payable in connection with such registration of transfer (Section 3.05).

Payment and Paying Agents

Distributions on the debt securities other than those represented by global notes will be made in the designated currency against surrender of the debt securities at the principal corporate trust office of the trustee named in the applicable prospectus supplement. Payment will be made to the registered holder at the close of business on the record date for such payment. Interest payments will be made at the principal corporate trust office of the trustee named in the applicable prospectus supplement, or by a check mailed to the holder at his registered address. Payments in any other manner will be specified in the applicable prospectus supplement.

Calculation Agents

Calculations relating to floating rate debt securities and indexed debt securities will be made by the calculation agent, an institution that we appoint as our agent for this purpose. We may appoint one of our affiliates as calculation agent.We may appoint a different institution to serve as calculation agent from time to time after the original issue date of the debt security without your consent and without notifying you of the change. The initial calculation agent will be identified in the applicable prospectus supplement.

Senior Debt

We may issue senior debt securities under the senior debt indenture. Senior debt will constitute our unsecured and unsubordinated obligations and will rank on a basis equal in priority with all our other unsecured and unsubordinated debt.

Subordinated Debt

We may issue subordinated debt securities under the subordinated debt indenture. Subordinated debt will constitute our unsecured and subordinated obligations and will be junior in right of payment to our senior debt (including senior debt securities), which is defined as "senior indebtedness" in the subordinated debt indenture (Section 16.01).

If we default in the payment of any principal of, or premium, ifany, or interest on any senior debt when it becomes due and payable after any applicable grace period, then, unless and until the default is cured or waived or ceases to exist, we cannot make a payment on account of or redeem or otherwise acquire the subordinated debt securities (Section 16.04).

If there is any insolvency, bankruptcy, liquidation or other similar proceeding relating to us or our property, then all senior debt must be paid in full before any payment may be made to any holders of subordinated debt securities (Section 16.02).

Furthermore, if we default in the payment of the principal of and accrued interest on any subordinated debt securities that is declared due and payable upon an event of default under the subordinated debt indenture, holders of all our senior debt will first be entitled to receive payment in full in cash before holders of such subordinated debt can receive any payments (Section 16.03).

Except as may be otherwise set forth in an accompanying prospectus supplement, senior debt means:

- the principal, premium, if any, and interest in respect of indebtedness for money borrowed and indebtedness evidenced by securities, notes, debentures, bonds or other similar instruments issued, including, as to us, the senior debt securities;
- all capitalized lease obligations;
- all obligations representing the deferred purchase price of property; and
- all deferrals, renewals, extensions and refundings of obligations of the type referred to above (Section 1.01 of Subordinated Indenture).

However, senior debt does not include:

- the subordinated debt securities (Section 16.01 of Subordinated Indenture);
- any indebtedness that by its terms is subordinated to, or ranks in priority on an equal basis with, subordinated debt securities (Section 1.01 of Subordinated Indenture); and
- items of indebtedness (other than capitalized lease obligations) that would not appear as liabilities on a balance sheet prepared in accordance with accounting principles generally accepted in the United States of America.

Covenants

The accompanying prospectus supplement will contain any covenants applicable to the debt securities.

Modification of the Indentures

The indentures will provide that we and the relevant trustee may enter into supplemental indentures to establish the form and terms of any new series of debt securities without obtaining the consent of any holder of debt securities (Section 9.01).

We and the trustee may, with the consent of the holders of at least a majority in aggregate outstanding principal amount of the debt securities of a series, modify the applicable indenture or the rights of the holders of the securities of such series (Section 9.02).

No such modification may, without the consent of each holder of an affected security:

- extend the fixed maturity of any such security;
- reduce the rate or change the time of payment of interest on such security;
- reduce the principal amount of such securities or the premium, if any, on such security;
- change any obligation of ours to pay additional amounts with respect to such security;
- reduce the amount of the principal payable on acceleration of such security if issued originally at a discount;
- adversely affect the right of repayment or repurchase of such security at the option of the holder;
- reduce or postpone any sinking fund or similar provision with respect to such security;
- change the currency or currency unit in which such security is payable or the right of selection thereof;
- impair the right to sue for the enforcement of any payment with respect to such security on or after the maturity of such security;
- reduce the percentage of the aggregate outstanding principal amount of debt securities of the series referred to above whose holders need to consent to the modification or a waiver without the consent of such holders; or
- change any obligation of ours with respect to such security to maintain an office or agency.

Defaults

Except as may be otherwise set forth in an accompanying prospectus supplement, each indenture will provide that events of default regarding any series of debt securities will be:

- our failure to pay for 30 days required interest on any debt security of such series;
- our failure to pay principal or premium, if any, on any debt security of such series when due;
- our failure to make any required scheduled installment payment for 30 days on debt securities of such series;

- our failure to perform for 90 days after notice any other covenant in the relevant indenture otherthan a covenant included in the relevant indenture solely for the benefit of a series of debt securities other than such series; and

- certain events of bankruptcy or insolvency, whether voluntary or not (Section 5.01).

Except as may be otherwise set forth in an accompanying prospectus supplement, if an event of default regarding debt securities of any series issued under the indentures should occur and be continuing, either the trustee or the holders of 25% in the principal amount of outstanding debt securities of such series may declare each debt security of that series due and payable (Section 5.02). We may be required to file annually with the trustee a statement of an officer as to the fulfillment by us of our obligations under the indenture during the preceding year.

No event of default regarding one series of debt securities issued under an indenture is necessarily an event of default regarding any other series of debt securities.

Holders of a majority in aggregate principal amount of the outstanding debt securities of any series will be entitled to control certain actions of the trustee under the indentures and to waive past defaults regarding such series (Sections 5.12 and 5.13). The holders of debt securities generally will not be able to require the trustee to take any action, unless one or more of such holders provides to the trustee reasonable security or indemnity (Section 6.02).

If an event of default occurs and is continuing regarding a series of debt securities, the trustee may use any sums that it holds under the relevant indenture for its own reasonable compensation and expenses incurred prior to paying the holders of debt securities of such series (Section 5.06).

Before any holder of any series of debt securities may institute action for any remedy, except payment on such holder's debt security when due, the holders of not less than 25% in principal amount of the debt securities of that series outstanding must request the trustee to take action. Holders must also offer and give the satisfactory security and indemnity against liabilities incurred by the trustee for taking such action (Section 5.07).

Defeasance

Except as may otherwise be set forth in an accompanying prospectus supplement, after we have deposited with the trustee, cash or government securities, in trust for the benefit of the holders sufficient to pay the principal of, premium, if any, and interest on the debt securities of such series when due, and satisfied certain other conditions, including receipt of an opinion of counsel that holders will not recognize taxable gain or loss for United States federal income tax purposes, then:

- we will be deemed to have paid and satisfied our obligations on all outstanding debt securities of such series, which is known as defeasance and discharge (Section 14.02); or

- we will cease to be under any obligation, other than to pay when due the principal of, premium, if any, and interest on such debt securities, relating to the debt securities of such series, which is known as covenant defeasance (Section 14.03).

When there is a defeasance and discharge, the applicable indenture will no longer govern the debt securities of such series, we will no longer be liable for payments required by the terms of the debt securities of such series and the holders of such debt securities will be entitled only to the deposited funds. When there is a covenant defeasance, however, we will continue to be obligated to make payments when due if the deposited funds are not sufficient.

Governing Law

Unless otherwise stated in the prospectus supplement, the debt securities and the indentures will be governed by Pennsylvania law (Section 1.12).

Concerning the Trustee Under the Indentures

We may have banking and other business relationships with the trustee named in the prospectus supplement, or any subsequent trustee, in the ordinary course of business.

Form, Exchange and Transfer

We will issue debt securities only in registered form; no debt securities will be issued in bearer form (Section 2.03). We will issue each debt security in book-entry form only, unless otherwise specified in the applicable prospectus supplement. We will issue any common stock issuable upon conversion of any debt security being offered in both certificated and book-entry form, unless otherwise specified in the applicable prospectus supplement. Debt securities in book-entry form will be represented by a global security registered in the name of a depositary, which will be the holder of all the debt securities represented by the global security (Section 2.04). Those who own beneficial interests in a global security will do so through participants in the depositary's system, and the rights of these indirect owners will be governed solely by the applicable procedures of the depositary and its participants. Only the depositary will be entitled to transfer or exchange a debt security in global form, since it will be the sole holder of the debt security (Section 3.05). These book-entry securities are described below under "Book-Entry Procedures and Settlement."

If any debt securities are issued in non-global form or cease to be book-entry securities (in the circumstances described in the next section), the following will apply to them:

- The debt securities will be issued in fully registered form in denominations stated in the prospectus supplement. You may exchange debt securities for debt securities of the same series in smaller denominations or combined into fewer debt securities of the same series of larger denominations, as long as the total amount is not changed (Section 3.05).

- You may exchange, transfer, present for payment or exercise debt securities at the office of the relevant trustee or agent indicated in the prospectus supplement (Section 3.05). You may also replace lost, stolen, destroyed or mutilated debt securities at that office. We may appoint another entity to perform these functions or may perform them (Section 3.06).

- You will not be required to pay a service charge to transfer or exchange the debt securities, but you may be required to pay any tax or other governmental charge associated with the transfer or exchange (Sections 3.05 and 3.06). The transfer or exchange, and any replacement, will be made only if our transfer agent is satisfied with your proof of legal ownership. The transfer agent may also require an indemnity before replacing any debt securities (Section 3.06).

- If we have the right to redeem, accelerate or settle any debt securities before their maturity or expiration, and we exercise that right as to less than all those debt securities, we may block the transfer or exchange of those debt securities during the period beginning 15 days before the day we mail the notice of exercise and ending on the day of that mailing, in order to freeze the list of holders to prepare the mailing. We may also refuse to register transfers of or exchange any debt security selected for early settlement, except that we will continue to permit transfers and exchanges of the unsettled portion of any debt security being partially settled (Section 3.05).

- If fewer than all of the debt securities represented by a certificate that are payable or exercisable in part are presented for payment or exercise, a new certificate will be issued for the remaining amount of securities (Section 15.02).

Book-Entry Procedures and Settlement

Most offered debt securities will be book-entry (global) securities. Upon issuance, all book-entry securities will be represented by one or more fully registered global securities, without coupons (Section 3.02). Each global security will be deposited with, or on behalf of, The Depository Trust Company, or DTC, a securities depository, and will be registered in the name of DTC or a nominee of DTC (Section 3.01). DTC will thus be the only registered holder of these debt securities.

Purchasers of debt securities may only hold interests in the global notes through DTC if they are participants in the DTC system. Purchasers may also hold interests through a securities intermediary—banks, brokerage houses and other institutions that maintain securities accounts for customers—that has an account with DTC or its nominee. DTC will maintain accounts showing the security holdings of its participants, and these participants will in turn maintain accounts showing the security holdings of their customers. Some of these customers may themselves be securities intermediaries holding securities for their customers. Thus, each beneficial owner of a book-entry security will hold that debt security indirectly through a hierarchy of intermediaries, with DTC at the top and the beneficial owner's own securities intermediary at the bottom.

The debt securities of each beneficial owner of a book-entry security will be evidenced solely by entries on the books of the beneficial owner's securities intermediary. The actual purchaser of the debt securities will generally not be entitled to have the debt securities represented by the global securities registered in its name and will not be considered the owner under the declaration. In most cases, a beneficial owner will also not be able to obtain a paper certificate evidencing the holder's ownership of debt securities. The book-entry system for holding securities eliminates the need for physical movement of certificates and is the system through which most publicly traded common stock is held in the United States. However, the laws of some jurisdictions require some purchasers of securities to take physical delivery of their securities in definitive form. These laws may impair the ability to transfer book-entry securities.

A beneficial owner of book-entry securities represented by a global security may exchange the securities for definitive (paper) securities only if:

- DTC is unwilling or unable to continue as depositary for such global security and we do not appoint a qualified replacement for DTC within 90 days; or

- We in our sole discretion decide to allow some or all book-entry securities to be exchangeable for definitive securities in registered form (Section 3.05).

Unless we indicate otherwise, any global security that is exchangeable will be exchangeable in whole for definitive securities in registered form, with the same terms and of an equal aggregate principal amount. Definitive securities will be registered in the name or names of the person or persons specified by DTC in a written instruction to the registrar of the securities (Section 3.05). DTC may base its written instruction upon directions that it receives from its participants.

In this prospectus, for book-entry securities, references to actions taken by security holders will mean actions taken by DTC upon instructions from its participants, and references to payments and notices of redemption to security holders will mean payments and notices of redemption to DTC as the registered holder of the securities for distribution to participants in accordance with DTC's procedures.

DTC is a limited purpose trust company organized under the laws of the State of New York, a member of the Federal Reserve System, a clearing corporation within the meaning of the New York Uniform Commercial Code and a clearing agency registered under section 17A of the Securities Exchange Act of 1934. The rules applicable to DTC and its participants are on file with the SEC.

We will not have any responsibility or liability for any aspect of the records relating to, or payments made on account of, beneficial ownership interest in the book-entry securities or for maintaining, supervising or reviewing any records relating to the beneficial ownership interests.

PLAN OF DISTRIBUTION

We may sell any of the securities being offered by this prospectus separately or together:

- through agents;
- to or through underwriters who may act directly or through a syndicate represented by one or more managing underwriters;
- through dealers;
- through a block trade in which the broker or dealer engaged to handle the block trade will attempt to sell the securities as agent, but may position and resell a portion of the block as principal to facilitate the transaction;
- through "at the market" offerings, within the meaning of Rule 415(a)(4) of the Securities Act of 1933, to or through a market maker or into an existing trading market on an exchange or otherwise;
- in exchange for our outstanding indebtedness;
- directly to purchasers, through a specific bidding, auction or other process; or
- through a combination of any of these methods of sale.

If the securities offered under this prospectus are issued in exchange for our outstanding securities, the applicable prospectus supplement will describe the terms of the exchange, and the identity and the terms of sale of the securities offered under this prospectus by the selling security holders.

The distribution of securities may be effected from time to time in one or more transactions at a fixed price or prices that may be changed, at market prices prevailing at the time of sale or prices related to prevailing market prices or at negotiated prices.

Agents designated by us from time to time may solicit offers to purchase the securities. We will name any agent involved in the offer or sale of the securities and set forth any commissions payable by us to an agent in the prospectus supplement for that transaction. Unless otherwise indicated in the prospectus supplement, any agent will be acting on a best efforts basis for the period of its appointment. Any agent may be deemed to be an "underwriter" of the securities as that term is defined in the Securities Act of 1933.

If we utilize an underwriter or underwriters in the sale of securities, we will execute an underwriting agreement with the underwriter or underwriters at the time we reach an agreement for sale. We will set forth in the prospectus supplement the names of the specific managing underwriter or underwriters, as well as any other underwriters, and the terms of the transactions, including compensation of the underwriters and dealers. This compensation may be in the form of discounts, concessions or commissions. Underwriters and others participating in any offering of securities may engage in transactions that stabilize, maintain or otherwise affect the price of securities. We will describe any of these activities in the prospectus supplement.

If a dealer is utilized in the sale of the securities, we or an underwriter will sell securities to the dealer, as principal. The dealer may then resell the securities to the public at varying prices to be determined by the dealer at the time of resale. The prospectus supplement will set forth the name of the dealer and the terms of the transactions.

We may directly solicit offers to purchase the securities, and we may sell directly to institutional investors or others. These persons may be deemed to be underwriters within the meaning of the Securities Act of 1933 with respect to any resale of the securities. The prospectus supplement will describe the terms of any direct sales, including the terms of any bidding or auction process, if utilized.

Agreements we enter into with agents, underwriters and dealers may entitle them to indemnification by us against specified liabilities, including liabilities under the Securities Act of 1933, or to contribution by us to payments they may be required to make in respect of these liabilities. The prospectus supplement will describe the terms and conditions of indemnification or contribution.

Certain of the agents, underwriters and dealers that we sell the securities offered under this prospectus to or through, and certain of their affiliates, engage in transactions with and perform services for us in the ordinary course of business. We may enter into hedging transactions in connection with any particular issue of the securities offered under this prospectus, including forwards, futures, options, interest rate or exchange rate swaps and repurchase or reverse repurchase transactions with, or arranged by, the applicable agent, underwriter or dealer, an affiliate of that agent, underwriter or dealer or an unrelated entity. We, the applicable agent, underwriter or dealer or other parties may receive compensation, trading gain or other benefits in connection with these transactions. We are not required to engage in any of these transactions. If we commence these transactions, we may discontinue them at any time. Counterparties to these hedging activities also may engage in market transactions involving the securities offered under this prospectus.

No securities may be sold under this prospectus without delivery (in paper format, in electronic format, in electronic format on the Internet, or by other means) of the applicable prospectus supplement describing the method and terms of the offering.

LEGAL MATTERS

Unless otherwise indicated in the applicable prospectus supplement, the validity of the securities that may be offered hereby will be passed upon for us by Ballard Spahr LLP, Philadelphia, Pennsylvania. If legal matters in connection with the offering made by this prospectus are passed on by counsel for the underwriters, dealers or agents, if any, that counsel will be named in the applicable prospectus supplement.

EXPERTS

The financial statements and management's assessment of the effectiveness of internal control over financial reporting (which is included in Management's Report on Internal Control over Financial Reporting) incorporated in this Prospectus by reference to the Annual Report on Form 10-K for the year ended December 31, 2017, have been so incorporated in reliance on the report of PricewaterhouseCoopers LLP, an independent registered public accounting firm, given on the authority of said firm as experts in auditing and accounting.

WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the SEC. You may read and copy any document we file at the SEC's Public Reference Room at 100 F Street N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the Public Reference Room. You may also obtain our SEC filings from the SEC's website at www.sec.gov or from our website at http:// ir.aquaamerica.com/.

We have filed with the SEC a "shelf" registration statement on Form S-3 under the Securities Act of 1933 relating to the securities that may be offered by this prospectus. This prospectus is a part of that registration statement, but does not contain all of the information in the registration statement. We have omitted certain parts of the registration statement in accordance with rules and regulations of the SEC. Statements made in this prospectus as to the contents of any contract, agreement or other documents are not necessarily complete, and, in each instance, we refer you to a copy of such document filed as an exhibit to the registration statement, of which this prospectus is a part, or otherwise filed with the SEC. For more detail about us and any securities that may be offered by this prospectus, you may examine the registration statement on Form S-3 and the exhibits filed with it at the locations listed in the previous paragraph.

The SEC allows us to "incorporate by reference" the information we file with them, which means that we can disclose important information to you by referring you to those documents. The information incorporated by reference is considered to be part of this prospectus. When we file information with the SEC in the future, that information will automatically update and supersede this information. We incorporate by reference the documents listed below and any future filings we will make with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934 until we sell all of the securities covered by this prospectus; provided, however, that we are not incorporating, in each case, any documents or information deemed to have been furnished and not filed in accordance with SEC rules:

- Our Annual Report on Form 10-K for the year ended December 31, 2017 filed with the SEC on February 28, 2018; and
- The description of our common stock set forth in our Registration Statement on Form 8-A, including any amendments or reports filed for the purpose of updating such description.

These documents contain important business and financial information about us that is not included in or delivered with this prospectus. You may request a copy of any or all documents that we incorporate by reference at no cost, by writing or telephoning us at:

Aqua America, Inc.
762 W. Lancaster Avenue
Bryn Mawr, PA 19010-3489
Telephone: 610-527-8000
Attention: Corporate Secretary

You should rely only on the information contained in or incorporated by reference in this prospectus and any supplements to this prospectus.We have not authorized anyone to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. You should not assume that the information provided in this prospectus or incorporated by reference in this prospectus is accurate as of any date other than the date on the front of this prospectus or the date of those documents. Our business, financial condition, results of operations and prospects may have changed since those dates.

If you find inconsistencies between the documents, or between the documents and this prospectus or the applicable prospectus supplement, you should rely on the most recent document, prospectus or prospectus supplement.

AQUA AMERICA, INC.

12,000,000 6.00% TANGIBLE EQUITY UNITS

PROSPECTUS SUPPLEMENT

Joint Bookrunners

RBC Capital Markets | **Goldman Sachs & Co. LLC**

BofA Merrill Lynch | **Morgan Stanley** | **Wells Fargo Securities**

Co-Managers

PNC Capital Markets LLC | **Barclays** | **Citizens Capital Markets** | **Huntington Capital Markets**
MUFG | **J.P. Morgan** | **TD Securities** | **Baird**

Boenning & Scattergood | **Janney Montgomery Scott** | **HSBC**

April 17, 2019

Filed Pursuant to Rule 424(b)(5)
Registration No. 333-223306

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Amount to be Registered	Proposed Maximum Offering Price Per Unit(1)	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee(2)
Common Stock, par value $0.50 per share	6,700,000	$ 46.40	$310,880,000	$ 40,352.22

(1) Publicly communicated offering price.
(2) Calculated pursuant to Rule 457(r) of the Securities Act of 1933, as amended.

Prospectus Supplement
(To Prospectus dated February 28, 2018)

6,700,000 Shares

ESSENTIAL UTILITIES, INC.

Common Stock

The forward seller referred to below is offering 6,700,000 shares of our common stock, par value $0.50 per share. We have entered into a forward sale agreement with Royal Bank of Canada (through its agent RBC Capital Markets), whom we refer to in such capacity as the "forward purchaser," with respect to 6,700,000 Shares of our common stock. In connection with the forward sale agreement, the forward purchaser or its affiliate and/or agent, whom we refer to in such capacity as the "forward seller," at our request, is borrowing from third parties and selling to the underwriter 6,700,000 shares of our common stock. If in the good faith, commercially reasonable judgment of the forward purchaser, it or its affiliate is unable to borrow and deliver for sale on the anticipated closing date a number of shares of our common stock underlying the forward sale agreement, or it or its affiliate would be unable to borrow, at a stock loan rate not greater than a specified rate, and deliver for sale on the anticipated closing date such number of shares of our common stock, or if certain other conditions to the forward seller's obligations have not been satisfied, then we will issue and sell directly to the underwriter a number of shares of our common stock equal to the number of shares that the forward seller does not borrow and deliver.

We will not initially receive any proceeds from the sale of our common stock sold by the forward seller to the underwriter, except in certain circumstances described in this prospectus supplement, including the last sentence of the previous paragraph. The forward sale agreement provides for settlement on a settlement date or dates to be specified at our discretion on or prior to August 10, 2021. If we elect to cash settle all or a portion of the forward sale agreement, we may not receive any proceeds from such election, and we may owe cash to the forward purchaser. If we elect to net share settle all or a portion of the forward sale agreement, we will not receive any cash proceeds from such election, and we may owe shares of our common stock to the forward purchaser. See "Underwriting (Conflicts of Interest)—Forward Sale Agreement" for a description of the forward sale agreement.

The underwriter proposes to offer shares of our common stock from time to time to purchasers directly or through agents, or through brokers in brokerage transactions on the NYSE, in the over-the-counter market, or to dealers in negotiated transactions, or in a combination of such methods of sale or otherwise, at a fixed price or prices, which may be changed, or at market prices prevailing at the time of sale, at prices related to such prevailing market prices, or at negotiated prices. In connection with the sale of shares of our common stock, the underwriter may be deemed to have received compensation in the form of underwriting discount.

The underwriter has agreed to purchase shares of our common stock from the forward seller at a price of $46.00 per share. We expect to receive estimated net proceeds from the sale of shares of our common stock, before expenses, of approximately $308.2 million upon full physical settlement of the forward sale agreement, which we expect to occur on or prior to August 10, 2021. For the purpose of calculating the estimated net proceeds to us, we have assumed that the forward sale agreement is fully physically settled based on the initial forward sale price of $46.00 per share. The forward sale price is subject to adjustment pursuant to the forward sale agreement, and the actual proceeds, if any, will be calculated as described in this prospectus supplement.

Although we expect to settle the forward sale agreement entirely by the full physical delivery of shares of our common stock to the forward purchaser in exchange for cash proceeds, we may elect cash settlement or net share settlement for all or a portion of our obligations under the forward sale agreement. See "Underwriting (Conflicts of Interest)—Forward Sale Agreement" for a description of the forward sale agreement.

Our common stock is listed on the New York Stock Exchange (the "NYSE") under the symbol "WTRG." The last reported sale price of our common stock on the NYSE on August 10, 2020 was $47.81 per share.

Investing in our common stock involves risks. See "Risk Factors" on page S-7 of this prospectus supplement, page 6 of the accompanying prospectus and in the documents we incorporate by reference in this prospectus supplement and the accompanying prospectus to read important factors you should consider before investing in our common stock.

Neither the Securities and Exchange Commission (the "SEC") nor any other regulatory body has approved or disapproved of these securities or passed upon the adequacy or accuracy of this prospectus supplement or the accompanying prospectus. Any representation to the contrary is a criminal offense.

The underwriter expects that the shares of our common stock will be delivered against payment on or about August 13, 2020.

Sole Book Running Manager

RBC Capital Markets

August 11, 2020

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ABOUT THIS PROSPECTUS SUPPLEMENT

Unless otherwise specified or the context requires otherwise, references in this prospectus supplement to (1) "Essential Utilities," the "Company," "we," "us," "our" and similar references refer to Essential Utilities, Inc. and its subsidiaries and (2) "this offering" refers to this offering of the shares pursuant to this prospectus supplement and the accompanying prospectus. Essential Utilities, Inc. was formerly known as Aqua America, Inc. prior to its name change on February 3, 2020, and accordingly, unless otherwise specified or the context requires otherwise, references in the accompanying prospectus and the documents incorporated by reference in the accompanying prospectus to Aqua America, Inc. refer to Essential Utilities, Inc and its subsidiaries.

This document is in two parts. The first part is this prospectus supplement, which describes the specific terms of this offering of the shares of our common stock and also adds to and updates information contained in the accompanying prospectus and the documents incorporated by reference in the accompanying prospectus. The second part is the accompanying prospectus, which gives more general information about us, some of which does not apply to this offering of the shares of our common stock. To the extent the information in this prospectus supplement is inconsistent with the information in the accompanying prospectus, you should rely on the information in this prospectus supplement.

We have not, and the underwriter and the forward seller have not, authorized anyone to provide you with any information other than that contained or incorporated by reference in this prospectus supplement, the accompanying prospectus or in any free writing prospectus we may provide to you in connection with this offering. Neither we nor the underwriter or the forward seller take any responsibility for, or provide any assurances as to the reliability of, any additional or different information that others may give you. Neither we nor the underwriter or the forward seller are offering to sell the shares or seeking offers to buy the shares in jurisdictions where offers or sales are not permitted. You should assume that the information contained in this prospectus supplement, the accompanying prospectus and any related free writing prospectus is accurate only as of their respective dates or as of the respective dates specified in such information, as applicable, and the information contained in documents incorporated by reference is accurate only as of the respective dates of those documents or as of the respective dates specified in such information, as applicable, in each case regardless of the time of delivery of this prospectus supplement or the accompanying prospectus or any such free writing prospectus or any sale of the shares of our common stock. Our business, financial condition, results of operations and prospects may have changed since those dates.

The distribution of this prospectus supplement, the accompanying prospectus and any related free writing prospectus and the offering of the shares of our common stock in certain jurisdictions may be restricted by law. Persons into whose possession this prospectus supplement, the accompanying prospectus and any such free writing prospectus come should inform themselves about and observe any such restrictions. This prospectus supplement, the accompanying prospectus and any such free writing prospectus do not constitute, and may not be used in connection with, an offer or solicitation by anyone in any jurisdiction in which such offer or solicitation is not authorized or in which the person making such offer or solicitation is not qualified to do so or to any person to whom it is unlawful to make such offer or solicitation. See "Underwriting (Conflicts of Interest)."

BASIS OF PRESENTATION

On March 16, 2020, we completed the acquisition of all of the issued and outstanding limited liability company membership interests of LDC Funding LLC (the "Peoples Acquisition"), which is the parent of a group of natural gas public utility companies that we refer to as "Peoples". Unless otherwise specified or the context requires otherwise, the information as of or in respect of periods prior to the closing of the Peoples Acquisition included in this prospectus supplement and the accompanying prospectus, including the documents incorporated by reference herein or therein, does not give effect to the Peoples Acquisition.

The unaudited pro forma consolidated combined statement of net income for the year ended December 31, 2019 and for the six months ended June 30, 2020 included or incorporated by reference in this prospectus supplement and the accompanying prospectus gives pro forma effect to the Peoples Acquisition and certain related transactions as if we had completed such transactions as of January 1, 2019, unless otherwise specified. The unaudited pro forma consolidated combined balance sheet as of June 30, 2020 is not presented in this prospectus supplement or the accompanying prospectus as Peoples is reflected in our historical consolidated balance sheet as of June 30, 2020. The unaudited pro forma consolidated combined statement of net income for the year ended December 31, 2019 and for the six months ended June 30, 2020 included in our Current Report on Form 8-K/A filed with the U.S. Securities and Exchange Commission (the "SEC") on August 10, 2020, which is incorporated by reference in this prospectus supplement and the accompanying prospectus and may be obtained as described in this prospectus supplement under the heading "Where You Can Find Additional Information; Incorporation of Certain Documents by Reference," does not give effect to our issuance of common stock in this offering. Moreover, the unaudited pro forma consolidated combined statement of net income for the year ended December 31, 2019 and for the six months ended June 30, 2020 included in our Current Report on Form 8-K/A filed with the SEC on August 10, 2020 has been calculated on the basis of assumptions made by our management at the time such information was prepared.

As a result, purchasers of shares in this offering should not place undue reliance on the pro forma and as adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus.

All references to currency amounts included in this prospectus supplement are in U.S. dollars unless specifically noted otherwise.

FORWARD-LOOKING STATEMENTS

Certain statements in this prospectus supplement, the accompanying prospectus and the documents they incorporate by reference contain, and any free writing prospectus we may provide to you in connection with this offering are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Exchange Act that are made based upon, among other things, our current assumptions, expectations, plans, and beliefs concerning future events and their potential effect on us. These forward-looking statements involve risks, uncertainties and other factors, many of which are outside our control that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. In some cases you can identify forward-looking statements where statements are preceded by, followed by or include the words "believes," "expects," "anticipates," "plans," "future," "potential," "probably," "predictions," "intends," "will," "continue," "in the event" or the negative of such terms or similar expressions. Such forward-looking statements include, but are not limited to, statements regarding:

- recovery of capital expenditures and expenses in rates;
- projected capital expenditures and related funding requirements;
- our capability to pursue timely rate increases;
- expectations regarding the impact of the Peoples Acquisition, including statements regarding the impact of the transaction on the Company;
- developments, trends and consolidation in the water, wastewater and natural gas utility and infrastructure industries;
- opportunities for future acquisitions, both within and outside the water, wastewater, and natural gas industries, the success of pending acquisitions and the impact of future acquisitions;
- the capacity of our water and natural gas supplies and facilities;
- the availability and cost of capital financing;
- dividend payment projections;
- the impact of geographic diversity on our exposure to unusual weather;
- the impact of conservation awareness of customers and more efficient fixtures and appliances on water usage and gas consumption per customer;
- our authority to carry on our business without unduly burdensome restrictions;
- the continuation of investments in strategic ventures;
- our ability to obtain fair market value for condemned assets;
- the impact of fines and penalties;
- the impact of changes in and compliance with governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- the impact of decisions of governmental and regulatory bodies, including decisions to raise or lower rates and decisions regarding potential acquisitions;
- the development of new services and technologies by us or our competitors;
- the availability of qualified personnel;
- the condition of our assets;
- the impact of legal proceedings;

- general economic conditions;
- acquisition-related costs and synergies;
- the sale of water and wastewater divisions;
- the impact of federal and/or state tax policies and the regulatory treatment of the effects of those policies;
- the amount of income tax deductions for qualifying utility asset improvements and the Internal Revenue Service's ultimate acceptance of the deduction methodology; and
- the impact of the novel coronovirus ("COVID-19") or the measures implemented by the Company as a result of COVID-19.

Because forward-looking statements involve risks and uncertainties, there are important factors that could cause actual results to differ materially from those expressed or implied by these forward-looking statements, including but not limited to:

- the diversion of our management's time and resources caused by integration efforts with respect to the Peoples Acquisition;
- our ability to manage the expansion of our business, including our ability to manage our expanded operations following the closing of the Peoples Acquisition;
- our ability to treat and supply water or collect and treat wastewater;
- our ability to source a sufficient supply of natural gas to meet the demands of our gas utility customers in a timely manner;
- the continuous and reliable operation of our information technology systems, including the impact of cyber security attacks or other cyber-related events;
- our ability to integrate and otherwise realize all of the anticipated benefits of businesses, technologies or services which we may acquire;
- changes in general economic, business, credit and financial market conditions;
- changes in governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- the profitability of future acquisitions;
- changes to the rules or our assumptions underlying our determination of what qualifies for an income tax deduction for qualifying utility asset improvements;
- the decisions of governmental and regulatory bodies, including decisions on rate increase requests and decisions regarding potential acquisitions;
- our ability to file rate cases on a timely basis to minimize regulatory lag;
- abnormal weather conditions, including those that result in water use restrictions and seasonality effects;
- changes in, or unanticipated, capital requirements;
- changes in our credit ratings or the market price of our common stock;
- changes in valuation of strategic ventures;
- the phase-out of LIBOR, or the replacement of LIBOR with a different reference rate or modification of the method used to calculate LIBOR, which may adversely affect interest rates;

- the extent to which we are able to develop and market new and improved services;
- the effect of the loss of major customers;
- our ability to retain the services of key personnel and to hire qualified personnel as we expand;
- labor disputes;
- increasing difficulties in obtaining insurance and increased cost of insurance;
- cost overruns relating to improvements to, or the expansion of, our operations;
- increases in the costs of goods and services and commodity prices;
- civil disturbance or terroristic threats or acts;
- changes in accounting pronouncements;
- litigation and claims;
- changes in environmental conditions, including the effects of climate change;
- restrictions on our subsidiaries' ability to make dividends and other distributions; and
- impacts from the global outbreak of COVID-19, including on consumption and collections.

Given these risks and uncertainties, you should not place undue reliance on any forward-looking statements. You should read this prospectus supplement, the accompanying prospectus and the documents that we incorporate by reference into this prospectus supplement completely and with the understanding that our actual results, performance and achievements may be materially different from what we expect. These forward-looking statements represent assumptions, expectations, plans and beliefs only as of the date of this prospectus supplement, the date of the document containing the applicable statement or the date specified in such statement, as applicable. Except for our ongoing obligations to disclose certain information under the federal securities laws, we are not obligated, and assume no obligation, to update these forward-looking statements, even though our situation may change in the future. For further information or other factors which could affect our financial results and such forward-looking statements, see "Risk Factors." We qualify all of our forward-looking statements by these cautionary statements.

Investing in our common stock involves risks. You should review and consider carefully the risks, uncertainties and other factors that affect our business, financial condition and results of operations and the value of the shares, including those described in the "Business," "Risk Factors," "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Management's Discussion and Analysis of Financial Condition and Results of Operations of Peoples" sections and other sections in our Annual Report on Form 10-K for the fiscal year ended December 31, 2019 and our Quarterly Reports on Form 10-Q for the quarter ended March 31, 2020 filed with the SEC on May 8, 2020 and the quarter ended June 30, 2020 filed with the SEC on August 6, 2020, and those described in the "Risk Factors" sections and other sections of this prospectus supplement and the accompanying prospectus. You may obtain copies of these reports and documents as described under "Where You Can Find Additional Information; Incorporation of Certain Documents by Reference" in this prospectus supplement. These risks, uncertainties and other factors could cause you to suffer a loss of all or part of your investment in the shares. Before making an investment decision, you should carefully consider these risks, uncertainties and other factors, as well as other information contained or incorporated by reference in this prospectus supplement and the accompanying prospectus and any related free writing prospectus we may provide to you in connection with this offering. However, additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our business, operations, financial condition and financial results and the value of the shares.

MARKET AND INDUSTRY DATA

This prospectus supplement, the accompanying prospectus and the documents incorporated by reference in this prospectus supplement and the accompanying prospectus include, and any free writing prospectus we may provide to you in connection with this offering may include, market, demographic and industry data and forecasts related to our business that are based on or derived from sources such as independent industry publications, publicly available information, government data and other information from third parties or that have been compiled or prepared by our management or employees. We do not guarantee the accuracy or completeness of any of this information, and we have not independently verified any of the information provided by third-party sources.

In addition, market, demographic and industry data and forecasts involve estimates, assumptions and other uncertainties and are subject to change based on various factors, including those discussed under the heading “Risk Factors” in this prospectus supplement and under similar headings in the documents that are incorporated by reference in this prospectus supplement and the accompanying prospectus. Accordingly, you should not place undue reliance on any of this information.

PROSPECTUS SUPPLEMENT SUMMARY

The following summary highlights, and should be read together with, the information contained elsewhere in this prospectus supplement, the accompanying prospectus and the documents incorporated by reference herein and therein. This summary may not contain all of the information that may be important to you, and you should carefully read this entire prospectus supplement, the accompanying prospectus, any free writing prospectus we may provide to you in connection with this offering and the documents incorporated by reference herein and therein before making an investment decision. You may obtain a copy of the documents incorporated by reference by following the instructions in the section titled "Where You Can Find Additional Information; Incorporation of Certain Documents by Reference," in this prospectus supplement. Unless we state otherwise or the context otherwise requires, references appearing in this prospectus supplement to "Essential Utilities," the "Company," "we," "us" and "our" should be read to refer to Essential Utilities, Inc. and its subsidiaries.

Essential Utilities, Inc.

Essential Utilities, Inc., formerly known as Aqua America, Inc., is a Pennsylvania corporation and the holding company for regulated utilities providing water, wastewater or natural gas distribution services to an estimated five million people in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana, Virginia, West Virginia and Kentucky under the Aqua and Peoples brands. One of our largest operating subsidiaries, Aqua Pennsylvania, Inc. ("Aqua Pennsylvania"), provides water or wastewater services to approximately one-half of the total number of water or wastewater customers we serve, who are located in the suburban areas in counties north and west of the City of Philadelphia and in 27 other counties in Pennsylvania. Our other regulated water or wastewater utility subsidiaries provide similar services in seven other states.

Pursuant to the Company's growth strategy, commencing on March 16, 2020, with the completion of the Peoples Gas Acquisition, the Company began to provide natural gas distribution services to customers in western Pennsylvania, Kentucky, and West Virginia. Approximately 93% of the total number of natural gas utility customers we serve are in western Pennsylvania. Lastly, the Company's market-based activities are conducted through Aqua Infrastructure, LLC and Aqua Resources, Inc. and certain other non-regulated subsidiaries of Peoples. Aqua Infrastructure provides non-utility raw water supply services for firms in the natural gas drilling industry. Aqua Resources manages a water system operating and maintenance contract, and offers, through a third-party, water and sewer service line protection solutions and repair services to households. The non- regulated subsidiaries of Peoples provide utility service line protection solutions and repair services to households and operates gas marketing and production entities.

Our growth in revenues over the past five years is primarily a result of increases in rates and customer growth. The increase in our utility customer base, as shown below, has been due to customers added through acquisitions, partnerships with developers, and organic growth (excluding dispositions):

Year	Utility Customer Growth Rate
2019	2.1%
2018	2.3%
2017	1.1%
2016	1.6%
2015	1.9%

In 2019, our customer count increased by 21,108 customers, primarily due to utility systems that we acquired and organic growth. Overall, for the five-year period of 2015 through 2019, our utility customer base,

adjusted to exclude customers associated with utility system dispositions, increased at an annual compound rate of 1.8%. During the five-year period ended December 31, 2019, our utility customer base, including customers associated with utility system acquisitions and dispositions, increased from 940,119 at January 1, 2015 to 1,026,704 at December 31, 2019.

The Peoples Acquisition brings Essential Utilities' total water, wastewater and natural gas customer count to approximately 1,773,000 on a pro forma basis as of December 31, 2019.

Our principal executive office is located at 762 W. Lancaster Avenue, Bryn Mawr, Pennsylvania 19010-3489, and our telephone number is 610-527-8000. Our website may be accessed at *www.essential.co*. The reference to our website is intended to be an inactive textual reference only, and the contents of our website are not incorporated by reference herein and should not be considered part of this prospectus supplement.

Recent Developments

COVID-19

The impact of the global outbreak of the COVID-19 pandemic has created significant volatility in the global economy and led to reduced economic activity. We are monitoring the global outbreak of COVID-19 and taking steps to mitigate the potential risks to our employees and our customers posed by its spread. For information regarding the COVID-19 pandemic and its impact on our business, see our Quarterly Reports on Form 10-Q for the quarter ended March 31, 2020 filed with the SEC on May 8, 2020 and the quarter ended June 30, 2020 filed with the SEC on August 6, 2020.

THE OFFERING

The following summary contains basic information about this offering and may not contain all of the information that may be important to you. You should read this entire prospectus supplement, the accompanying prospectus, any free writing prospectus we may provide to you in connection with this offering and the documents incorporated by reference herein and therein before making an investment decision.

As used in this section, unless the context otherwise requires, references to "Essential Utilities," the "Company," "we," "us," "our" and similar references refer only to Essential Utilities, Inc. and not to its consolidated subsidiaries.

Issuer	Essential Utilities, Inc., a Pennsylvania corporation
Common Stock Offered by this Prospectus Supplement	6,700,000 shares
Common Stock to be Outstanding Immediately Before this Offering	245,154,699 shares(1)
Common Stock to be Outstanding Immediately After the Offering	245,154,699 shares(1)(2)
Common Stock to be Outstanding After Settlement of the Forward Sale Agreement Assuming Physical Settlement	251,854,699 shares(1)(2)(3)

(1) This amount is based on the total number of shares of our common stock that was outstanding on August 7, 2020. In calculating that number of shares, we did not take into account shares issuable upon settlement of the purchase contracts that are part of the tangible equity units, reserved for issuance upon exercise or vesting of stock options, restricted stock units or performance share units or issuable under the dividend reinvestment plan, employee stock purchase plan or 401(k) savings plan.

(2) Such number of shares of our common stock assumes that we will not be required to issue the shares of our common stock that are the subject of this offering in lieu of the forward seller borrowing and selling such shares to the underwriter as further described elsewhere in this prospectus supplement. For more information, see "Underwriting (Conflicts of Interest)."

(3) The forward seller has advised us that it intends to acquire shares of our common stock to be sold in this offering through borrowings from third-party stock lenders. Subject to the occurrence of certain events, we will not be obligated to deliver shares of our common stock under the forward sale agreement (if at all) until later settlement of the forward sale agreement, which provides for settlement on a settlement date or dates to be specified at our discretion on or prior to August 10, 2021. Except in certain circumstances, we have the right to elect cash settlement or net share settlement under the forward sale agreement. Although we intend to elect full physical settlement under the forward sale agreement, if we elect cash settlement we will not issue any shares and if we elect net share settlement, the number of shares we issue upon settlement of the forward sale agreement may be substantially less than the amount we would have issued upon full physical settlement, or we may not issue any shares upon such net share settlement at all. See "Underwriting (Conflicts of Interest)–Forward Sale Agreement" for a description of the forward sale agreement.

Use of Proceeds	We will not initially receive any proceeds from the sale of the shares of our common stock offered by the forward seller in this offering, unless an event occurs that requires us to issue and sell such shares to the underwriter in lieu of the forward seller selling such shares to the underwriter as further described elsewhere in this prospectus supplement, in which case we intend to use all net proceeds we receive from any such sales for the same purposes described below. We expect to receive net proceeds (after deducting estimated expenses) of approximately $307.5 million, subject to the price adjustment and other provisions of the forward sale agreement, in the event of full physical settlement of the forward sale agreement, which we expect to occur on or prior to August 10, 2021. For purposes of calculating the proceeds to us upon settlement of the forward sale agreement, we have assumed that the forward sale agreement is physically settled based upon the initial forward sale price of $46.00 per share on the effective date of the forward sale agreement, which will be August 11, 2020. We will not receive any proceeds under the forward sale agreement on the closing date of this offering. The actual proceeds from the forward sales are subject to the final settlement of the forward sale agreement. The forward sale price that we expect to receive upon physical settlement of the forward sale agreement is subject to adjustment on a daily basis based on a floating interest rate factor equal to the overnight bank funding rate less a spread and will be decreased based on amounts related to expected dividends on shares of our common stock during the term of the forward sale agreement, including the dividend declared on August 4, 2020 and having a record date of August 14, 2020. If the overnight bank funding rate is less than the spread on any day, the interest rate factor will result in a daily reduction of the forward sale price for such day.

We currently intend to elect full physical settlement of the forward sale agreement and to use the net proceeds, if any, that we would receive upon settlement of the forward sale agreement for general corporate purposes, including for water and wastewater utility acquisitions, working capital and capital expenditures. If we elect to cash settle all or a portion of the forward sale agreement, we will not receive any proceeds from the sale of shares of our common stock related to such election of cash settlement of the forward sale agreement and we may either receive a cash payment from, or owe a cash payment to, the forward purchaser. If we elect to net share settle all or a portion of the forward sale agreement, we will not receive any proceeds from the sale of shares of our common stock related to such election, and we may either receive shares of our common stock from, or owe shares of our common stock to, the forward purchaser.

Certain United States Federal Income and Estate Tax Considerations	Certain United States federal income and estate tax considerations to non-U.S. holders of purchasing, owning and disposing of our common stock are described in “Certain United States Federal Income and Estate Tax Considerations to Non-U.S. Holders” included in this prospectus supplement.

Listing	Our common stock is listed on the New York Stock Exchange (the "NYSE") under the symbol "WTRG."
Dividend Policy	We have historically paid quarterly dividends on our common stock; however, the declaration, amount, timing and payment of any future dividends are subject to the determination and approval of our board of directors based on then-current or anticipated future conditions including our results of operations, capital requirements, financial condition, legal requirements or other factors deemed relevant by our board of directors. See "Listing of Our Common Stock and Dividends."
Transfer Agent and Registrar	The registrar and transfer agent for our common stock is Computershare Trust Company, N.A.
Accounting Treatment	Before the issuance of shares of our common stock, if any, upon settlement of the forward sale agreement, we expect that the shares issuable upon settlement of the forward sale agreement will be reflected in our diluted earnings per share calculation using the treasury stock method. Under this method, the number of shares of our common stock used in calculating diluted earnings per share is deemed to be increased by the excess, if any, of the number of shares of common stock that would be issued upon full physical settlement of the forward sale agreement over the number of shares of common stock that could be purchased by us in the market (based on the average market price of our common stock during the applicable reporting period) using the proceeds receivable upon full physical settlement (based on the adjusted forward sale price at the end of the reporting period). Consequently, we anticipate there will be no dilutive effect on our earnings per share except during periods when the average market price of shares of our common stock is above the applicable adjusted forward sale price, which is initially $46.00 per share, subject to increase or decrease based on the overnight bank funding rate, less a spread, and subject to decrease by amounts related to expected dividends on shares of our common stock during the term of the forward sale agreement. However, if we decide to physically settle or net share settle the forward sale agreement, delivery of our shares to the forward purchaser on the physical settlement or net share settlement of the forward sale agreement would result in dilution to our earnings per share.
Conflicts of Interest	All of the proceeds of this offering (excluding proceeds to us with respect to any shares of common stock that we may issue and sell directly to the underwriter in lieu of the forward seller selling our common stock to the underwriter) will be paid to the forward purchaser (or its affiliate). Because RBC Capital Markets, or its affiliate, will receive more than 5% of the net proceeds of this offering, not including underwriting compensation, RBC Capital Markets is deemed to have a conflict of interest within the meaning of Rule 5121 (Public Offerings of Securities with Conflicts of Interest)

	of the Financial Industry Regulatory Authority, Inc. ("FINRA"). Accordingly, this offering will be conducted in compliance with the applicable requirements of FINRA Rule 5121. Pursuant to that rule, the appointment of a "qualified independent underwriter" is not required in connection with this offering, as the shares of our common stock have a "bona fide public market" (as such terms are defined in FINRA Rule 5121). In accordance with FINRA Rule 5121, RBC Capital Markets may not confirm any sales to any account over which it exercises discretionary authority without the prior written approval of the transaction from the account holder.
Risk Factors	Investing in our common stock involves risks. See "Risk Factors" in this prospectus supplement, the accompanying prospectus and in the documents we incorporate by reference in this prospectus supplement and the accompanying prospectus for a discussion of some of the risks and other factors you should carefully consider before deciding to invest in shares of our common stock.

In this prospectus supplement, unless otherwise indicated, the number of shares of our common stock outstanding and the other information based thereon is based on 245,154,699 shares of our common stock outstanding as of August 7, 2020, and does not reflect:

- 11.1 million shares of our common stock issuable upon settlement of the tangible equity units ("TEUs") purchase contracts outstanding as of June 30, 2020, assuming the maximum number of shares issuable upon automatic settlement of such TEU purchase contracts that are components of the TEUs; and
- 18.7 million shares of our common stock reserved for issuance upon exercise of stock options outstanding, upon vesting of our time based restricted stock units, upon vesting of our performance based restricted stock units or performance share units, as well as additional shares we may issue under our dividend reinvestment program, employee stock purchase plan or 401(k) savings plans.

RISK FACTORS

Investing in our common stock involves risks. You should review and carefully consider the risks, uncertainties and other factors described below and all of the information included elsewhere in this prospectus supplement, the accompanying prospectus, any free writing prospectus we may provide to you in connection with this offering and the documents incorporated by reference herein and therein before deciding to invest in the shares. We also urge you to consider carefully the risks, uncertainties and other factors set forth under the headings "Forward-Looking Statements" and "Market and Industry Data." However, additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our business, operations, financial condition and financial results and the value of the shares.

Risks Related to Our Business

For a discussion of specific risks related to our business, operations, financial condition and financial results, please see the "Business," "Risk Factors," "Management's Discussion and Analysis of Financial Condition and Results of Operations" sections in our Annual Report on Form 10-K for our fiscal year ended December 31, 2019 and the "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" sections in our Quarterly Reports on Form 10-Q for the quarter ended March 31, 2020 filed with the SEC on May 8, 2020 and the quarter ended June 30, 2020 filed with the SEC on August 6, 2020, in each case, as updated by our annual, quarterly and other reports and documents we file with the SEC that are incorporated by reference in this prospectus supplement and the accompanying prospectus. See "Where You Can Find Additional Information; Incorporation of Certain Documents by Reference," in this prospectus supplement.

Risks Related to the Forward Sale Agreement

Settlement provisions contained in the forward sale agreement subject us to certain risks.

The forward purchaser will have the right to accelerate the forward sale agreement (or, in certain cases, the portion thereof that it determines is affected by the relevant event) and require us to physically settle the forward sale agreement on a date specified by the forward purchaser if:

- in the commercially reasonable judgment of the forward purchaser, it or its affiliate is unable to hedge its exposure to the transactions contemplated by the forward sale agreement because of the lack of sufficient shares of our common stock being made available for borrowing by stock lenders or it or its affiliate is unable to borrow such number of shares at a rate equal to or less than an agreed maximum stock loan rate;
- we declare any dividend, issue or distribution on shares of our common stock (i) payable in cash in excess of a specified amount or that otherwise constitutes an extraordinary dividend under the forward sale agreement, (ii) payable in securities of another company as a result of a spin-off or similar transaction, (iii) of any other type of securities (other than our common stock), rights, warrants or other assets for payment (cash or other consideration) at less than the prevailing market price, as reasonably determined by the forward purchaser or (iv) any other special dividend or distribution that is outside the normal course of our operations of normal dividend policies or practices;
- certain ownership thresholds applicable to the forward purchaser are exceeded;
- an event is announced that, if consummated, would result in an extraordinary event (as defined in the forward sale agreement) including, among other things, certain mergers and tender offers, as well as certain events such as a delisting of our common stock (each as more fully described in the forward sale agreement); or
- certain other events of default or termination events occur, including, among other things, any material misrepresentation made by us in connection with our entry into the forward sale agreement, our bankruptcy (except as described below) or certain changes in law (each as more fully described in the forward sale agreement).

The forward purchaser's decision to exercise its right to accelerate the forward sale agreement (or, in certain cases, the portion thereof that it determines is affected by the relevant event) and to require us to settle the forward sale agreement will be made irrespective of our interests, including our need for capital. In such cases, we could be required to issue and deliver shares of our common stock under the terms of the physical settlement provisions of the forward sale agreement irrespective of our capital needs, which would result in dilution to our earnings per share and may adversely affect the market price of our common stock. In addition, upon certain events of bankruptcy or insolvency related to us, the forward sale agreement will automatically terminate without further liability of either party to such agreement (other than in the event of a breach by us of certain representations or warranties contained in the forward sale agreement). Following any such termination, we would not issue any shares of common stock or receive any proceeds pursuant to the forward sale agreement.

The forward sale agreement provides for settlement on a settlement date or dates to be specified at our discretion on or prior to August 10, 2021. The forward sale agreement will be physically settled, unless we elect to settle the forward sale agreement in cash or to net share settle the forward sale agreement. If we decide to physically settle or net share settle the forward sale agreement, delivery of shares of our common stock upon any physical settlement or net share settlement of the forward sale agreement will result in dilution to our earnings per share. If we elect cash or net share settlement for all or a portion of the shares of our common stock underlying the forward sale agreement, we would expect the forward purchaser or one of its affiliates to repurchase a number of shares of our common stock equal to the portion for which we elect cash or net share settlement in order to satisfy its obligation to return the shares of our common stock the forward purchaser or its affiliate had borrowed in connection with sales of our common stock under this prospectus supplement and, if applicable in connection with net share settlement, to deliver shares of our common stock to us. If the market value of our common stock at the time of the purchase is above the forward sale price at that time, we will pay or deliver, as the case may be, to the forward purchaser under the forward sale agreement, an amount in cash, or a number of shares of our common stock with a market value, equal to such difference. Any such difference could be significant. Conversely, if the market value of our common stock at the time of such purchase is below the forward sale price at that time, the forward purchaser will pay or deliver, as the case may be, to us under the forward sale agreement, an amount in cash, or a number of shares of our common stock with a market value, equal to such difference. See "Underwriting (Conflicts of Interest)—Forward Sale Agreement" for a description of the forward sale agreement.

The forward sale price that we expect to receive upon physical settlement of the forward sale agreement is subject to adjustment on a daily basis based on a floating interest rate factor equal to the overnight bank funding rate less a spread and will be decreased based on amounts related to expected dividends on shares of our common stock during the term of the forward sale agreement. If the overnight bank funding rate is less than the spread on any day, the interest rate factor will result in a daily reduction of the forward sale price for such day. As of the date of this prospectus supplement, the overnight bank funding rate is less than the spread, and if the overnight bank funding rate remains constant or decreases prior to the settlement of the forward sale agreement, we may receive less than the initial forward sale price per share upon physical settlement of the forward sale agreement.

In addition, the purchase of shares of our common stock by the forward purchaser or its affiliate to unwind the forward purchaser's hedge position could cause the market price of our common stock to increase over time, thereby increasing the amount of cash we would owe to the forward purchaser upon a cash settlement or increasing the number of shares of our common stock we would owe to the forward purchaser upon a net share settlement, as the case may be, of the forward sale agreement, or decreasing the amount of cash that the forward purchaser would owe us upon a cash settlement or decreasing the number of shares of our common stock that the forward purchaser would owe us upon a net share settlement, as the case may be, of the forward sale agreement. We will not be able to control the manner in which the forward purchaser unwinds its hedge positions.

In certain bankruptcy or insolvency events, the forward sale agreement will automatically terminate, and we would not receive the expected proceeds from the forward sales of our common stock.

If we institute or consent to, or an appropriate regulatory or other authority institutes against us, a proceeding seeking a judgment in bankruptcy or insolvency or any other relief under any bankruptcy or insolvency law or other similar law affecting creditors' rights or if we or such authority presents a petition for our winding up or liquidation or we consent to such a petition, the forward sale agreement will automatically terminate. If the forward sale agreement so terminates, we would not be obligated to deliver to the forward purchaser any shares of our common stock not previously delivered (or for which physical settlement has not been elected), and the forward purchaser would be discharged from its obligation to pay the forward sale price per share in respect of any shares of our common stock not previously settled (or for which physical settlement has not been elected). Therefore, to the extent there are any shares of our common stock with respect to which we have not elected to physically settle under the forward sale agreement at the time of the institution of or consent to any such bankruptcy or insolvency proceedings or any such petition, we would not receive the forward sale price per share in respect of those shares of our common stock.

Risks Related to this Offering and Our Common Stock

The unaudited pro forma consolidated combined financial information and other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus are presented for illustrative purposes only and do not purport to represent what the financial position or results of operations of the combined company would have been had the Peoples Acquisition been completed on the dates assumed for purposes of that information, nor do they represent the actual financial position or results of operations of the combined company following the Peoples Acquisition.

The unaudited pro forma consolidated combined financial information and other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus are presented for illustrative purposes only, are based on numerous adjustments, assumptions and estimates, are subject to numerous other uncertainties and do not purport to reflect what the combined company's financial position or results of operations would have been had the Peoples Acquisition been completed as of the dates assumed for purposes of that information, nor do they reflect the financial position or results of operations of the combined company following the Peoples Acquisition. Such unaudited pro forma consolidated combined financial information and certain other adjusted information reflects the assumptions of our management at the time that such information was initially prepared.

In any event, our actual financial positions and results of operations following the Peoples Acquisition may not be consistent with, or evident from, the unaudited pro forma consolidated combined financial information or other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus.

For purposes of the unaudited pro forma consolidated combined financial information as of December 31, 2019, the $3.465 billion base cash purchase price payable in connection with the Peoples Acquisition (the "Cash Acquisition Consideration") has been preliminarily allocated to the identifiable assets acquired and liabilities assumed based on limited information presently available to estimate fair values. The Cash Acquisition Consideration will be allocated among the relative fair values of the identifiable assets acquired and liabilities assumed based on their estimated fair values as of the date of the Peoples Acquisition. The relative fair values of the assets acquired and liabilities assumed are estimates, which are subject to change pending further review. The actual amounts recorded with respect to the Peoples Acquisition may differ materially from the information presented in the unaudited pro forma consolidated combined financial information.

As a result of the foregoing, investors should not place undue reliance on unaudited pro forma consolidated combined financial information and other adjusted information included or incorporated by reference in this prospectus supplement and the accompanying prospectus.

The price of our common stock may be volatile. This volatility may affect the price at which you could sell our common stock, and the sale or resale of substantial amounts of our common stock could adversely affect the market price of our common stock.

The sale or issuance of substantial amounts of our common stock, or the perception that additional sales or issuances could occur, could adversely affect the market price of our common stock, even if the business is doing well. In addition, the availability for sale of substantial amounts of our common stock could adversely impact its market price. Shares of our common stock will also be issuable upon settlement or redemption of the TEU purchase contracts and the number of shares may be substantial. The settlement rates for the TEU purchase contracts will be subject to certain anti-dilution adjustments that could increase, potentially significantly, the number of shares of our common stock issuable upon such settlement or redemption. Any of the foregoing may also impair our ability to raise additional capital through the sale of our equity securities.

Raising additional funds by issuing additional equity securities or with additional debt financing in the future may cause dilution to shareholders or restrict our operations.

We expect that we will need to raise additional capital in the future in order to, among other things, repay indebtedness and fund our operations and future acquisitions, which we may do through equity and equity-linked securities offerings or additional debt financings, as well as borrowings under our credit facilities. Additional issuances of equity securities, including shares of our common stock, or debt or other securities that are convertible into or exchangeable for, or that represent the right to receive, common stock could dilute the economic and other rights and interests of holders of shares of our common stock and cause the market price of our common stock to decline. Subject to certain exceptions, such issuances may be made without any action or approval by our shareholders.

Any new debt financing we enter into may involve covenants that restrict our operations more than our current outstanding debt and credit facilities. These restrictive covenants could include limitations on additional borrowings, and specific restrictions on the use of our assets, as well as prohibitions or limitations on our ability to create liens, pay dividends, receive distributions from our subsidiaries, redeem or repurchase our stock or make investments. These covenants could hinder our access to capital markets and limit or delay our ability to carry out our capital expenditure program.

Anti-takeover provisions in our organizational documents and under Pennsylvania law might discourage, delay or prevent changes in control of our company and may result in an entrenchment of management and diminish the value of our common stock.

Certain provisions of our articles of incorporation and bylaws could have the effect of delaying, deterring or preventing another party from acquiring or seeking to acquire control of us. These provisions are intended to discourage certain types of coercive takeover practices and inadequate takeover bids and to encourage anyone seeking to acquire control of us to negotiate first with our board of directors. However, these provisions could also delay, deter or prevent a change of control or other takeover of our company that our shareholders might consider to be in their best interests, including transactions that might result in a premium being paid over the market prices of our common stock, and may also limit the prices that investors are willing to pay in the future for our common stock. These provisions may also have the effect of preventing changes in our management.

For example, our articles of incorporation and bylaws include anti-takeover provisions that:

- authorize our board of directors, without a vote or other action by our shareholders, to cause the issuance of preferred stock in one or more series and, with respect to each series, to fix the number of shares constituting that series and to establish the rights, preferences, privileges and restrictions of that series, which may include, among other things, dividend and liquidation rights and preferences, rights to convert such shares into common stock, voting rights and other rights which may adversely affect the voting or other rights and the economic interests of holders of our common stock;

- require that certain fundamental transactions must be approved by the holders of 75% of the outstanding shares of our capital stock entitled to vote on the matter unless at least a majority of the members of the board of directors has approved the transaction, in which case the required shareholder approval will be the minimum approval required by applicable law;
- establish advance notice requirements and procedures for shareholders to submit nominations of candidates for election to our board of directors and to propose other business to be brought before a shareholders meeting;
- provide that vacancies in our board of directors, including vacancies created by the removal of any director, or any increase in the number of directors may be filled by a majority of the directors then in office or by the sole remaining director;
- provide that no shareholder may cumulate votes in the election of directors, which means that the holders of a majority of our outstanding shares of common stock can elect all directors standing for election by our common shareholders;
- require that any action to be taken by our shareholders must be taken either (1) at a duly called annual or special meeting of shareholders or (2) by the unanimous written consent of all of our shareholders; and
- require action by shareholders entitled to cast a majority of the votes which all shareholders are entitled to cast at the particular meeting in order for our shareholders to call a special meeting of shareholders.

In addition, anti-takeover provisions in Pennsylvania law could make it more difficult for a third party to acquire control of us including, but not limited to, provisions relating to (1) control share acquisitions, (2) disgorgement of profits by certain controlling persons, (3) business combination transactions with interested shareholders, and (4) the rights of shareholders to demand fair value for their stock following a control transaction. Pennsylvania law permits corporations to opt-out of these anti-takeover provisions, but we have not done so. Such provisions could have the effect of deterring takeovers or delaying changes in control or management of us. Additionally, such provisions could limit the price that some investors might be willing to pay in the future for shares of our common stock.

We may be unable to, or may choose not to, continue to pay dividends on our common stock at current or planned rates or at all.

Any future payments of cash dividends, and the amount of any cash dividends we pay, on our common stock will depend on, among other things, our financial condition, capital requirements and results of operations, and the ability of our subsidiaries to distribute cash to us, as well as other factors that our board of directors may consider relevant. If we were to reduce the amount of cash dividends per share payable on our common stock, fail to increase the amount of those cash dividends per share in the future or cease paying those cash dividends altogether, it would likely have an adverse impact on the market price of our common stock. In addition, under Pennsylvania law, our board of directors (or an authorized committee thereof) may not declare and pay dividends on shares of our common stock if, after giving effect to the dividend (1) we would be unable to pay our debts as they become due in the ordinary course of business, or (2) our total assets would be less than the sum of our total liabilities plus the amount that would be needed, if we were to be dissolved as of the date for measuring the dividend, to satisfy the preferential rights upon dissolution of shareholders whose preferential rights are superior to those receiving the dividend.

Essential Utilities' ability to pay dividends and to meet its debt obligations largely depends on the performance of its subsidiaries and the ability to utilize the cash flows from those subsidiaries.

Essential Utilities is a holding company substantially all of whose assets are owned by its subsidiaries and substantially all of whose operations are conducted through its subsidiaries. Essential Utilities' ability to pay dividends and meet its debt and other obligations depends almost entirely on cash flows from its subsidiaries and,

in the short term, its ability to raise capital from external sources. In the long term, cash flows from its subsidiaries depend on their ability to generate operating cash flows in excess of their own expenditures, common and preferred stock dividends (if any), and debt or other obligations. Its subsidiaries are separate and distinct legal entities that are not obligated to pay dividends or make loans or distributions to Essential Utilities (whether to enable Essential Utilities to pay dividends on its common stock, to pay principal and interest on its debt, to settle, repurchase or redeem its debt (including the amortizing notes components of its TEUs) or other securities (including the purchase contracts components of its TEUs)), or to satisfy its other obligations). In addition, notwithstanding its controlling interest in such subsidiaries, many of them, including certain entities of Peoples, are limited in their ability to pay dividends or make loans or distributions to Essential Utilities, including, without limitation, as a result of legislation, regulation, court order, contractual restrictions and other restrictions or in times of financial distress. As a result, Essential Utilities may not be able to cause its subsidiaries and other entities to distribute funds or provide loans sufficient to enable it to pay dividends and meet its debt and other obligations.

USE OF PROCEEDS

We will not initially receive any proceeds from the sale of the shares of our common stock offered by the forward seller in this offering, unless an event occurs that requires us to issue and sell such shares to the underwriter in lieu of the forward seller selling such shares to the underwriter as further described elsewhere in this prospectus supplement, in which case we intend to use all net proceeds we receive from any such sales for the same purposes described below.

We expect to receive net proceeds (after deducting estimated expenses) of approximately $307.5 million, subject to the price adjustment and other provisions of the forward sale agreement, in the event of full physical settlement of the forward sale agreement, which we expect to occur on or prior to August 10, 2021. For purposes of calculating the proceeds to us upon settlement of the forward sale agreement, we have assumed that the forward sale agreement is physically settled based upon the initial forward sale price of $46.00 per share on the effective date of the forward sale agreement, which will be August 11, 2020. We will not receive any proceeds under the forward sale agreement on the closing date of this offering. The actual proceeds from the forward sales are subject to the final settlement of the forward sale agreement. The forward sale price that we expect to receive upon physical settlement of the forward sale agreement is subject to adjustment on a daily basis based on a floating interest rate factor equal to the overnight bank funding rate less a spread and will be decreased based on amounts related to expected dividends on shares of our common stock during the term of the forward sale agreement, including the dividend declared on August 4, 2020 and having a record date of August 14, 2020. If the overnight bank funding rate is less than the spread on any day, the interest rate factor will result in a daily reduction of the forward sale price for such day. See “Underwriting (Conflicts of Interest)—Forward Sale Agreement” for a description of the forward sale agreement.

We currently intend to elect full physical settlement of the forward sale agreement and to use the net proceeds, if any, that we would receive upon settlement of the forward sale agreement for general corporate purposes, including for water and wastewater utility acquisitions, working capital and capital expenditures. If we elect to cash settle all or a portion of the forward sale agreement, we will not receive any proceeds from the sale of shares of our common stock related to such election of cash settlement of the forward sale agreement and we may either receive a cash payment from, or owe a cash payment to, the forward purchaser. If we elect to net share settle all or a portion of the forward sale agreement, we will not receive any proceeds from the sale of shares of our common stock related to such election, and we may either receive shares of our common stock from, or owe shares of our common stock to, the forward purchaser.

LISTING OF OUR COMMON STOCK AND DIVIDENDS

Our common stock is listed on the NYSE under the symbol “WTRG.” As of August 7, 2020, there were 245,154,699 shares of our common stock outstanding.

On August 10, 2020, the last reported sale price of our common stock on the NYSE was $47.81.

We have historically paid quarterly dividends on our common stock; however, the declaration, amount, timing and payment of any future dividends are subject to the determination and approval of our board of directors based on then-current or anticipated future conditions including our results of operations, capital requirements, financial condition, legal requirements or other factors deemed relevant by our board of directors. See “Risk Factors—Risks Related to Our Common Stock—We may be unable to, or may choose not to, continue to pay dividends on our common stock at current or planned rates or at all.”

CERTAIN UNITED STATES FEDERAL INCOME AND ESTATE TAX CONSIDERATIONS TO NON-U.S. HOLDERS

The following is a summary of certain United States federal income and estate tax consequences of the purchase, ownership and disposition of our common stock as of the date hereof. Except where noted, this summary deals only with common stock that is held as a capital asset by a non-U.S. holder (as defined below).

A "non-U.S. holder" means a beneficial owner of our common stock (other than an entity treated as a partnership for United States federal income tax purposes) that is not, for United States federal income tax purposes, any of the following:

- an individual citizen or resident of the United States;
- a corporation (or any other entity treated as a corporation for United States federal income tax purposes) created or organized in or under the laws of the United States, any state thereof or the District of Columbia;
- an estate the income of which is subject to United States federal income taxation regardless of its source; or
- a trust if it (1) is subject to the primary supervision of a court within the United States and one or more United States persons have the authority to control all substantial decisions of the trust or (2) has a valid election in effect under applicable United States Treasury regulations to be treated as a United States person.

This summary is based upon provisions of the Internal Revenue Code of 1986, as amended (the "Code"), and regulations, rulings and judicial decisions as of the date hereof. Those authorities may be changed, perhaps retroactively, so as to result in United States federal income and estate tax consequences different from those summarized below. This summary does not address all aspects of United States federal income and estate taxes and does not deal with foreign, state, local or other tax considerations that may be relevant to non-U.S. holders in light of their particular circumstances. In addition, it does not represent a detailed description of the United States federal income and estate tax consequences applicable to you if you are subject to special treatment under the United States federal income tax laws (including if you are a United States expatriate, foreign pension fund, "controlled foreign corporation," "passive foreign investment company" or a partnership or other pass-through entity for United States federal income tax purposes). We cannot assure you that a change in law will not alter significantly the tax considerations that we describe in this summary.

If a partnership (or other entity treated as a partnership for United States federal income tax purposes) holds our common stock, the tax treatment of a partner will generally depend upon the status of the partner and the activities of the partnership. If you are a partner of a partnership holding our common stock, you should consult your tax advisors.

If you are considering the purchase of our common stock, you should consult your own tax advisors concerning the particular United States federal income and estate tax consequences to you of the purchase, ownership and disposition of our common stock, as well as the consequences to you arising under other United States federal tax laws and the laws of any other taxing jurisdiction.

Dividends

In the event that we make a distribution of cash or other property (other than certain pro rata distributions of our stock) in respect of our common stock, the distribution generally will be treated as a dividend for United States federal income tax purposes to the extent it is paid from our current or accumulated earnings and profits, as determined under United States federal income tax principles. Any portion of a distribution that exceeds our current and accumulated earnings and profits generally will be treated first as a tax-free return of capital, causing

a reduction in the adjusted tax basis of a non-U.S. holder's common stock, and to the extent the amount of the distribution exceeds a non-U.S. holder's adjusted tax basis in our common stock, the excess will be treated as gain from the disposition of our common stock (the tax treatment of which is discussed below under "—Gain on Disposition of Common Stock").

Dividends paid to a non-U.S. holder generally will be subject to withholding of United States federal income tax at a 30% rate or such lower rate as may be specified by an applicable income tax treaty. However, dividends that are effectively connected with the conduct of a trade or business by the non-U.S. holder within the United States (and, if required by an applicable income tax treaty, are attributable to a United States permanent establishment) are not subject to the withholding tax, provided certain certification and disclosure requirements are satisfied. Instead, such dividends are subject to United States federal income tax on a net income basis in the same manner as if the non-U.S. holder were a United States person as defined under the Code. Any such effectively connected dividends received by a foreign corporation may be subject to an additional "branch profits tax" at a 30% rate or such lower rate as may be specified by an applicable income tax treaty.

A non-U.S. holder who wishes to claim the benefit of an applicable treaty rate and avoid backup withholding, as discussed below, for dividends will be required (a) to provide the applicable withholding agent with a properly executed Internal Revenue Service ("IRS") Form W-8BEN or Form W-8BEN-E (or other applicable form) certifying under penalty of perjury that such holder is not a United States person as defined under the Code and is eligible for treaty benefits or (b) if our common stock is held through certain foreign intermediaries, to satisfy the relevant certification requirements of applicable United States Treasury regulations. Special certification and other requirements apply to certain non-U.S. holders that are pass-through entities rather than corporations or individuals.

A non-U.S. holder eligible for a reduced rate of United States federal withholding tax pursuant to an income tax treaty may obtain a refund of any excess amounts withheld by timely filing an appropriate claim for refund with the IRS.

Gain on Disposition of Common Stock

Subject to the discussion of backup withholding below, any gain realized by a non-U.S. holder on the sale or other disposition of our common stock generally will not be subject to United States federal income tax unless:

- the gain is effectively connected with a trade or business of the non-U.S. holder in the United States (and, if required by an applicable income tax treaty, is attributable to a United States permanent establishment of the non-U.S. holder);
- the non-U.S. holder is an individual who is present in the United States for 183 days or more in the taxable year of that disposition, and certain other conditions are met; or
- we are or have been a "United States real property holding corporation" for United States federal income tax purposes and certain other conditions are met.

A non-U.S. holder described in the first bullet point immediately above will be subject to tax on the gain derived from the sale or other disposition in the same manner as if the non-U.S. holder were a United States person as defined under the Code. In addition, if any non-U.S. holder described in the first bullet point immediately above is a foreign corporation, the gain realized by such non-U.S. holder may be subject to an additional "branch profits tax" at a 30% rate or such lower rate as may be specified by an applicable income tax treaty. An individual non-U.S. holder described in the second bullet point immediately above will be subject to a 30% (or such lower rate as may be specified by an applicable income tax treaty) tax on the gain derived from the sale or other disposition, which gain may be offset by United States source capital losses even though the individual is not considered a resident of the United States.

Generally, a corporation is a "United States real property holding corporation" if the fair market value of its United States real property interests equals or exceeds 50% of the sum of the fair market value of its worldwide

real property interests and its other assets used or held for use in a trade or business (all as determined for United States federal income tax purposes). We believe we are not and do not anticipate becoming a "United States real property holding corporation" for United States federal income tax purposes. If, however, we are or become a "United States real property holding corporation," so long as our common stock is regularly traded on an established securities market during the calendar year in which the sale or other disposition occurs, only a non-U.S. holder who holds or held (at any time during the shorter of the five year period preceding the date of disposition or the holder's holding period) more than 5% of our common stock will be subject to United States federal income tax on the sale or other disposition of our common stock.

Federal Estate Tax

Common stock held by an individual non-U.S. holder at the time of death will be included in such holder's gross estate for United States federal estate tax purposes, unless an applicable estate tax treaty provides otherwise.

Information Reporting and Backup Withholding

Distributions paid to a non-U.S. holder and the amount of any tax withheld with respect to such distributions generally will be reported to the IRS. Copies of the information returns reporting such distributions and any withholding may also be made available to the tax authorities in the country in which the non-U.S. holder resides under the provisions of an applicable income tax treaty.

A non-U.S. holder will not be subject to backup withholding on dividends received if such holder certifies under penalty of perjury that it is a non-U.S. holder (and the payor does not have actual knowledge or reason to know that such holder is a United States person as defined under the Code), or such holder otherwise establishes an exemption.

Information reporting and, depending on the circumstances, backup withholding will apply to the proceeds of a sale or other disposition of our common stock made within the United States or conducted through certain United States-related financial intermediaries, unless the beneficial owner certifies under penalty of perjury that it is a non-U.S. holder (and the payor does not have actual knowledge or reason to know that the beneficial owner is a United States person as defined under the Code), or such owner otherwise establishes an exemption.

Backup withholding is not an additional tax and any amounts withheld under the backup withholding rules will be allowed as a refund or a credit against a non-U.S. holder's United States federal income tax liability provided the required information is timely furnished to the IRS.

Additional Withholding Requirements

Under Sections 1471 through 1474 of the Code (such Sections commonly referred to as "FATCA"), a 30% United States federal withholding tax may apply to any dividends paid on our common stock to (1) a "foreign financial institution" (as specifically defined in the Code) which does not provide sufficient documentation, typically on IRS Form W-8BEN-E, evidencing either (a) an exemption from FATCA, or (b) its compliance (or deemed compliance) with FATCA (which may alternatively be in the form of compliance with an intergovernmental agreement with the United States) in a manner which avoids withholding, or (2) a "non- financial foreign entity" (as specifically defined in the Code) which does not provide sufficient documentation, typically on IRS Form W-8BEN-E, evidencing either (a) an exemption from FATCA, or (b) adequate information regarding certain substantial United States beneficial owners of such entity (if any). If a dividend payment is both subject to withholding under FATCA and subject to the withholding tax discussed above under "—Dividends," the withholding under FATCA may be credited against, and therefore reduce, such other withholding tax. You should consult your own tax advisors regarding these requirements and whether they may be relevant to your ownership and disposition of our common stock.

CERTAIN ERISA CONSIDERATIONS

The following is a summary of certain considerations associated with the purchase of our common stock by (i) "employee benefit plans" within the meaning of Section 3(3) of the Employee Retirement Income Security Act of 1974, as amended ("ERISA") that are subject to Title I of ERISA, (ii) plans, individual retirement accounts and other arrangements that are subject to Section 4975 of the Code or provisions under any other federal, state, local, non-U.S. or other laws or regulations that are similar to such provisions of ERISA or the Code (collectively, "Similar Laws"), and (iii) entities which are deemed to hold the assets of any of the foregoing types of plans, accounts or arrangements (each of the foregoing described in clauses (i), (ii), and (iii) being referred to herein as a "Plan").

General fiduciary matters and prohibited transaction issues

ERISA and the Code impose certain duties on persons who are fiduciaries of a Plan subject to Title I of ERISA or Section 4975 of the Code (a "Covered Plan") and prohibit certain transactions involving the assets of a Covered Plan and its fiduciaries or other interested parties. Under ERISA and the Code, any person who exercises any discretionary authority or control over the administration of such a Covered Plan or the management or disposition of the assets of such a Covered Plan, or who renders investment advice for a fee or other compensation to such a Covered Plan, is generally considered to be a fiduciary of the Covered Plan.

Section 406 of ERISA and Section 4975 of the Code prohibit Covered Plans from engaging in specified transactions involving plan assets with persons or entities who are "parties in interest," within the meaning of ERISA, or "disqualified persons," within the meaning of Section 4975 of the Code, unless an exemption is available. The issuer and/or the underwriter, or any of their respective affiliates, may be a "party in interest" or a "disqualified person" within the meaning of ERISA and the Code. A party in interest or disqualified person who engaged in a non-exempt prohibited transaction may be subject to excise taxes and other penalties and liabilities under ERISA and the Code. In addition, the fiduciary of the Covered Plan that engaged in such a non-exempt prohibited transaction may be subject to penalties and liabilities under ERISA and the Code.

In considering an investment in our common stock with a portion of the assets of any Plan, a fiduciary should determine whether the investment is in accordance with the documents and instruments governing the Plan and the applicable provisions of ERISA, the Code or any Similar Law relating to a fiduciary's duty to the Plan, including without limitation, the prudence, diversification, delegation of control and prohibited transaction provisions of ERISA, the Code and any other applicable Similar Laws.

Government plans, foreign plans and certain church plans, while not subject to the fiduciary responsibility provisions of Title I of ERISA or the prohibited transaction provisions of Section 406 of ERISA or Section 4975 of the Code, may nevertheless be subject to Similar Laws. Fiduciaries of such Plans should consult with their counsel before acquiring shares of our common stock.

Representation

By its acceptance of our common stock, each purchaser and subsequent transferee will be deemed to have represented and warranted that either (i) no portion of the assets used by such purchaser or transferee to acquire our common stock constitutes assets of any Plan or (ii) the acquisition of our common stock by such purchaser or transferee will not constitute or result in a non-exempt prohibited transaction under Section 406 of ERISA or Section 4975 of the Code or a similar violation under any applicable Similar Laws.

The foregoing discussion is general in nature and is not intended to be all-inclusive. Due to the complexity of these rules and the penalties that may be imposed upon persons involved in non-exempt prohibited transactions, it is particularly important that fiduciaries or other persons considering purchasing our common stock on behalf of, or with the assets of, any Plan, consult with their counsel regarding the potential applicability of ERISA, Section 4975 of the Code or any Similar Law and whether an exemption would be required.

Neither this discussion nor anything provided in this prospectus is, or is intended to be, investment advice directed at any potential Plan purchasers, or at Plan purchasers generally, and such purchasers of our common stock should consult and rely on their own counsel and advisers as to whether an investment in our common stock is suitable for the Plan. The sale of our common stock to any Plan is in no respect a representation by us, an underwriter or any of our or their affiliates or representatives that such an investment meets all relevant legal requirements with respect to investments by Plans generally or any particular Plan, or that such investment is prudent or appropriate for Plans generally or any particular Plan.

UNDERWRITING (CONFLICTS OF INTEREST)

Subject to the terms and conditions stated in the underwriting agreement dated the date of this prospectus supplement, RBC Capital Markets has agreed to purchase, and the forward seller has agreed to sell to the underwriter, 6,700,000 shares of our common stock.

The underwriting agreement provides that the obligation of the underwriter to purchase the shares of our common stock included in this offering are subject to approval of certain legal matters by its counsel and to certain other customary conditions. The underwriter is obligated to purchase all of the shares of our common stock being offered pursuant to this prospectus supplement if it purchases any of such shares of our common stock. The offering of the shares of our common stock by the underwriter is subject to receipt and acceptance and to the underwriter's right to reject any order in whole or in part.

The underwriter may offer the shares from time to time to purchasers directly or through agents, or through brokers in brokerage transactions on the NYSE, in the over-the-counter market, or to dealers in negotiated transactions, or in a combination of such methods of sale or otherwise, at a fixed price or prices, which may be changed, or at market prices prevailing at the time of sale, at prices related to such prevailing market prices, or at negotiated prices. In connection with the sale of shares of our common stock, the underwriter may be deemed to have received compensation in the form of underwriting discounts. The underwriter may effect such transactions by selling shares to or through dealers, and such dealers may receive compensation in the form of discounts, concessions, or commissions from the underwriter and/or purchasers of shares for whom it may act as an agent or to whom it may sell as principal. The difference between the price at which the underwriter purchases shares and the price at which the underwriter resells such shares may be deemed underwriting compensation.

We estimate that the total expenses related to this offering will be approximately $700,000.

We have agreed to indemnify the underwriter, the forward purchaser and the forward seller against certain liabilities, including liabilities under the Securities Act, or to contribute to payments the underwriter, the forward seller or the forward purchaser may be required to make in respect of those liabilities.

Forward Sale Agreement

We have entered into a forward sale agreement on the date of this prospectus supplement with the forward purchaser, relating to 6,700,000 shares of our common stock. In connection with the execution of the forward sale agreement, and at our request, the forward seller is borrowing from third parties and selling in this offering 6,700,000 shares of our common stock.

If in the commercially reasonable judgment of the forward purchaser, it or its affiliate is unable to borrow, or it or its affiliate is unable to borrow at a stock loan rate not greater than a specified rate, and deliver for sale on the anticipated closing date, any shares of our common stock then the forward sale agreement will be terminated in its entirety. If in the commercially reasonable judgment of the forward purchaser, it or its affiliate is unable to borrow and deliver for sale on the anticipated closing date a number of shares of our common stock underlying the forward sale agreement, or it or its affiliate would be unable to borrow, at a stock loan rate not greater than a specified rate, and deliver for sale on the anticipated closing date such number of shares of our common stock, then we will issue and sell directly to the underwriter a number of shares of our common stock equal to the number of shares that the forward seller does not borrow and deliver, and the number of shares of our common stock to which the forward sale agreement relates will be reduced to the number that the forward seller can so borrow and deliver. In the event that the number of shares of our common stock to which the forward sale agreement relates is so reduced, the commitment of the underwriter to purchase shares of our common stock from the forward seller and the forward seller's obligation to borrow such shares for delivery and sale to the underwriter, as described above, will be replaced with the commitment to purchase from us and our

corresponding obligation to issue and sell directly to the underwriter all or such portion of the number of shares of our common stock not borrowed and delivered by the forward seller. In such event, we or the underwriter will have the right to postpone the closing date for up to three business days to effect any necessary changes to the documents or arrangements in connection with such closing.

We expect to receive net proceeds (after deducting estimated expenses) of approximately $307.5 million, subject to the price adjustment and other provisions of the forward sale agreement, in the event of full physical settlement of the forward sale agreement, which we expect to occur on or prior to August 10, 2021. For purposes of calculating the proceeds to us upon settlement of the forward sale agreement, we have assumed that the forward sale agreement is physically settled based upon the initial forward sale price of $46.00 per share on the effective date of the forward sale agreement, which will be August 11, 2020. We will not receive any proceeds under the forward sale agreement on the closing date of this offering. The actual proceeds from the forward sales are subject to the final settlement of the forward sale agreement. The forward sale price that we expect to receive upon physical settlement of the forward sale agreement is subject to adjustment on a daily basis based on a floating interest rate factor equal to the overnight bank funding rate less a spread and will be decreased based on amounts related to expected dividends on shares of our common stock during the term of the forward sale agreement, including the dividend declared on August 4, 2020 and having a record date of August 14, 2020. If the overnight bank funding rate is less than the spread on any day, the interest rate factor will result in a daily reduction of the forward sale price for such day.

The forward sale agreement provides for settlement on a settlement date or dates to be specified at our discretion, but which we expect to occur on or prior to August 10, 2021. On a settlement date or dates, if we decide to physically settle the forward sale agreement, we will issue shares of our common stock to the forward purchaser at the then-applicable forward sale price. The forward sale price will initially be $46.00 per share, which is the price at which the underwriter has agreed to buy the shares of common stock offered hereby. The forward sale agreement provides that the initial forward sale price will be subject to adjustment based on a floating interest rate factor equal to the overnight bank funding rate less a spread, and will be subject to decrease on each of certain dates specified in the forward sale agreement by amounts related to expected dividends on shares of our common stock during the term of the forward sale agreement. If the overnight bank funding rate is less than the spread on any day, the interest rate factor will result in a daily reduction of the forward sale price. As of the date of this prospectus supplement, the overnight bank funding rate is less than the spread, and if the overnight bank funding rate remains constant or decreases prior to the settlement of the forward sale agreement, we may receive less than the initial forward sale price per share upon physical settlement of the forward sale agreement.

Before the issuance of shares of our common stock, if any, upon settlement of the forward sale agreement, we expect that the shares issuable upon settlement of the forward sale agreement will be reflected in our diluted earnings per share calculation using the treasury stock method. Under this method, the number of shares of our common stock used in calculating diluted earnings per share is deemed to be increased by the excess, if any, of the number of shares of our common stock that would be issued upon full physical settlement of the forward sale agreement over the number of shares of common stock that could be purchased by us in the market (based on the average market price of our common stock during the applicable reporting period) using the proceeds receivable upon full physical settlement (based on the adjusted forward sale price at the end of the reporting period). Consequently, we anticipate there will be no dilutive effect on our earnings per share except during periods when the average market price of shares of our common stock is above the applicable adjusted forward sale price, which is initially $46.00 per share, subject to increase or decrease based on the overnight bank funding rate, less a spread, and subject to decrease by amounts related to expected dividends on shares of our common stock during the term of the forward sale agreement.

However, if we decide to physically settle or net share settle the forward sale agreement, delivery of shares of our common stock to the forward purchaser on any such physical settlement or net share settlement of the forward sale agreement would result in dilution to our earnings per share.

The forward purchaser will have the right to accelerate the forward sale agreement (or, in certain cases, the portion thereof that it determines is affected by the relevant event) and require us to physically settle the forward sale agreement on a date specified by the forward purchaser if:

- in the commercially reasonable judgment of the forward purchaser, it or its affiliate is unable to hedge its exposure to the transactions contemplated by the forward sale agreement because of the lack of sufficient shares of our common stock being made available for borrowing by stock lenders or it or its affiliate is unable to borrow such number of shares at a rate equal to or less than an agreed maximum stock loan rate;
- we declare any dividend, issue or distribution on shares of our common stock (i) payable in cash in excess of a specified amount or that otherwise constitutes an extraordinary dividend under the forward sale agreement, (ii) payable in securities of another company as a result of a spin-off or similar transaction, (iii) of any other type of securities (other than our common stock), rights, warrants or other assets for payment (cash or other consideration) at less than the prevailing market price, as reasonably determined by the forward purchaser or (iv) any other special dividend or distribution that is outside the normal course of our operations of normal dividend policies or practices;
- certain ownership thresholds applicable to the forward purchaser are exceeded;
- an event is announced that, if consummated, would result in an extraordinary event (as defined in the forward sale agreement) including, among other things, certain mergers and tender offers, as well as certain events such as a delisting of our common stock (each as more fully described in the forward sale agreement); or
- certain other events of default or termination events occur, including, among other things, any material misrepresentation made by us in connection with our entry into the forward sale agreement, our bankruptcy (except as described below) or certain changes in law (each as more fully described in the forward sale agreement).

The forward purchaser's decision to exercise its right to accelerate the forward sale agreement (or, in certain cases, the portion thereof that it determines is affected by the relevant event) and to require us to settle the forward sale agreement will be made irrespective of our interests, including our need for capital. In such cases, we could be required to issue and deliver shares of our common stock under the terms of the physical settlement provisions of the forward sale agreement irrespective of our capital needs, which would result in dilution to our earnings per share and may adversely affect the market price of our common stock. In addition, upon certain events of bankruptcy or insolvency related to us, the forward sale agreement will automatically terminate without further liability of either party to such agreement (other than in the event of a breach by us of certain representations or warranties contained in the forward sale agreement). Following any such termination, we would not issue any shares of common stock or receive any proceeds pursuant to the forward sale agreement.

The forward sale agreement will be physically settled, unless we elect to settle the forward sale agreement in cash or to net share settle the forward sale agreement (which we have the right to do, subject to certain conditions, other than in the limited circumstances described above). If we decide to physically settle or net share settle the forward sale agreement, delivery of shares of our common stock upon any physical settlement or net share settlement of the forward sale agreement will result in dilution to our earnings per share. If we elect cash or net share settlement for all or a portion of the shares of our common stock underlying the forward sale agreement, we would expect the forward purchaser or one of its affiliates to repurchase a number of shares of our common stock equal to the portion for which we elect cash or net share settlement in order to satisfy its obligation to return the shares of our common stock the forward purchaser or its affiliate had borrowed in connection with sales of our common stock under this prospectus supplement and, if applicable in connection with net share settlement, to deliver shares of our common stock to us. If the market value of our common stock at the time of such purchase is above the forward sale price at that time, we will pay or deliver, as the case may be, to the forward purchaser under the forward sale agreement, an amount in cash, or a number of shares of our common stock with a market value, equal to such difference. Any such difference could be significant.

Conversely, if the market value of our common stock at the time of such purchase is below the forward sale price at that time, the forward purchaser will pay or deliver, as the case may be, to us under the forward sale agreement, an amount in cash, or a number of shares of our common stock with a market value, equal to such difference.

In addition, the purchase of shares of our common stock by the forward purchaser or its affiliate to unwind the forward purchaser's hedge position could cause the market price of our common stock to increase over time, thereby increasing the amount of cash we would owe to the forward purchaser upon a cash settlement or increasing the number of shares of our common stock we would owe to the forward purchaser upon a net share settlement, as the case may be, of the forward sale agreement, or decreasing the amount of cash that the forward purchaser would owe us upon a cash settlement or decreasing the number of shares of our common stock that the forward purchaser would owe us upon a net share settlement, as the case may be, of the forward sale agreement. We will not be able to control the manner in which the forward purchaser unwinds its hedge positions.

The foregoing is a description of certain provisions, and their anticipated effects, of the forward sale agreement we have entered into in connection with this offering, a copy of which is available upon request from us at the address set forth in the section of the accompanying prospectus entitled "Where You Can Find More Information." This description of certain terms of the forward sale agreement is not complete and is subject to, and qualified in its entirety by reference to, the provisions of such agreement.

Our common stock is listed on the NYSE under the symbol "WTRG."

We and all of our continuing directors (as described in our Definitive Proxy Statement on Schedule 14A filed with the SEC on March 27, 2020) and officers, through entering into lock-up agreements, have agreed that, without the prior written consent of the underwriter, we and they will not, during the period ending 60 days after the date of this prospectus supplement (the "restricted period"): (i) offer, sell, contract to sell, pledge, grant any option to purchase, make any short sale or otherwise transfer or dispose of, directly or indirectly, our common stock, any options, rights or warrants to purchase our common stock or any securities convertible into or exchangeable for, or substantially similar to, our common stock (collectively, "restricted securities"); (ii) enter into any swap or other agreement that transfers to another, in whole or in part, any of the economic consequences of ownership of the common stock or any such other securities, whether any such transaction described in (i) or (ii) is to be settled by delivery of common stock or such other securities, in cash or otherwise or (iii) publicly disclose the intention to take any of the foregoing actions. In addition, we agreed not to file with the SEC any registration statement relating to any restricted securities, and our continuing directors and officers each agreed not to make any demand for, or exercise any right with respect to, the registration of any restricted securities, in each case during the restricted period and without the prior written consent of the underwriter.

The restrictions described in the immediately preceding paragraph do not apply to:

- the sale of the shares to the underwriter in this offering (including upon settlement of the forward sale agreement);
- the issuance by us of, or the receipt by our continuing directors and officers of, restricted securities pursuant to our existing employee equity or equity-based incentive plans, employee stock purchase plans or dividend reinvestment plans, or upon the conversion or exchange of convertible or exchangeable securities outstanding as of the date of this prospectus supplement;
- the filing by us of registration statements relating to securities issuable under our existing employee equity or equity-based plans or employee stock purchase plans;
- the issuance of shares of common stock in connection with certain investments, acquisitions, with joint ventures, commercial relationships or other strategic transactions, provided that the aggregate number of shares issued or issuable pursuant to this clause does not exceed 10% of the number of shares of common stock outstanding immediately after this offering and prior to such issuance;

- in the case of our continuing directors and officers, (i) the establishment of a trading plan pursuant to Rule 10b5-1 under the Exchange Act for the transfer of our common stock following expiration of the restricted period, (ii) transfers in accordance with the terms of existing trading plans pursuant to Rule 10b5-1 under the Exchange Act, (iii) certain transfers of shares held as of the date of this prospectus supplement through our existing 401(k) plan pursuant to portfolio balancing opportunities provided by the terms of such plan, (iv) transfers to us to satisfy certain tax obligations in connection with vesting of restricted stock units, restricted shares, performance share units or phantom shares and (v) certain other transfers to us;
- in the case of our continuing directors and officers, transfers to us upon death, disability or termination or employment, in each case, of such person;
- the receipt by us or our subsidiaries of shares (a) in the exercise of outstanding options, warrants, restricted stock units or other equity interests, including transfers deemed to occur upon the "net" or "cashless" exercise of options or (b) for the sole purpose of paying the exercise price of such options, warrants, restricted stock units or other equity interests or for paying taxes (including estimated taxes) due as a result of the exercise of such options, warrants, restricted stock units or other equity interests or as a result of the vesting of shares under restricted stock awards or restricted stock units pursuant to our existing employee benefit plans disclosed herein relating to this public offering, in each case on a "cashless" or "net exercise" basis, provided that any such shares received upon such exercise shall be subject to the terms of the lock-up agreement;
- tenders, sales or other transfers pursuant to a bona fide third-party tender offer, merger, consolidation or other similar transaction made to all holders of restricted securities involving a "change of control" of us (provided that if such transaction is not consummated, our continuing directors' and officers' shares shall remain subject to the restrictions set forth in the lock-up agreements);
- the exercise for cash of options to purchase shares disclosed as outstanding herein, provided that any such shares received upon such exercise shall be subject to the terms of the lock-up agreements;
- in the case of our continuing directors and officers, the disposition of shares acquired in this offering or in open market transactions after completion of this offering; and
- transfers of shares or other of our securities pursuant to an order of a court or regulatory agency or to comply with any regulations related to ownership by our continuing directors and officers of their shares.

The underwriter, in its sole discretion, may release the common stock and other securities subject to the lock-up agreements described above in whole or in part at any time.

In order to facilitate the offering of the shares, the underwriter may engage in transactions that stabilize, maintain or otherwise affect the price of the shares. Specifically, the underwriter may sell more shares than it is obligated to purchase under the underwriting agreement, creating a naked short position. The underwriter must close out any naked short position by purchasing shares of our common stock in the open market. A naked short position is more likely to be created if the underwriter is concerned that there may be downward pressure on the price of the shares in the open market after pricing that could adversely affect investors who purchase in this offering. As an additional means of facilitating this offering, the underwriter may bid for, and purchase, shares of our common stock in the open market to stabilize the price of the shares. These activities may raise or maintain the market price of the shares above independent market levels or prevent or retard a decline in the market price of the shares. The underwriter is not required to engage in these activities and may end any of these activities at any time.

Conflicts of Interest

The underwriter and its affiliates are full-service financial institutions engaged in various activities, which may include securities trading, commercial and investment banking, financial advisory, investment management, investment research, principal investment, hedging, financing and brokerage activities. The underwriter and its affiliates have, from time to time, performed, and may in the future perform, various financial advisory and investment banking services for us, for which they received or will receive customary fees and expenses. For example, RBC Capital Markets, LLC acted as a financial adviser in connection with the Peoples Acquisition, for which they received customary fees and expenses. The underwriter and/or its affiliates are also lenders and/or agents under certain of our credit facilities, including the Revolving Credit Facility, and receive customary fees and expenses in connection therewith.

In addition, in the ordinary course of its various business activities, the underwriter and its affiliates may make or hold a broad array of investments and actively trade debt and equity securities (or related derivative securities) and financial instruments (including bank loans) for their own account and for the accounts of their customers and may at any time hold long and short positions in such securities and instruments. Such investment and securities activities may involve our securities and instruments. The underwriter and/or its affiliates have lending relationships with us and may hedge their credit exposure to us consistent with their customary risk management policies. Typically, the underwriter and its affiliates would hedge such exposure by entering into transactions which consist of either the purchase of credit default swaps or the creation of short positions in our securities or the securities of our affiliates. Any such credit default swaps or short positions could adversely affect future trading prices of the shares offered hereby. The underwriter and its affiliates may also make investment recommendations or publish or express independent research views in respect of such securities or instruments and may at any time hold, or recommend to clients that they acquire, long or short positions in such securities and instruments.

All of the proceeds of this offering (excluding proceeds to us with respect to any shares of common stock that we may issue and sell directly to the underwriter in lieu of the forward seller selling our common stock to the underwriter) will be paid to the forward purchaser (or its affiliate). Because RBC Capital Markets, or its affiliate, will receive more than 5% of the net proceeds of this offering, not including underwriting compensation, RBC Capital Markets is deemed to have a conflict of interest within the meaning of FINRA Rule 5121. Accordingly, this offering will be conducted in compliance with the applicable requirements of FINRA Rule 5121. Pursuant to that rule, the appointment of a “qualified independent underwriter” is not required in connection with this offering, as the shares of our common stock have a “bona fide public market” (as such terms are defined in FINRA Rule 5121). In accordance with FINRA Rule 5121, RBC Capital Markets may not confirm any sales to any account over which it exercises discretionary authority without the prior written approval of the transaction from the account holder.

Selling Restrictions

Canada

The shares may be sold only to purchasers purchasing, or deemed to be purchasing, as principal that are accredited investors, as defined in National Instrument 45-106 Prospectus Exemptions or subsection 73.3(1) of the Securities Act (Ontario), and are permitted clients, as defined in National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations. Any resale of the shares must be made in accordance with an exemption from, or in a transaction not subject to, the prospectus requirements of applicable securities laws.

Securities legislation in certain provinces or territories of Canada may provide a purchaser with remedies for rescission or damages if this prospectus supplement (including any amendment thereto) contains a misrepresentation, provided that the remedies for rescission or damages are exercised by the purchaser within the time limit prescribed by the securities legislation of the purchaser’s province or territory. The purchaser should

refer to any applicable provisions of the securities legislation of the purchaser's province or territory for particulars of these rights or consult with a legal advisor.

Pursuant to section 3A.3 (or, in the case of securities issued or guaranteed by the government of a non-Canadian jurisdiction, section 3A.4) of National Instrument 33-105 Underwriting Conflicts (NI 33-105), the underwriter is not required to comply with the disclosure requirements of NI 33-105 regarding underwriter conflicts of interest in connection with this offering.

Prohibition of Sales to European Economic Area and United Kingdom Retail Investors

The shares are not intended to be offered, sold or otherwise made available to and should not be offered, sold or otherwise made available to any retail investor in the European Economic Area (the "EEA") or in the United Kingdom. For these purposes, a retail investor means a person who is one (or more) of: (i) a retail client as defined in point (11) of Article 4(1) of Directive 2014/65/EU (as amended, "MiFID II"); or (ii) a customer within the meaning of Directive (EU) 2016/97 (as amended or superseded, the "Insurance Distribution Directive"), where that customer would not qualify as a professional client as defined in point (10) of Article 4(1) of MiFID II; or (iii) not a qualified investor as defined in Regulation (EU) 2017/1129 (as amended or superseded, the "Prospectus Regulation"). Consequently, no key information document required by Regulation (EU) No 1286/2014 (as amended, the "PRIIPs Regulation") for offering or selling the shares or otherwise making them available to retail investors in the EEA or in the United Kingdom has been prepared and therefore offering or selling the shares or otherwise making them available to any retail investor in the EEA or in the United Kingdom may be unlawful under the PRIIPs Regulation. This prospectus supplement and the accompanying prospectus have been prepared on the basis that any offer of the shares in any Member State of the EEA or in the United Kingdom will be made pursuant to an exemption under the Prospectus Regulation from the requirement to publish a prospectus for offers of the shares. This prospectus supplement and the accompanying prospectus are not a prospectus for the purposes of the Prospectus Regulation.

United Kingdom

In addition, this document is being distributed only to, and is directed only at, and any offer subsequently made may only be directed at: (i) in the United Kingdom, persons having professional experience in matters relating to investments falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005, as amended (the "Order"), and/or persons falling within Article 49(2)(a) to (d) of the Order; (ii) persons who are outside the United Kingdom; and (iii) any other persons to whom it may otherwise lawfully be distributed (all such persons together being referred to as "relevant persons"). This document must not be acted on or relied on by persons who are not relevant persons. Any investment or investment activity to which this document relates is available only to, and will be engaged in only with, relevant persons.

Australia

No placement document, prospectus, product disclosure statement or other disclosure document has been lodged with the Australian Securities and Investments Commission ("ASIC") in relation to the offering. This prospectus supplement, the accompanying prospectus and any other offering or marketing material relating to the shares or this offering do not constitute a prospectus, product disclosure statement or other disclosure document under the prospectus, product disclosure statement or other disclosure document under the Corporations Act 2001 (Cth) (the "Corporations Act"), and do not purport to include the information required for a prospectus, product disclosure statement or other disclosure document under the Corporations Act.

Any offer in Australia of the shares may only be made to persons (the "Exempt Investors") who are "sophisticated investors" (within the meaning of section 708(8) of the Corporations Act), "professional investors" (within the meaning of section 708(11) of the Corporations Act) or otherwise pursuant to one or more exemptions contained in section 708 of the Corporations Act so that it is lawful to offer the shares without disclosure to investors under Chapter 6D of the Corporations Act.

The shares applied for by Exempt Investors in Australia must not be offered for sale in Australia for a period of 12 months after the date of allotment under the offering, except in circumstances where disclosure to investors under Chapter 6D of the Corporations Act would not be required pursuant to an exemption under section 708 of the Corporations Act or otherwise or where the offer is pursuant to a disclosure document which complies with Chapter 6D of the Corporations Act. Any person acquiring shares must observe such Australian on-sale restrictions.

This prospectus supplement and the accompanying prospectus contain general information only and do not take account of the investment objectives, financial situation or particular needs of any particular person. They do not contain any securities recommendations or financial product advice. Before making an investment decision, investors need to consider whether the information in this prospectus supplement and the accompanying prospectus is appropriate to their needs, objectives and circumstances, and, if necessary, seek expert advice on those matters.

Hong Kong

The shares may not be offered or sold in Hong Kong by means of any document other than (i) in circumstances which do not constitute an offer to the public within the meaning of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32, Laws of Hong Kong), or (ii) to "professional investors" within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder, or (iii) in other circumstances which do not result in the document being a "prospectus" within the meaning of the Companies Ordinance (Cap. 32, Laws of Hong Kong) and no advertisement, invitation or document relating to the shares may be issued or may be in the possession of any person for the purpose of issue (in each case whether in Hong Kong or elsewhere), which is directed at, or the contents of which are likely to be accessed or read by, the public in Hong Kong (except if permitted to do so under the laws of Hong Kong) other than with respect to shares which are or are intended to be disposed of only to persons outside Hong Kong or only to "professional investors" within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder.

Japan

The shares have not been and will not be registered under the Financial Instruments and Exchange Act of Japan (Act No. 25 of 1948, as amended) (the "FIEA"). The shares may not be offered or sold, directly or indirectly, in Japan or to or for the benefit of any resident of Japan (including any person resident in Japan or any corporation or other entity organized under the laws of Japan) or to others for reoffering or resale, directly or indirectly, in Japan or to or for the benefit of any resident of Japan, except pursuant to an exemption from the registration requirements of the FIEA and otherwise in compliance with any relevant laws, regulations and ministerial guidelines of Japan.

Korea

Neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the shares or the offering should be construed in any way as our (or any of our affiliates or agents) soliciting investment or offering to sell the shares in the Republic of Korea ("Korea"). We are not making any representation with respect to the eligibility of any recipients of this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the shares or the offering to acquire the shares under the laws of Korea, including, without limitation, the Financial Investment Services and Capital Markets Act (the "FSCMA"), the Foreign Exchange Transaction Act (the "FETA"), and any regulations thereunder. The shares have not been registered with the Financial Services Commission of Korea (the "FSC") in any way pursuant to the FSCMA, and the shares may not be offered, sold or delivered, or offered or sold to any person for reoffering or resale, directly or indirectly, in Korea or to any resident of Korea except pursuant to applicable laws and regulations of Korea. Furthermore, the shares may not be resold to any Korean resident

unless such Korean resident as the purchaser of the resold shares complies with all applicable regulatory requirements (including, without limitation, reporting or approval requirements under the FETA and regulations thereunder) relating to the purchase of the resold shares.

Singapore

Neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the shares or the offering has been registered as a prospectus with the Monetary Authority of Singapore. Accordingly, neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the shares or the offering may be circulated or distributed, nor may the shares be offered or sold, or be made the subject of an invitation for subscription or purchase, whether directly or indirectly, to persons in Singapore, other than (a) to an institutional investor under Section 274 of the Securities and Futures Act, Chapter 289 of Singapore (the "SFA"), (b) to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions specified in Section 275 of the SFA or (c) pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA.

Where the shares are subscribed or purchased under Section 275 by a relevant person which is: (i) a corporation (which is not an accredited investor) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or (ii) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary is an accredited investor, shares, debentures and units of shares and debentures of that corporation or the beneficiaries' rights and interest in that trust shall not be transferable for six months after that corporation or that trust has acquired the shares under Section 275 except: (1) to an institutional investor under Section 274 of the SFA or to a relevant person, or any person pursuant to Section 275(1A) or Section 276(4)(i)(B), and in accordance with the conditions, specified in Section 275 of the SFA; (2) where no consideration is given for the transfer; (3) by operation of law, (4) as specified in Section 276(7) of the SFA or (5) as specified in Regulation 37A of the Securities and Futures (Offers of Investments) (Securities and Securities-based Derivatives Contracts) Regulations 2018 of Singapore.

Solely for the purposes of its obligations pursuant to sections 309B(1)(a) and 309B(1)(c) of the SFA, we have determined, and hereby notify all relevant persons (as defined in Section 309A of the SFA) that the shares are "prescribed capital markets products" (as defined in the Securities and Futures (Capital Markets Products) Regulations 2018) and Excluded Investment Products (as defined in MAS Notice SFA 04-N12: Notice on the Sale of Investment Products and MAS Notice FAA-N16: Notice on Recommendations on Investment Products).

Switzerland

The shares may not be publicly offered in Switzerland and will not be listed on the SIX Swiss Exchange ("*SIX*") or on any other exchange or regulated trading facility in Switzerland. This prospectus supplement, the accompanying prospectus and any other offering or marketing material relating to the shares or this offering do not constitute a prospectus within the meaning of and have been prepared without regard to the disclosure standards for issuance prospectuses under art. 652a or art. 1156 of the Swiss Code of Obligations or the disclosure standards for listing prospectuses under art. 27 ff. of the SIX Listing Rules or the listing rules of any other exchange or regulated trading facility in Switzerland.

Neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the shares or the offering may be publicly distributed or otherwise made publicly available in Switzerland. Neither this prospectus supplement, the accompanying prospectus nor any other offering or marketing material relating to the offering, the Company or the shares has been or will be filed with or approved by any Swiss regulatory authority. In particular, this prospectus supplement and the accompanying prospectus will not be filed with, and the offer of shares will not be supervised by, the Swiss Financial Market Supervisory Authority, and the offer of shares has not been and will not be authorized under the Swiss Federal Act on

Collective Investment Schemes (the "*CISA*"). The investor protection afforded to acquirers of interests in collective investment schemes under the CISA does not extend to acquirers of the shares.

Taiwan

The shares have not been and will not be registered or filed with, or approved by, the Financial Supervisory Commission of Taiwan and/or any other regulatory authority of Taiwan pursuant to relevant securities laws and regulations and may not be sold, issued or offered within Taiwan through a public offering or in circumstances which could constitute an offer within the meaning of the Securities and Exchange Act of Taiwan or relevant laws and regulations that require a registration, filing or approval of the Financial Supervisory Commission of Taiwan and/or other regulatory authority of Taiwan. No person or entity in Taiwan has been authorized to offer or sell the shares in Taiwan.

United Arab Emirates

The shares have not been, and are not being, publicly offered, sold, promoted or advertised in the United Arab Emirates (including the Abu Dhabi Global Market and the Dubai International Financial Centre) other than in compliance with the laws, regulations and rules of the United Arab Emirates, the Abu Dhabi Global Market and the Dubai International Financial Centre governing the issue, offering and sale of securities. Further, this prospectus supplement, the accompanying prospectus and any other offering or marketing material relating to the shares or the offering do not constitute a public offer of securities in the United Arab Emirates (including the Abu Dhabi Global Market and the Dubai International Financial Centre) and are not intended to be a public offer. This prospectus supplement, the accompanying prospectus and any other offering or marketing material relating to the shares or the offering have not been approved by or filed with the Central Bank of the United Arab Emirates, the Securities and Commodities Authority, the Financial Services Regulatory Authority or the Dubai Financial Services Authority.

LEGAL MATTERS

Certain legal matters will be passed upon for us by Simpson Thacher & Bartlett LLP, New York, New York. Ballard Spahr LLP, Philadelphia, Pennsylvania will issue an opinion regarding certain matters of Pennsylvania law, including the validity of the securities offered by the prospectus supplement. Certain legal matters will be passed upon for the underwriter by Cravath, Swaine & Moore LLP, New York, New York.

EXPERTS

The financial statements and management's assessment of the effectiveness of internal control over financial reporting (which is included in Management's Report on Internal Control over Financial Reporting) incorporated in this prospectus supplement by reference to the Annual Report on Form 10-K for the year ended December 31, 2019 have been so incorporated in reliance on the report of PricewaterhouseCoopers LLP, an independent registered public accounting firm, given on the authority of said firm as experts in auditing and accounting.

The consolidated financial statements of LDC Funding LLC as of December 31, 2019 and 2018 and for each of the three years in the period ended December 31, 2019, incorporated by reference in this prospectus supplement and in the accompanying prospectus from Essential Utilities' Current Report on Form 8-K/A filed on April 13, 2020, have been audited by Deloitte & Touche LLP, independent auditors, as stated in their report, which is incorporated by reference herein, and are incorporated in reliance upon the report of such firm given upon their authority as experts in accounting and auditing.

WHERE YOU CAN FIND ADDITIONAL INFORMATION; INCORPORATION OF CERTAIN DOCUMENTS BY REFERENCE

We file annual, quarterly and current reports, proxy statements and other information with the SEC. The SEC maintains a website at *www.sec.gov* that contains periodic and current reports, proxy and information statements, and other information regarding registrants that are filed electronically with the SEC.

These documents are also available, free of charge, through the Investors section of our website, which is located at *www.essential.co*. Information contained on our website is not incorporated by reference into this prospectus supplement or the accompanying prospectus and you should not consider information on our website to be part of this prospectus supplement or the accompanying prospectus.

We have filed with the SEC a "shelf" registration statement on Form S-3 under the Securities Act of 1933 relating to the securities that may be offered by this prospectus supplement. This prospectus supplement is a part of that registration statement, but does not contain all of the information in the registration statement. We have omitted certain parts of the registration statement in accordance with rules and regulations of the SEC. Statements made in this prospectus supplement as to the contents of any contract, agreement or other documents are not necessarily complete, and, in each instance, we refer you to a copy of such document filed as an exhibit to the registration statement, of which this prospectus supplement is a part, or otherwise filed with the SEC. For more detail about us and any securities that may be offered by this prospectus supplement, you may examine the registration statement on Form S-3 and the exhibits filed with it at the locations listed in the previous paragraph.

The SEC allows us to "incorporate by reference" into this prospectus supplement and the accompanying prospectus the information we file with them, which means that we can disclose important information to you by referring you to those documents. The information incorporated by reference is considered to be part of this prospectus supplement. When we file information with the SEC in the future, that information will automatically update and supersede this information. We incorporate by reference the documents listed below and any future

filings we will make with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934 until we sell all of the securities covered by this prospectus supplement or this offering is terminated; provided, however, that we are not incorporating, in each case, any portions of documents or information furnished or deemed to have been furnished and not filed in accordance with SEC rules:

- Our Annual Report on Form 10-K for the year ended December 31, 2019 filed with the SEC on February 28, 2020;
- Our Quarterly Reports on Form 10-Q for the quarter ended March 31, 2020 filed with the SEC on May 8, 2020 and the quarter ended June 30, 2020 filed with the SEC on August 6, 2020;
- The portions of our Definitive Proxy Statement on Schedule 14A filed with the SEC on March 27, 2020, that are incorporated by reference into our Annual Report on Form 10-K for the fiscal year ended December 31, 2019;
- Our Current Reports on Form 8-K filed with the SEC on January 16, 2020, February 3, 2020, February 27, 2020 (solely Item 8.01 and related exhibits), March 16, 2020, April 3, 2020, April 13, 2020, April 15, 2020, May 11, 2020 and May 18, 2020 and our Current Reports on Form 8-K/A filed with the SEC on March 18, 2020, April 13, 2020 and August 10, 2020, each of which amended our Current Report on Form 8-K filed with the SEC on March 16, 2020; and
- The description of our common stock set forth in our Registration Statement on Form 8-A, including any amendments or reports filed for the purpose of updating such description.

These documents contain important business and financial information about us that is not included in or delivered with this prospectus supplement. You may request a copy of any or all documents that we incorporate by reference at no cost, by writing or telephoning us at:

Essential Utilities, Inc.
762 W. Lancaster Avenue
Bryn Mawr, PA 19010-3489
Telephone: 610-527-8000
Attention: Corporate Secretary

We have not, and the underwriter and the forward seller have not, authorized anyone to provide you with any information other than that contained or incorporated by reference in this prospectus supplement, the accompanying prospectus or in any free writing prospectus we may provide to you in connection with this offering. Neither we nor the underwriter or the forward seller take any responsibility for, or provide any assurances as to the reliability of, any additional or different information that others may give you. You should assume that the information contained in this prospectus supplement, the accompanying prospectus and any free writing prospectus we may provide to you in connection with this offering is accurate only as of their respective dates or as of the respective dates specified in such information, as applicable, and the information contained in documents incorporated by reference is accurate only as of the respective dates of those documents or as of the respective dates specified in such information, as applicable, in each case regardless of the time of delivery of this prospectus supplement or the accompanying prospectus or any such free writing prospectus or any sale of the shares of our common stock. Our business, financial condition, results of operations and prospects may have changed since those dates.

Any statement contained herein or in a document incorporated or deemed to be incorporated by reference herein shall be deemed to be modified or superseded for purposes of this prospectus supplement to the extent that a statement contained herein, in any other subsequently filed document which also is or is deemed to be incorporated by reference herein or in the accompanying prospectus, modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified and superseded, to constitute a part of this prospectus supplement.

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PROSPECTUS

AQUA AMERICA, INC.

Common Stock
Preferred Stock
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Debt Securities

Aqua America, Inc. may, from time to time, in one or more offerings, offer and sell common stock, preferred stock, common stock purchase contracts, warrants, units, depositary shares and debt securities. The debt securities and preferred stock may be convertible into or exchangeable or exercisable for other securities. We will provide specific terms of any offering and the offered securities in supplements to this prospectus. The prospectus supplements may also add, update or change information contained in this prospectus.

We may offer and sell these securities to or through underwriters, dealers or agents, directly to purchasers or through a combination of these methods. If an offering of securities involves any underwriters, dealers or agents, then the names of the underwriters, dealers or agents and the terms of the arrangements with such entities will be stated in an accompanying prospectus supplement.

Our common stock is listed on the New York Stock Exchange under the symbol "WTR." We have not yet determined whether any of the other securities that may be offered by this prospectus will be listed on any exchange, inter-dealer quotation system or over-the-counter market. If we decide to seek listing of any such securities upon issuance, an accompanying prospectus supplement will disclose the exchange, quotation system or market on which the securities will be listed.

The prospectus may not be used to sell our securities unless it is accompanied by a prospectus supplement.

Investing in our securities involves risk. Before you invest, you should carefully read and evaluate the risk factors and other information included in this prospectus and any applicable prospectus supplement, including the documents incorporated by reference. See "Risk Factors" beginning on page 6 of this prospectus.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is February 28, 2018.

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ABOUT THIS PROSPECTUS

This document is called a prospectus and is part of a registration statement that we filed with the Securities and Exchange Commission (SEC) using a "shelf" registration process. Under this shelf process, we may, from time to time, in one or more offering, offer and sell common stock, preferred stock, common stock purchase contracts, warrants, units, depositary shares and debt securities. This prospectus provides you with a general description of the securities we may offer. Each time we sell any securities under this prospectus, we will provide a prospectus supplement that will contain specific information about the terms of that offering and the offered securities. That prospectus supplement may include a discussion of any risk factors or other special considerations applicable to those securities. The prospectus supplement also may add, update or change information contained in this prospectus. You should read both this prospectus and the applicable prospectus supplement and the exhibits filed with our registration statement together with the additional information described below under the heading "Where You Can Find More Information" before you decide whether to invest in the securities.

The registration statement (including the exhibits) of which this prospectus is a part contains additional information about us and the securities we may offer by this prospectus. Specifically, we have filed certain legal documents that control the terms of the securities offered by this prospectus as exhibits to the registration statement. We will file certain other legal documents that will control the terms of the securities we may offer by this prospectus as exhibits to the registration statement or to reports we file with the SEC. The registration statement and the reports can be read at the SEC website or at the SEC offices mentioned under the heading "Where You Can Find More Information."

You should rely only upon the information contained in, or incorporated by reference into, this prospectus and the applicable prospectus supplement that contains specific information about the securities we are offering. We have not authorized any other person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should assume that the information appearing in this document is accurate only as of the date on the front cover of this document. Our business, financial condition, results of operations and prospects may have changed since that date.

Except as otherwise provided in this prospectus, unless the context otherwise requires, references in this prospectus to "Aqua America," "we," "us" or "our" refer to Aqua America, Inc. and its direct and indirect subsidiaries. In addition, references to "Aqua Pennsylvania" refer to our wholly-owned subsidiary, Aqua Pennsylvania, Inc., and its subsidiaries.

FORWARD-LOOKING STATEMENTS

Certain statements in this prospectus, or incorporated by reference into this prospectus, are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 and are made based upon, among other things, our current assumptions, expectations, plans, and beliefs concerning future events and their potential effect on us. These forward-looking statements involve risks, uncertainties and other factors, many of which are outside our control, that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. In some cases you can identify forward-looking statements where statements are preceded by, followed by, or include the words "believes," "expects," "anticipates," "plans," "future," "potential," "probably," "predictions," "intends," "will," "continue" or the negative of such terms or similar expressions. Forward-looking statements in this prospectus, or incorporated by reference into this prospectus, include, but are not limited to, statements regarding:

- recovery of capital expenditures and expenses in rates;

- projected capital expenditures and related funding requirements;
- our capability to pursue timely rate increase requests;
- the availability and cost of capital financing;
- developments, trends and consolidation in the water and wastewater utility and infrastructure industries;
- dividend payment projections;
- opportunities for future acquisitions, both within and outside the water and wastewater industry, the success of pending acquisitions and the impact of future acquisitions;
- the capacity of our water supplies, water facilities and wastewater facilities;
- the impact of federal and/or state tax laws or policies and the regulatory treatment of the effects of those laws or policies, including the Tax Cuts and Jobs Act;
- the impact of geographic diversity on our exposure to unusual weather;
- the impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer;
- our authority to carry on our business without unduly burdensome restrictions;
- the continuation of investments in strategic ventures;
- our ability to obtain fair market value for condemned assets;
- the impact of fines and penalties;
- the impact of changes in and compliance with governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- the impact of decisions of governmental and regulatory bodies, including decisions to raise or lower rates;
- the development of new services and technologies by us or our competitors;
- the availability of qualified personnel;
- the condition of our assets;
- the impact of legal proceedings;
- general economic conditions;
- acquisition-related costs and synergies;
- the sale of water and wastewater divisions; and
- the amount of income tax deductions for qualifying utility asset improvements and the Internal Revenue Service’s ultimate acceptance of the deduction methodology.

Because forward-looking statements involve risks and uncertainties, there are important factors that could cause actual results to differ materially from those expressed or implied by these forward-looking statements, including but not limited to:

- changes in general economic, business, credit and financial market conditions;
- changes in governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- the profitability of future acquisitions;

- changes to the rules or our assumptions underlying our determination of what qualifies for an income tax deduction for qualifying utility asset improvements;
- the decisions of governmental and regulatory bodies, including decisions on rate increase requests;
- our ability to file rate cases on a timely basis to minimize regulatory lag;
- abnormal weather conditions, including those that result in water use restrictions;
- changes in, or unanticipated, capital requirements;
- changes in our credit rating or the market price of our common stock;
- changes in valuation of strategic ventures;
- our ability to integrate businesses, technologies or services which we may acquire;
- our ability to manage the expansion of our business;
- our ability to treat and supply water or collect and treat wastewater;
- the extent to which we are able to develop and market new and improved services;
- the effect of the loss of major customers;
- our ability to retain the services of key personnel and to hire qualified personnel as we expand;
- labor disputes;
- increasing difficulties in obtaining insurance and increased cost of insurance;
- cost overruns relating to improvements to, or the expansion of, our operations;
- increases in the costs of goods and services;
- civil disturbance or terroristic threats or acts;
- the continuous and reliable operation of our information technology systems, including the impact of cyber security attacks or other cyber-related events;
- changes in accounting pronouncements;
- litigation and claims; and
- changes in environmental conditions, including the effects of climate change.

Given these risks and uncertainties, you should not place undue reliance on any forward-looking statements. You should read this prospectus and the documents that we incorporate by reference into this prospectus completely and with the understanding that our actual future results, performance and achievements may be materially different from what we expect. These forward-looking statements represent assumptions, expectations, plans and beliefs only as of the date of this prospectus. Except for our ongoing obligations to disclose certain information under the federal securities laws, we are not obligated, and assume no obligation, to update these forward-looking statements, even though our situation may change in the future. For further information or other factors which could affect our financial results and such forward-looking statements, see “Risk Factors.” We qualify all of our forward-looking statements by these cautionary statements.

AQUA AMERICA, INC.

Aqua America, Inc. is the holding company for regulated utilities providing water or wastewater services to an estimated three million people in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana, and Virginia. Our largest operating subsidiary is Aqua Pennsylvania, Inc., which accounted for approximately

52% of our operating revenues and approximately 74% of our net income for 2017. As of December 31, 2017, Aqua Pennsylvania provided water or wastewater services to approximately one-half of the total number of people we serve. Aqua Pennsylvania's service territory is located in the suburban areas in counties north and west of the City of Philadelphia and in 27 other counties in Pennsylvania. Our other regulated utility subsidiaries provide similar services in seven other states. In addition, the Company's market-based activities are conducted through Aqua Infrastructure, LLC and Aqua Resources Inc. Aqua Infrastructure provides non-utility raw water supply services for firms in the natural gas drilling industry. Aqua Resources provides water and wastewater service through two operating and maintenance contracts with municipal authorities close to our utility companies' service territory; and offers, through a third party, water and wastewater line repair service and protection solutions to households. In 2017, we completed the sale of business units that are reported within Aqua Resources, which installed and tested devices that prevent the contamination of potable water and repaired water and wastewater systems, and repaired and performed maintenance on water and wastewater systems. Additionally, during 2016, we completed the sale of business units within Aqua Resources, which provided liquid waste hauling and disposal services and inspection, and cleaning and repair of storm and sanitary wastewater lines.

Aqua America, which prior to its name change in 2004 was known as Philadelphia Suburban Corporation, was formed in 1968 as a holding company for its primary subsidiary, Aqua Pennsylvania, formerly known as Philadelphia Suburban Water Company. In the early 1990s, we embarked on a growth through acquisition strategy focused on water and wastewater operations. Our most significant transactions to date have been the merger with Consumers Water Company in 1999, the acquisition of the regulated water and wastewater operations of AquaSource, Inc. in 2003, the acquisition of Heater Utilities, Inc. in 2004, and the acquisition of American Water Works Company, Inc.'s regulated water and wastewater operations in Ohio in 2012. Since the early 1990s, our business strategy has been primarily directed toward the regulated water and wastewater utility industry, where we have more than quadrupled the number of regulated customers we serve, and have extended our regulated operations from southeastern Pennsylvania to include our current regulated utility operations throughout Pennsylvania and in seven other states. During 2010 through 2013, we sold our utility operations in six states, pursuant to a portfolio rationalization strategy to focus our operations in areas where we have critical mass and economic growth potential. Currently, the Company seeks to acquire businesses in the U.S. regulated sector, which includes water and wastewater utilities and other regulated utilities, and to pursue growth ventures in market-based activities, such as infrastructure opportunities that are supplementary and complementary to our regulated businesses.

Our growth in revenues over the past five years is primarily a result of increases in water and wastewater rates and customer growth. The increase in our utility customer base has been due to customers added through acquisitions, partnerships with developers, and organic growth (excluding dispositions) as shown below:

Year	Utility Customer Growth Rate
2017	1.1%
2016	1.6%
2015	1.9%
2014	1.3%
2013	1.3%

In 2017, our customer count increased by 10,584 customers, primarily due to utility systems that we acquired and organic growth. Overall, for the five-year period of 2013 through 2017, our utility customer base, adjusted to exclude customers associated with utility system dispositions, increased at an annual compound rate of 1.4%. During the five-year period ended December 31, 2017, our utility customer base including customers associated with utility system acquisitions and dispositions increased from 968,357 at January 1, 2013 to 982,849 at December 31, 2017. This five-year period includes the impact of the condemnation of our Fort Wayne, IN system in 2014, which resulted in the loss of approximately 13,000 connections.

Our principal executive office is located at 762 W. Lancaster Avenue, Bryn Mawr, Pennsylvania 19010-3489, and our telephone number is 610-527-8000. Our website may be accessed at www.aquaamerica.com. The references to our website and the SEC's website are intended to be inactive textual references only, and the contents of those websites are not incorporated by reference herein and should not be considered part of this prospectus.

RISK FACTORS

Investing in our securities involves risks. Please see the risk factors described under the section captioned “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2017, as such risk factors may be updated from time to time in filings we make with the SEC subsequent to the date hereof. Before making an investment decision, you should carefully consider these risk factors, together with all other information contained in or incorporated by reference into this prospectus or any applicable prospectus supplement (which includes information contained in certain filings we make with the SEC subsequent to the date hereof as set forth in the section below captioned “Where You Can Find More Information”). Please also refer to the section above captioned “Forward-Looking Statements.”

USE OF PROCEEDS

Unless we otherwise specify in the applicable prospectus supplement, we intend to use the net proceeds from the sale of the securities we may offer by this prospectus to fund our capital expenditures, to provide capital for our growth strategy, which includes potential future acquisitions of municipally owned and investor-owned water and wastewater systems, regulated utilities and infrastructure projects, and market-based activities complementary to our regulated business, to fund the integration of any businesses that we acquire into our existing business, and to purchase and maintain plant equipment, as well as for working capital and other general corporate purposes. Our management will have broad discretion in the allocation of net proceeds from the sale of any securities sold by us.

CERTAIN RATIOS

Our ratio of earnings to fixed charges and ratio of earnings to combined fixed charges and preferred stock dividends for the periods indicated below were as follows:

	Year Ended December 31,				
	2017	2016	2015	2014	2013
Ratio of earnings to fixed charges	3.90	4.17	4.15	4.05	3.79
Ratio of earnings to combined fixed charges and preferred stock dividends	3.90	4.17	4.15	4.05	3.79

The ratios of earnings to fixed charges and the ratios of earnings to combined fixed charges and preferred stock dividends were computed by dividing our earnings by fixed charges and by combined fixed charges and preferred stock dividends, respectively. For the purpose of these computations, earnings include the sum of income from continuing operations before income taxes and non-controlling interest, and fixed charges, less capitalized interest. Fixed charges consist of interest on all indebtedness, whether expensed or capitalized, amortization of debt expense, and the estimated interest attributable to rental and lease expense calculated using an assumed interest factor of 33% of rental and lease expense.

DESCRIPTION OF CAPITAL STOCK

As of February 13, 2018 our authorized capital stock was 301,770,819 shares, consisting of:

- 300,000,000 shares of common stock, par value $0.50 per share, of which 177,750,505 shares were outstanding; and
- 1,770,819 shares of preferred stock, par value $1.00 per share, of which no shares were outstanding.

The following summary of certain terms of our common stock and preferred stock is qualified in its entirety by the provisions of our articles of incorporation and bylaws each of which is incorporated by reference as an exhibit to the registration statement of which this prospectus constitutes a part.

Common Stock

This section describes the general terms of our common stock. For more detailed information, you should refer to our articles of incorporation and bylaws, including any amendments thereto, copies of which have been filed with the SEC. These documents are incorporated by reference into this prospectus.

Voting Rights

Holders of our common stock are entitled to one vote for each share held by them at all meetings of the shareholders and are not entitled to cumulate their votes for the election of directors.

Dividend Rights and Limitations

Holders of our common stock may receive dividends when declared by our board of directors. Because we are a holding company, the funds we use to pay any dividends on our common stock are derived predominantly from the dividends that we receive from our subsidiaries and the dividends they receive from their subsidiaries. Therefore, our ability to pay dividends to holders of our common stock depends upon our subsidiaries' earnings, financial condition and ability to pay dividends. Most of our subsidiaries are subject to regulation by state utility commissions and the amounts of their earnings and dividends are affected by the manner in which they are regulated. In addition, they are subject to restrictions on the payment of dividends contained in their various debt agreements. Under our most restrictive debt agreements, the amount available for payment of dividends to us as of December 31, 2017 was approximately $1.4 billion of Aqua Pennsylvania's retained earnings and $143 million of the retained earnings of certain other subsidiaries. Payment of dividends on our common stock is also subject to the preferential rights of the holders of any outstanding preferred stock.

Liquidation Rights

In the event that we liquidate, dissolve or wind-up, the holders of our common stock are entitled to share ratably in all of the assets that remain after we pay our liabilities. This right is subject, however, to the prior distribution rights of any outstanding preferred stock.

Preferred Stock

Our board of directors has the authority, from time to time and without further action by our shareholders, to divide our unissued capital stock into one or more classes and one or more series within any class and to make determinations of the designation and number of shares of any class or series and determinations of the voting rights, preferences, limitations and special rights, if any, of the shares of any class or series. The rights, preferences, limitations and special rights of different classes of capital stock may differ with respect to dividend rates, amounts payable on liquidation, voting rights, conversion rights, redemption provisions, sinking fund provisions and other matters. The rights, preferences, privileges and restrictions of each series may be fixed by the designations of that series set forth in either a restated version of our articles of incorporation or a certificate of designations relating to that series, which will be filed with the SEC as an exhibit to or incorporated by reference in the registration statement of which this prospectus constitutes a part.

The issuance of preferred stock may be perceived by some as possibly having the effect of delaying, deferring or preventing a change of control of us without further action by our shareholders. The issuance of preferred stock with voting and conversion rights may also adversely affect the voting power of the holders of our common stock. In certain circumstances, an issuance of preferred stock could possibly have the effect of decreasing the market price of our common stock.

Whenever preferred stock is to be sold pursuant to this prospectus, we will file a prospectus supplement relating to that sale which will specify:

- the number of shares in the series of preferred stock;

- the designation for the series of preferred stock by number, letter or title that will distinguish the series from any other series of preferred stock;
- the dividend rate, if any, and whether dividends on that series of preferred stock will be cumulative, noncumulative or partially cumulative;
- the voting rights of that series of preferred stock, if any;
- any conversion provisions applicable to that series of preferred stock;
- any redemption or sinking fund provisions applicable to that series of preferred stock;
- any preemptive rights provisions applicable to that series of preferred stock;
- the liquidation preference per share of that series of preferred stock; and
- the terms of any other preferences or rights, if any, applicable to that series of preferred stock.

Anti-Takeover Provisions

Pennsylvania State Law Provisions

Under Section 1712 of the Pennsylvania Business Corporation Law of 1988, as amended (PBCL), which is applicable to us, directors stand in a fiduciary relation to their corporation and, as such, are required to perform their duties in good faith, in a manner they reasonably believe to be in the best interests of the corporation and with such care, including reasonable inquiry, skill and diligence, as a person of ordinary prudence would use under similar circumstances. Under Section 1715 of the PBCL, in discharging their duties, directors may, in considering the best interests of their corporation, consider various constituencies, including, shareholders, employees, suppliers, customers and creditors of the corporation, and upon communities in which offices or other establishments of the corporation are located. Directors are not required to give prominent consideration to the interests of any particular constituency. Absent a breach of fiduciary duty, a lack of good faith or self-dealing, any act of the board of directors, a committee thereof or an individual director is presumed to be in the best interests of the corporation. Actions by directors relating to an acquisition or potential acquisition of control of the corporation are not subject to any greater obligation to justify, or higher burden of proof, than is applied to any other acts of directors. The PBCL expressly provides that the fiduciary duty of directors does not require them to (i) redeem or otherwise render inapplicable outstanding rights issued under any shareholder rights plan; (ii) render inapplicable the anti-takeover statutes set forth in Chapter 25 of the PBCL (described below); or (iii) take any action solely because of the effect it may have on a proposed acquisition or the consideration to be received by shareholders in such a transaction. In addition, Section 2513 of the PBCL specifically validates shareholder rights plans, or “poison pills,” and the discriminatory dilution provisions contained in such plans.

Chapter 25 of the PBCL contains several anti-takeover statutes applicable to publicly-traded corporations. Corporations may opt-out of such anti-takeover statutes under certain circumstances. We have not opted-out of any of such statutes.

Section 2538 of Subchapter 25D of the PBCL requires certain transactions with an “interested shareholder” to be approved by a majority of disinterested shareholders. “Interested shareholder” is defined broadly to include any shareholder who is a party to the transaction or who is treated differently than other shareholders and affiliates of the interested shareholder.

Subchapter 25E of the PBCL requires a person or group of persons acting in concert which acquires 20% or more of the voting shares of the corporation to offer to purchase the shares of any other shareholder at “fair value.” “Fair value” means the value not less than the highest price paid per share by the controlling person or group during the 90-day period prior to the control transaction, plus a control premium. Among other exceptions, Subchapter 25E does not apply to shares acquired directly from the corporation in a transaction exempt from the registration requirements of the Securities Act of 1933, or to a one-step merger.

Subchapter 25F of the PBCL generally establishes a 5-year moratorium on a "business combination" with an "interested shareholder." "Interested shareholder" is defined generally to be any beneficial owner of 20% or more of the corporation's voting stock or an affiliate or associate of the corporation that at any time within the prior five-year period was a beneficial owner of 20% or more of the corporation's voting stock. "Business combination" is defined broadly to include mergers, consolidations, asset sales and certain self-dealing transactions. Certain restrictions apply to business combination following the 5-year period. Among other exceptions, Subchapter 25F will be rendered inapplicable if the board of directors approves the proposed business combination, or approves the interested shareholder's acquisition of 20% of the voting shares, in either case prior to the date on which the shareholder first becomes an interested shareholder.

Subchapter 25G of the PBCL provides that "control shares" lose voting rights unless such rights are restored by the affirmative vote of a majority of (i) the disinterested shares (generally, shares held by persons other than the acquiror, executive officers of the corporation and certain employee stock plans) and (ii) the outstanding voting shares of the corporation. "Control shares" are defined as shares which, upon acquisition, will result in a person or group acquiring for the first time voting control over (a) 20%, (b) 33 1/3% or (c) 50% or more of the outstanding shares, together with shares acquired within 180 days of attaining the applicable threshold and shares purchased with the intention of attaining such threshold. A corporation may redeem control shares if the acquiring person does not request restoration of voting rights as permitted by Subchapter 25G. Among other exceptions, Subchapter 25G does not apply to a merger, consolidation or a share exchange if the corporation is a party to the transaction agreement.

Subchapter 25H of the PBCL provides in certain circumstances for the recovery by the corporation of profits realized from the sale of its stock by a controlling person or group if the sale occurs within 18 months after the controlling person or group became a controlling person or group, and the stock was acquired during such 18-month period or within 24 months before such period. A controlling person or group is a person or group that has acquired, offered to acquire, or publicly disclosed an intention to acquire 20% or more of the voting shares of the corporation or a person or group that has otherwise publicly disclosed or caused to be disclosed that it may seek to acquire control of the corporation through any means. Among other exceptions, Subchapter 25H does not apply to transactions approved by both the board of directors and the shareholders prior to the acquisition or distribution, as appropriate.

Subchapter 25I of the PBCL mandates severance compensation for eligible employees who are terminated within 24 months after the approval of a control-share acquisition. Eligible employees generally are all employees employed in Pennsylvania for at least two years prior to the control-share approval. Severance equals the weekly compensation of the employee multiplied by the employee's years of service (up to 26 years), less payments made due to the termination.

Subchapter 25J of the PBCL requires the continuation of certain labor contracts relating to business operations owned at the time of a control-share approval.

Articles of Incorporation and Bylaw Provisions

Certain provisions of our articles of incorporation and bylaws may have the effect of discouraging unilateral tender offers or other attempts to take over and acquire our business. These provisions might discourage some potentially interested purchaser from attempting a unilateral takeover bid for us on terms which some shareholders might favor. Our articles of incorporation require that certain fundamental transactions must be approved by the holders of 75% of the outstanding shares of our capital stock entitled to vote on the matter unless at least a majority of the members of the board of directors has approved the transaction, in which case the required shareholder approval will be the minimum approval required by applicable law. The fundamental transactions that are subject to this provision are those transactions that require approval by shareholders under applicable law or the articles of incorporation. These transactions include certain amendments of our articles of incorporation or bylaws, certain sales or other dispositions of our assets, certain issuances of our capital stock, or

certain transactions involving our merger, consolidation, division, reorganization, dissolution, liquidation or winding up. Our articles of incorporation and bylaws provide that:

- a special meeting of shareholders may only be called by the chairman, the president, the board of directors or shareholders entitled to cast a majority of the votes which all shareholders are entitled to cast at the particular meeting;
- nominations for election of directors may be made by any shareholder entitled to vote for election of directors if the name of the nominee and certain information relating to the nominee is filed with our corporate secretary not less than 14 days nor more than 50 days before any meeting of shareholders to elect directors; and
- certain advance notice procedures must be met for shareholder proposals to be made at annual meetings of shareholders. These advance notice procedures generally require a notice to be delivered not less than 90 days nor more than 120 days before the anniversary date of the immediately preceding annual meeting of shareholders.

Transfer Agent and Registrar

The transfer agent and registrar for our common stock is Computershare Trust Company, N.A.

DESCRIPTION OF COMMON STOCK PURCHASE CONTRACTS

We may issue stock purchase contracts, representing contracts entitling or obligating holders to purchase from us, and us to sell to the holders, a specified number of shares or amount of common stock at a future date or dates. The price per share of common stock may be fixed at the time each contract is issued or may be determined by reference to a specific formula set forth in the contract. Each common stock purchase contract may be issued separately or as a part of a unit, each consisting of a common stock purchase contract and, as security for the holder's obligation to purchase the common stock under the contract, the following:

- our senior debt securities or subordinated debt securities described under "Description of Debt Securities;"
- debt obligations of third parties, including U.S. Treasury securities;
- any other asset as security described in the applicable prospectus supplement; or
- any combination of the foregoing.

Each common stock purchase contract may require us to make periodic payments to the holder of the unit or vice versa, and such payments may be unsecured or prefunded on some basis discussed in the applicable prospectus supplement. Each common stock purchase contract may require holders to secure their obligations thereunder in a specified manner and, in certain circumstances, we may deliver a newly issued prepaid common stock purchase contract, which is referred to as a "prepaid security," upon release to a holder of any collateral securing such holder's obligations under the original contract.

The applicable prospectus supplement will describe the terms of any common stock purchase contract and, if applicable, prepaid security. The description in the prospectus supplement will not purport to be complete and will be qualified in its entirety by reference to the contracts, the collateral arrangements and depositary arrangements, if applicable, relating to such contracts and, if applicable, the prepaid securities and the documents pursuant to which such prepaid securities will be issued. The applicable prospectus supplement will also describe the material United States federal income tax considerations applicable to the common stock purchase contracts.

DESCRIPTION OF WARRANTS

General

The following summary of certain provisions of the warrants does not purport to be complete and is subject to, and qualified in its entirety by reference to, the provisions of the warrant agreement that will be filed with the SEC in connection with the offering of such warrants.

We may issue warrants for the purchase of debt securities, preferred stock or common stock. Warrants may be issued independently or together with debt securities, preferred stock or common stock offered by any prospectus supplement and may be attached to or separate from any such offered securities. Each series of warrants will be issued under a separate warrant agreement to be entered into between the Company and a bank or trust company, as warrant agent. The warrant agent will act solely as the Company's agent in connection with the warrants and will not assume any obligation or relationship of agency or trust for or with any holders or beneficial owners of warrants.

Debt Warrants

The prospectus supplement relating to a particular issue of debt warrants will describe the terms of such debt warrants, including the following: (a) the title of such debt warrants; (b) the offering price for such debt warrants, if any; (c) the aggregate number of such debt warrants; (d) the designation and terms of the debt securities purchasable upon exercise of such debt warrants; (e) if applicable, the designation and terms of the debt securities with which such debt warrants are issued and the number of such debt warrants issued with each such debt security; (f) if applicable, the date from and after which such debt warrants and any debt securities issued therewith will be separately transferable; (g) the principal amount of debt securities purchasable upon exercise of a debt warrant and the price at which such principal amount of debt securities may be purchased upon exercise (which price may be payable in cash, securities, or other property); (h) the date on which the right to exercise such debt warrants shall commence and the date on which such right shall expire; (i) if applicable, the minimum or maximum amount of such debt warrants that may be exercised at any one time; (j) whether the debt warrants represented by the debt warrant certificates or debt securities that may be issued upon exercise of the debt warrants will be issued in registered or bearer form; (k) information with respect to book-entry procedures, if any; (1) the currency or currency units in which the offering price, if any, and the exercise price are payable; (m) if applicable, a discussion of material United States federal income tax considerations; (n) the anti-dilution provisions of such debt warrants, if any; (o) the redemption or call provisions, if any, applicable to such debt warrants; (p) any provisions for changes to or adjustments in the exercise price for the debt warrants and (q) any additional terms of such debt warrants, including terms, procedures, and limitations relating to the exchange and exercise of such debt warrants.

Stock Warrants

The prospectus supplement relating to any particular issue of preferred stock warrants or common stock warrants will describe the terms of such warrants, including the following: (a) the title of such warrants; (b) the offering price for such warrants, if any; (c) the aggregate number of such warrants; (d) the designation and terms of the common stock or preferred stock purchasable upon exercise of such warrants; (e) if applicable, the designation and terms of the offered securities with which such warrants are issued and the number of such warrants issued with each such offered security; (f) if applicable, the date from and after which such warrants and any offered securities issued therewith will be separately transferable; (g) the number of shares of common stock or preferred stock purchasable upon exercise of a warrant and the price at which such shares may be purchased upon exercise; (h) the date on which the right to exercise such warrants shall commence and the date on which such right shall expire; (i) if applicable, the minimum or maximum amount of such warrants that may be exercised at any one time; (j) the currency or currency units in which the offering price, if any, and the exercise price are payable, (k) if applicable, a discussion of material United States federal income tax considerations; (l) the anti-dilution provisions of such warrants, if any; (m) the redemption or call provisions, if any, applicable

to such warrants; (m) any provisions for changes to or adjustments in the exercise price for the stock warrants and (n) any additional terms of such warrants, including terms, procedures and limitations relating to the exchange and exercise of such warrants.

DESCRIPTION OF UNITS

We may, from time to time, issue units comprised of one or more of the other securities that may be offered under this prospectus, in any combination. Each unit will be issued so that the holder of the unit is also the holder of each security included in the unit. Thus, the holder of a unit will have the rights and obligations of a holder of each included security. The unit agreement under which a unit is issued may provide that the securities included in the unit may not be held or transferred separately at any time, or at any time before a specified date.

The applicable prospectus supplement will describe the terms of any unit. The description in the prospectus supplement will not purport to be complete and will be qualified in its entirety by reference to units, the collateral arrangements and depositary arrangements, if applicable, relating to such units and, if applicable, the prepaid securities and the documents pursuant to which such prepaid securities will be issued. The applicable prospectus supplement will also describe the material United States federal income tax considerations applicable to the units.

DESCRIPTION OF DEPOSITORY SHARES

We may, at our option, offer fractional shares of our preferred stock, rather than whole shares of our preferred stock. In the event we do so, we will issue receipts for depositary shares, each of which will represent a fraction (to be set forth in the prospectus supplement relating to offering of the depositary shares) of a share of the related series of preferred stock.

The shares of our preferred stock represented by depositary shares will be deposited under a deposit agreement between us and a bank or trust company selected by us having its principal office in the United States and that meets certain other requirements. Subject to the terms of the deposit agreement, each owner of a depositary share will be entitled, in proportion to the applicable fraction of a share of preferred stock, represented by the depositary share to all of the rights and preferences of the preferred stock represented by the depositary shares (including dividend, voting, redemption, conversion and liquidation rights).

The above description of depositary shares is only a summary, is not complete and is subject to, and is qualified in its entirety by the description in the applicable prospectus supplement and the provisions of the deposit agreement, which will contain the form of depository receipt. A copy of the deposit agreement will be filed with the SEC as an exhibit to or incorporated by reference in the registration statement of which this prospectus is a part.

DESCRIPTION OF DEBT SECURITIES

Please note that in this section entitled “Description of Debt Securities,” references to “we,” “us,” “ours” or “our” refer only to Aqua America, Inc. and not to its consolidated subsidiaries. Also, in this section, references to “holders” mean those who own debt securities registered in their own names, on the books that we maintain or the trustee maintains for this purpose, and not those who own beneficial interests in debt securities registered in street name or in debt securities issued in book-entry form through one or more depositaries. Owners of beneficial interests in the debt securities should read the section below entitled “Book-Entry Procedures and Settlement.”

General

The debt securities offered by this prospectus will be our unsecured obligations, except as otherwise set forth in an accompanying prospectus supplement, and will be either senior or subordinated debt. We will issue senior debt under a senior debt indenture, and we will issue subordinated debt under a subordinated debt indenture. We sometimes refer to the senior debt indenture and the subordinated debt indenture, individually, as an indenture and, collectively, as the indentures. We have filed forms of the indentures with the SEC as exhibits to the registration statement of which this prospectus forms a part. You can obtain copies of the indentures by following the directions outlined in "Where You Can Find More Information," or by contacting the applicable indenture trustee.

A form of each debt security, reflecting the particular terms and provisions of a series of offered debt securities, will be filed with the SEC at the time of the offering and incorporated by reference as exhibits to the registration statement of which this prospectus forms a part.

The following briefly summarizes certain material provisions that may be included in the indentures. Other terms, including pricing and related terms, will be disclosed for a particular issuance in an accompanying prospectus supplement. You should read the more detailed provisions of the applicable indenture, including the defined terms, for provisions that may be important to you. You should also read the particular terms of a series of debt securities, which will be described in more detail in an accompanying prospectus supplement. So that you may easily locate the more detailed provisions, the numbers in parentheses below refer to sections in the applicable indenture or, if no indenture is specified, to sections in each of the indentures. Wherever particular sections or defined terms of the applicable indenture are referred to, such sections or defined terms are incorporated into this prospectus by reference, and the statement in this prospectus is qualified by that reference.

The trustee under each indenture will be determined at the time of issuance of debt securities, and the name of the trustee will be provided in an accompanying prospectus supplement.

The indentures provide that our senior or subordinated debt securities may be issued in one or more series, with different terms, in each case as we authorize from time to time. We also have the right to "reopen" a previous issue of a series of debt securities by issuing additional debt securities of such series without the consent of the holders of debt securities of the series being reopened or any other series. Any additional debt securities of the series being reopened will have the same ranking, interest rate, maturity and other terms as the previously issued debt securities of that series. These additional debt securities, together with the previously issued debt securities of that series, will constitute a single series of debt securities under the terms of the applicable indenture.

Types of Debt Securities

We may issue fixed or floating rate debt securities. Fixed rate debt securities will bear interest at a fixed rate described in the prospectus supplement. This type includes zero coupon debt securities, which bear no interest and are often issued at a price lower than the principal amount. United States federal income tax consequences and other special considerations applicable to any debt securities issued at a discount will be described in the applicable prospectus supplement.

Upon the request of the holder of any floating rate debt security, the calculation agent will provide the interest rate then in effect for that debt security, and, if determined, the interest rate that will become effective on the next interest reset date. The calculation agent's determination of any interest rate, and its calculation of the amount of interest for any interest period, will be final and binding in the absence of manifest error.

All percentages resulting from any interest rate calculation relating to a debt security will be rounded upward or downward, as appropriate, to the next higher or lower one hundred-thousandth of a percentage point.

All amounts used in or resulting from any calculation relating to a debt security will be rounded upward or downward, as appropriate, to the nearest cent, in the case of U.S. dollars, or to the nearest corresponding hundredth of a unit, in the case of a currency other than U.S. dollars, with one-half cent or one-half of a corresponding hundredth of a unit or more being rounded upward.

In determining the base rate that applies to a floating rate debt security during a particular interest period, the calculation agent may obtain rate quotes from various banks or dealers active in the relevant market, as described in the prospectus supplement. Those reference banks and dealers may include the calculation agent itself and its affiliates, as well as any underwriter, dealer or agent participating in the distribution of the relevant floating rate debt securities and its affiliates.

Information in the Prospectus Supplement

The prospectus supplement for any offered series of debt securities will describe the following terms, as applicable:

- the title;
- whether the debt is senior or subordinated;
- whether the debt securities are secured or unsecured and, if secured, the collateral securing the debt;
- the total principal amount offered;
- the percentage of the principal amount at which the debt securities will be sold and, if applicable, the method of determining the price;
- the maturity date or dates;
- whether the debt securities are fixed rate debt securities or floating rate debt securities;
- if the debt securities are fixed rate debt securities, the yearly rate at which the debt security will bear interest, if any, and the interest payment dates;
- if the debt security is an original issue discount debt security, the yield to maturity;
- if the debt securities are floating rate debt securities, the interest rate basis; any applicable index currency or maturity, spread or spread multiplier or initial, maximum or minimum rate; the interest reset, determination, calculation and payment dates, and the day count used to calculate interest payments for any period;
- the date or dates from which any interest will accrue, or how such date or dates will be determined, and the interest payment dates and any related record dates;
- if other than in U.S. dollars, the currency or currency unit in which payment will be made;
- the denominations in which the currency or currency unit of the securities will be issuable if other than denominations of $1,000 and integral multiples thereof;
- the terms and conditions on which the debt securities may be redeemed at our option;
- any obligation we may have to redeem, purchase or repay the debt securities at the option of a holder upon the happening of any event and the terms and conditions of redemption, purchase or repayment;
- the names and duties of the trustee and any co-trustees, depositaries, authenticating agents, calculation agents, paying agents, transfer agents or registrars for the debt securities;
- any material provisions of the applicable indenture described in this prospectus that do not apply to the debt securities;
- a discussion of United States federal income tax, accounting and special considerations, procedures and limitations with respect to the debt securities;

- whether and under what circumstances we will pay additional amounts to holders in respect of any tax assessment or government charge, and, if so, whether we will have the option to redeem the debt securities rather than pay such additional amounts; and
- any other specific terms of the debt securities that are consistent with the provisions of the indenture.

The terms on which a series of debt securities may be convertible into or exchangeable for other of our securities or any other entity will be set forth in the prospectus supplement relating to such series. Such terms will include provisions as to whether conversion or exchange is mandatory, at the option of the holder or at our option. The terms may include provisions pursuant to which the number of other securities to be received by the holders of such series of debt securities may be adjusted.

We will issue the debt securities only in registered form. As currently anticipated, debt securities of a series will trade in book-entry form, and global notes will be issued in physical (paper) form, as described below under “Book-Entry Procedures and Settlement.” Unless otherwise provided in the accompanying prospectus supplement, we will issue debt securities denominated in U.S. dollars and only in denominations of $1,000 and integral multiples thereof.

The prospectus supplement relating to offered debt securities denominated in a foreign or composite currency will specify the denomination of the offered debt securities.

The debt securities may be presented for exchange, and debt securities other than a global security may be presented for registration of transfer, at the principal corporate trust office of the trustee named in the applicable prospectus supplement. Holders will not have to pay any service charge for any registration of transfer or exchange of debt securities, but we may require payment of a sum sufficient to cover any tax or other governmental charge payable in connection with such registration of transfer (Section 3.05).

Payment and Paying Agents

Distributions on the debt securities other than those represented by global notes will be made in the designated currency against surrender of the debt securities at the principal corporate trust office of the trustee named in the applicable prospectus supplement. Payment will be made to the registered holder at the close of business on the record date for such payment. Interest payments will be made at the principal corporate trust office of the trustee named in the applicable prospectus supplement, or by a check mailed to the holder at his registered address. Payments in any other manner will be specified in the applicable prospectus supplement.

Calculation Agents

Calculations relating to floating rate debt securities and indexed debt securities will be made by the calculation agent, an institution that we appoint as our agent for this purpose. We may appoint one of our affiliates as calculation agent. We may appoint a different institution to serve as calculation agent from time to time after the original issue date of the debt security without your consent and without notifying you of the change. The initial calculation agent will be identified in the applicable prospectus supplement.

Senior Debt

We may issue senior debt securities under the senior debt indenture. Senior debt will constitute our unsecured and unsubordinated obligations and will rank on a basis equal in priority with all our other unsecured and unsubordinated debt.

Subordinated Debt

We may issue subordinated debt securities under the subordinated debt indenture. Subordinated debt will constitute our unsecured and subordinated obligations and will be junior in right of payment to our senior debt

(including senior debt securities), which is defined as "senior indebtedness" in the subordinated debt indenture (Section 16.01).

If we default in the payment of any principal of, or premium, if any, or interest on any senior debt when it becomes due and payable after any applicable grace period, then, unless and until the default is cured or waived or ceases to exist, we cannot make a payment on account of or redeem or otherwise acquire the subordinated debt securities (Section 16.04).

If there is any insolvency, bankruptcy, liquidation or other similar proceeding relating to us or our property, then all senior debt must be paid in full before any payment may be made to any holders of subordinated debt securities (Section 16.02).

Furthermore, if we default in the payment of the principal of and accrued interest on any subordinated debt securities that is declared due and payable upon an event of default under the subordinated debt indenture, holders of all our senior debt will first be entitled to receive payment in full in cash before holders of such subordinated debt can receive any payments (Section 16.03).

Except as may be otherwise set forth in an accompanying prospectus supplement, senior debt means:

- the principal, premium, if any, and interest in respect of indebtedness for money borrowed and indebtedness evidenced by securities, notes, debentures, bonds or other similar instruments issued, including, as to us, the senior debt securities;
- all capitalized lease obligations;
- all obligations representing the deferred purchase price of property; and
- all deferrals, renewals, extensions and refundings of obligations of the type referred to above (Section 1.01 of Subordinated Indenture).

However, senior debt does not include:

- the subordinated debt securities (Section 16.01 of Subordinated Indenture);
- any indebtedness that by its terms is subordinated to, or ranks in priority on an equal basis with, subordinated debt securities (Section 1.01 of Subordinated Indenture); and
- items of indebtedness (other than capitalized lease obligations) that would not appear as liabilities on a balance sheet prepared in accordance with accounting principles generally accepted in the United States of America.

Covenants

The accompanying prospectus supplement will contain any covenants applicable to the debt securities.

Modification of the Indentures

The indentures will provide that we and the relevant trustee may enter into supplemental indentures to establish the form and terms of any new series of debt securities without obtaining the consent of any holder of debt securities (Section 9.01).

We and the trustee may, with the consent of the holders of at least a majority in aggregate outstanding principal amount of the debt securities of a series, modify the applicable indenture or the rights of the holders of the securities of such series (Section 9.02).

No such modification may, without the consent of each holder of an affected security:

- extend the fixed maturity of any such security;
- reduce the rate or change the time of payment of interest on such security;
- reduce the principal amount of such securities or the premium, if any, on such security;
- change any obligation of ours to pay additional amounts with respect to such security;
- reduce the amount of the principal payable on acceleration of such security if issued originally at a discount;
- adversely affect the right of repayment or repurchase of such security at the option of the holder;
- reduce or postpone any sinking fund or similar provision with respect to such security;
- change the currency or currency unit in which such security is payable or the right of selection thereof;
- impair the right to sue for the enforcement of any payment with respect to such security on or after the maturity of such security;
- reduce the percentage of the aggregate outstanding principal amount of debt securities of the series referred to above whose holders need to consent to the modification or a waiver without the consent of such holders; or
- change any obligation of ours with respect to such security to maintain an office or agency.

Defaults

Except as may be otherwise set forth in an accompanying prospectus supplement, each indenture will provide that events of default regarding any series of debt securities will be:

- our failure to pay for 30 days required interest on any debt security of such series;
- our failure to pay principal or premium, if any, on any debt security of such series when due;
- our failure to make any required scheduled installment payment for 30 days on debt securities of such series;
- our failure to perform for 90 days after notice any other covenant in the relevant indenture other than a covenant included in the relevant indenture solely for the benefit of a series of debt securities other than such series; and
- certain events of bankruptcy or insolvency, whether voluntary or not (Section 5.01).

Except as may be otherwise set forth in an accompanying prospectus supplement, if an event of default regarding debt securities of any series issued under the indentures should occur and be continuing, either the trustee or the holders of 25% in the principal amount of outstanding debt securities of such series may declare each debt security of that series due and payable (Section 5.02). We may be required to file annually with the trustee a statement of an officer as to the fulfillment by us of our obligations under the indenture during the preceding year.

No event of default regarding one series of debt securities issued under an indenture is necessarily an event of default regarding any other series of debt securities.

Holders of a majority in aggregate principal amount of the outstanding debt securities of any series will be entitled to control certain actions of the trustee under the indentures and to waive past defaults regarding such series (Sections 5.12 and 5.13). The holders of debt securities generally will not be able to require the trustee to take any action, unless one or more of such holders provides to the trustee reasonable security or indemnity (Section 6.02).

If an event of default occurs and is continuing regarding a series of debt securities, the trustee may use any sums that it holds under the relevant indenture for its own reasonable compensation and expenses incurred prior to paying the holders of debt securities of such series (Section 5.06).

Before any holder of any series of debt securities may institute action for any remedy, except payment on such holder's debt security when due, the holders of not less than 25% in principal amount of the debt securities of that series outstanding must request the trustee to take action. Holders must also offer and give the satisfactory security and indemnity against liabilities incurred by the trustee for taking such action (Section 5.07).

Defeasance

Except as may otherwise be set forth in an accompanying prospectus supplement, after we have deposited with the trustee, cash or government securities, in trust for the benefit of the holders sufficient to pay the principal of, premium, if any, and interest on the debt securities of such series when due, and satisfied certain other conditions, including receipt of an opinion of counsel that holders will not recognize taxable gain or loss for United States federal income tax purposes, then:

- we will be deemed to have paid and satisfied our obligations on all outstanding debt securities of such series, which is known as defeasance and discharge (Section 14.02); or
- we will cease to be under any obligation, other than to pay when due the principal of, premium, if any, and interest on such debt securities, relating to the debt securities of such series, which is known as covenant defeasance (Section 14.03).

When there is a defeasance and discharge, the applicable indenture will no longer govern the debt securities of such series, we will no longer be liable for payments required by the terms of the debt securities of such series and the holders of such debt securities will be entitled only to the deposited funds. When there is a covenant defeasance, however, we will continue to be obligated to make payments when due if the deposited funds are not sufficient.

Governing Law

Unless otherwise stated in the prospectus supplement, the debt securities and the indentures will be governed by Pennsylvania law (Section 1.12).

Concerning the Trustee Under the Indentures

We may have banking and other business relationships with the trustee named in the prospectus supplement, or any subsequent trustee, in the ordinary course of business.

Form, Exchange and Transfer

We will issue debt securities only in registered form; no debt securities will be issued in bearer form (Section 2.03). We will issue each debt security in book-entry form only, unless otherwise specified in the applicable prospectus supplement. We will issue any common stock issuable upon conversion of any debt security being offered in both certificated and book-entry form, unless otherwise specified in the applicable prospectus supplement. Debt securities in book-entry form will be represented by a global security registered in the name of a depositary, which will be the holder of all the debt securities represented by the global security (Section 2.04). Those who own beneficial interests in a global security will do so through participants in the depositary's system, and the rights of these indirect owners will be governed solely by the applicable procedures of the depositary and its participants. Only the depositary will be entitled to transfer or exchange a debt security in global form, since it will be the sole holder of the debt security (Section 3.05). These book-entry securities are described below under "Book-Entry Procedures and Settlement."

If any debt securities are issued in non-global form or cease to be book-entry securities (in the circumstances described in the next section), the following will apply to them:

- The debt securities will be issued in fully registered form in denominations stated in the prospectus supplement. You may exchange debt securities for debt securities of the same series in smaller denominations or combined into fewer debt securities of the same series of larger denominations, as long as the total amount is not changed (Section 3.05).
- You may exchange, transfer, present for payment or exercise debt securities at the office of the relevant trustee or agent indicated in the prospectus supplement (Section 3.05). You may also replace lost, stolen, destroyed or mutilated debt securities at that office. We may appoint another entity to perform these functions or may perform them (Section 3.06).
- You will not be required to pay a service charge to transfer or exchange the debt securities, but you may be required to pay any tax or other governmental charge associated with the transfer or exchange (Sections 3.05 and 3.06). The transfer or exchange, and any replacement, will be made only if our transfer agent is satisfied with your proof of legal ownership. The transfer agent may also require an indemnity before replacing any debt securities (Section 3.06).
- If we have the right to redeem, accelerate or settle any debt securities before their maturity or expiration, and we exercise that right as to less than all those debt securities, we may block the transfer or exchange of those debt securities during the period beginning 15 days before the day we mail the notice of exercise and ending on the day of that mailing, in order to freeze the list of holders to prepare the mailing. We may also refuse to register transfers of or exchange any debt security selected for early settlement, except that we will continue to permit transfers and exchanges of the unsettled portion of any debt security being partially settled (Section 3.05).
- If fewer than all of the debt securities represented by a certificate that are payable or exercisable in part are presented for payment or exercise, a new certificate will be issued for the remaining amount of securities (Section 15.02).

Book-Entry Procedures and Settlement

Most offered debt securities will be book-entry (global) securities. Upon issuance, all book-entry securities will be represented by one or more fully registered global securities, without coupons (Section 3.02). Each global security will be deposited with, or on behalf of, The Depository Trust Company, or DTC, a securities depository, and will be registered in the name of DTC or a nominee of DTC (Section 3.01). DTC will thus be the only registered holder of these debt securities.

Purchasers of debt securities may only hold interests in the global notes through DTC if they are participants in the DTC system. Purchasers may also hold interests through a securities intermediary—banks, brokerage houses and other institutions that maintain securities accounts for customers—that has an account with DTC or its nominee. DTC will maintain accounts showing the security holdings of its participants, and these participants will in turn maintain accounts showing the security holdings of their customers. Some of these customers may themselves be securities intermediaries holding securities for their customers. Thus, each beneficial owner of a book-entry security will hold that debt security indirectly through a hierarchy of intermediaries, with DTC at the top and the beneficial owner's own securities intermediary at the bottom.

The debt securities of each beneficial owner of a book-entry security will be evidenced solely by entries on the books of the beneficial owner's securities intermediary. The actual purchaser of the debt securities will generally not be entitled to have the debt securities represented by the global securities registered in its name and will not be considered the owner under the declaration. In most cases, a beneficial owner will also not be able to obtain a paper certificate evidencing the holder's ownership of debt securities. The book-entry system for holding securities eliminates the need for physical movement of certificates and is the system through which most

publicly traded common stock is held in the United States. However, the laws of some jurisdictions require some purchasers of securities to take physical delivery of their securities in definitive form. These laws may impair the ability to transfer book-entry securities.

A beneficial owner of book-entry securities represented by a global security may exchange the securities for definitive (paper) securities only if:

- DTC is unwilling or unable to continue as depositary for such global security and we do not appoint a qualified replacement for DTC within 90 days; or
- We in our sole discretion decide to allow some or all book-entry securities to be exchangeable for definitive securities in registered form (Section 3.05).

Unless we indicate otherwise, any global security that is exchangeable will be exchangeable in whole for definitive securities in registered form, with the same terms and of an equal aggregate principal amount. Definitive securities will be registered in the name or names of the person or persons specified by DTC in a written instruction to the registrar of the securities (Section 3.05). DTC may base its written instruction upon directions that it receives from its participants.

In this prospectus, for book-entry securities, references to actions taken by security holders will mean actions taken by DTC upon instructions from its participants, and references to payments and notices of redemption to security holders will mean payments and notices of redemption to DTC as the registered holder of the securities for distribution to participants in accordance with DTC's procedures.

DTC is a limited purpose trust company organized under the laws of the State of New York, a member of the Federal Reserve System, a clearing corporation within the meaning of the New York Uniform Commercial Code and a clearing agency registered under section 17A of the Securities Exchange Act of 1934. The rules applicable to DTC and its participants are on file with the SEC.

We will not have any responsibility or liability for any aspect of the records relating to, or payments made on account of, beneficial ownership interest in the book-entry securities or for maintaining, supervising or reviewing any records relating to the beneficial ownership interests.

PLAN OF DISTRIBUTION

We may sell any of the securities being offered by this prospectus separately or together:

- through agents;
- to or through underwriters who may act directly or through a syndicate represented by one or more managing underwriters;
- through dealers;
- through a block trade in which the broker or dealer engaged to handle the block trade will attempt to sell the securities as agent, but may position and resell a portion of the block as principal to facilitate the transaction;
- through "at the market" offerings, within the meaning of Rule 415(a)(4) of the Securities Act of 1933, to or through a market maker or into an existing trading market on an exchange or otherwise;
- in exchange for our outstanding indebtedness;
- directly to purchasers, through a specific bidding, auction or other process; or
- through a combination of any of these methods of sale.

If the securities offered under this prospectus are issued in exchange for our outstanding securities, the applicable prospectus supplement will describe the terms of the exchange, and the identity and the terms of sale of the securities offered under this prospectus by the selling security holders.

The distribution of securities may be effected from time to time in one or more transactions at a fixed price or prices that may be changed, at market prices prevailing at the time of sale or prices related to prevailing market prices or at negotiated prices.

Agents designated by us from time to time may solicit offers to purchase the securities. We will name any agent involved in the offer or sale of the securities and set forth any commissions payable by us to an agent in the prospectus supplement for that transaction. Unless otherwise indicated in the prospectus supplement, any agent will be acting on a best efforts basis for the period of its appointment. Any agent may be deemed to be an "underwriter" of the securities as that term is defined in the Securities Act of 1933.

If we utilize an underwriter or underwriters in the sale of securities, we will execute an underwriting agreement with the underwriter or underwriters at the time we reach an agreement for sale. We will set forth in the prospectus supplement the names of the specific managing underwriter or underwriters, as well as any other underwriters, and the terms of the transactions, including compensation of the underwriters and dealers. This compensation may be in the form of discounts, concessions or commissions. Underwriters and others participating in any offering of securities may engage in transactions that stabilize, maintain or otherwise affect the price of securities. We will describe any of these activities in the prospectus supplement.

If a dealer is utilized in the sale of the securities, we or an underwriter will sell securities to the dealer, as principal. The dealer may then resell the securities to the public at varying prices to be determined by the dealer at the time of resale. The prospectus supplement will set forth the name of the dealer and the terms of the transactions.

We may directly solicit offers to purchase the securities, and we may sell directly to institutional investors or others. These persons may be deemed to be underwriters within the meaning of the Securities Act of 1933 with respect to any resale of the securities. The prospectus supplement will describe the terms of any direct sales, including the terms of any bidding or auction process, if utilized.

Agreements we enter into with agents, underwriters and dealers may entitle them to indemnification by us against specified liabilities, including liabilities under the Securities Act of 1933, or to contribution by us to payments they may be required to make in respect of these liabilities. The prospectus supplement will describe the terms and conditions of indemnification or contribution.

Certain of the agents, underwriters and dealers that we sell the securities offered under this prospectus to or through, and certain of their affiliates, engage in transactions with and perform services for us in the ordinary course of business. We may enter into hedging transactions in connection with any particular issue of the securities offered under this prospectus, including forwards, futures, options, interest rate or exchange rate swaps and repurchase or reverse repurchase transactions with, or arranged by, the applicable agent, underwriter or dealer, an affiliate of that agent, underwriter or dealer or an unrelated entity. We, the applicable agent, underwriter or dealer or other parties may receive compensation, trading gain or other benefits in connection with these transactions. We are not required to engage in any of these transactions. If we commence these transactions, we may discontinue them at any time. Counterparties to these hedging activities also may engage in market transactions involving the securities offered under this prospectus.

No securities may be sold under this prospectus without delivery (in paper format, in electronic format, in electronic format on the Internet, or by other means) of the applicable prospectus supplement describing the method and terms of the offering.

LEGAL MATTERS

Unless otherwise indicated in the applicable prospectus supplement, the validity of the securities that may be offered hereby will be passed upon for us by Ballard Spahr LLP, Philadelphia, Pennsylvania. If legal matters in connection with the offering made by this prospectus are passed on by counsel for the underwriters, dealers or agents, if any, that counsel will be named in the applicable prospectus supplement.

EXPERTS

The financial statements and management's assessment of the effectiveness of internal control over financial reporting (which is included in Management's Report on Internal Control over Financial Reporting) incorporated in this Prospectus by reference to the Annual Report on Form 10-K for the year ended December 31, 2017, have been so incorporated in reliance on the report of PricewaterhouseCoopers LLP, an independent registered public accounting firm, given on the authority of said firm as experts in auditing and accounting.

WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the SEC. You may read and copy any document we file at the SEC's Public Reference Room at 100 F Street N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the Public Reference Room. You may also obtain our SEC filings from the SEC's website at www.sec.gov or from our website at http://ir.aquaamerica.com/.

We have filed with the SEC a "shelf" registration statement on Form S-3 under the Securities Act of 1933 relating to the securities that may be offered by this prospectus. This prospectus is a part of that registration statement, but does not contain all of the information in the registration statement. We have omitted certain parts of the registration statement in accordance with rules and regulations of the SEC. Statements made in this prospectus as to the contents of any contract, agreement or other documents are not necessarily complete, and, in each instance, we refer you to a copy of such document filed as an exhibit to the registration statement, of which this prospectus is a part, or otherwise filed with the SEC. For more detail about us and any securities that may be offered by this prospectus, you may examine the registration statement on Form S-3 and the exhibits filed with it at the locations listed in the previous paragraph.

The SEC allows us to "incorporate by reference" the information we file with them, which means that we can disclose important information to you by referring you to those documents. The information incorporated by reference is considered to be part of this prospectus. When we file information with the SEC in the future, that information will automatically update and supersede this information. We incorporate by reference the documents listed below and any future filings we will make with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934 until we sell all of the securities covered by this prospectus; provided, however, that we are not incorporating, in each case, any documents or information deemed to have been furnished and not filed in accordance with SEC rules:

- Our Annual Report on Form 10-K for the year ended December 31, 2017 filed with the SEC on February 28, 2018; and
- The description of our common stock set forth in our Registration Statement on Form 8-A, including any amendments or reports filed for the purpose of updating such description.

These documents contain important business and financial information about us that is not included in or delivered with this prospectus. You may request a copy of any or all documents that we incorporate by reference at no cost, by writing or telephoning us at:

Aqua America, Inc.
762 W. Lancaster Avenue
Bryn Mawr, PA 19010-3489
Telephone: 610-527-8000
Attention: Corporate Secretary

You should rely only on the information contained in or incorporated by reference in this prospectus and any supplements to this prospectus. We have not authorized anyone to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. You should not assume that the information provided in this prospectus or incorporated by reference in this prospectus is accurate as of any date other than the date on the front of this prospectus or the date of those documents. Our business, financial condition, results of operations and prospects may have changed since those dates.

If you find inconsistencies between the documents, or between the documents and this prospectus or the applicable prospectus supplement, you should rely on the most recent document, prospectus or prospectus supplement.

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6,700,000 Shares

ESSENTIAL UTILITIES, INC.

Common Stock

PROSPECTUS SUPPLEMENT

Sole Book Running Manager

RBC Capital Markets

August 11, 2020

As filed with the Securities and Exchange Commission on June 21, 2021

Registration No. 333-

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM S-3

REGISTRATION STATEMENT
UNDER
THE SECURITIES ACT OF 1933

Essential Utilities, Inc.

(Exact name of registrant as specified in its charter)

Pennsylvania	**23-1702594**
(State or other jurisdiction of incorporation or organization)	**I.R.S. Employer Identification No.)**

762 W. Lancaster Avenue
Bryn Mawr, Pennsylvania 19010-3489
(610) 527-8000
(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

Christopher P. Luning
Essential Utilities, Inc.
Executive Vice President, General Counsel and Corporate Secretary
762 W. Lancaster Avenue
Bryn Mawr, Pennsylvania 19010-3489
(610) 527-8000
(Name, address, including zip code, and telephone number, including area code, of agent for service)

Copies to:

Roxane F. Reardon	**Mary J. Mullany**
Ryan Bekkerus	**Ballard Spahr LLP**
Simpson Thacher & Bartlett LLP	**1735 Market Street, 51st Floor**
425 Lexington Avenue	**Philadelphia, Pennsylvania 19103-7599**
New York, New York 10017-3954	**(215) 665-8500**
(212) 455-2000	

Approximate date of commencement of proposed sale to the public: From time to time after this Registration Statement becomes effective.

If the only securities being registered on this Form are being offered pursuant to dividend or interest reinvestment plans, please check the following box. o

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box. ☒

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. o

If this Form is a registration statement pursuant to General Instruction I.D. or a post-effective amendment thereto that shall become effective upon filing with the Commission pursuant to Rule 462(e) under the Securities Act, check the following box. ☒

If this Form is a post-effective amendment to a registration statement filed pursuant to General Instruction I.D. filed to register additional securities or additional classes of securities pursuant to Rule 413(b) under the Securities Act, check the following box. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	x	Accelerated filer	o
Non-accelerated filer	o	Smaller reporting company	o
		Emerging growth company	o

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of Securities Act. o

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities To Be Registered(1)	**Amount To Be Registered**	**Proposed Maximum Offering Price**	**Proposed Maximum Aggregate**	**Amount of Registration Fee**

		Per Unit(2)	Offering Price(2)	
Common Stock, par value $.50 per share(3)	21,661,095	$47.59	$1,030,851,511.05	$112,465.90

(1) Pursuant to Rule 416 under the Securities Act, this Registration Statement also covers such additional number of our shares of common stock as may be issuable from time to time as a result of stock splits, stock dividends, capitalizations or similar events.

(2) Estimated solely for the purposes of calculating the registration fee. Pursuant to Rule 457(c) under the Securities Act, the registration fee has been calculated based upon the average of the high and low prices, as reported by the New York Stock Exchange, for our shares of common stock on June 18, 2021.

(3) All the shares of common stock being registered hereby are offered for the account of the selling shareholder who acquired such shares of common stock in a private transaction.

PROSPECTUS

ESSENTIAL UTILITIES, INC.

Common Stock

This prospectus relates to the proposed resale or other disposition of up to 21,661,095 shares of Essential Utilities, Inc. common stock, par value $.50 per share, by the selling shareholder named in this prospectus. We are not offering any securities under this prospectus and will not receive any proceeds from the sale of shares of common stock offered by the selling shareholder. The selling shareholder acquired the shares of common stock pursuant to a Stock Purchase Agreement dated March 29, 2019 (the "Purchase Agreement") entered into by and between Essential Utilities, Inc. (formerly known as Aqua America, Inc.) and Canada Pension Plan Investment Board, a federal Canadian Crown corporation ("CPP Investments"), and assigned by CPP Investments to CPP Investment Board PMI-2 Inc., a Canadian corporation ("PMI-2"). PMI-2 is a wholly-owned subsidiary of CPP Investments. We are registering the offer and sale of the shares of common stock to satisfy registration rights we have granted to the selling shareholder.

The selling shareholder may offer and sell or otherwise dispose of the shares of common stock described in this prospectus from time to time through public or private transactions at prevailing market prices, at prices related to prevailing market prices or at privately negotiated prices. The selling shareholder will bear all underwriting fees, commissions and discounts, if any, attributable to the sales of shares of common stock and any transfer taxes. We will bear all other costs, expenses and fees in connection with the registration of the shares of common stock. See "Plan of Distribution" for more information about how the selling shareholder may sell or dispose of their shares of common stock.

Our common stock is traded on the New York Stock Exchange under the symbol "WTRG". On June 18, 2021, the last reported sale price for our common stock on the New York Stock Exchange was $46.63 per share.

Investing in our securities involves risk. Before you invest, you should carefully read and evaluate the risk factors and other information included in this prospectus and any applicable prospectus supplement, including the documents incorporated by reference. See "Risk Factors" beginning on page 5 of this prospectus.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is June 21, 2021.

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ABOUT THIS PROSPECTUS

This document is called a prospectus and is part of a registration statement that we filed with the Securities and Exchange Commission (SEC) using a "shelf" registration process. Under this shelf process, the selling shareholder may, from time to time, offer and/or sell shares of common stock in one or more offerings or resales. This prospectus provides you with a general description of the shares of common stock that the selling shareholder may offer. This prospectus may be supplemented from time to time by one or more prospectus supplements, and we may also provide you with a free writing prospectus. A prospectus supplement and any free writing prospectus will contain more specific information about the offering and the shares of common stock being offered and the prices at which those shares of common stock are sold. A prospectus supplement may also add, update, change or clarify information contained in or incorporated by reference into this prospectus. If there is any inconsistency between the information in this prospectus and the information in the applicable prospectus supplement, you should rely on the information in the applicable prospectus supplement.

The rules of the SEC allow us to incorporate by reference information into this prospectus. This means that important information is contained in other documents that are considered to be a part of this prospectus. Additionally, information that we file later with the SEC will automatically update and supersede this information. You should carefully read both this prospectus and the applicable prospectus supplement together with the additional information that is incorporated or deemed incorporated by reference into this prospectus or the applicable prospectus supplement. See "Where You Can Find Additional Information" before making an investment in our common stock. This prospectus contains summaries of certain provisions contained in some of the documents described herein, but reference is made to the actual documents for complete information. All of the summaries are qualified in their entirety by the actual documents. Copies of the documents referred to herein have been filed or will be filed or incorporated by reference as exhibits to the registration statement of which this prospectus is a part. The registration statement, including the exhibits and documents incorporated or deemed incorporated by reference into this prospectus, can be read on the SEC website or at the SEC offices mentioned under the heading "Where You Can Find Additional Information."

We are responsible only for the information contained in or incorporated by reference in this prospectus or any applicable prospectus supplement. Neither we nor the selling shareholder has authorized anyone to give you different information and we and the selling shareholder take no responsibility for any information that is not contained or incorporated by reference in this prospectus or an applicable prospectus supplement. We and the selling shareholder are not making an offer to sell securities in any jurisdiction where the offer or sale of such securities is not permitted.

Except as otherwise provided in this prospectus, unless the context otherwise requires, references in this prospectus to "Essential Utilities," "we", "us", "our", or the "Company" refer to Essential Utilities, Inc. and its direct and indirect subsidiaries. References in this prospectus to "Registrant" refer to Essential Utilities, Inc. In addition, references to "Aqua Pennsylvania" refer to our wholly-owned subsidiary, Aqua Pennsylvania, Inc., and its subsidiaries. On March 16, 2020, we completed our acquisition of a natural gas distribution company consisting of Peoples Natural Gas Company LLC, Peoples Gas Company LLC, Peoples Gas West Virginia, Inc., Peoples Gas Kentucky, Inc., and Delta Natural Gas Company Inc., expanding the Company's regulated utility business to include natural gas distribution. This acquisition is referred to as the "Peoples Gas Acquisition," and collectively these businesses are referred to as "Peoples Gas." As used in this prospectus, the term "selling shareholder" includes the selling shareholder listed under the heading "Selling Shareholder", together with any additional selling shareholders listed in a prospectus supplement after the date of this prospectus.

FORWARD-LOOKING STATEMENTS

Certain statements in this prospectus, or incorporated by reference into this prospectus, are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act") that are made based upon, among other things, our current assumptions, expectations, plans, and beliefs concerning future events and their potential effect on us. These forward-looking statements involve risks, uncertainties and other factors, many of which are outside our control that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. In some cases you can identify forward-looking statements where statements are preceded by, followed by or include the words "believes," "expects," "anticipates," "plans," "future," "potential," "probably," "predictions," "intends," "will," "continue" "in the event" or the negative of such terms or similar expressions. Forward-looking statements in this prospectus, or incorporated by reference into this prospectus, include, but are not limited to, statements regarding:

- the impact of the novel coronavirus ("COVID-19") pandemic or the measures implemented by the Company as a result of the COVID-19 pandemic.
- expectations regarding the impact of the integration of the Peoples Gas Acquisition;
- opportunities for future acquisitions, both within and outside the water, wastewater, and natural gas industries, the success of pending acquisitions and the impact of future acquisitions;
- acquisition-related costs and synergies;
- the sale of water, wastewater, and/or gas subsidiaries;
- the impact of conservation awareness of customers and more efficient fixtures and appliances on water and natural gas usage per customer;
- our authority to carry on our business without unduly burdensome restrictions;
- our capability to pursue timely rate increase requests;
- the capacity of our water supplies, water facilities, wastewater facilities, and natural gas supplies and storage facilities;
- the impact of decisions of governmental and regulatory bodies, including decisions to raise or lower rates and decisions regarding potential acquisitions;
- developments, trends and consolidation in the water, wastewater, and natural gas utility and infrastructure industries;
- the impact of changes in and compliance with governmental laws, regulations and policies, including those dealing with the environment, health and water quality, taxation, and public utility regulation;
- the development of new services and technologies by us or our competitors;
- the availability of qualified personnel;
- the condition of our assets;
- recovery of capital expenditures and expenses in rates;
- projected capital expenditures and related funding requirements;

- the availability and cost of capital financing;
- dividend payment projections;
- the impact of geographic diversity on our exposure to unusual weather;
- the continuation of investments in strategic ventures;
- our ability to obtain fair market value for condemned assets;
- the impact of fines and penalties;
- the impact of legal proceedings;
- general economic conditions;
- the impact of federal and/or state tax policies and the regulatory treatment of the effects of those policies; and
- the amount of income tax deductions for qualifying utility asset improvements and the Internal Revenue Service's ultimate acceptance of the deduction methodology.

Because forward-looking statements involve risks and uncertainties, there are important factors that could cause actual results to differ materially from those expressed or implied by these forward-looking statements, including but not limited to:

- impacts from the global outbreak of COVID-19, including on consumption, usage and collections
- the diversion of our management's time and resources caused by the integration efforts with respect to the Peoples Gas business and associated system implementations;
- the success in the closing of, and the profitability of future acquisitions;
- changes in general economic, business, credit and financial market conditions;
- our ability to manage the expansion of our business, including our ability to manage our expanded operations resulting from the Peoples Gas Acquisition;
- our ability to integrate and otherwise realize all of the anticipated benefits of businesses, technologies or services which we may acquire;
- changes in environmental conditions, including the effects of climate change;
- the decisions of governmental and regulatory bodies, including decisions on regulatory filings, including rate increase requests and decisions regarding potential acquisitions;
- our ability to file rate cases on a timely basis to minimize regulatory lag;
- abnormal weather conditions, including those that result in water availability, water use restrictions, gas availability or usage, or electricity interruptions;
- the seasonality of our business;
- our ability to treat and supply water or collect and treat wastewater;

- our ability to source sufficient natural gas to meet customer demand in a timely manner;
- the continuous and reliable operation of our information technology systems, including the impact of cyber security attacks or other cyber-related events;
- changes in governmental laws, regulations and policies, including those dealing with taxation, the environment, health and water quality, and public utility regulation;
- the extent to which we are able to develop and market new and improved services;
- the effect of the loss of major customers;
- our ability to retain the services of key personnel and to hire qualified personnel as we expand;
- labor disputes;
- increasing difficulties in obtaining insurance and increased cost of insurance;
- cost overruns relating to improvements to, or the expansion of, our operations;
- increases in the costs of goods and services;
- the effect of natural gas price volatility;
- civil disturbance or terroristic threats or acts;
- changes to the rules or our assumptions underlying our determination of what qualifies for an income tax deduction for qualifying utility asset improvements;
- changes in, or unanticipated, capital requirements;
- changes in our credit rating or the market price of our common stock;
- changes in valuation of strategic ventures;
- the phase-out of the London Interbank Offered Rate (“LIBOR”), or the replacement of LIBOR with a different reference rate or modification of the method used to calculate LIBOR, which may adversely affect interest rates;
- changes in accounting pronouncements;
- litigation and claims; and
- restrictions on our subsidiaries’ ability to make dividends and other distributions.

Given these risks and uncertainties, you should not place undue reliance on any forward-looking statements. You should read this prospectus and the documents that we incorporate by reference into this prospectus completely and with the understanding that our actual results, performance and achievements may be materially different from what we expect. These forward-looking statements represent assumptions, expectations, plans and beliefs only as of the date of this prospectus, the date of the document containing the applicable statement or the date specified in such statement, as applicable. Except for our ongoing obligations to disclose certain information under the federal securities laws, we are not obligated, and assume no obligation, to update these forward-looking statements, even though our situation may change in the future. For further information or other factors which could affect our financial results and such forward-looking statements, see “Risk Factors.” We qualify all of our forward-looking statements by these cautionary statements.

ESSENTIAL UTILITIES, INC.

Essential Utilities, Inc. is a Pennsylvania corporation and the holding company for regulated utilities providing water, wastewater, or natural gas services to an estimated five million people in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana, Virginia, West Virginia, and Kentucky under the Aqua and Peoples brands. Essential Utilities, which prior to its name change on February 3, 2020 was known as Aqua America, Inc., was formed in 1968 as a holding company for its primary subsidiary, Aqua Pennsylvania, formerly known as Philadelphia Suburban Water Company.

Our principal executive office is located at 762 W. Lancaster Avenue, Bryn Mawr, Pennsylvania 19010-3489, and our telephone number is 610-527-8000. Our website may be accessed at www.essential.co. The references to our website and the SEC's website are intended to be inactive textual references only, and the contents of those websites are not incorporated by reference herein and should not be considered part of this prospectus.

RISK FACTORS

Investing in our securities involves risks. Please see the risk factors described under the section captioned "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2020, as such risk factors may be updated from time to time in filings we make with the SEC subsequent to the date hereof. Before making an investment decision, you should carefully consider these risk factors, together with all other information contained in or incorporated by reference into this prospectus or any applicable prospectus supplement (which includes information contained in certain filings we make with the SEC subsequent to the date hereof as set forth in the section below captioned "Where You Can Find More Information"). Please also refer to the section above captioned "Forward-Looking Statements."

USE OF PROCEEDS

We will not receive any of the proceeds from the sale of shares of common stock by the selling shareholder.

DESCRIPTION OF CAPITAL STOCK

As of June 1, 2021, our authorized capital stock was 601,770,819 shares, consisting of:

- 600,000,000 shares of common stock, par value $0.50 per share, of which 245,734,735 shares were outstanding; and
- 1,770,819 shares of preferred stock, par value $1.00 per share, of which no shares were outstanding.

The following summary of certain terms of our common stock and preferred stock is qualified in its entirety by the provisions of our Amended and Restated Articles of Incorporation and Amended and Restated Bylaws, each of which is incorporated by reference as an exhibit to the registration statement of which this prospectus constitutes a part.

Common Stock

This section describes the general terms of our common stock. For more detailed information, you should refer to our articles of incorporation and bylaws, including any amendments thereto, copies of which have been filed with the SEC. These documents are incorporated by reference into this prospectus.

Voting Rights

Holders of our common stock are entitled to one vote for each share held by them at all meetings of the shareholders and are not entitled to cumulate their votes for the election of directors.

Dividend Rights and Limitations

Holders of our common stock may receive dividends when declared by our board of directors. Because we are a holding company, the funds we use to pay any dividends on our common stock are derived predominantly from the dividends that we receive from our direct and indirect subsidiaries. Therefore, our ability to pay dividends to holders of our common stock depends upon the subsidiaries' earnings, financial condition and ability to pay dividends. Most of our subsidiaries are subject to regulation by state utility commissions and the amounts of their earnings and dividends are affected by the manner in which they are regulated. In addition, they are subject to restrictions on the payment of dividends contained in their various debt agreements. Under the most restrictive debt agreements, the amount available for payment of dividends to us as of December 31, 2020 was approximately $1,729,269,000 of Aqua Pennsylvania's retained earnings and $276,283,000 of the retained earnings of certain other subsidiaries. Payment of dividends on common stock is also subject to the preferential rights of the holders of any outstanding preferred stock.

Liquidation Rights

In the event that we liquidate, dissolve or wind-up, the holders of our common stock are entitled to share ratably in all of the assets that remain after we pay our liabilities. This right is subject, however, to the prior distribution rights of any outstanding preferred stock.

Listing

Our common stock is listed on the New York Stock Exchange, or NYSE, under the symbol "WTRG."

Preferred Stock

Our board of directors has the authority, from time to time and without further action by our shareholders, to divide our unissued capital stock into one or more classes and one or more series within any class and to make determinations of the designation and number of shares of any class or series and determinations of the voting rights, preferences, limitations and special rights, if any, of the shares of any class or series. The rights, preferences, limitations and special rights of different classes of capital stock may differ with respect to dividend rates, amounts payable on liquidation, voting rights, conversion rights, redemption provisions, sinking fund provisions and other matters. The rights, preferences, privileges and restrictions of each series may be fixed by the designations of that series set forth in either a restated version of our articles of incorporation or a certificate of designations relating to that series.

The issuance of preferred stock may be perceived by some as possibly having the effect of delaying, deferring or preventing a change of control of us without further action by our shareholders. The issuance of preferred stock with voting and conversion rights may also adversely affect the voting power of the holders of our common stock. In certain circumstances, an issuance of preferred stock could possibly have the effect of decreasing the market price of our common stock.

Anti-Takeover Provisions

Pennsylvania State Law Provisions

Under Section 1712 of the Pennsylvania Business Corporation Law of 1988, as amended, or the PBCL, which is applicable to us, directors stand in a fiduciary relation to their corporation and, as such, are required to perform their duties in good faith, in a manner they reasonably believe to be in the best interests of the corporation and with such care, including reasonable inquiry, skill and diligence, as a person of ordinary prudence would use under similar circumstances. Under Section 1715 of the PBCL, in discharging their duties, directors may, in considering the best interests of their corporation, consider various constituencies, including, shareholders, employees, suppliers, customers and creditors of the corporation, and upon communities in which offices or other establishments of the corporation are located. Directors are not required to give prominent consideration to the interests of any particular constituency. Absent a breach of fiduciary duty, a lack of good faith or self-dealing, any act of the board of directors, a committee thereof or an individual director is presumed to be in the best interests of the corporation. Actions by directors relating to an acquisition or potential acquisition of control of the corporation are not subject to any greater obligation to justify, or higher burden of proof, than is applied to any other acts of directors. The PBCL expressly provides that the fiduciary duty of directors does not require them to (i) redeem or otherwise render inapplicable outstanding rights issued under any shareholder rights plan; (ii) render inapplicable the anti-takeover statutes set forth in Chapter 25 of the PBCL (described below); or (iii) take any action solely because of the effect it may have on a proposed acquisition or the consideration to be received by shareholders in such a transaction. In addition, Section 2513 of the PBCL specifically validates shareholder rights plans, or "poison pills," and the discriminatory dilution provisions contained in such plans.

Chapter 25 of the PBCL contains several anti-takeover statutes applicable to publicly-traded corporations. Corporations may opt-out of such anti-takeover statutes under certain circumstances. We have not opted-out of any of such statutes.

Section 2538 of Subchapter 25D of the PBCL requires certain transactions with an "interested shareholder" to be approved by a majority of disinterested shareholders. "Interested shareholder" is defined broadly to include any shareholder who is a party to the transaction or who is treated differently than other shareholders and affiliates of the interested shareholder.

Subchapter 25E of the PBCL requires a person or group of persons acting in concert which acquires 20% or more of the voting shares of the corporation to offer to purchase the shares of any other shareholder at "fair value." "Fair value" means the value not less than the highest price paid per share by the controlling person or group during the 90-day period prior to the control transaction, plus a control premium. Among other exceptions, Subchapter 25E does not apply to shares acquired directly from the corporation in a transaction exempt from the registration requirements of the Securities Act, or to a one-step merger.

Subchapter 25F of the PBCL generally establishes a 5-year moratorium on a "business combination" with an "interested shareholder." "Interested shareholder" is defined generally to be any beneficial owner of 20% or more of the corporation's voting stock or an affiliate or associate of the corporation that at any time within the prior five-year period was a beneficial owner of 20% or more of the corporation's voting stock. "Business combination" is defined broadly to include mergers, consolidations, asset sales and certain self-dealing transactions. Certain restrictions apply to business combination following the 5-year period. Among other exceptions, Subchapter 25F will be rendered inapplicable if the board of directors approves the proposed business combination, or approves the interested shareholder's acquisition of 20% of the voting shares, in either case prior to the date on which the shareholder first becomes an interested shareholder.

Subchapter 25G of the PBCL provides that "control shares" lose voting rights unless such rights are restored by the affirmative vote of a majority of (i) the disinterested shares (generally, shares held by persons other than the acquiror, executive officers of the corporation and certain employee stock plans) and (ii) the outstanding voting shares of the corporation. "Control shares" are defined as shares which, upon acquisition, will result in a person or group acquiring for the first time voting control over (a) 20%, (b) 33 1/3% or (c) 50% or more of the outstanding shares, together with shares acquired within 180 days of attaining the applicable threshold and shares purchased with the intention of attaining such threshold. A corporation may redeem control shares if the acquiring person does not request restoration of voting rights as permitted by Subchapter 25G. Among other exceptions, Subchapter 25G does not apply to a merger, consolidation or a share exchange if the corporation is a party to the transaction agreement.

Subchapter 25H of the PBCL provides in certain circumstances for the recovery by the corporation of profits realized from the sale of its stock by a controlling person or group if the sale occurs within 18 months after the controlling person or group became a controlling person or group, and the stock was acquired during such 18-month period or within 24 months before such period. A controlling person or group is a person or group that has acquired, offered to acquire, or publicly disclosed an intention to acquire 20% or more of the voting shares of the corporation or a person or group that has otherwise publicly disclosed or caused to be disclosed that it may seek to acquire control of the corporation through any means. Among other exceptions, Subchapter 25H does not apply to transactions approved by both the board of directors and the shareholders prior to the acquisition or distribution, as appropriate.

Subchapter 25I of the PBCL mandates severance compensation for eligible employees who are terminated within 24 months after the approval of a control-share acquisition. Eligible employees generally are all employees employed in Pennsylvania for at least two years prior to the control-share approval. Severance equals the weekly compensation of the employee multiplied by the employee's years of service (up to 26 years), less payments made due to the termination.

Subchapter 25J of the PBCL requires the continuation of certain labor contracts relating to business operations owned at the time of a control-share approval.

Articles of Incorporation and Bylaw Provisions

Certain provisions of our articles of incorporation and bylaws may have the effect of discouraging unilateral tender offers or other attempts to take over and acquire our business. These provisions might discourage some potentially interested purchaser from attempting a unilateral takeover bid for us on terms which some shareholders might favor. Our articles of incorporation require that certain fundamental transactions must be approved by the holders of 75% of the outstanding shares of our capital stock entitled to vote on the matter unless at least a majority of the members of the board of directors has approved the transaction, in which case the required shareholder approval will be the minimum approval required by applicable law. The fundamental transactions that are subject to this provision are those transactions that require approval by shareholders under applicable law or the articles of incorporation. These transactions include certain amendments of our articles of incorporation or bylaws, certain sales or other dispositions of our assets, certain issuances of our capital stock, or certain transactions involving our merger, consolidation, division, reorganization, dissolution, liquidation or winding up. Our articles of incorporation and bylaws provide that:

- a special meeting of shareholders may only be called by the chairman, the president, the board of directors or shareholders entitled to cast a majority of the votes which all shareholders are entitled to cast at the particular meeting;

- nominations for election of directors may be made by any shareholder entitled to vote for election of directors if the name of the nominee and certain information relating to the nominee is filed with our corporate secretary not less than 14 days nor more than 50 days before any meeting of shareholders to elect directors; and

- certain advance notice procedures must be met for shareholder proposals to be made at annual meetings of shareholders. These advance notice procedures generally require a notice to be delivered not less than 90 days nor more than 120 days before the anniversary date of the immediately preceding annual meeting of shareholders.

Transfer Agent and Registrar

The transfer agent and registrar for our common stock is Computershare Trust Company, N.A.

SELLING SHAREHOLDER

We have prepared this prospectus to allow the selling shareholder to offer and sell from time to time up to 21,661,095 shares of common stock for its own account. The selling shareholder acquired the shares of common stock pursuant to the Stock Purchase Agreement (the "Stock Purchase Agreement") dated March 29, 2019 entered into by and between the Registrant and CPP Investments, and assigned by CPP Investments to PMI-2. On March 16, 2020, in connection with the Peoples Gas Acquisition, the Registrant issued and sold 21,661,095 shares of common stock to PMI-2 (the "Private Placement") in accordance with the terms of the Stock Purchase Agreement. In connection with the Private Placement, the Company entered into a Shareholders Agreement with PMI-2 (the "Shareholders Agreement") dated March 16, 2020.

We are registering the offer and sale of the shares of common stock to satisfy certain registration obligations that we agreed to pursuant to the Shareholders Agreement. Pursuant to the Shareholders Agreement, we have agreed to use our commercially reasonable efforts to keep the registration statement, of which this prospectus forms a part, effective until the date on which there are no longer any Registrable Securities (as defined in the Shareholders Agreement).

As used in this prospectus, the term "selling shareholder" includes the selling shareholder listed in the table below, together with any additional selling shareholders listed in a prospectus supplement after the date of this prospectus.

The following table sets forth the name of the selling shareholder, the number of shares of common stock owned by the selling shareholder, the number of shares of common stock that may be offered under this prospectus and the number of shares of common stock owned by the selling shareholder, assuming all of the shares of common stock covered hereby are sold. The selling shareholder may sell some, all or none of their shares of common stock. We do not know how long the selling shareholder will hold the shares of common stock before selling them, and we currently have no agreements, arrangements or understandings with the selling shareholder regarding the sale or other disposition of any of the shares of common stock. The selling shareholder named below and its permitted transferees, pledgees, donees or other successors may from time to time offer shares of common stock under this prospectus. The selling shareholder named below may have sold, transferred, otherwise disposed of or purchased, or may sell, transfer, otherwise dispose of or purchase, at any time and from time to time, shares of common stock in transactions exempt from the registration requirements of the Securities Act or in the open market after the date on which it provided the information set forth in the table below.

The information set forth below is based upon information obtained from the selling shareholder and from the Schedule 13D filed by CPP Investments with the SEC on March 24, 2020. Beneficial ownership of the selling shareholder is determined in accordance with Rule 13d-3(d) of the Exchange Act. The percentage of shares of common stock beneficially owned prior to and after the offering is based on 245,734,735 shares of common stock outstanding as of June 1, 2021.

	Beneficial Ownership Prior to this Offering			Beneficial Ownership After Offering	
Name of Selling Shareholder	Number of Shares	% of Outstanding Common Stock	Number of Shares that May be Offered under this Prospectus	Number of Shares	% of Outstanding Common Stock
CPP Investment Board PMI-2 Inc. (1)	21,661,095	8.8%	21,661,095	0	0%

(1) PMI-2 is a wholly-owned subsidiary of CPP Investments, and investment and voting power with regard to shares held by PMI-2 rests with CPP Investments. John Graham is the President and Chief Executive Officer of CPP Investments and, in such capacity, may be deemed to have voting and dispositive power with respect to the shares of common stock beneficially owned by CPP Investments. Mr. Graham disclaims beneficial ownership over any such shares. The address of CPP Investments is One Queen Street East, Suite 2500, Toronto, Ontario, M5C 2W5, Canada.

PLAN OF DISTRIBUTION

We have prepared this prospectus to allow the selling shareholder to offer and sell from time to time after the date of this prospectus up to 21,661,095 shares of common stock for its own account. We are not offering any securities under this prospectus and will not receive any proceeds from the sale of shares of common stock offered by the selling shareholder.

The selling shareholder, its permitted transferees, pledgees, donees and other successors may sell the shares of common stock covered by this prospectus in any of the following ways (or in any combination):

- to or through underwriters, brokers or dealers (acting as agent or principal);
- through a block trade in which the broker or dealer engaged to handle the block trade will attempt to sell the securities as an agent, but may position and resell a portion of the block as principal to facilitate the transaction;
- directly to one or more purchasers, including through a specific bidding or auction process or otherwise;
- directly to or through agents;
- in "at the market offerings," within the meaning of Rule 415(a)(4) of the Securities Act;
- through a distribution by the selling shareholder or its successor in interest to its members, general or limited partners or shareholders (or their respective members, general or limited partners or shareholders);
- settlement of short sales;
- through options, swaps or derivatives;
- through a combination of any of these methods of sale; or
- through any other methods described in a prospectus supplement.

The distribution of securities may be effected from time to time in one or more transactions, including block transactions and transactions on the NYSE or any other organized market where the securities may be traded.

The selling shareholder may enter into sale, forward sale and derivative transactions with third parties, or may sell securities not covered by this prospectus to third parties in privately negotiated transactions

Any offering price and any discounts, commissions, concessions or agency fees allowed or reallowed or paid to dealers may be changed from time to time. The selling shareholder may determine the price or other terms relating to the shares of common stock offered under this prospectus by use of an electronic auction. To the extent required, we will describe how any auction will determine the price or any other terms, how potential investors may participate in the auction and the nature of the obligations of the underwriter, dealer or agent in the applicable prospectus supplement.

If the selling shareholder sells securities to a dealer acting as a principal, the dealer may resell such securities at varying prices to be determined by such dealer in its discretion at the time of resale without consulting with the selling shareholder and such resale prices may not be disclosed in the applicable prospectus supplement.

The selling shareholder may distribute the shares of common stock from time to time in one or more transactions:

- at a fixed price or at prices that may be changed from time to time;
- at market prices prevailing at the time of sale;

- at prices relating to such prevailing market prices; or

- at negotiated prices.

Any of the prices may represent a discount of then-prevailing market prices.

The selling shareholder may enter into hedging transactions from time to time in which a selling shareholder may:

- enter into transactions with a broker-dealer or any other person in connection with which such broker-dealer or other person will engage in short sales of the shares, in which case such broker-dealer or other person may use the shares of common stock received from the selling shareholder to close out its short positions;

- sell shares of common stock short and re-deliver shares of common stock offered by this prospectus to close out its short positions;

- enter into options or other types of transactions that require the selling shareholder to deliver the shares of common stock to a broker-dealer, affiliate or third party, who will then resell or transfer the shares of common stock under this prospectus; or

- loan or pledge the shares to a broker-dealer or any other person, who may sell the loaned shares of common stock or, in an event of default in the case of a pledge, sell the pledged shares of common stock under this prospectus.

Underwriters, dealers or any other third parties described above may offer and sell the offered shares of common stock from time to time in one or more transactions, including negotiated transactions, at a fixed public offering price or at varying prices determined at the time of sale. If underwriters or dealers are used in the sale of any shares, the shares of common stock will be acquired by the underwriters or dealers for their own account and may be resold from time to time in one or more transactions, including negotiated transactions, at a fixed public offering price or at varying prices determined at the time of sale. The shares of common stock may be either offered to the public through underwriting syndicates represented by managing underwriters, or directly by underwriters. Generally, the underwriters' obligations to purchase the shares of common stock will be subject to certain conditions precedent. The underwriters will be obligated to purchase all of the shares of common stock if they purchase any of the shares of common stock (other than any shares of common stock purchased upon exercise of any option to purchase additional shares), unless otherwise specified in the applicable prospectus supplement. The selling shareholder may use underwriters with whom we have a material relationship. We will describe the nature of any such relationship, if required, in the applicable prospectus supplement, naming the underwriter or underwriters.

The selling shareholder may sell the shares of common stock through agents from time to time. A prospectus supplement would name any agent involved in the offer or sale of the shares of common stock and any commissions paid to them. Generally, any agent will be acting on a best efforts basis for the period of its appointment. The selling shareholder may engage in at-the-market offerings into an existing trading market in accordance with Rule 415(a)(4) under the Securities Act. The selling shareholder may authorize underwriters, dealers, brokers or agents to solicit offers by certain purchasers to purchase the shares of common stock from the selling shareholder at the public offering price set forth in the applicable prospectus supplement pursuant to delayed delivery contracts providing for payment and delivery on a specified date in the future. These contracts will be subject only to those conditions set forth in the applicable prospectus supplement, and the applicable prospectus supplement would set forth any commissions to be paid for solicitation of these contracts. Any underwriters, dealers, brokers and agents that participate in the distribution of the shares of common stock may be deemed to be "underwriters" as defined in the Securities Act. Any commissions paid or any discounts or concessions allowed to any such persons, and any profits they receive on resale of the shares, may be deemed to be underwriting discounts and commissions under the Securities Act. As applicable, we will identify any underwriters or agents and describe their compensation in a prospectus supplement.

Underwriters or agents may purchase and sell the shares of common stock in the open market. These transactions may include over-allotments or short sales of the securities, stabilizing transactions, syndicate covering transactions and penalty bids.

Over-allotment or short sales involve sales by persons participating in the offering of more securities than were sold to them. In these circumstances, these persons would cover such over-allotments or short positions by making purchases in the open market or by exercising their over-allotment option, if any. Stabilizing transactions consist of bids or purchases for the purpose of preventing or retarding a decline in the market price of the shares of common stock and are permitted so long as the stabilizing bids do not exceed a specified maximum. Syndicate covering transactions involve the placing of any bid on behalf of the underwriting syndicate or the effecting of any purchase to reduce a short position created in connection with the offering. The underwriters or agents also may impose a penalty bid, which permits them to reclaim selling concessions allowed to syndicate members or certain dealers if they repurchase the shares of common stock in stabilizing or covering transactions. These activities may stabilize, maintain or otherwise affect the market price of the shares, which may be higher than the price that might otherwise prevail in the open market. These activities, if begun, may be discontinued at any time. These transactions may be effected on any exchange on which the shares of common stock are traded, in the over-the-counter market or otherwise.

Our common stock is listed on the NYSE under the symbol “WTRG”.

If at the time of any offering made under this prospectus a member of the Financial Industry Regulatory Authority Inc. (“FINRA”) participating in the offering has a “conflict of interest” as defined in FINRA’s Rule 5121 (“Rule 5121”), that offering will be conducted in accordance with the relevant provisions of Rule 5121.

The selling shareholder may also sell shares of common stock under Rule 144 of the Securities Act, if available, rather than under this prospectus.

There can be no assurance that the selling shareholder will sell all or any of the shares of common stock offered by this prospectus.

In order to comply with the securities laws of some states or countries, if applicable, shares of common stock may only be sold in those jurisdictions through registered or licensed brokers or dealers and in compliance with applicable laws and regulations. In addition, in certain states or countries the shares of common stock may not be sold unless they have been registered or qualified for sale in the applicable state or country or an exemption from registration or qualification requirements is available.

We have agreed to indemnify the selling shareholder against certain liabilities, including liabilities under the Securities Act. In addition, agents, dealers and underwriters may be entitled to indemnification by us and the selling shareholder against certain civil liabilities, including liabilities under the Securities Act, or to contribution with respect to payments which the agents, dealers or underwriters may be required to make in respect thereof.

LEGAL MATTERS

Unless otherwise indicated in an applicable prospectus supplement, the validity of the securities in respect of which this prospectus is being delivered will be passed upon for us by Ballard Spahr LLP, Philadelphia, Pennsylvania. If legal matters in connection with the offering made by this prospectus are passed on by counsel for the underwriters, dealers or agents, if any, that counsel will be named in the applicable prospectus supplement.

EXPERTS

The financial statements and management’s assessment of the effectiveness of internal control over financial reporting (which is included in Management’s Report on Internal Control over Financial Reporting) incorporated in this prospectus by reference to the Annual Report on Form 10-K for the year ended December 31, 2020 have been so incorporated in reliance on the report (which contains an explanatory paragraph on the effectiveness of internal control over financial reporting due to the exclusion of Peoples Gas because it was acquired by the Company in a purchase business combination during 2020) of PricewaterhouseCoopers LLP, an independent registered public accounting firm, given on the authority of said firm as experts in auditing and accounting.

The consolidated financial statements of LDC Funding LLC as of December 31, 2019 and 2018 and for each of the three years in the period ended December 31, 2019, incorporated in this prospectus by reference to our Current Report on Form 8-K filed on April 15, 2021, have been audited by Deloitte & Touche LLP, independent auditors, as stated in their report, which is incorporated by reference herein, and are incorporated in reliance upon the report of such firm given upon their authority as experts in accounting and auditing.

WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the SEC. You may obtain our SEC filings from the SEC's website at www.sec.gov or from our website at www.essential.co.

We have filed with the SEC a "shelf" registration statement on Form S-3 under the Securities Act relating to the shares of common stock that may be offered by this prospectus. This prospectus is a part of that registration statement, but does not contain all of the information in the registration statement. We have omitted certain parts of the registration statement in accordance with rules and regulations of the SEC. Statements made in this prospectus as to the contents of any contract, agreement or other documents are not necessarily complete, and, in each instance, we refer you to a copy of such document filed as an exhibit to the registration statement, of which this prospectus is a part, or otherwise filed with the SEC. For more detail about us and any securities that may be offered by this prospectus, you may examine the registration statement on Form S-3 and the exhibits filed with it at the locations listed in the previous paragraph.

The SEC allows us to "incorporate by reference" the information we file with them, which means that we can disclose important information to you by referring you to those documents. The information incorporated by reference is considered to be part of this prospectus. When we file information with the SEC in the future, that information will automatically update and supersede this information. We incorporate by reference the documents listed below and any future filings we will make with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act until all of the securities covered by this prospectus are sold; provided, however, that we are not incorporating, in each case, any documents or information deemed to have been furnished and not filed in accordance with SEC rules:

- Our Annual Report on Form 10-K for the year ended December 31, 2020, filed with the SEC on March 1, 2021;
- Our Quarterly Report on Form 10-Q filed with the SEC for the quarter ended March 31, 2021, filed with the SEC on May 10, 2021;
- Our Current Reports on Form 8-K filed with the SEC on April 15, 2021, April 19, 2021 and May 10, 2021;
- The portions of our Definitive Proxy Statement on Schedule 14A filed with the SEC on March 22, 2021, that are incorporated by reference into our Annual Report on Form 10-K for the year ended December 31, 2020; and
- The description of our common stock set forth in our Registration Statement on Form 8-A, including any amendments or reports filed for the purpose of updating such description.

These documents contain important business and financial information about us that is not included in or delivered with this prospectus. You may request a copy of any or all documents that we incorporate by reference at no cost, by writing or telephoning us at:

Essential Utilities, Inc.
762 W. Lancaster Avenue
Bryn Mawr, PA 19010-3489
Telephone: 610-527-8000
Attention: Corporate Secretary

We and the selling shareholder have not authorized anyone to provide you with information different from that contained or incorporated by reference in this prospectus, any prospectus supplements or any free writing prospectus prepared by or on behalf of us or to which we have referred you. We and the selling shareholder take no responsibility for, and can provide no assurance as to the reliability of, any other information that others may give you. You should not assume that the information provided in this prospectus or incorporated by reference in this prospectus is accurate as of any date other than the date on the front of this prospectus or the date of those documents. Our business, financial condition, results of operations and prospects may have changed since those dates.

If you find inconsistencies between the documents, or between the documents and this prospectus or the applicable prospectus supplement, you should rely on the most recent document, prospectus or prospectus supplement.

PART II

INFORMATION NOT REQUIRED IN PROSPECTUS

ITEM 14. Other Expenses of Issuance and Distribution

The following table sets forth an estimate of the costs and expenses payable by the Registrant in connection with the issuance and distribution of the securities being registered hereby.

SEC registration fee	$112,466
Legal fees and expenses	100,000*
Accounting fees and expenses	50,000*
Transfer Agent and Registrar fees and expenses	7,500*
Printing fees	3,000*
Miscellaneous	7,500*
Total	$280,466

***** The foregoing estimates the expenses that we will incur in connection with the preparation and filing of this registration statement. Estimated expenses to be incurred in connection with any future offering by the selling shareholder are not presently known.

ITEM 15. Indemnification of Directors and Officers

The Registrant is a Pennsylvania corporation. Sections 1741 and 1742 of the Pennsylvania Business Corporation Law of 1988, as amended, or the PBCL, provide that, unless otherwise restricted in its bylaws, a business corporation may indemnify directors and officers against liabilities they may incur as such, provided that the particular person acted in good faith and in a manner he or she reasonably believed to be in, or not opposed to, the best interests of the corporation, and, with respect to any criminal proceeding, had no reasonable cause to believe his or her conduct was unlawful. In general, the power to indemnify under these sections does not exist in the case of actions against a director or officer by or in the right of the corporation if the person otherwise entitled to indemnification shall have been adjudged to be liable to the corporation unless it is judicially determined that, despite the adjudication of liability but in view of all the circumstances of the case, the person is fairly and reasonably entitled to indemnification for specified expenses. Section 1743 of the PBCL requires a business corporation to indemnify directors and officers against expenses they may incur in defending actions against them in such capacities if they are successful on the merits or otherwise in the defense of such actions.

Section 1713 of the PBCL permits the shareholders to adopt a bylaw provision relieving a director (but not an officer) of personal liability for monetary damages except where (i) the director has breached or failed to perform the duties of directorship in accordance with the applicable standard of care, and (ii) such conduct constitutes self-dealing, willful misconduct or recklessness. Section 1713 also provides that a director may not be relieved of liability for the payment of taxes pursuant to any federal, state or local law or of liability or responsibility under a criminal statute. Section 4.01 of the Registrant's bylaws limits the liability of any director of the Registrant to the fullest extent permitted by Section 1713 of the PBCL.

Section 1746 of the PBCL grants a corporation broad authority to indemnify its directors, officers and other agents for liabilities and expenses incurred in such capacity, except in circumstances where the act or failure to act giving rise to the claim for indemnification is determined by a court to have constituted willful misconduct or recklessness. Article VII of the Registrant's bylaws provides indemnification of directors, officers and other agents of the Registrant, which is broader than the indemnification permitted by Section 1741 of the PBCL and pursuant to the authority of Section 1746 of the PBCL.

Article VII of the Registrant's bylaws provides, except as expressly prohibited by law, an unconditional right to indemnification for expenses and any liability paid or incurred by any director or officer of the Registrant, or any other person designated by the board of directors as an indemnified representative, in connection with any actual or threatened claim, action, suit or proceeding (including derivative suits) in which he or she may be involved by reason of being or having been a director, officer, employee or agent of the Registrant or, at the request of the Registrant, of another corporation, partnership, joint venture, trust, employee benefit plan or other entity. The bylaws specifically authorize indemnification against both judgments and amounts paid in settlement of derivative suits, unlike Section 1742 of the PBCL which authorizes indemnification only of expenses incurred in defending and in settlement of a derivative action. In addition, Article VII of the bylaws also allows indemnification for punitive damages and liabilities incurred under the federal securities laws.

Unlike the provisions of PBCL Sections 1741 and 1742, Article VII does not require the Registrant to determine the availability of indemnification by the procedures or the standard of conduct specified in Sections 1741 or 1742 of the PBCL. A person who has incurred an indemnifiable expense or liability has a right to be indemnified independent of any procedures or determinations that would otherwise be required, and that right is enforceable against the Registrant as long as indemnification is not prohibited by law. To the extent indemnification is permitted only for a portion of a liability, the bylaw provisions require the Registrant to indemnify such portion. If the indemnification provided for in Article VII is unavailable for any reason in respect of any liability or portion thereof, the bylaws require the Registrant to make a contribution toward the liability. Indemnification rights under the bylaws do not depend upon the approval of any future board of directors.

Section 7.04 of the Registrant's bylaws also authorizes the Registrant to further effect or secure its indemnification obligations by entering into indemnification agreements, maintaining insurance, creating a trust fund, granting a security interest in its assets or property, establishing a letter of credit, or using any other means that may be available from time to time. Section 1747 of the PBCL also enables a business corporation to purchase and maintain insurance on behalf of a person who is or was serving as a representative of the corporation or is or was serving at the request of the corporation as a representative of another entity against any liability asserted against that representative in his capacity as such, whether or not the corporation would have the power to indemnify him against that liability under the PBCL. The Registrant maintains, on behalf of its directors and officers, insurance protection against certain liabilities arising out of the discharge of their duties, as well as insurance covering the Registrant for indemnification payments made to its directors and officers for certain liabilities. The premiums for such insurance are paid by the Registrant.

ITEM 16. Exhibits

Exhibit No.	**Description**
1.1**	Form of Underwriting Agreement
4.1	Amended and Restated Articles of Incorporation (filed as Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed on May 18, 2020 and incorporated herein by reference).
4.2	Amended and Restated Bylaws, effective as of December 23, 2020 (filed as Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed on December 28, 2020 and incorporated herein by reference).
5.1*	Opinion of Ballard Spahr LLP.
23.1*	Consent of PricewaterhouseCoopers LLP.
23.2*	Consent of Deloitte & Touche LLP.
23.3*	Consent of Ballard Spahr LLP (included in Exhibit 5.1).
24.1*	Power of Attorney (See page II-6 of this Registration Statement).

* Filed herewith.

** To be filed, if necessary, as an exhibit to a post-effective amendment to this registration statement or as an exhibit to a Current Report on Form 8-K and incorporated herein by reference.

ITEM 17. Undertakings

(a) The undersigned Registrant hereby undertakes:

(1) To file, during any period in which offers or sales are being made, a post-effective amendment to this registration statement:

(i) to include any prospectus required by Section 10(a)(3) of the Securities Act;

(ii) to reflect in the prospectus any facts or events arising after the effective date of this registration statement (or the most recent post-effective amendment thereof) which, individually or in the aggregate, represent a fundamental change in the information set forth in this registration statement. Notwithstanding the foregoing, any increase or decrease in volume of securities offered (if the total dollar value of securities offered would not exceed that which was registered) and any deviation from the low or high end of the estimated maximum offering range may be reflected in the form of prospectus filed with the Commission pursuant to Rule 424(b) if, in the aggregate, the changes in volume and price represent no more than 20 percent change in the maximum aggregate offering price set forth in the "Calculation of Registration Fee" table in the effective registration statement;

(iii) to include any material information with respect to the plan of distribution not previously disclosed in this registration statement or any material change to such information in this registration statement;

provided, *however*, that: paragraphs (a)(1)(i), (a)(1)(ii) and (a)(1)(iii) of this section do not apply if the registration statement is on Form S-3 and the information required to be included in a post-effective amendment by those paragraphs is contained in reports filed with or furnished to the Commission by the Registrant pursuant to Section 13 or Section 15(d) of the Securities Exchange Act that are incorporated by reference in this registration statement, or is contained in a form of prospectus filed pursuant to Rule 424(b) that is part of the registration statement.

(2) That, for the purpose of determining any liability under the Securities Act, each such post-effective amendment shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at that time shall be deemed to be the initial bona fide offering thereof.

(3) To remove from registration by means of a post-effective amendment any of the securities being registered which remain unsold at the termination of the offering.

(4) That, for the purpose of determining liability under the Securities Act to any purchaser:

(A) Each prospectus filed by the Registrant pursuant to Rule 424(b)(3) shall be deemed to be part of this registration statement as of the date the filed prospectus was deemed part of and included in this registration statement; and

(B) Each prospectus required to be filed pursuant to Rule 424(b)(2), (b)(5), or (b)(7) as part of a registration statement in reliance on Rule 430B relating to an offering made pursuant to Rule 415(a)(1)(i), (vii) or (x) for the purpose of providing the information required by Section 10(a) of the Securities Act shall be deemed to be part of and included in this registration statement as of the earlier of the date such form of prospectus is first used after effectiveness or the date of the first contract of sale of securities in the offering described in the prospectus. As provided in Rule 430B, for liability purposes of the issuer and any person that is at that date an underwriter, such date shall be deemed to be a new effective date of this registration statement relating to the securities in this registration statement to which that prospectus relates, and the offering of such securities at that time shall be deemed to be the initial bona fide offering thereof. Provided, however, that no statement made in a registration statement or a prospectus that is part of this registration statement or made in a document incorporated or deemed incorporated by reference into this registration statement or prospectus that is part of this registration statement will, as to a purchaser with a time of contract of sale prior to such effective date, supersede or modify any statement that was made in this registration statement or prospectus that was part of this registration statement or made in any such document immediately prior to such effective date.

(b) The undersigned Registrant hereby undertakes that, for purposes of determining any liability under the Securities Act, each filing of the Registrant's annual report pursuant to Section 13(a) or Section 15(d) of the Securities Exchange Act (and, where applicable, each filing of an employee benefit plan's annual report pursuant to Section 15(d) of the Securities Exchange Act) that is incorporated by reference in this registration statement shall be deemed to be a new registration statement relating to the securities offered therein, and the offering of such securities at that time shall be deemed to be the initial bona fide offering thereof.

(c) Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers and controlling persons of the Registrant pursuant to the foregoing provisions, or otherwise, the Registrant has been advised that in the opinion of the Securities and Exchange Commission such indemnification is against public policy as expressed in the Securities Act and is, therefore, unenforceable. In the event that a claim for indemnification against such liabilities (other than the payment by the Registrant of expenses incurred or paid by a director, officer or controlling person of the Registrant in the successful defense of any action, suit or proceeding) is asserted by such director, officer or controlling person in connection with the securities being registered, the Registrant will, unless in the opinion of its counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question whether such indemnification by it is against public policy as expressed in the Securities Act and will be governed by the final adjudication of such issue.

SIGNATURES

Pursuant to the requirements of the Securities Act, the Registrant certifies that it has reasonable grounds to believe that it meets all of the requirements for filing on Form S-3 and has duly caused this Registration Statement to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Bryn Mawr, Commonwealth of Pennsylvania, on this 21st day of June, 2021.

ESSENTIAL UTILITIES, INC.

By: /s/ Christopher H. Franklin
Christopher H. Franklin
Chairman, President and Chief Executive Officer

POWER OF ATTORNEY

Each person whose signature appears below hereby appoints Daniel J. Schuller, Chief Financial Officer of Registrant, and Christopher P. Luning, Executive Vice President, General Counsel and Corporate Secretary of Registrant, and each of them acting individually, as his or her true and lawful attorneys-in-fact, with full power of substitution and resubstitution, with the authority to execute in the name of each such person, and to file with the Securities and Exchange Commission, together with any exhibits thereto and other documents therewith, any and all amendments to this registration statement (including post-effective amendments and all other related documents) necessary or advisable to enable the registrant to comply with the Securities Act of 1933, and any rules, regulations and requirements of the Securities and Exchange Commission in respect thereof, which amendments may make such changes in the registration statement as the aforesaid attorney-in-fact executing the same deems appropriate. Pursuant to the requirements of the Securities Act of 1933, as amended, this Registration Statement has been signed below by the following persons in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Christopher H. Franklin Christopher H. Franklin	President, Chief Executive Officer and Chairman (Principal Executive Officer)	June 21, 2021
/s/ Daniel J. Schuller Daniel J. Schuller	Executive Vice President and Chief Financial Officer (Principal Financial Officer)	June 21, 2021
/s/ Robert A. Rubin Robert A. Rubin	Senior Vice President, Controller and Chief Accounting Officer (Principal Accounting Officer)	June 21, 2021
/s/ Elizabeth B. Amato Elizabeth B. Amato	Director	June 21, 2021
/s/ Daniel J. Hilferty Daniel J. Hilferty	Director	June 21, 2021
s/ Francis O. Idehen Francis O. Idehen	Director	June 21, 2021
/s/ Edwina Kelly Edwina Kelly	Director	June 21, 2021
s/ Ellen T. Ruff Ellen T. Ruff	Director	June 21, 2021
/s/ Lee C. Stewart Lee C. Stewart	Director	June 21, 2021
/s/ Christopher C. Womack Christopher C. Womack	Director	June 21, 2021

Ballard Spahr LLP

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June 21, 2021

Essential Utilities, Inc.
762 West Lancaster Avenue
Bryn Mawr, PA 19010

Re: Essential Utilities, Inc. - Registration Statement on Form S-3, filed on June 21, 2021

Ladies and Gentlemen:

We have acted as counsel to Essential Utilities, Inc., a Pennsylvania corporation (the "Company"), in connection with the preparation and filing with the Securities and Exchange Commission (the "Commission") of the Company's Registration Statement on Form S-3, dated the date hereof (the "Registration Statement"), under the Securities Act of 1933, as amended (the "Securities Act"), relating to the resale by the selling shareholder named therein (the "Selling Shareholder") from time to time of 21,661,095 shares (the "Shares") of common stock, par value $0.50 per share (the "Common Stock").

The Shares may be sold by the Selling Shareholder from time to time on a delayed or continuous basis pursuant to Rule 415 under the Securities Act.

In so acting, we have examined originals or copies (certified or otherwise identified to our satisfaction) of (i) the Amended and Restated Articles of Incorporation of the Company together with all amendments thereto; (ii) the Amended and Restated Bylaws of the Company; (iii) the Registration Statement and the exhibits thereto; (iv) the prospectus contained within the Registration Statement; (v) such corporate records, agreements, documents and other instruments; and (vi) such certificates or comparable documents of public officials and other sources believed by us to be reliable, and of officers and representatives of the Company, and have made such inquiries of such officers and representatives, as we have deemed relevant and necessary as a basis for the opinions hereinafter set forth.

In such examination, we have assumed the genuineness of all signatures, the legal capacity of all natural persons, the authenticity of all documents submitted to us as originals, the conformity to original documents of all documents submitted to us as certified, conformed or photostatic copies and the authenticity of the originals of such latter documents. As to all questions of fact material to this opinion that have not been independently established, we have relied upon certificates or comparable documents of officers and representatives of the Company.

We have also assumed that (i) the Registration Statement and any amendments or supplements thereto (including any post-effective amendments) will have become effective and comply with all applicable laws and no stop order suspending the Registration Statement's effectiveness will have been issued and remain in effect, in each case, at the time the Securities are offered or issued as contemplated by the Registration Statement, (ii) the Company has timely filed all necessary reports pursuant to the Securities Exchange Act of 1934, as amended, which are incorporated into the Registration Statement by reference, and (iii) the Shares will be issued and sold in compliance with applicable federal and state securities laws and in the manner stated in the Registration Statement.

Based on the foregoing, and subject to the qualifications stated herein, we are of the opinion that the Shares issued to the Selling Shareholder have been duly authorized and are validly issued, fully paid and non-assessable.

The opinion expressed above with respect to validity, binding effect and enforceability are subject to applicable bankruptcy, insolvency, fraudulent conveyance, reorganization, moratorium and similar laws affecting creditors' rights and remedies generally, and subject, as to enforceability, to general principles of equity, including principles of commercial reasonableness, good faith and fair dealing (regardless of whether enforcement is sought in a proceeding at law or in equity) and except that rights to indemnification and contribution thereunder may be limited by federal or state securities laws or public policy relating thereto.

We express no opinion as to the laws of any jurisdiction other than the federal laws of the United States of America and the laws of the Commonwealth of Pennsylvania.

We hereby consent to the use of this letter as an exhibit to the Registration Statement and to any and all references to our firm in the prospectus which is a part of the Registration Statement. In giving this consent, we do not admit that we are within the category of persons whose consent is required by Section 7 of the Securities Act and the rules and regulations promulgated thereunder.

Very truly yours,

/s/ Ballard Spahr LLP

Exhibit 23.1

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We hereby consent to the incorporation by reference in this Registration Statement on Form S-3 of Essential Utilities, Inc. of our report dated March 1, 2021 relating to the financial statements, financial statement schedule and the effectiveness of internal control over financial reporting, which appears in Essential Utilities, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2020. We also consent to the reference to us under the heading "Experts" in such Registration Statement.

/s/ PricewaterhouseCoopers LLP
Philadelphia, Pennsylvania
June 21, 2021

Exhibit 23.2

CONSENT OF INDEPENDENT AUDITORS

We consent to the incorporation by reference in this Registration Statement on Form S-3 of Essential Utilities, Inc. of our report dated April 1, 2020, relating to the consolidated financial statements of LDC Funding LLC and its subsidiaries as of December 31, 2019 and 2018 and for each of the three years in the period ended December 31, 2019, which appears in Essential Utilities, Inc.’s Current Report on Form 8-K filed on April 15, 2021. We also consent to the reference to us under the heading "Experts" in such Registration Statement.

DELOITTE & TOUCHE LLP

/s/ Deloitte & Touche LLP

Pittsburgh, Pennsylvania

June 21, 2021

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR13. Attach a chart explaining company's corporate relationship to its affiliates showing system structure.

A. Please see the attached.

ESSENTIAL UTILITIES, INC.
Company and Subsidiary List - 8/18/2021

Company Name	State of Inc.	Regulated or Non-Regulated	Type of Business	Date Acquired or Created
A. Essential Utilities, Inc.	PA	Non-regulated	Parent Company	11/11/1968
1 Aqua Acquisition Corporation	PA	Non-regulated	Holding Company	8/2/2002
2 Essential Assistance Initiatives, Inc.	PA	Non-regulated	Charitable Non profit	4/3/2018
3 Essential Foundation	PA	Non-regulated	Non profit, non stock	12/21/1998
4 Aqua Development, Inc.	TX	Regulated	Regulated services	7/29/2003
5 Aqua Georgia, Inc.	GA	Non-regulated	Wastewater services	12/7/2009
6 Aqua Holdings, Inc.	PA	Non-regulated	Infrastructure Co.	2/15/2011
a. Aqua Tanks, LLC	PA	Non-regulated	Infrastructure Investment	6/4/2013
b. Old Dominion Pipeline Company, LLC	PA		Infrastructure Investment	7/16/2013
7 Aqua Illinois, Inc.	IL	Regulated	Regulated utility	3/10/1999
8 Aqua Indiana, Inc.	IN	Regulated	Regulated utility	7/31/2003
a. Hendricks County Wastewater, LLC	IN	Non-Regulated	Wastewater services	7/31/2003
9 Aqua Indiana - Western Hancock	IN	Non-regulated	Holding Company	12/4/2007
a. Western Hancock Utilities, LLC	IN	Regulated	Wastewater services	12/4/2007
b. SaniTech, Inc.	IN			11/17/2016
c. Southeastern Utilities, Inc.	IN			9/30/2016
10 Aqua Infrastructure, LLC	PA	Non-regulated Joint Venture	Infrastructure Investment	7/22/2011
a. Charlevoix Capital Ventures, LLC	PA	Non-regulated	Infrastructure Investment	2/14/2012
11 Aqua New Jersey, Inc.	NJ	Regulated	Regulated utility	7/31/2003
12 Aqua North Carolina, Inc.	NC	Regulated	Regulated utility	3/10/1999
13 Aqua Ohio, Inc.	OH	Regulated	Regulated utility	3/10/1999
a. Aqua Ohio Wastewater, Inc	OH	Regulated	Regulated utility	4/22/2016
14 Aqua Operations, Inc.	DE	Non-regulated	Non-regulated services	7/31/2003
15 Aqua Pennsylvania	PA	Regulated	Regulated utility	5/7/1984
a. Aqua Pennsylvania Wastewater, Inc.	PA	Regulated	Regulated utility	11/22/2000
b. Honesdale Consolidated Water Company	PA	Regulated	Regulated utility	7/31/1989
16 Aqua Resources, Inc.	DE	Non-regulated	Non-regulated services	3/18/2005
a. Aqua Water Specialties, LLC	PA			
b. Aqua Wastewater Management, Inc.	PA	Non-regulated	Non-regulated services	4/22/1996
c. Aqua Infrastructure Rehabilitation Co., LLC	DE	Non-regulated	Non-regulated services	6/25/2014
17 Aqua Services, Inc.	PA	Non-regulated	Intercompany support	7/31/2003
18 Aqua Texas, Inc.	TX	Regulated	Regulated utility	4/22/1996
a. Harper Water Company, Inc.	TX	Regulated	Regulated utility	7/31/2003
19 Aqua Utilities Florida	FL	Regulated	Regulated utility	6/27/2007
20 Aqua Utilities, Inc.	TX	Regulated	Regulated utility	7/2/2003
a. Kerrville South Water Co				
21 Aqua Virginia, Inc.	VA	Regulated	Regulated utility	7/31/2003
a. Great Bay Utilities, Inc.	VA	Regulated	Regulated utility	7/19/2018
22 Utility & Municipal Services, Inc.	PA	Non-regulated	Non-regulated services	2/15/1989
23 LDC Funding, LLC	DE	Non-regulated	Holding Company	9/9/2008
a. LDC Holdings LLC	DE	Non-regulated	Holding Company	6/24/2008
i PNG Companies LLC	DE	Non-regulated	Holding Company	9/9/2008
1 PNG Homeworks LLC	DE	Non-Regulated	Competitive Warranty Services	9/3/2013
2 PNG Gathering LLC	DE	Non-Regulated	Gathering Asset Holdings	9/30/2013
3 Peoples Natural Gas Company LLC	PA	Regulated	Regulated services	1/29/2010
4 Peoples Gas Company LLC	PA	Regulated	Regulated services	5/18/2011
5 Peoples Gas WV LLC	WV	Regulated	Regulated services	7/16/2013
6 Peoples Gas KY LLC	KY	Regulated	Regulated services	7/9/2013
7 Delta Natural Gas Company Inc.	KY	Regulated		10/7/1949
8 Delta Resources LLC	KY	Non-regulated		4/12/1984
9 Delgasco LLC	KY	Non-regulated		5/23/1986
10 Enpro LLC	KY	Non-regulated		5/23/1986
b Peoples Service Company	PA	Non-Regulated		5/15/2012
c Peoples Gas Marketing LLC	PA	Non-Regulated		10/24/2010

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR14. If the utility plans to make a formal claim for a specified allowable rate of return, provide the following data in statement or exhibit form:

a. Claimed capitalization and capitalization ratios with supporting data.

b. Claimed cost of long-term debt with supporting data.

c. Claimed cost of short-term debt with supporting data.

d. Claimed cost of total debt with supporting data.

e. Claimed cost of preferred stock with supporting data.

f. Claimed cost of common equity with supporting data.

A. Please refer to the direct testimony of Paul R. Moul and the accompanying Exhibit 4-A for the Company's claim for a specified allowable rate of return, including the details requested in items (a) through (f).

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR15. Supply copies of the following documents for the company and, if applicable, its parent:

a. Most recent annual report to shareholders including any statistical supplements.

b. Most recent SEC form 10K.

c. All SEC form 10Q reports issued within the preceding 12 months of the date of submittal of the rate increase request.

A. This information is publicly available on the Company's website:
(a) https://www.essential.co/financial-information/annual-reports
(b) https://www.essential.co/sec-filings/sec-filing/10-k/0001562762-21-000081
(c) https://www.essential.co/financial-information/sec-filings

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR16. Supply copies of the company's balance sheets for each month for the last 2 years.

A. Please refer to the Company's response to OD1.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR17. Please provide the bond rating history for the Company and, if applicable, its parent from the major credit rating agencies for the last five years.

A. The bond ratings history from the credit rating agencies is as follows:

Year	S&P Global Ratings Aqua PA	S&P Global Ratings Essential Utilities	Moody's Investor Service Essential Utilities
2016	A+	Not Rated	Not Rated
2017	A+	Not Rated	Not Rated
2018	A+	Not Rated	Not Rated
2019	A+	A	Baa2
2020	A	A	Baa2

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR18. Provide copies of all bond rating reports relating to the company and, if applicable, its parent for the past 2 years.

A. Please refer to the Company's response to RR17.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR19. Supply copies of all presentations by the company's and, if applicable, its parent's management and securities analysts during the past 2 years, including presentations of financial projections.

A. Below is a link to the parent company's, Essential Utilities, Inc., material presented to analysts in August 2021. These presentations are substantially the same as those presented over the past two years, but has been continually updated with current information. Please refer to https://www.essential.co/events-and-presentations/events-calendar for previously presented presentations

The presentations have also included copies of the parent company's Annual Report and SEC Filings.

https://www.essential.co/static-files/ad1b100c-bed4-466f-87f6-7928808eba63

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR20. Provide a listing of all securities issuances for the company and, if applicable, its parent projected for the next 2 years. The response shall identify for each projected issuance the date, dollar amount, type of security, and effective cost rate.

A. On January 26, 2021, the Company filed a securities certificate application with the PAPUC requesting authority to issue first mortgage bonds no later than December 31, 2021 in an amount not to exceed $100,000,000 at current market rates.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR21. Identify any plan by the company to refinance high cost long-term debt or preferred stock.

A. The Company continually looks for ways to lower its cost of debt. Please refer to the Company's response to RR9 for refinancing activity since the prior rate case.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR22. Provide copies of all securities analysts' reports relating to the company and its parent, or both, issued within the past 2 years.

A. Please refer to the files that were electronically submitted to the Secretary's Bureau and is available for review on the electronic docket associated with this filing on the commission's website under Docket Nos. R-2021-3027385 and R-2021-3027386.

Americas Utilities

Analyzing water utility premiums - Upgrade AWK to Buy, Initiate WTRG at Neutral

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We initiate coverage on Essential Utilities Inc. (WTRG) and transfer primary coverage on American Water (AWK) from Michael Lapides to Insoo Kim with the following updated views:

Analyzing the water utility premium valuation: fundamentals + ESG. While we recognize the current 10-11x relative P/E premium versus electric/gas utilities, we view this as justified given two quantifiable advantages: 1) our analysis shows every $1 invested in water assets is worth more given a longer depreciable life vs electric, and 2) long visibility of above-average growth due to significant water pipe investment needs. In addition, we see continued ESG momentum sustaining additional relative premium for water utilities. With this in mind:

- **We upgrade AWK to Buy with a $146 price target (16% total return)** as we see 1) best-in-class 8.3% EPS CAGR, 2) one of the highest beta-adjusted returns among Regulated Utilities (Exhibit 3), and 3) its ESG-favorable position as the only large-cap, pure-play water utility in the U.S. We view this defensive utility offering investors an attractive investment opportunity with double-digit upside potential.
- **We initiate coverage of WTRG at Neutral with a $45 price target (7% total return)** given 1) robust 6.6% EPS CAGR post Peoples Gas acquisition, but 2) current multiples that largely reflect the water/gas sum-of-the-parts valuation.
- **AWK/WTRG both remain relatively defensive in the current COVID-19 environment,** outperforming the XLU by 7%/3% since March 1. Also, we favorably view their heavy residential revenue mix which could help offset potential near-term demand impact from commercial/industrial customers.

As highlighted in our recent note, we remain positive on the Utilities sector, both on an absolute and relative basis, given 10-year treasury yields below 1% and the regulated utilities' more resilient earnings power relative to that for the broader market, especially in the current COVID-19 environment. We see 15%/25% total return for Regulated Utilities and Diversified Utilities, respectively.

Goldman Sachs does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision. For Reg AC certification and other important disclosures, see the Disclosure Appendix, or go to www.gs.com/research/hedge.html. Analysts employed by non-US affiliates are not registered/qualified as research analysts with FINRA in the U.S.

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PM Summary: Premium water utility multiples are justified; buy AWK

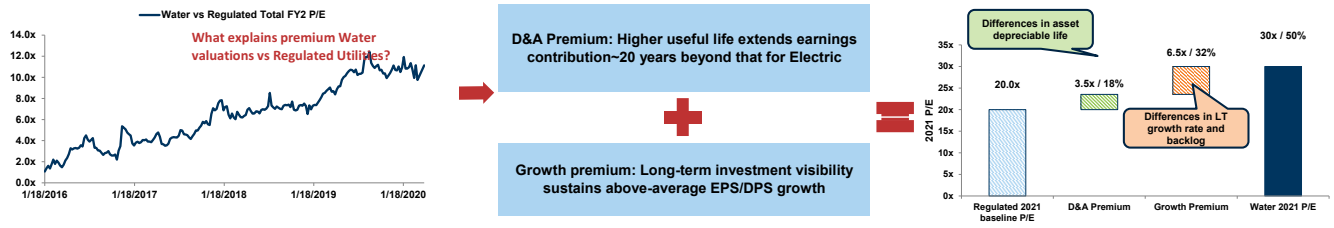
Despite the large relative P/E premiums for water utilities currently, we see two quantifiable advantages versus electric utilities that provide justification: 1) every $1 invested in water assets is worth more given a longer depreciable life, and 2) material organic/inorganic growth visibility that should sustain above-average earnings growth longer-term. Combined with a favorable ESG screen, we believe water utilities could see further relative multiple expansion from current levels.

To this end, we transfer primary coverage of AWK from Michael Lapides to Insoo Kim and upgrade from Neutral to Buy given best-in-class growth, more robust credit metrics, and its ESG-friendly status as a large-cap pure-play water utility, while we initiate on WTRG with a Neutral rating as we believe valuations fairly reflect the water/gas business mix.

Do water utilities deserve the current premium? We believe so. Based on our new and detailed analysis (please refer to the following section), we see certain fundamental advantages that justify the current 11.3x premium versus electric utilities. The primary drivers include:

1. **D&A premium (3.5x):** Every $1 invested to longer useful-life water assets (50 years vs. 30 years for electric) extends their value - translating into roughly 2% higher earnings growth.
2. **Growth premium (6.5x):** We see water utilities sustaining their above-average earnings/dividend growth over electric utilities over at least the next 15 years, given significant water investment needs in the U.S.
3. **Other qualitative factors:** 1) scarcity of water investor-owned utilities (IOUs), 2) ESG-related premium for pure-play water utilities (which we believe may impact WTRG given its new exposure to gas utilities).

Exhibit 1: Longer useful life and long-term investment visibility largely justify premium water valuations vs. electric/gas



Source: Goldman Sachs Global Investment Research

Following our analysis, we revise our regulated baseline water multiple from 25.5x to 30.0x, which incorporates the 10x D&A/growth premium to our 20x base P/E for electric/gas utilities on 2021E EPS.

With this revised base, we make the following recommendations:

- **Upgrade AWK to Buy**: **best-in-class growth and a pure-play large-cap water utility.** We expect AWK to continue to achieve above-average EPS growth, with our

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estimates (1% above consensus) implying an 8.3% EPS CAGR from 2019-2022 - at the middle of the company's 7-10% guidance - driven by a combination of core regulated investments, continued municipal utility acquisitions, and contributions from its contracted segments. Despite the 16% total return screening as comparable to 15% for Regulated Utilities, we believe AWK's below-average beta and ESG-friendly profile could drive further relative multiple expansion for this secular growth story.

- **Initiate on WTRG at Neutral**: **water/gas mix fully reflected in valuations.** We see WTRG's recent acquisition of Peoples Gas, a private gas utility business boosting consolidated rate base growth to 9.7% from 2019-2022 versus 9% prior as a stand-alone water utility, along with benefits from acquisition synergies. Our estimates - largely in-line with consensus - reflect a 6.6% EPS CAGR from 2019-2022, although we expect long-run growth to trend closer to rate base growth. We see the current 4.3x valuation discount versus water peers as largely appropriate given our view that gas utilities warrant a lower multiple. Our $45 target incorporates a 27.3x blended P/E multiple, resulting in a 7% total return versus the sector average at 15%.

Balance sheet/credit metrics favor AWK. While both AWK and WTRG maintain an A issuer rating by S&P, we see AWK's 15-17% FFO/debt, versus WTRG's 12%, through 2022 more favorably in the current economic environment. Parent debt levels - sub-20% for AWK verus 25-30% for WTRG - also screen better for AWK, as WTRG's recently completed Peoples Gas acquisition contributing to a more levered balance sheet.

How much near-term demand impact do AWK/WTRG face from COVID-19? Could be modest. We note that both AWK and WTRG derive less than 10% of revenues from industrial customers, while more than 60% from residential customers. GIven our view (see recent note) that residential volumes should see an increase in demand, we estimate that a +3%/-5%/-10% change in residential/commercial/industrial demand could actually result in a relatively neutral net income impact, while acknowledging the difficulty in estimating the net outcome.

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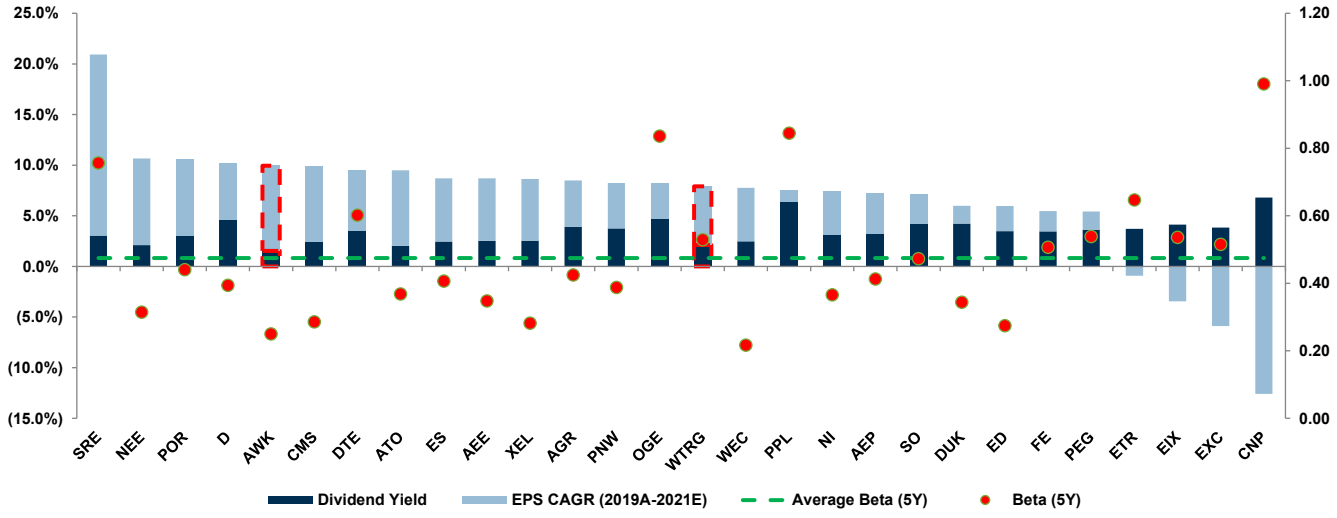
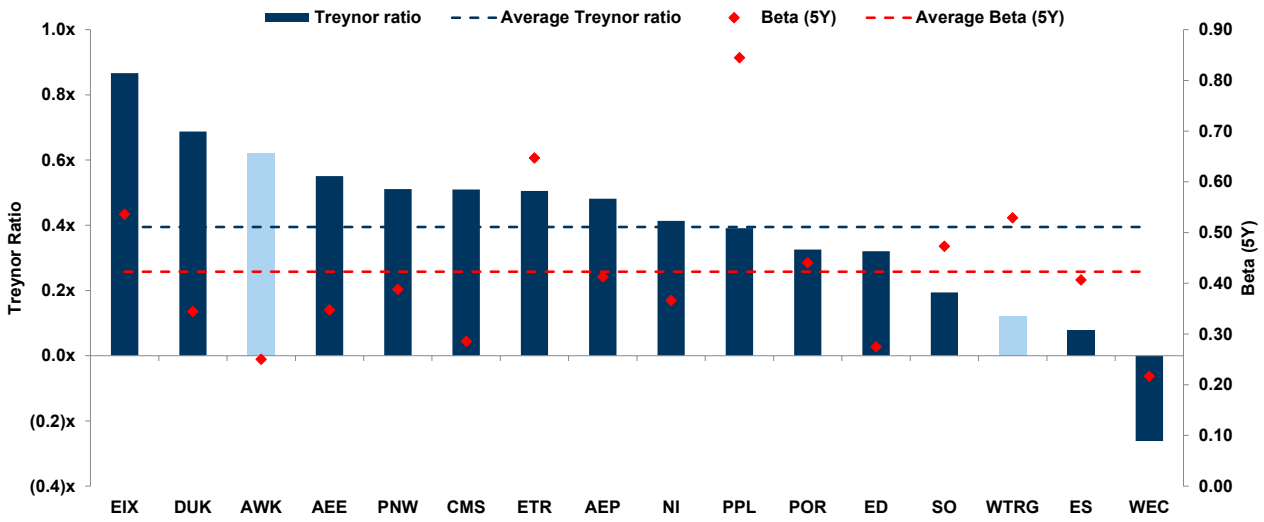
Exhibit 2: We see AWK providing one of the best EPS growth and dividend yield in our coverage universe, all at a below-average beta...
Utilities coverage Dividend yield, EPS CAGR (2019A-2021E) & 5Y Beta



Source: FactSet, Company data, Goldman Sachs Global Investment Research

Exhibit 3: ...with one of the best beta-adjusted total return potential among Regulated Utilities.
AWK/WTRG Risk-adjusted total return (Treynor ratio) vs Regulated Utilities coverage



Source: FactSet, Goldman Sachs Global Investment Research

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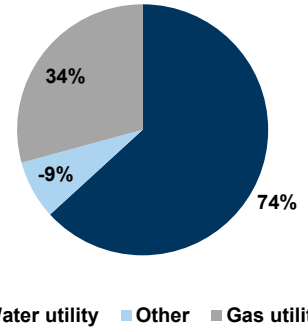
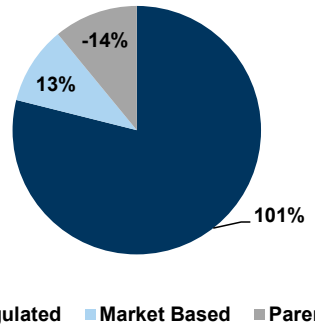
Exhibit 4: We favor AWK for its best-in-class EPS growth and ESG-friendly pure-play water profile
Company Summary

	WTRG	AWK
Rating	**Neutral (Initiating)**	**Buy (from Neutral)**
Total Return	**7%**	**16%**
Market Cap	**$9.6bn**	**$23.0bn**
EPS Mix (2020E)		
Utility States	**Water:** PA, TX, IL, IN, OH, NC, VA, NJ **Gas:** PA. WV, KY	**Water (regulated):** NJ, PA, MO, IL, CA, IN, WV, GA, HI, IA, KY, MD, MI, NY, TN, VA
Customer Growth/ Customer count (2018A)	**Water utility -** 2.3% (Growth through acquisition - 1.4%, Organic growth - 0.9%) **Customer count** - 10.1 mn	**Water utility -** 0.7% **(**Growth through acquisition - 0.3%, organic growth - 0.4%**)** **Customer count -** 31.8 mn
Reg. Utility Earnings Growth ('19-'22E)	6.6%	8.3%
Investment Thesis	(+) Peoples Gas acquisition boosts rate base growth to 9-10% and 6-7% EPS growth through 2022 (+) Synergy from Peoples Gas acquisition (-) Water/gas mix a potential headwind to further multiple expansion from an ESG perspective	(+) Above-average 8.3% EPS CAGR from 2019-2022E and 10% DPS CAGR (+) Size benefits to take advantage of accretive municipal acquisition (+) Status as the only large-cap, pure-play water utility - favorable from a scarcity/ESG perspective
Near-term Risk	* Lower than expected synergy benefits from the acquisition of Peoples gas * Water/gas utility growth impacted by current COVID-19 pandemic	* Regulated/non-regulated segment growth impacted by current COVID-19 pandemic
Company Overview	*Water utility business in 8 states (PA being the largest one) *Recent acquisition of Peoples Gas adds PA, WV and KY gas jurisdictions * 2nd largest publicly traded water/gas utility company	* Largest publicly traded utility company in the US *Owns water and waste water utility services to residential, commercial and industrial customers *Operates in 46 states in the US and Ontario, Canada
Credit Rating (Issuer Credit) (Moody's/S&P)	--/A	Baa1/A
Sub-Sector (% earnings)	Water utility (70%) Gas utility (30%)	Water utility (87%) Non-regulated businesses (13%)

Source: Company data, Goldman Sachs Global Investment Research

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Exhibit 5: AWK has largely maintained its ESG fund overweight status, while WTRG has dropped more meaningfully since prior to Peoples Gas acquisition completion

Top 10 ESG Relative overweight companies in US as of Sept 2019 and Apr 2020

Top 10 ESG Relative overweight companies in US (April 2020)

	Company	GICS 1
1	NASDAQ INC ORD	Financials
2	XYLEM INC ORD	Industrials
3	IDEX CORP ORD	Industrials
4	EPAM SYSTEMS INC ORD	Information Technology
5	TRIMBLE INC ORD	Information Technology
6	UBER TECHNOLOGIES INC ORD	Industrials
7	GUIDEWIRE SOFTWARE INC ORD	Information Technology
8	PTC INC ORD	Information Technology
9	DENTSPLY SIRONA INC ORD	Health Care
10	VERISK ANALYTICS INC ORD	Industrials
14	**AMERICAN WATER WORKS COMPANY IN**	**Utilities**
21	**ESSENTIAL UTILITIES INC ORD**	**Utilities**

Top 10 ESG Relative overweight companies in US (Sept 2019)

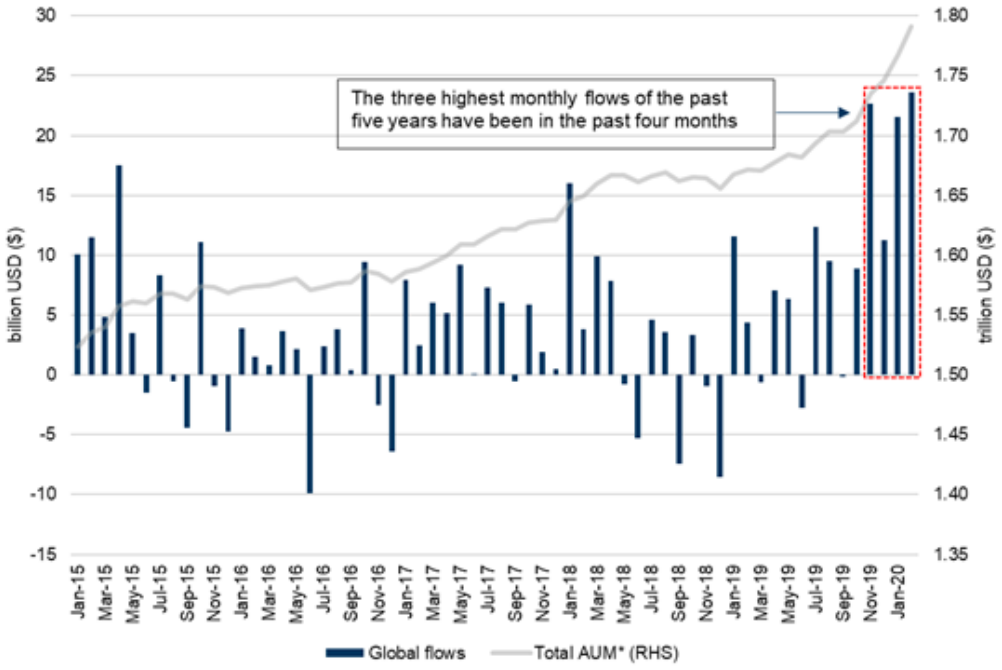
	Company	GICS 1
1	Xylem Inc	Industrials
2	Trimble Inc	Information Technology
3	**Aqua America Inc**	**Utilities**
4	First Solar Inc	Information Technology
5	A.O. Smith Corp	Industrials
6	Hologic Inc	Health Care
7	**American Water Works Company Inc**	**Utilities**
8	Gap Inc	Consumer Discretionary
9	Toro Co	Industrials
10	First American Financial Corp	Financials

Companies with market caps > $5B and domiciled in US; *ESG Relative overweights are calculated by dividing a company's ESG fund universe ACWI constituent weighting over its ACWI weighting; ACWI= MSCI All Country Weight Index

Source: Bloomberg, Morningstar, Goldman Sachs Global Investment Research

Exhibit 6: GS SUSTAIN: Positive ESG flows have persisted remaining robust through the early phases of the COVID-19 crisis

Monthly ESG fund flows (January 2015 through February 2020)



*AUM values are derived from historical flows and agnostic of market effect

Source: Morningstar

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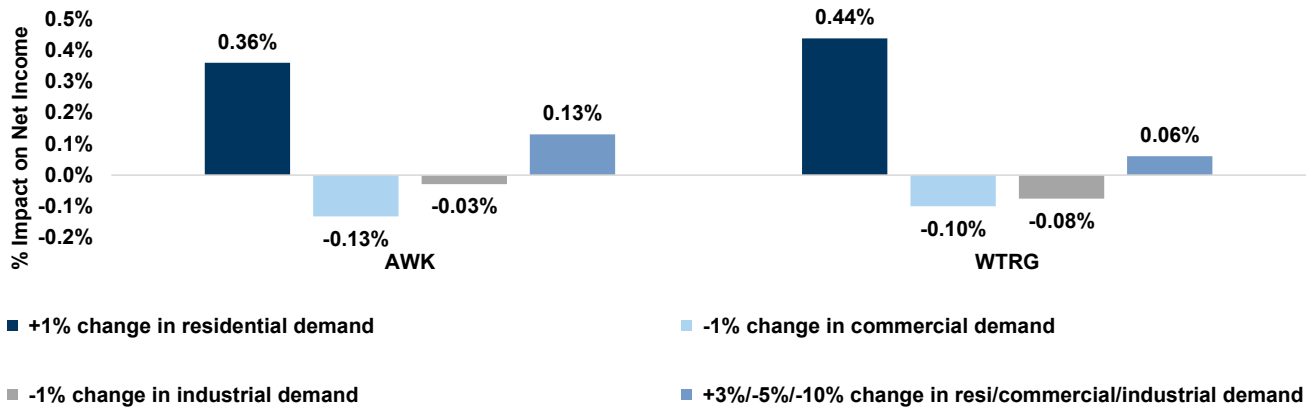
Exhibit 7: We see a moderate earnings impact for every 1% change in water demand, with higher residential demand that could potentially offset commercial/industrial declines
% Impact on Net Income from change in residential/commercial/industrial demand



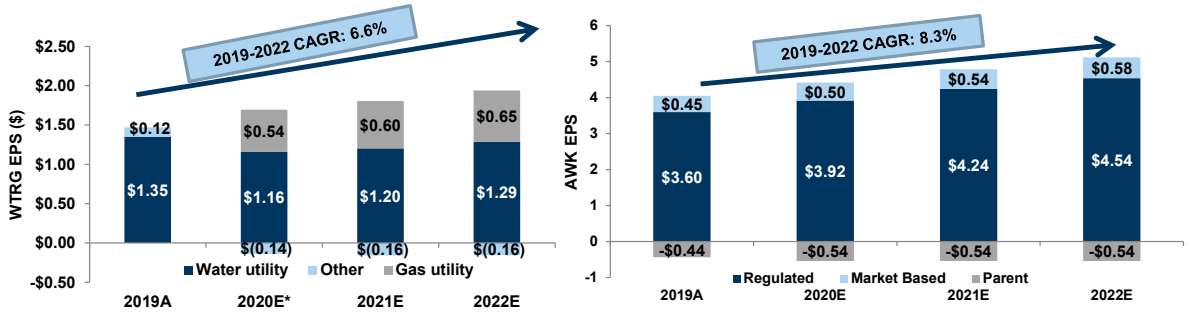
Source: Company data, Goldman Sachs Global Investment Research

Exhibit 8: We favor AWK's balance sheet and credit metrics versus WTRG, although both screen relatively stable in our view
AWK/WTRG GSe Credit metrics

Credit metrics (Gse)	AWK			WTRG		
	2020	2021	2022	2020	2021	2022
Net Debt/cap	61%	60%	58%	49%	51%	52%
Net Debt/EBITDA	5.2x	5.0x	4.7x	7.3x	6.4x	6.4x
FFO/Debt	15%	16%	17%	11%	12%	12%
Holdco debt (% of total debt)	19%	18%	18%	34%	29%	27%
Credit rating (Parent)	A/Baa1 (S&P/Moody's)			A/NR (S&P/Moody's)		

Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 9: We see robust EPS growth at AWK, with a more modest growth at WTRG through 2022 given timing of rate recovery and transitions in tax-advantaged mechanisms...
EPS 2019A-2022E



* 2020 incorporates full-year of Peoples Gas earnings ; 2021 summation for WTRG off by $0.01 due to rounding issue

Source: Company data, Goldman Sachs Global Investment Research

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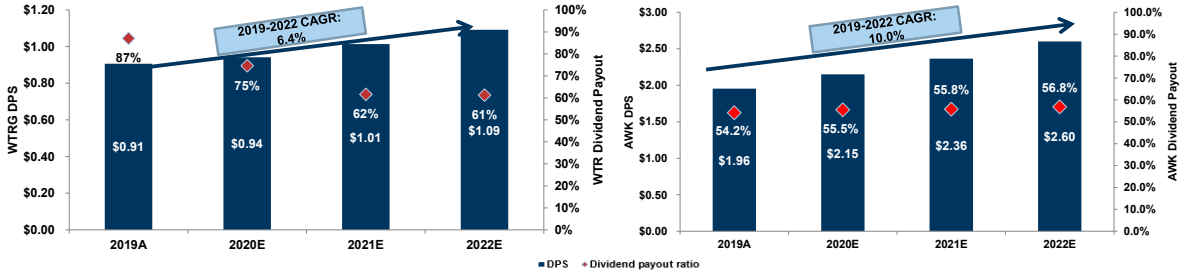
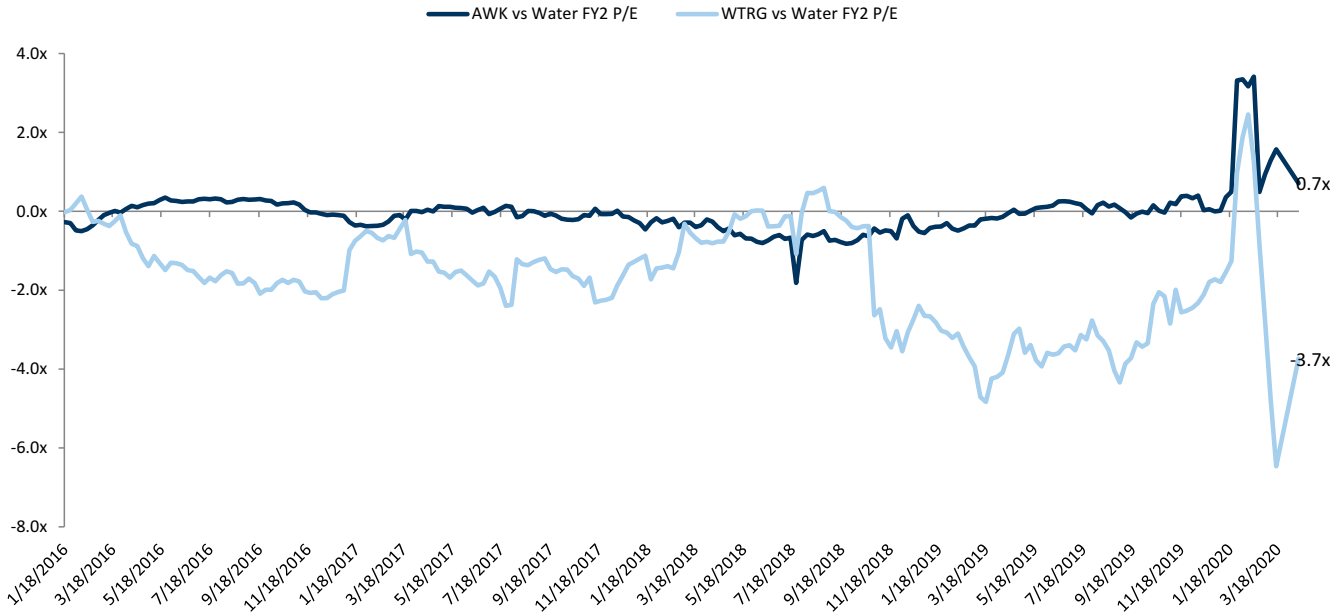
Exhibit 10: ...with a more robust dividend growth for AWK
DPS and payout as % of consolidated EPS



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 11: We view AWK's premium valuation as sustainable given its best-in-class growth and ESG-friendly profile, while WTRG's relative discount screens appropriate given its gas utility exposure
AWK & WTRG vs Water FY2 P/E



Source: Goldman Sachs Global Investment Research, FactSet

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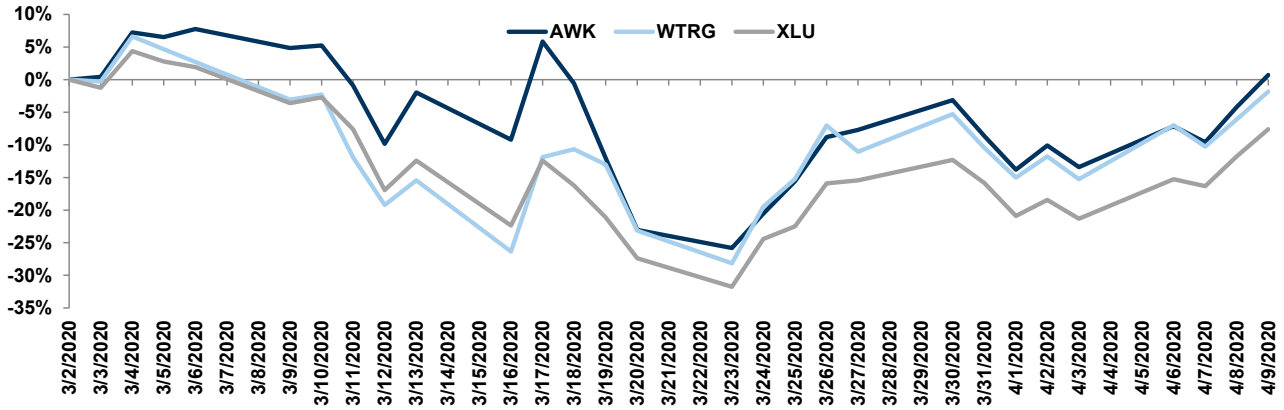
Exhibit 12: Both AWK and WTRG continue to remain relatively defensive in the current COVID-19 environment, outperforming the XLU since March 1

AWK/WTRG/XLU Performance since March 2020



Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 13: We expect further multiple expansion for AWK given best-in-class growth, low beta, and favorable ESG profile

Water Comparable Valuation

Water Utilities Comparable Analysis													
			Close	12-Mo	Tot Ret	EPS			P/E			Dividend	EPS CAGR
	Ticker	Rating	4/13/20	Px. Tgt	to Target	2019A	2020E	2021E	2019E	2020E	2021E	Yield	2019A-21E
American Water	**AWK**	**Buy**	**$127.24**	**$146**	**16%**	**$3.61**	**$3.88**	**$4.24**	**35.3x**	**32.8x**	**30.0x**	**1.5%**	**8.4%**
American States Water	AWR	NC	$86.42	--	--	$2.24	$2.21	$2.34	38.6x	39.0x	36.9x	1.3%	2.2%
Essential Utilities	**WTRG**	**Neutral**	**$42.80**	**$45**	**7%**	**$1.47**	**$1.56**	**$1.65**	**29.1x**	**27.5x**	**26.0x**	**2.1%**	**5.8%**
California Water Service	CWT	NC	$52.87	--	--	$1.31	$1.53	$1.70	40.4x	34.6x	31.1x	1.5%	14.0%
Middlesex Water Company	MSEX	NC	$62.37	--	--	$2.01	$2.04	$2.19	31.0x	30.6x	28.5x		4.3%
SJW Corp.	SJW	NC	$62.66	--	--	$0.82	$2.31	$2.50	76.4x	27.1x	25.1x	1.9%	74.5%
York Water Company	YORW	NC	$42.39	--	--	$1.11	$1.21	$1.25	38.2x	35.2x	33.9x		6.1%
Water Utilities Mean					**12%**				**41.3x**	**32.4x**	**30.2x**	**1.7%**	**16.5%**
Water Utilities Median					**12%**				**38.2x**	**32.8x**	**30.0x**	**1.5%**	**6.1%**
Regulated Utilities Mean					**15%**				**20.8x**	**20.1x**	**18.9x**	**3.2%**	**5.4%**
Regulated Utilities Median					**16%**				**19.6x**	**19.4x**	**18.4x**	**3.2%**	**5.6%**

Estimates for Non-Covered Companies represent Factset Consensus

Source: Goldman Sachs Global Investment Research, FactSet

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Water Utilities – abundant growth opportunities in fragmented market

Water utilities are responsible for the operation and maintenance of water treatment plants and distribution networks, crucial for ensuring reliability and quality of supply. Water and wastewater services are primarily the two sources of revenue for a water utility.

- **Water services involve: (1) sourcing, (2) treatment and (3) distribution of water.** We outline the three steps in further detail below:
  - **Pumping Station:** A pumping station abstracts water from aquifers, rivers, reservoirs and lakes, using pumps, pipes and electricity.
  - **Treatment Facility:** After drawing the water, it is sent to a treatment facility, where chemicals and filtration systems minimize impurities and meet federal, state and local quality standards. Chemical and electric costs stand out as the two largest O&M expenses at a treatment facility.
  - **Distribution System:** The US water pipe network stretches across 70,000 miles, distributing water to the ultimate customers. Key periods of water pipe installations include: (1) late 1800s, (2) the 1920s and (3) the 1940s/1950s. Given the age of the current distribution system, pipe replacement spending represents the largest share of investor owned utilities' capital spending budget for the foreseeable future.
- **Wastewater services** involve the collection of wastewater from customers' premises through sewer lines. The wastewater is then transported through a sewer network to a treatment facility, where it is treated to meet required regulatory standards for wastewater before being returned to the environment. The solid waste by-product of the treatment process is disposed of or recycled in accordance with applicable standards and regulations.

Aging infrastructure and increased regulation in the sector are primary drivers for the need to modernize the country's water and wastewater infrastructure related to water quality and the management of water and wastewater residual discharges. Because pipe assets last a long time, water systems that were built in the latter part of the 19th century and throughout much of the 20th century have not, for the most part, experienced the need for pipe replacement on a large scale. To put this aging infrastructure into context, the American Water Works Association (AWWA) estimates that the cost of restoring underground pipes will total at least $1 trillion through 2035, without including the cost of constructing new infrastructure or repairing treatment plants. The estimate assumes pipes are replaced at the end of their useful lives. Over a 40-year period, through 2050, AWWA estimates the needs will exceed $1.7 trillion. Replacement needs account for about 54% of the national total, with the balance attributable to population changes over that period.

The key regulations that govern the distribution of water include the Safe Drinking Water Act and the Clean Water Act:

- **Federal Safe Drinking Water Act (1974):** The Federal Safe Drinking Water Act

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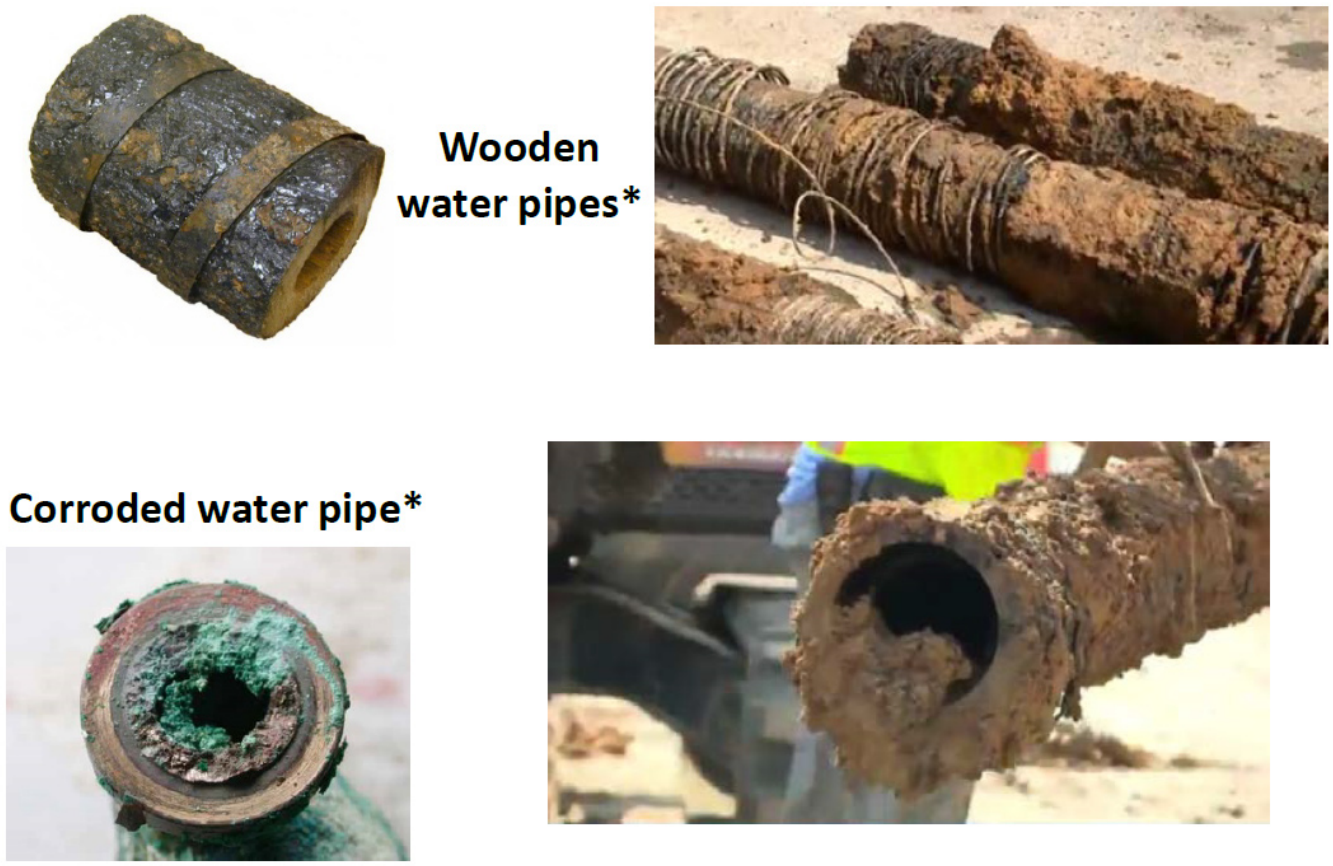
established national quality standards for drinking water. Under the SDWA, the EPA prescribes the legal limits of contaminants and sets water-testing schedules.

- **Clean Water Act (1972):** The Federal Clean Water Act regulates discharges from drinking water and wastewater treatment facilities into lakes, rivers, streams and groundwater.

Exhibit 14: The aging water and wastewater infrastructure in the United States require replacement and modernization, with at least $1 trillion investment potential through 2035
Aging US Pipe Infrastructure



*Not American Water Pipes

Source: AWK Dec 2017 Investor Presentation

The water utility sector is highly fragmented — more than 50,000 water utility systems exist nationwide — with investor-owned and privately held water utilities operating less than 15% of these systems. According to the U.S. Environmental Protection Agency (EPA), based on the 2015 U.S. Census American Housing Survey, approximately 89% of the U.S. population obtains its water from community water systems, and 11% of the U.S. population obtains its water from private wells. Of the approximately 50,000 community water systems in the U.S., 81% serve less than 3,300 customers, making the water industry the most fragmented of the major utility industries (natural gas, electric, water/wastewater). The majority of these community water systems are government-owned, and the balance of the systems are regulated utilities.

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Although not as fragmented as the water industry, the wastewater industry in the U.S. also presents opportunities for consolidation. According to the EPA's most recent survey of wastewater treatment facilities (which includes both government-owned facilities and regulated utility systems) in 2012, there were approximately 15,000 such facilities in the nation serving approximately 76% of the U.S. population. The remaining population represents individual homeowners with their own treatment facilities; for example, community on-lot disposal systems and septic tank systems. A majority of wastewater facilities are government-owned rather than regulated utilities.

Fair Market Value (FMV) legislation will continue to motivate consolidation of the water and wastewater industry, providing municipalities with an option for exiting the business if they are dealing with challenges associated with their aging, deteriorating water and wastewater assets, do not have the expertise or technical capabilities to continue to comply with ever-increasing environmental regulations or simply want to focus on other community priorities. The sector has been ripe for consolidation for decades and the largest water utilities have recently altered their strategic growth efforts to focus on buying mid-sized municipal water and wastewater systems fueled by fair market value (or FMV); legislation allows the water utilities to include into rate base the fair market value of the acquired municipal water assets instead of the depreciated original cost of water/wastewater assets. The legislation includes a process for engaging two independent utility valuation experts to perform appraisals that are filed with the public utility commission and then averaged and compared to the purchase price. The rate-making rate base is the lower of the average of the appraisals or the purchase price and is subject to regulatory approval. FMV is on the books in 10 states, including several of AWK/WTRG operating jurisdictions, and is pending before state legislatures in three more states.

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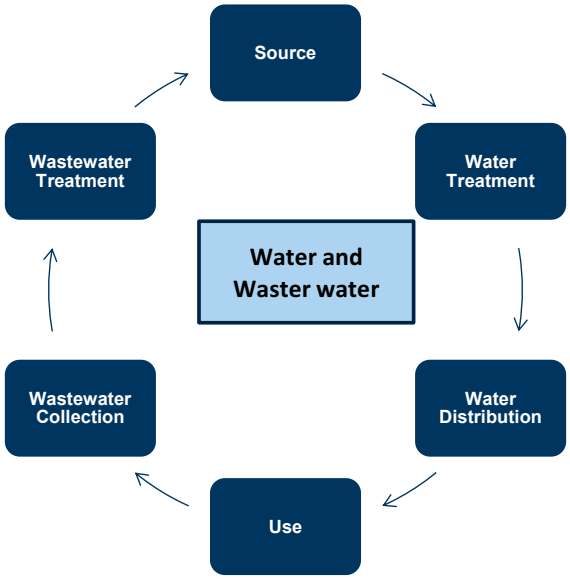
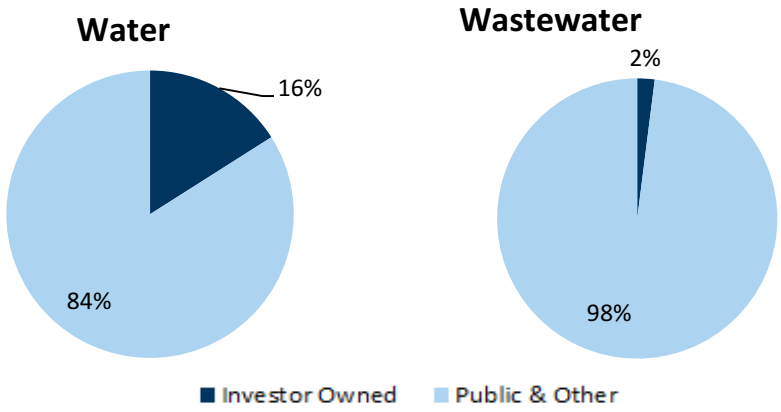
Exhibit 15: Water utilities are responsible for the operation and maintenance of water treatment plants and distribution networks, crucial for ensuring reliability and quality of supply
Water and Wastewater Cycle



Source: Goldman Sachs Global Investment Research

Exhibit 16: The sector remains ripe for consolidation given that investor-owned and privately held water utilities operate just 16% of these systems...
Water Industry- Investor Owned vs Public & Other market share



Source: Company data, Goldman Sachs Global Investment Research

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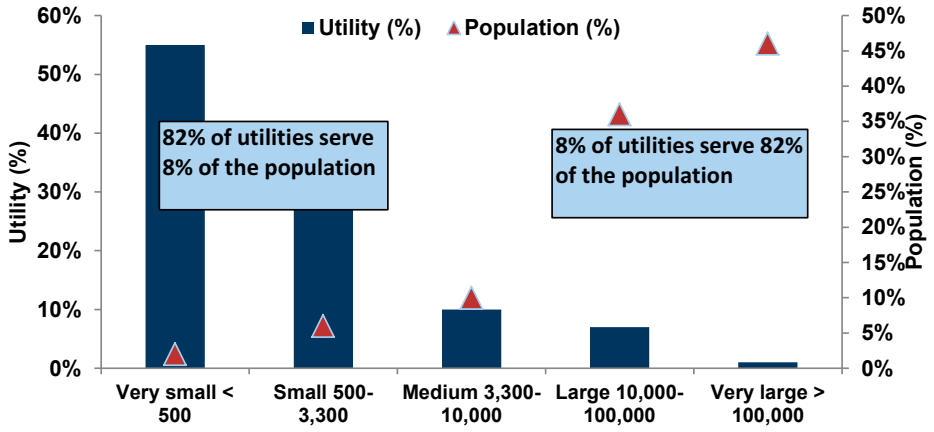
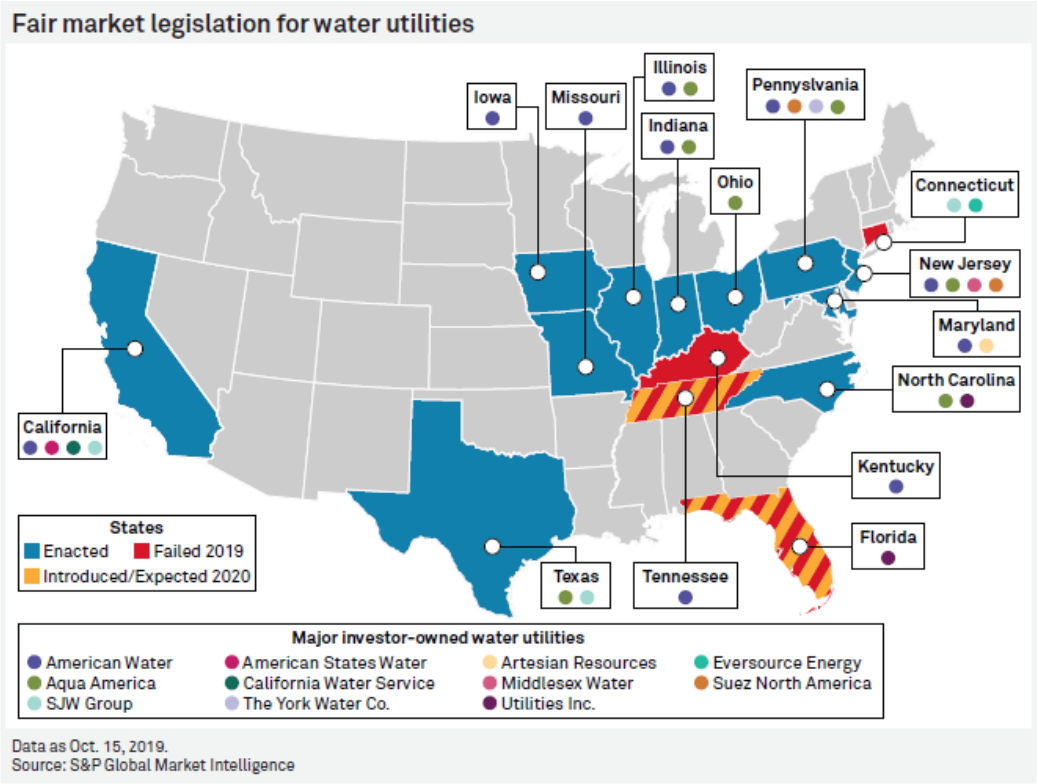
Exhibit 17: ... within a highly fragmented industry where of the 51,000 community water systems (CWS) only 4,221 or 8%, serve more than 246 million or 82%, of the total population.
State of the Water Industry - System size by population served



Source: Company data, Goldman Sachs Global Investment Research, AWWA, Environmental Protection Agency (EPA)

Exhibit 18: FMV legislation provides further impetus for consolidation in the sector and allows an accretive approach to valuing the acquired system's assets; currently in the books in 11 states and pending in 2 more states.
Fair Market Legislation for Water Utilities



Data as of Oct 25, 2019

Source: SNL

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What factors explain premium water valuations vs other regulated utilities?

Water utilities currently trade at a 30.2x FY2 P/E multiple, at a 11.3x premium to regulated electric/gas utilities trading at a 18.9x blended FY2 P/E multiple. Over the past few years, many investors had difficulty validating the valuation gap, questioning what level is justified. Fundamentally, we believe higher EPS/DPS growth trajectory, both historically and pro-forma, serves as the primary driver, with water utilities having grown EPS at a ~3%/2% CAGR above electric/gas utilities, respectively, over the past 10 years. The next task is determining how long water utilities can sustain this earnings gap, which we quantify in the following section. Below, we note a few factors (both quantitative and qualitative) that account for premium water valuations vs regulated electric detailed below:

Quantitative factors:

- **Longer asset life (D&A premium)** — Our analysis shows that every dollar invested in water assets yields a better return vs that for electric assets, driven by higher useful life (~20 years) extending the earnings potential. This D&A advantage translates into 2% in incremental EPS growth.
- **Continued robust capital program (Growth premium)** — As mentioned in the previous section, water IOUs have significant long-term investment opportunities (pipe replacement, treatment facilities, storage facilities, dams, wells and pumps), supported by favorable regulatory mechanisms to reduce lag in rate recovery. In addition, municipal acquisitions by IOUs continually add additional rate base backlog.

Qualitative factors:

- **Scarcity** — There are only a handful of investable water utilities for public investors. AWK, the largest water utility, has a market capitalization of more than $24 billion, and the remaining 11 investor-owned utilities have a combined market capitalization of just $22 billion. Trading volumes for the smallest water utilities average below 20,000 shares daily, which we believe could be beneficial for larger water IOUs like AWK and WTRG.
- **Take-out potential** — While initially slow, consolidation within the industry has accelerated during the past 30 years. Acquisitions by domestic and international utilities and by private equity has shrunk the group to just 12 investor-owned water utilities, while a handful of other large water utilities are owned by private equity investors. We attribute some of the relative premium of small-cap water utilities to take-out potential.
- **ESG focus** —Investor focus on ESG (environmental, social, governance) factors have increased meaningfully in recent years. While social and governance factors apply to many IOUs, pure-play water utilities satisfy the environmental factor, which could continue to support valuations. We note that AWK is a pure-play water utility, while WTRG now derives ~30% of its earnings from the recently acquired Peoples Gas business.

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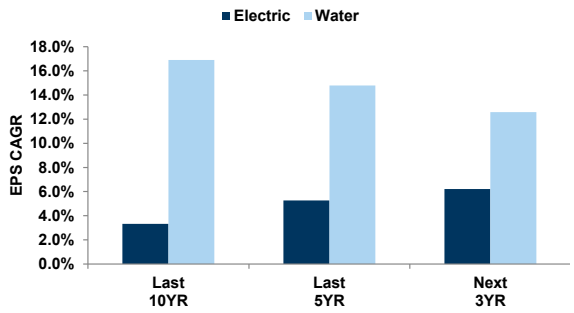
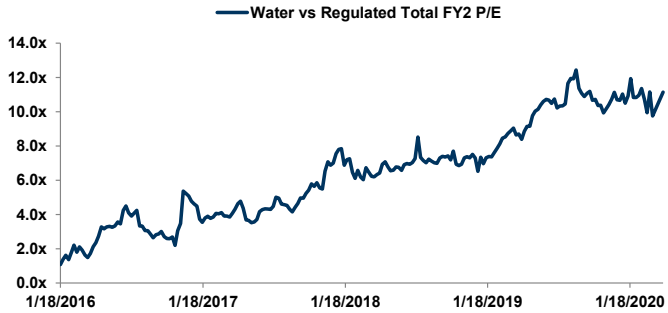
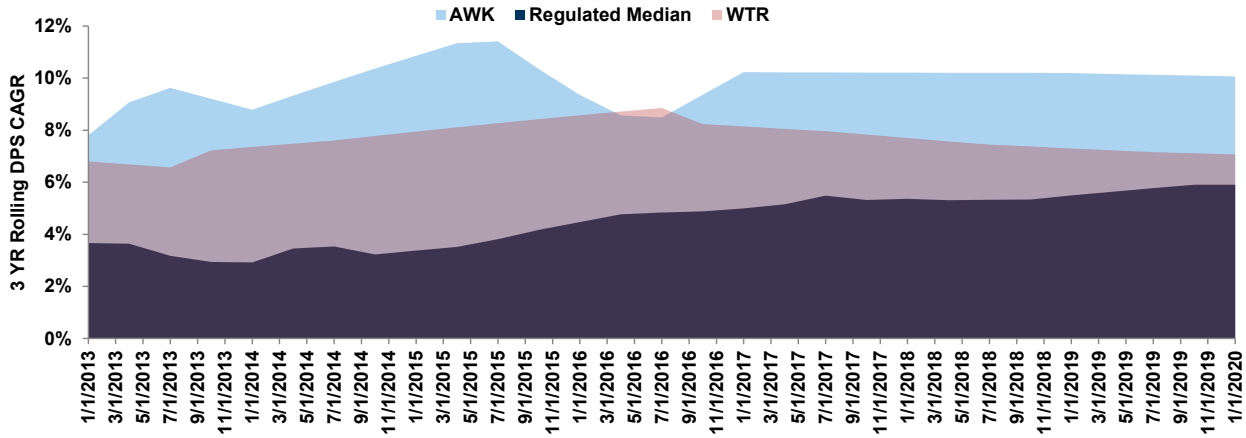
Exhibit 19: We note higher weighted average EPS growth CAGR for Water utilities vs Electric/Gas over the past 10 years have contributed to increasing relative premiums vs. Regulated Utilities...
Market cap weighted EPS Growth CAGRs - Water vs Electric; Water vs Regulated FY2 P/E





Source: Company data, Goldman Sachs Global Investment Research, FactSet

Exhibit 20: ... with AWK and WTRG consistently recording a DPS CAGR above regulated peers...
3 yr Rolling DPS CAGR



Source: Goldman Sachs Global Investment Research, FactSet

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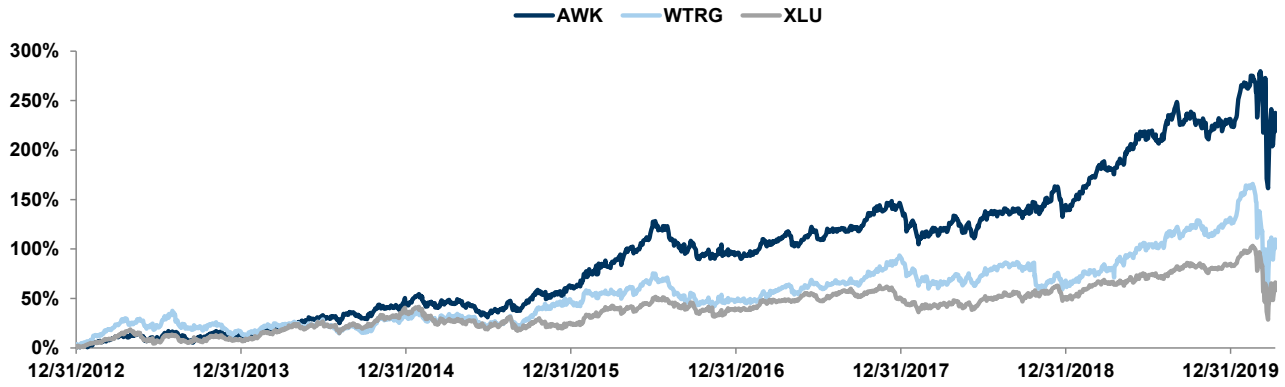
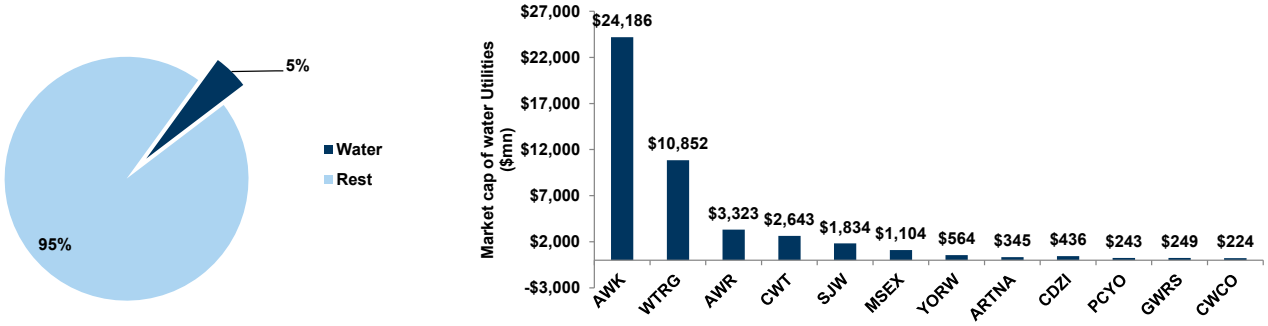
Exhibit 21: ... and rewarding investors with superior returns over the past 7 years vs the XLU
AWK/WTRG/XLU Performance since 2013



Source: Goldman Sachs Global Investment Research, FactSet

Exhibit 22: We note that the comparable group for Water companies remains limited, with 12 publicly traded water utilities in the US, including AWK and WTRG, and only 6 companies with a market capitalization in excess of $1 billion.
Water utilities market cap as % of total utilities market cap; Water utilities market cap ($mn)



Source: Goldman Sachs Global Investment Research, FactSet

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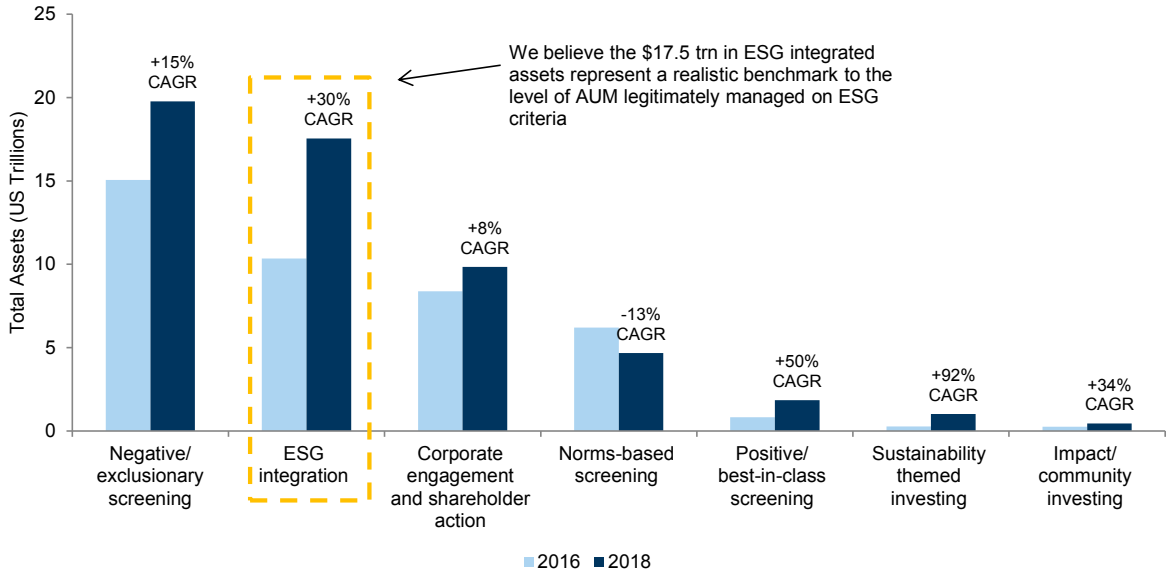
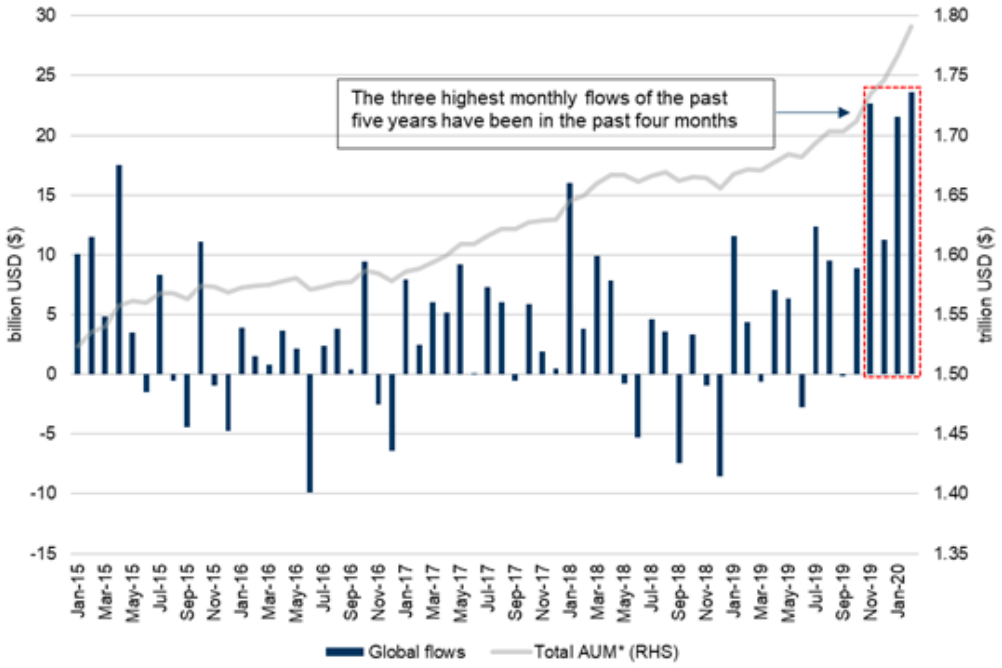
Exhibit 23: GS SUSTAIN: With ESG an increasingly important criteria for investors and fund flows...
Growth of investment assets incorporating ESG by type, including double counting (2016-2018)



Source: Global Sustainable Investment Alliance

Exhibit 24: ... that have remained robust through the early phases of the COVID-19 crisis (GS SUSTAIN)...
Monthly ESG fund flows (January 2015 through February 2020)



*AUM values are derived from historical flows and agnostic of market effects

Source: Morningstar

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Exhibit 25: ...we expect AWK's large-cap, pure-play water utility profile to benefit from ESG fund positioning.
AWK/WTRG Ranking based on ESG Relative overweight*

Top 10 ESG Relative overweight companies in US (April 2020)

	Company	GICS 1
1	NASDAQ INC ORD	Financials
2	XYLEM INC ORD	Industrials
3	IDEX CORP ORD	Industrials
4	EPAM SYSTEMS INC ORD	Information Technology
5	TRIMBLE INC ORD	Information Technology
6	UBER TECHNOLOGIES INC ORD	Industrials
7	GUIDEWIRE SOFTWARE INC ORD	Information Technology
8	PTC INC ORD	Information Technology
9	DENTSPLY SIRONA INC ORD	Health Care
10	VERISK ANALYTICS INC ORD	Industrials
14	**AMERICAN WATER WORKS COMPANY IN**	**Utilities**
21	**ESSENTIAL UTILITIES INC ORD**	**Utilities**

Top 10 ESG Relative overweight companies in US (Sept 2019)

	Company	GICS 1
1	Xylem Inc	Industrials
2	Trimble Inc	Information Technology
3	**Aqua America Inc**	**Utilities**
4	First Solar Inc	Information Technology
5	A.O. Smith Corp	Industrials
6	Hologic Inc	Health Care
7	**American Water Works Company Inc**	**Utilities**
8	Gap Inc	Consumer Discretionary
9	Toro Co	Industrials
10	First American Financial Corp	Financials

Companies with market caps > $5B and domiciled in US; *ESG Relative overweights are calculated by dividing a company's ESG fund universe ACWI constituent weighting over its ACWI weighting; ACWI= MSCI All Country Weight Index

Source: Bloomberg, Goldman Sachs Global Investment Research, Morningstar

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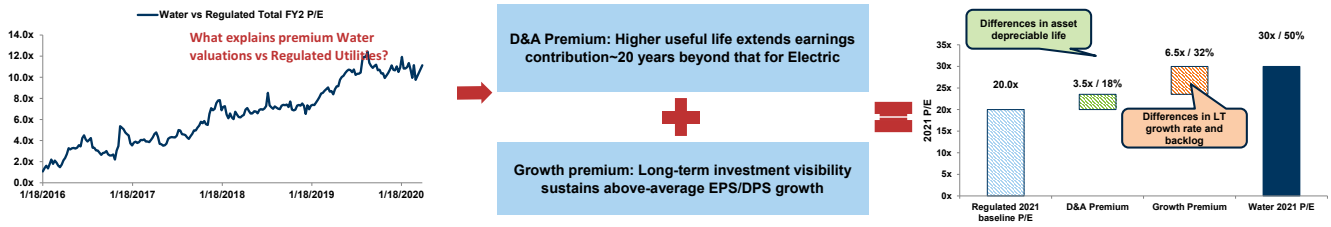
What premium do water utilities warrant?

Our analysis shows that water utilities deserve a meaningful P/E premium above electric utilities, with the current 11.3x premium largely justified.

We believe two quantifiable factors - D&A and investment growth - largely justify the current relative premium. We detail these calculations below.

Exhibit 26: We introduce our analysis on the earnings growth differential between water, electric and gas utilities, which we break into two components to arrive at our 30.0x baseline water multiple vs 20.0x baseline for our regulated coverage



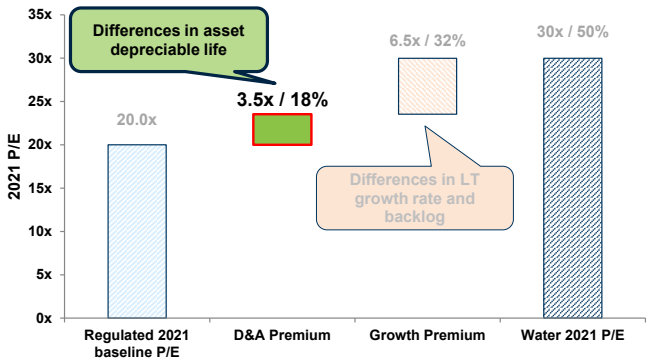
Source: Goldman Sachs Global Investment Research

1. D&A premium:

A higher useful life for water assets (50 years vs 30 years for electric) extends the earnings potential ~20 yrs beyond what that realized for electric assets, with earnings differential increasing steadily over time, warranting for a 17%/3.5x premium for each dollar invested in rate base.

Exhibit 27: We attribute around 18% (3.5x) of water utilities' current 57% (11.3x) premium vs Regulated Utilities to longer depreciable asset life for water assets

GS 2020 Water baseline multiple



Source: Goldman Sachs Global Investment Research

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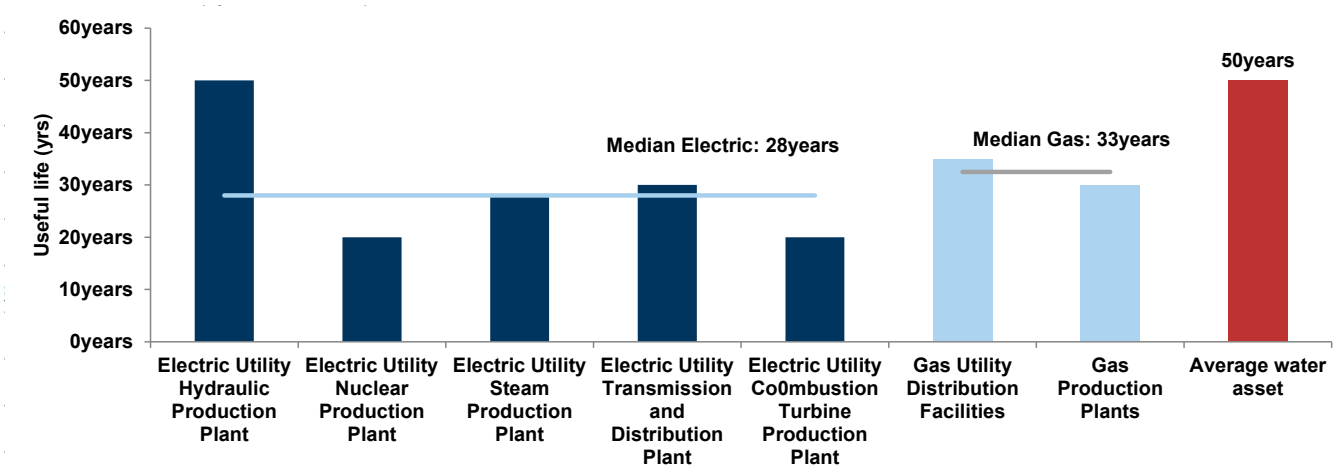
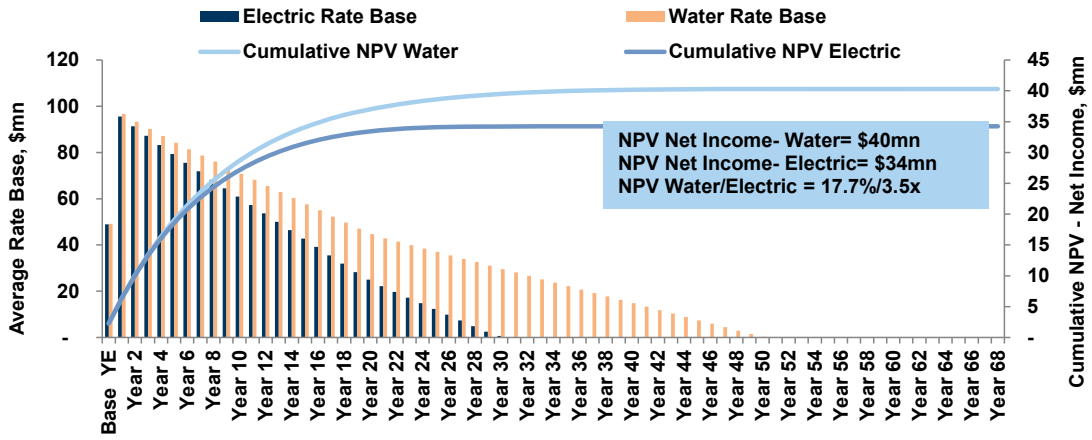
Exhibit 28: We note the useful life for the average water asset is ~20 years higher than that for electric/gas assets...
Asset Useful life by Subsector



Source: Thomson Reuters

Exhibit 29: ...which extends the asset's earnings potential for every $1 invested into regulated rate base...
Hypothetical average Rate Base/ Net Income ($mn) assuming an initial investment of $100mn and 30/50 yrs of useful life for an Electric/Water Utility



$100mn initial investment used for illustrative purposes

Source: Goldman Sachs Global Investment Research

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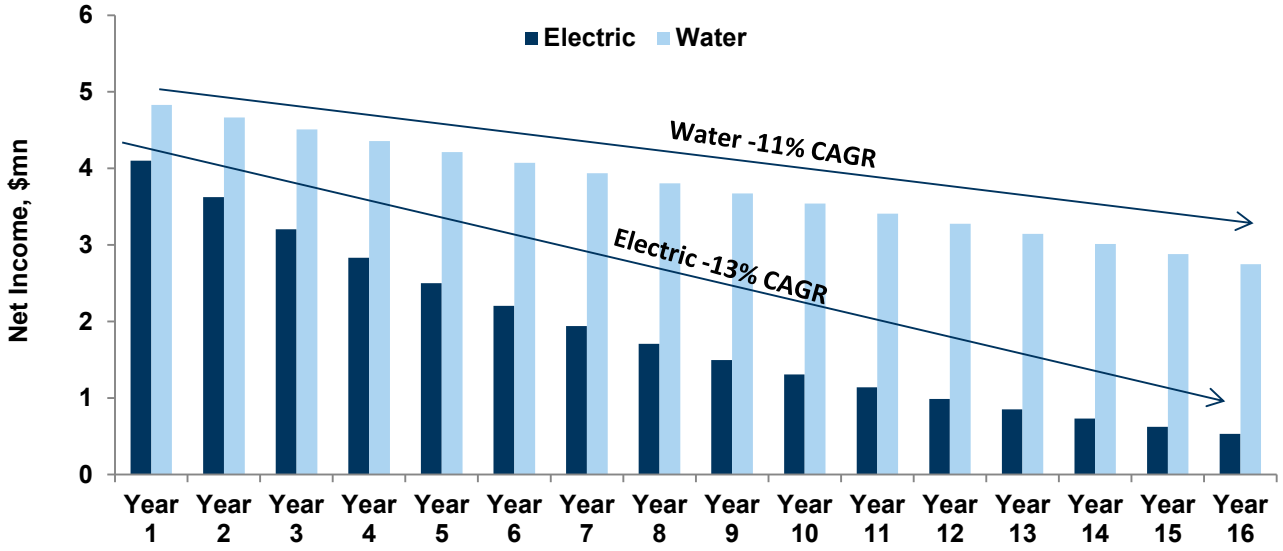
Exhibit 30: ...accounting for ~2% of incremental earnings CAGR for water vs electric...
Hypothetical average Rate Base/ Net Income ($mn) assuming an initial investment of $100mn and 30/50 yrs of useful life for an Electric/Water Utility

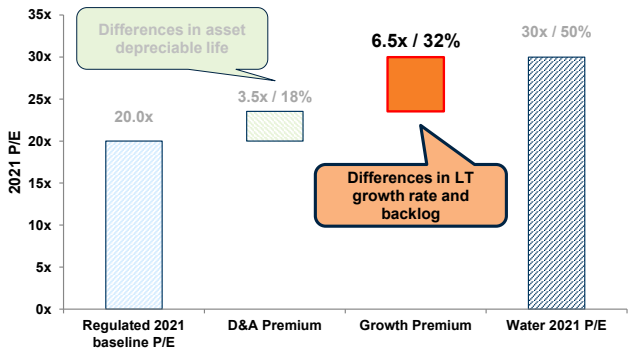


Source: Goldman Sachs Global Investment Research

2. Growth premium:

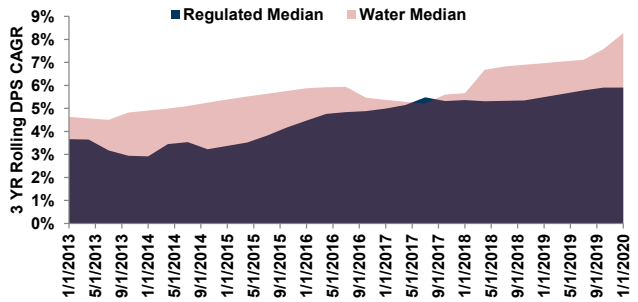
Even excluding the EPS advantage from D&A, we expect the water utility industry's significant investment backlog supporting continued above-average EPS growth (7% for water vs. 5% for electric) longer-term. We arrive at our 32%/6.5x premium based on a 15-year relative dividend-discount model (DDM), which we believe could prove conservative given AWWA's estimated $1 trillion in water pipe replacement needs through 2035.

Exhibit 31: We justify the remaining 32% (6.5x) premium based on significant water pipe investment needs that should sustain water utilities' higher EPS growth profile versus electric utilities
GS 2020 Water baseline multiple



Source: Goldman Sachs Global Investment Research

Exhibit 32: Given water utilities' ~3% higher DPS CAGR versus other regulated utility peers...
3 yr Rolling DPS CAGR



Source: Company data, Goldman Sachs Global Investment Research, FactSet

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Exhibit 33: ...we expect water utilities to continue growing EPS/DPS above other regulated utilities longer-term, even after excluding the D&A advantage

Growth premium for an average Water Utility based on DDM assuming a starting investment of $10,000mn, ke=8%, LT growth rate =4% and tax rate=26%

Year	Average Water Utility Dividend Growth rate (YR1-15 CAGR)	Water Dividend (mn)	Electric Dividend Growth rate (YR1-15 CAGR)	Electric Dividend (mn)
1	7.0%	$255	5.0%	$243
2	7.0%	$273	5.0%	$256
3	7.0%	$291	5.0%	$269
4	7.0%	$310	5.0%	$282
5	7.0%	$331	5.0%	$296
6	7.0%	$352	5.0%	$309
7	7.0%	$375	5.0%	$324
8	7.0%	$400	5.0%	$338
9	7.0%	$427	5.0%	$352
10	7.0%	$459	5.0%	$367
11	7.0%	$493	5.0%	$383
12	7.0%	$530	5.0%	$402
13	7.0%	$570	5.0%	$422
14	7.0%	$612	5.0%	$442
15	7.0%	$657	5.0%	$464
15+	4.0%	$17,087	4.0%	$12,058
NPV @ ke 8%		$8,671		$6,556

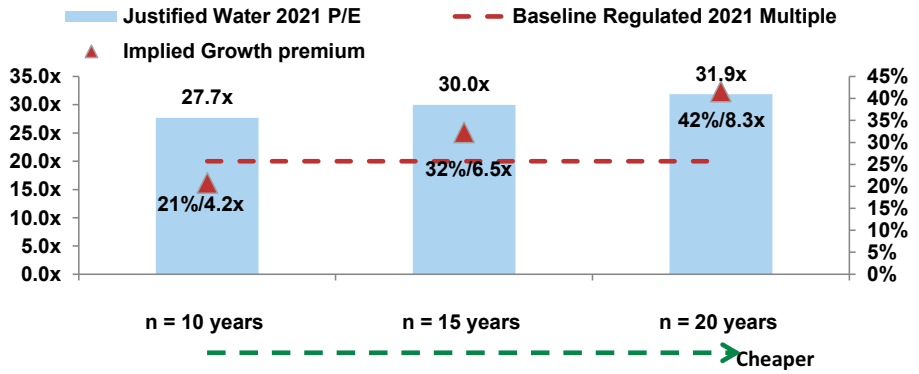
Implied Water Growth premium (post adjusting for D&A premium) =$8,671/$6,556 ~32%/6.5x

$10,000mn starting amount selected for illustrative purposes; ke, LT growth rate, and tax rate figures reflect normalized industry averages

Source: Company data, Goldman Sachs Global Investment Research

Exhibit 34: We note that our base case of 15 years growth at 7% growth could prove conservative given long-term visibility of water investment needs

Justified Growth Premium for Water vs Regulated Electric assuming High Growth stage of 10/15/20 years



n= High growth years, LT growth rate =4%

Source: Goldman Sachs Global Investment Research

Our revised 30.0x 2021 baseline multiple for water accounts for 3.5x/6.5x D&A/growth premium over the regulated baseline multiple of 20.0x.

We note that our analysis solely focuses on the longer useful life of water assets and higher growth opportunities to explain the premium water valuations; however, we note that qualitative drivers mentioned in the prior section - scarcity, take-out potential, ESG focus - could apply an additional layer of premium.

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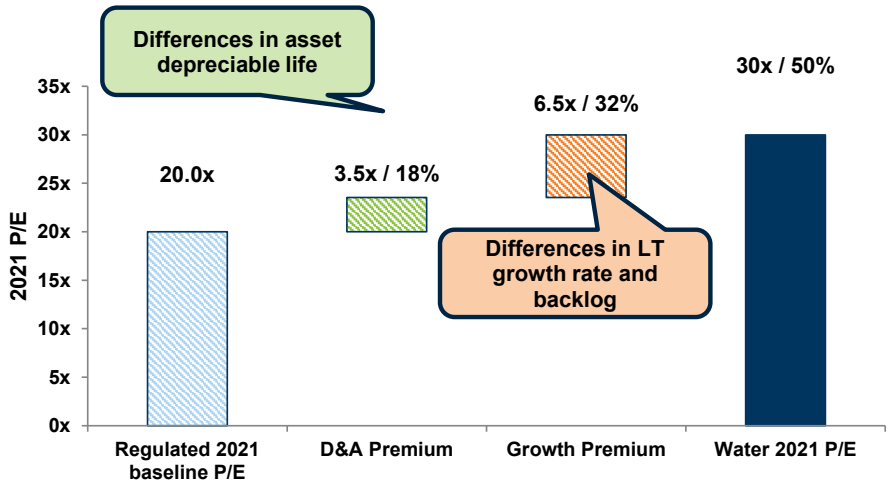
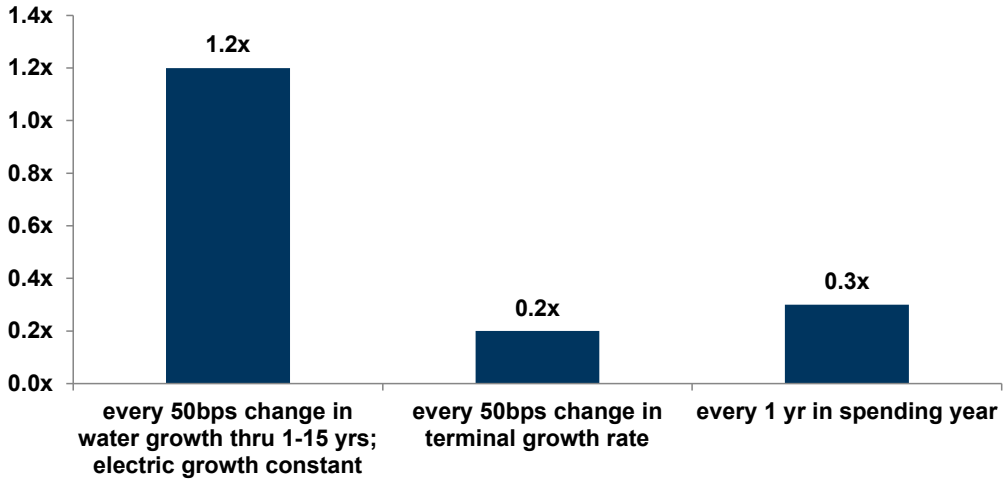
Exhibit 35: Accordingly, our revised 30.0x 2021 baseline multiple for water accounts for 3.5x/6.5x D&A/growth premium over the regulated baseline multiple of 20.0x...
Water 2021 baseline P/E vs Regulated



Source: Goldman Sachs Global Investment Research

Exhibit 36: ...while noting our analysis remains sensitive to changes in various assumptions
Premium sensitivity to change in growth rate (yr 1-15), terminal growth rate and spending years



AWK/WTRG both stand to benefit from robust investment backlog

We see both AWK and WTRG able to sustain their robust water rate base growth outlook for at least the next 15 years. The AWWA's estimated $1 trillion in water pipe replacement needs in the U.S. - through 2035 - could imply around $40bn/$10bn of investment backlog for AWK/WTRG based on their respective market share (by customer connections). Given $13.7bn/$5.0bn YE2019 rate base for AWK/WTRG, respectively, we believe the these investments could support 3x/2x in rate base by 2035, or a 6.5%/4.9% rate base CAGR. While this growth rate alone could signal a slowing of earnings growth power, we note this does not account for additional rate base opportunities from ongoing municipal acquisitions or investments in new

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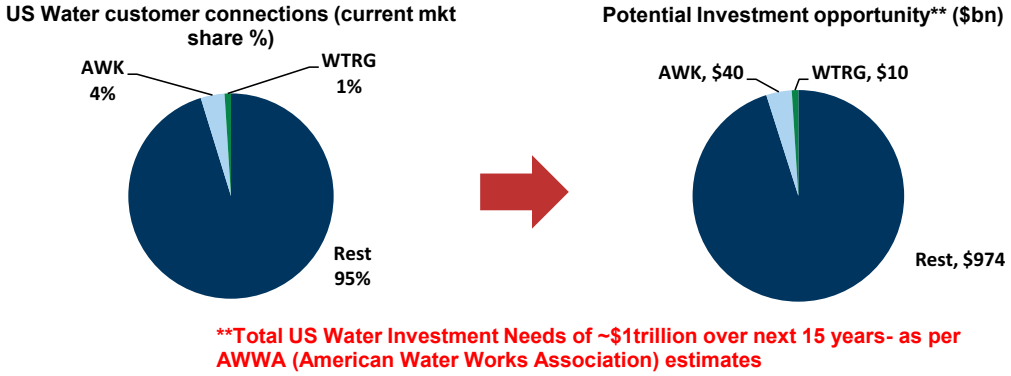
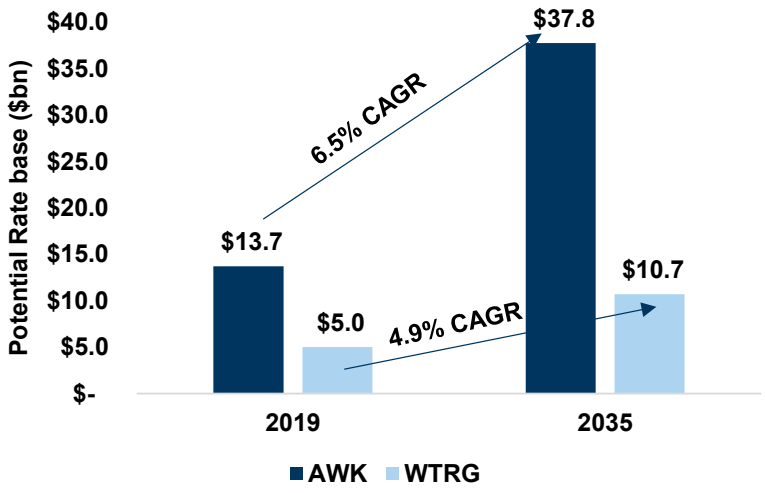
infrastructure, which we believe will continue to extend and expand organic investment opportunities. We view this long-term investment visibility as a key justifying factor for water utilities' relative premium valuations.

Exhibit 37: We see meaningful pipe replacement needs for both AWK/WTRG long-term...
Potential Investment Opportunity



Source: Company data, Goldman Sachs Global Investment Research, AWWA

Exhibit 38: ... that could support potential rate base growth of 6.5%/4.9% through 2035 for AWK/WTRG, not including potential upside from municipal acquisitions or new infrastructure spend
AWK/WTRG Potential rate base through 2035



Source: Company data, Goldman Sachs Global Investment Research, AWWA

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Upgrade AWK to Buy - Best-in-class growth, ESG-friendly profile justify premium

We view large-cap AWK's best-in-class 8.3% EPS growth, below-average beta, and its ESG-friendly profile as deserving of the highest premium valuation in our coverage universe and see 16% potential total return based on our $146 price target.

AWK	12m Price Target: $146	Price: $127.24			Upside: 14.7%
Buy	GS Forecast				
		12/19	12/20E	12/21E	12/22E
Market cap: $23.0bn	**Revenue ($ mn) New**	**3,610.0**	**3,800.8**	**3,992.0**	**4,175.0**
Enterprise value: $33.1bn	Revenue ($ mn) Old	3,610.0	3,800.8	3,992.0	4,175.0
3m ADTV :$187.1mn	EBITDA ($ mn)	1,752.0	1,947.1	2,097.8	2,240.3
United States	EBIT ($ mn)	1,170.0	1,335.6	1,443.7	1,544.3
America-Regulated Utilities:	**EPS ($) New**	**3.61**	**3.88**	**4.24**	**4.58**
	EPS ($) Old	3.61	3.88	4.24	4.58
M&A Rank: 3	P/E (X)	31.3	32.8	30.0	27.8
	Dividend yield (%)	1.7	1.7	1.9	2.0
	Net debt/EBITDA (X)	5.4	5.2	5.0	4.7
		12/19	**3/20E**	**6/20E**	**9/20E**
	EPS ($)	0.73	0.76	0.97	1.38

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 13 Apr 2020 close.

Source: Goldman Sachs Global Investment Research

We upgrade AWK from Neutral to Buy given 1) continued best-in-class earnings and dividend growth in our coverage universe, 2) long-term visibility of above-average growth from organic investments and municipal system acquisitions, 3) its ESG-friendly status as the only large-cap pure-play water utility, and 4) our updated target multiple and premium that imply a 16% total return.

We see a long runway of water infrastructure investment opportunities that should sustain AWK's above-average growth. The aging water and wastewater infrastructure in the United States is in need of replacement and modernization. In addition, increased regulation related to water quality and the management of water and wastewater residual discharges are also primary drivers for the need to modernize the country's water and wastewater infrastructure. We note AWK is well positioned to benefit from ~$40bn in potential investment over the next 15 years, given the company's ~4% market share (based on customers served) and AWWA's estimated $1 trillion in water investment needs. AWK already plans to invest almost $20 billion to the regulated utilities (pipe replacement, system upgrades) over the next 10 years, sustaining its 7-8% rate base CAGR target longer-term.

We expect municipal acquisitions continue to provide an additional growth layer. As mentioned in the previous sections, the water utility space is very fragmented, with the bulk of the customers in the U.S. still served by municipal utilities. With the majority of AWK's utility jurisdictions allowing fair market value (FMV) treatment for municipal acquisitions, we expect the company to continue its consistent acquisition track record

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that should contribute 1-2% of the 7-10% EPS CAGR guided range. Along with the inherent financial advantages of FMV, we note that acquisitions add incremental infrastructure investment opportunities to bolster AWK's rate base growth longevity.

AWK carries a stable balance sheet, improving through 2022. While we acknowledge AWK's relatively high ~60% debt/cap levels, management at the recent investor day announced plans to issue $500mn of equity at around the mid-point of the 2020-2024 investment plan. Our model continues to embed the $500mn issued by YE2022, resulting in a 58% debt/cap in 2022, and an improvement in FFO/debt from 15% in 2020 to 17% in 2022. Based on the current A/Baa1 credit rating, we do not anticipate any additional equity needs beyond the guided levels.

We keep our EPS estimates unchanged at $3.88/$4.24/$4.58 for 2020-2022 and see EPS growing at 8.3% CAGR from 2019-2022, at the mid-point of the company's 7-10% guidance range, contributed by 7-8% from regulated utilities and 1% from the market based business. Primary drivers of growth continue to include robust capital investments, customer growth (both organic and via municipal acquisitions), O&M management, with some dilution in 2022 from the $500mn equity issuance. We continue to assume 10% annual dividend through 2022, resulting in a 55%-57% payout.

We raise our 12-month price target to $146 (from $134 previously) derived using a 34.5x 2021E P/E multiple (vs 31.5x prior). Our revised P/E multiple incorporates our new water base P/E multiple of 30.0x (calculated in prior sections), as well as a 3x (10%) premium to account for AWK's above-average growth and favorable ESG profile. While the water utility peer group is fairly limited, AWK is currently trading at a 30.0x P/E on 2021E, largely in-line with peers. We believe AWK should trade at the highest multiple among water utilities and relative to our overall coverage universe.

Key downside risks include 1) water quality issues that result in customer health risks, leading to significant financial and regulatory impact, 2) inability to consistently manage operating costs, 3) unfavorable turn in regulatory environment that negatively impacts robust earnings growth potential, 4) lower-than-expected growth at the non-regulated segments, which lowers AWK's best-in-class growth rate, and 5) reduced ESG fund flows that impact further multiple expansion as investors turn to other qualifying investments.

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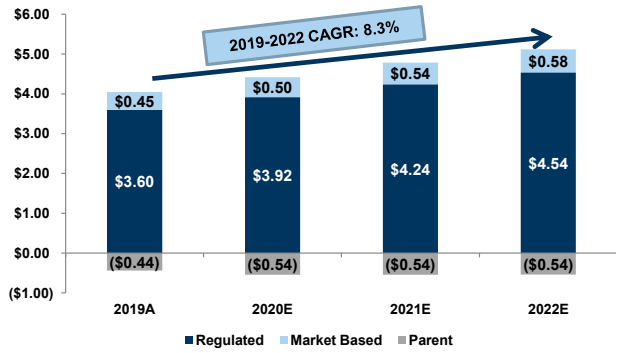
Exhibit 39: We keep our EPS estimates unchanged at $3.88/$4.24/$4.58 for 2020-2022 ...
GS new vs. old vs. consensus, 2019E-2022E

	EPS Estimates			% Difference	
	New	Old	Consensus	vs Old	vs Consensus
2020E	$3.88	$3.88	$3.85	0%	1%
2021E	$4.24	$4.24	$4.23	0%	0%
2022E	$4.58	$4.58	$4.56	0%	0%

Source: Goldman Sachs Global Investment Research, FactSet

Exhibit 40: ...reflecting 8.3% growth CAGR over 2019-2022...
EPS by segment, 2019A-2022E



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 41: We raise our TP to $146 using a 34.5x P/E multiple (vs 31.5x previously) using our revised base water multiple and a growth/ESP premium...
AWK Valuation

AWK Valuation	
AWK 2021 EPS	**$4.24**
GS Water Utility Base Multiple	30.0x
Premium / (Discount)	4.5x
Adjusted P/E	**34.5x**
Utility Valuation	**$146**
AWK Valuation	**$146**
Current Stock Price	$127.24
Price Return Potential	14.7%
Dividend Yield	1.4%
Total Return Potential	**16%**

Source: Goldman Sachs Global Investment Research

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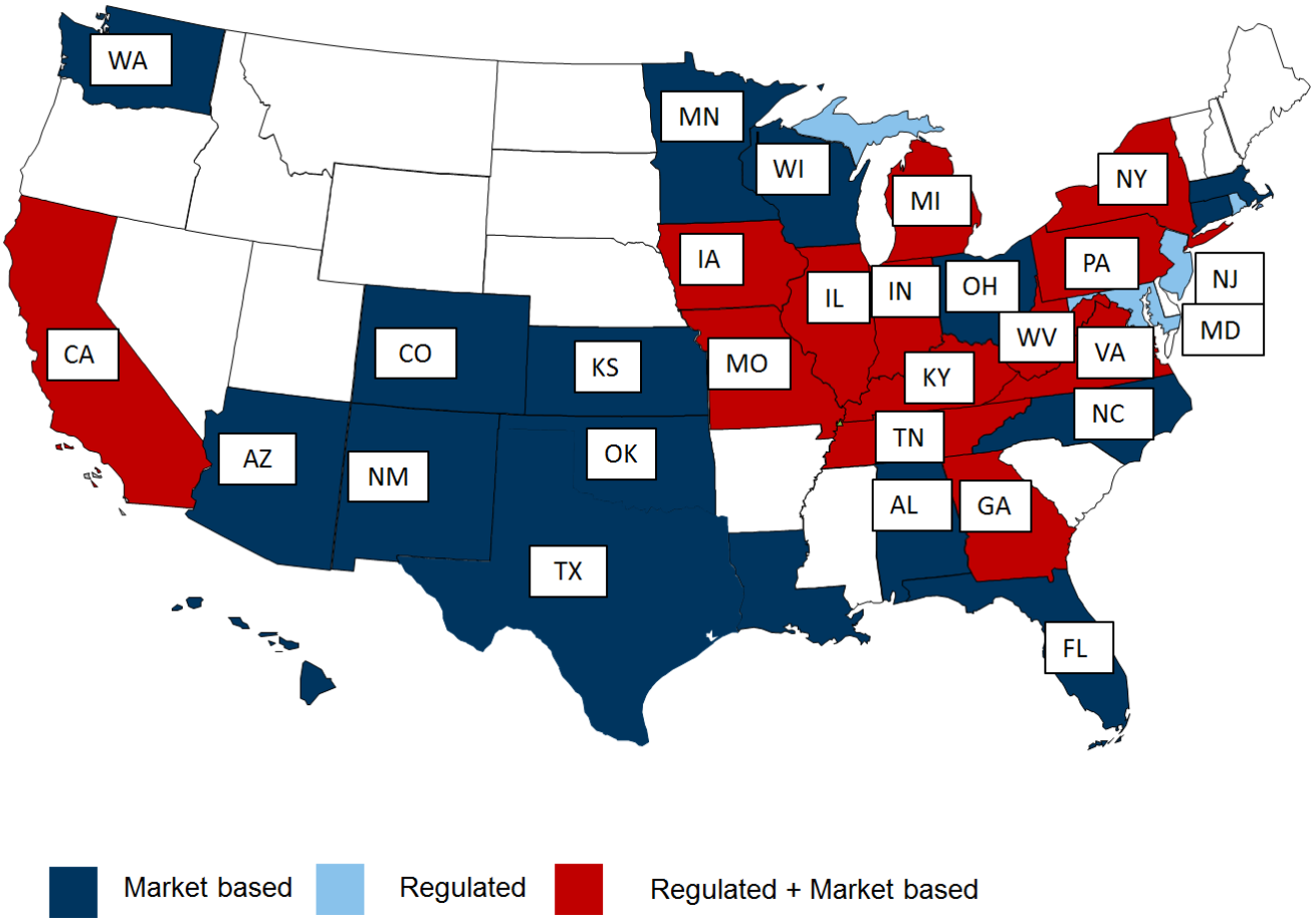
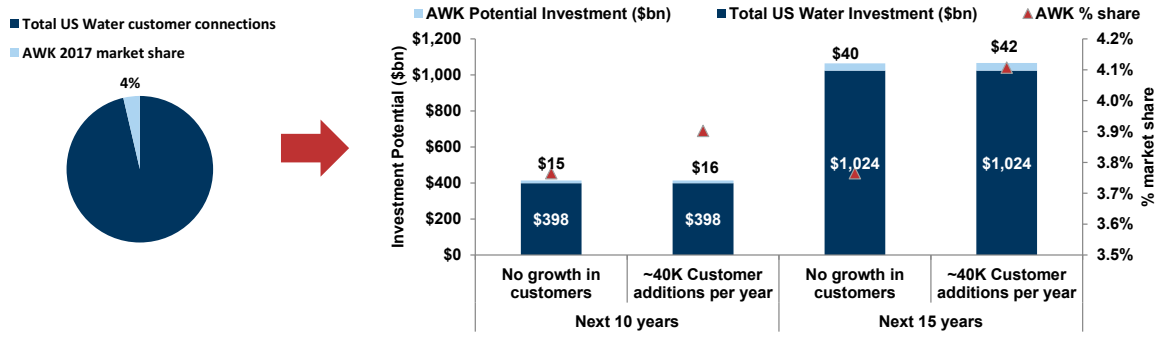
Exhibit 42: We see an impressive growth pipeline for AWK given its Regulated business presence in 16 U.S. states providing water and wastewater utility services to residential, commercial, industrial customers...
AWK Geographical footprint



*sale of NY Utility announced in 2019, currently not factored in our estimates

Source: Company data, Goldman Sachs Global Investment Research

Exhibit 43: ...and potential investment opportunity of ~$40bn over the next 15 years with potential upside from organic/inorganic customer additions.
AWK Potential Investment Opportunity



Source: Company data, Goldman Sachs Global Investment Research, AWWA

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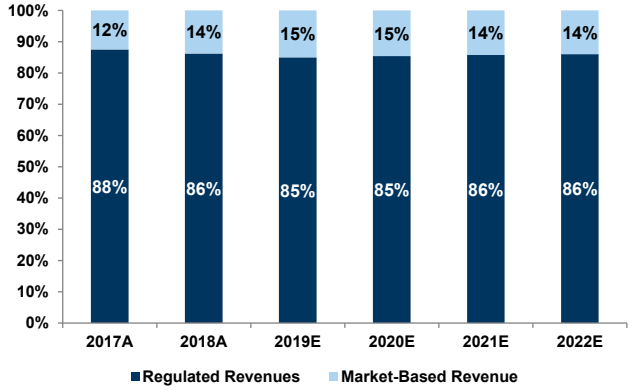
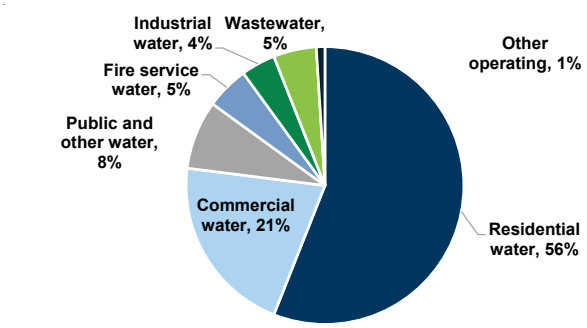
Exhibit 44: In addition to American Water's core regulated franchise, AWK owns and operates complementary water-related businesses with medium to long-term contracts, with low capital requirement fueling positive cash contribution
Regulated vs Unregulated Revenue mix (%)



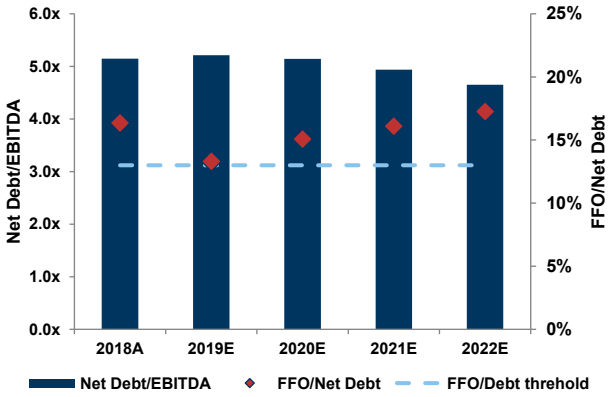
Source: Company data, Goldman Sachs Global Investment Research

Exhibit 45: AWK's regulated revenue base consists of 56% residential, 21% commercial and just 4% industrial
AWK Regulated Operating Revenue by customer class



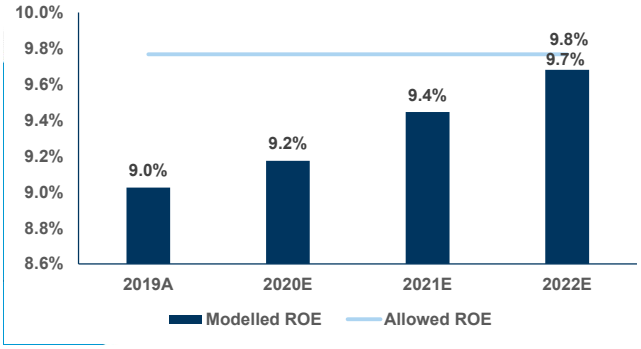
Source: Company data, Goldman Sachs Global Investment Research

Exhibit 46: We see FFO/debt improving through 2022, aided by $500mn of equity issuances across 2021-2022...
Net Debt/ EBITDA & FFO/Debt 2018A-2022E



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 47: ...and with AWK earning close to allowed by 2022
Earned vs Allowed ROE 2019A-2022E



Source: Company data, Goldman Sachs Global Investment Research

Company Overview

American Water Works (AWK), remains the largest publicly traded US water utility at more than $24bn in market cap, provides more than 14 million people with drinking water, wastewater and water-related services in almost 45 US states and 2 Canadian provinces. The company operates two divisions: (1) the Regulated segment, representing 86% of 2019 revenues and (2) the Market Based Operations segment, which comprises the remaining 14%. The key states served by AWK's regulated utilities are summarized in Exhibit 48.

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Exhibit 48: AWK's regulated segment exposure is distributed across sixteen states with bulk of earnings from seven states
State utility commission regulatory snapshot

AWK Regulatory Profile	New Jersey	Pennsylvania	Missouri	Illinois	California	Indiana	West Virginia
Commission Name	New Jersey Board of Public Utilities	Pennsylvania Public Utility Commission	Missouri Public Service Commission	Illinois Commerce Commission	California Public Utilities Commission	Indiana Utility Regulatory Commission	Public Service Commission of West Virginia
No. of Commissioners	5 of 5 (3 D, 2 R)	5 of 5 (3 D, 2 R)	5 of 5 (2 D, 3 R)	5 of 5 (1 D, 2 R, 2 Non-Partisan)	5 of 5 (5 D)	5 of 5 (3 D, 2 R)	3 of 3 (2 R, 1 D)
Test year for Rate Case	Historical test year	Future test year	Historical test year	Future test year	Future test year	Future test year	Historical test year
Infrastructure replacement surcharges	Yes	Yes	Yes	Yes	No	Yes	Yes
Revenue Stability mechanisms	No	No	No	Yes	Yes	No	No
Expense mechanisms	Yes	Yes	Yes	Yes	Yes	No	No
Utility plant recovery mechanisms	No	Yes	No	Yes	Yes	No	No
GS view on Regulation	Somewhat Restrictive	Constructive	Somewhat Restrictive	Constructive	Balanced	Somewhat Restrictive	Restrictive
Fair Market Legislation (FMV)	Yes	Yes	Yes	Yes	Yes	Yes	No
Company 2018 Revenue Exposure	AWK-24%	AWK-23%	AWK-10%	AWK-10%	AWK-7%	AWK-7%	AWK-5%

Infrastructure Replacement surcharges: Allows rates to change periodically, outside a general rate case proceeding, to reflect recovery of capital investments made to replace infrastructure necessary to sustain safe, reliable services for our customers. These mechanisms typically involve periodic filings and reviews to ensure transparency.
Utility plant recovery mechanisms: Allows recovery of the full return on utility plant costs during the construction period, instead of capitalizing an allowance for funds used during construction. In addition, some states allow the utility to seek pre-approval of certain capital projects and associated costs. In this pre-approval process, the PUC may assess the prudency of such projects.
Expense mechanisms: Allows changes in certain operating expenses, which may fluctuate based on conditions beyond the utility's control, to be recovered outside of a general rate case proceeding or deferred until the next general rate case proceeding.
Revenue stability mechanisms: Separates a utility's cost recovery from the amount of water it sells to recover its fixed costs and ongoing infrastructure investment needs. Such a mechanism adjusts rates periodically to ensure that a utility's revenue will be sufficient to cover its costs, regardless of sales volume, including recognition of declining sales resulting from reduced consumption, while providing an incentive for customers to use water more efficiently.
Future test year: A test period used for setting rates, which begins with the date new rates are effective. This allows current or projected revenues, expenses and capital investments to be collected on a timelier basis.
Fair Market Legislation(FMV): Allows regulated water companies to pay a fair market value for the purchase of water and wastewater systems. Before these changes, system values were determined by their depreciated original cost, which generally did not reflect a reasonable market value for those assets and became a barrier to a sale.

Source: SNL Financial, Company reports, Goldman Sachs Global Investment Research

In addition to American Water's core regulated franchise, AWK owns and operates complementary water-related businesses as part of its Market-based segment which include:

The Homeowner Services Group- which provides warranty protection programs to residential and smaller commercial customers to protect against repair costs for interior and exterior water and sewer lines, interior gas and electric lines, heating and cooling systems, water heaters and other home appliances, as well as power surge protection and other related services. The current porfolio includes the June 2018 acquisition of Pivotal Home Solutions, which increased the segment's customer base from 0.9mn to 1.5mn. The company also partners with municipalities, utilities and other organizations to offer protection programs to customers serviced by, or affiliated with, those municipalities, utilities and organizations. The term of these partnership agreements is typically three to five years, with mutual optional renewals; each customer generates around $20-$40mn of net income for this segment, which reflects around half or more of AWK's 14% market-based earnings. As of YE2019, the Homeowner Services Group had approximately 3 million customer contracts in 43 states.

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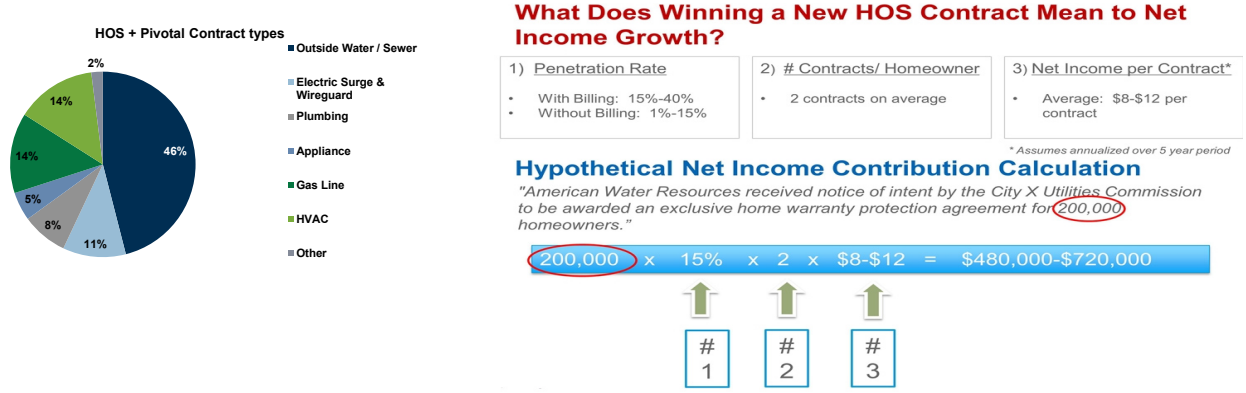
Exhibit 49: The Homeowner Services Group houses ~3 million contracts in 43 states, with a potential market opportunity of 30mn contracts...
Homeowner services business profile



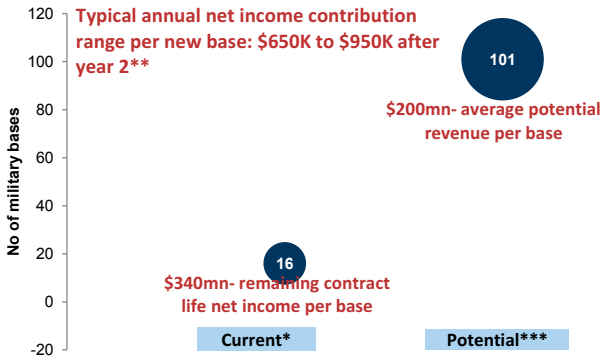
Source: Company data, Goldman Sachs Global Investment Research

Military Services Group - provides water and wastewater services to the U.S. government on military installations; operates on 16 military installations under 50-year contracts with the U.S. government as part of its Utility Privatization Program. The scope of these contracts generally includes the operation and maintenance of the installation's water and wastewater systems and a capital program focused on asset replacement and, in certain instances, systems expansion. The backlog of revenue associated with the current U.S. government contracts is approximately $4.3 billion, with an average remaining contract term of 42 years.

Exhibit 50: The Military Services Group generates stable revenues via 30-50 year contracts, with significant market expansion opportunities
Military services business profile

	Contract	Division	Contract Years remaining
1	Fort Sill	Army	35
2	Fort Leavenworth	Army	35
3	Fort Rucker	Army	36
4	Fort AP Hill	Army	39
5	Scott AFB	Air Force	39
6	Fort Hood	Army	40
7	Fort Polk	Army	40
8	Fort Belvoir	Army	41
9	Fort Meade	Army	42
10	Hill AFB	Air Force	46
11	Picatinny Arsenal	Army	46
12	Vadenberg AFB	Air Force	48
13	Wright- Patterson AFB	Air Force	50
14	Fort Leonard Wood	Army	50

2 more added in 2018-2019 as per latest 10K



*as per 2019 10K, ** as per Dec 2019 analyst presentation, ***as per Dec 2015 presentation

Source: Company data, Goldman Sachs Global Investment Research

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Initiate WTRG at Neutral – Robust water/gas growth already reflected in SOTP

While we see Aqua's recent acquisition of Peoples Gas providing upside to rate base and EPS growth longer-term, we view current valuations fairly crediting this growth in addition appropriately reflecting the company's water/gas utility mix (versus pure-play water prior). Our $45 price target implies an 7% total return versus 15% for Regulated Utilities.

WTRG	12m Price Target: $45	Price: $42.8			Upside: 5.1%
Neutral	GS Forecast				
		12/19	12/20E	12/21E	12/22E
Market cap: $9.2bn	**Revenue ($ mn) New**	**889.7**	**1,619.4**	**2,052.0**	**2,167.9**
Enterprise value: $14.9bn	Revenue ($ mn) Old	--	--	--	--
3m ADTV :$68.6mn	EBITDA ($ mn)	521.4	815.6	1,028.4	1,122.2
United States	EBIT ($ mn)	360.8	581.1	731.8	799.9
America-Regulated Utilities:	**EPS ($) New**	**1.47**	**1.56**	**1.65**	**1.78**
	EPS ($) Old	--	--	--	--
M&A Rank: 3	P/E (X)	27.6	27.5	26.0	24.0
	Dividend yield (%)	2.2	2.2	2.4	2.6
	Net debt/EBITDA (X)	2.3	7.0	6.2	6.2
		12/19	3/20E	6/20E	9/20E
	EPS ($)	0.29	0.57	0.17	0.27

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 13 Apr 2020 close.

Source: Goldman Sachs Global Investment Research

We initiate coverage on Essential Utilities, Inc. (WTRG) - formed by the merger of Aqua America and Peoples Gas - at Neutral with a 12-month price target of $45. We view the 9+% combined rate base growth (including municipal acquisitions) driving a robust 6.6% EPS CAGR from 2019A-2022E. However, we view current valuation already reflecting these positive qualities, with just 7% total return based on our water/gas SOTP price target, versus 15% for Regulated Utilities.

Peoples Gas acquisition provides additional growth...

Peoples Gas acquisition elevates rate base growth profile. We see 10%+ rate base growth at Peoples Gas from 2019A-2022E primarily driven by long-term visibility of pipeline replacement projects. We note that Peoples has identified more than 2,700 miles of bare steel and cast iron pipe to be replaced under its Long-term Infrastructure Improvement Plan (LTIIP) by 2034 in its PA service territory, which at ~180-200 miles/year of pipe replacement, implies more than 15 years of increased capital spending to support around 9% rate base CAGR during the period. Along with the majority of these investments eligible for distribution system improvement charge (DSIC) that help reduce regulatory lag, we expect Peoples Gas to benefit from favorable tax election, as detailed below.

Tax repairs election should help maintain robust EPS growth while providing incremental funding for investments. WTRG plans to elect tax repairs for Peoples

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Gas' PA utility, which comprises more than 90% of the gas customer base. **What is tax repair?** It essentially allows the company to expense certain utility asset improvement costs that were previously capitalized and depreciated for book and tax purposes. For PA, which allows flow-through accounting, the utility is able to keep the incremental earnings and cash from the lower tax rate (still collected in customer bills at the higher tax rate), supporting financing needs while reducing rate case cycles. We note WTRG's PA water utility elected tax repairs in 2012 (now expired), which enabled it to record robust earned ROEs while staying out of a rate case for almost 10 years. For the gas utility, we expect WTRG to allocate qualified assets over a longer investment period, reducing the sudden jump in earnings growth recorded when implemented for the water utility. Our model embeds ~10.5% earned ROEs for Peoples Gas through 2022 versus 10.2% allowed, reflecting the tax repairs benefit.

We expect merger synergies to benefit EPS through 2022. With the bulk of the Peoples Gas service jurisdictions - Pennsylvania - sitting on top of Aqua America's PA water utility area, we expect the combined company to benefit from merger synergies related to various operations and system integration. Our model embeds 5% of combined O&M as acquisition synergies, resulting in flat to 1% O&M CAGR from 2019A-2022E for both water and gas utilities.

...to a fundamentally robust water growth story

We expect combined 9.7% water rate base CAGR (including acquisitions) from 2019-2022 driven by a robust organic capital program... The water sector is extremely capital intensive, given its extensive pipe and main infrastructure system as well as treatment facilities, storage facilities, dams, wells and pumps. As shown in Exhibit 37, the American Water works Association's (AWWA), most recent estimates about $1 trillion will be needed in the next 15 years to upgrade the country's water systems, both public and private, to meet environmental standards. At the Water business, we expect ~$400-$500mn in capital spending each year underlying the company's 7% rate base growth CAGR.

...as well as growth via municipal transactions supported by FMV legislation. Given the fragmented nature of the water utility industry, as detailed in the prior sections of this note, we expect WTRG to continue its robust municipal acquisition strategy to support and sustain its growth. The vast majority of WTRG's jurisdictional states currently allow fair market value (FMV) accounting that should provide continued incentive for acquisitions. In 2018, Essential Utilities closed 6 municipal acquisitions, adding more than 13,700 customers and more than $100 million of rate base. In September 2019, the company entered into a purchase agreement to acquire the wastewater utility system assets of the Delaware County Regional Water Quality Control Authority ("DELCORA"), which consists of approximately 16,000 customers in 42 municipalities in Southeast Pennsylvania for $276,500. If approved by the Pennsylvania Public Utilities Commission (PUCO), this acquisition would be the largest water and wastewater deal in state history. We note that every $100 million in rate base from acquisitions that are added through municipals contributes ~$5 million in earnings, or $0.02 in EPS.

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Relatively stable balance sheet, although somewhat levered given Peoples acquisition

Following the Peoples Gas acquisition, we see WTRG maintaining around 50% debt/cap through 2022, along with FFO/debt at ~12% during the period. We note S&P's "A" issuer credit rating targets FFO/debt to remain at or above 12% longer-term, with sustained lower levels a potential risk for a downgrade. In addition, we note around 25-30% of debt resides at the parent, somewhat elevated in our view. However, we believe a one-notch credit downgrade would still place WTRG's rating around the utilities average; we do not see this as a meaningful risk.

Will ESG momentum continue post gas integration?

In recent years, the water industry has seen increased interest from ESG investors contributing to a significant expansion of water premium vs the average electric/gas multiple. During the period from 2014 to 2017, water utilities traded at an 11% to 28% premium to the regulated group. This premium expanded in 2018 and 2019 with the water premium currently at a 58% premium to the average regulated multiple. WTRG's premium also expanded from 19% in 2017 to 34% in 2019. However, we believe that a change in WTRG's profile from a pure play water utility to a gas/water utility could prove to be a headwind to this premium expansion going forward, in addition to investors' utilization of a more SOTP valuation approach (utilized in deriving our price target).

Robust growth largely priced in - Initiate Neutral

Our $45, 12-month price target is based on an SOTP valuation methodology. Our 2020-2022E EPS estimates of $1.56/$1.65/$1.78 reflects a 6.6% CAGR from 2019-2022E, with potential upside to growth beyond 2022 as WTRG reduces regulatory lag on both organic investments as well as added rate base from municipal acquisitions. To arrive at our SOTP-based price target, we apply our new 30x base water target P/E multiple to 2021E EPS for the water utility segment, along with a 22x P/E multiple to 2021E EPS for the gas utility segment. Our gas multiple reflects a 10% (or 2x) premium to our 20x base gas target P/E, which reflects above-average rate base and EPS growth, as well as our constructive view of PA regulation (which makes up over 90% of the gas utility customer base).

We view WTRG's current valuation as fairly representing the company's water/gas utility mix, with our $45 target reflecting a 27.3x P/E, a discount our 30x base water target P/E for pure-play water utilities like AWK. **Upside risks to our call** include: 1) Peoples Gas acquisition synergies exceed our expectations, elevating EPS growth profile, 2) tax repairs election for the PA gas utility elevates earned ROEs even above our estimate, and 3) WTRG continues to benefit from ESG fund flows, despite its water/gas utility mix profile on a pro-forma basis. **Downside risks to our call** include: 1) PA regulation turns less constructive, 2) growth from municipal acquisitions slows, and 3) WTRG credit rating is downgraded.

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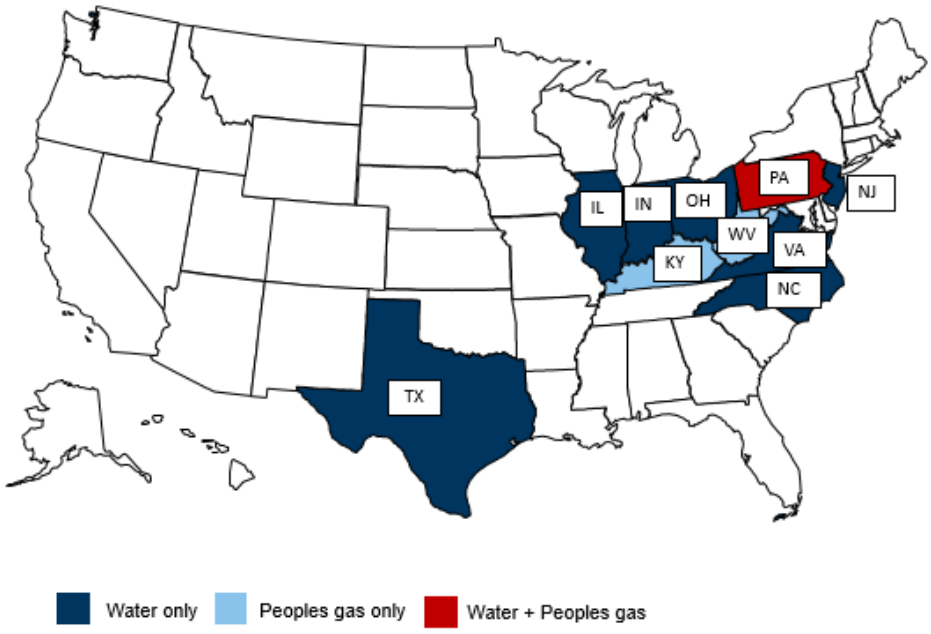
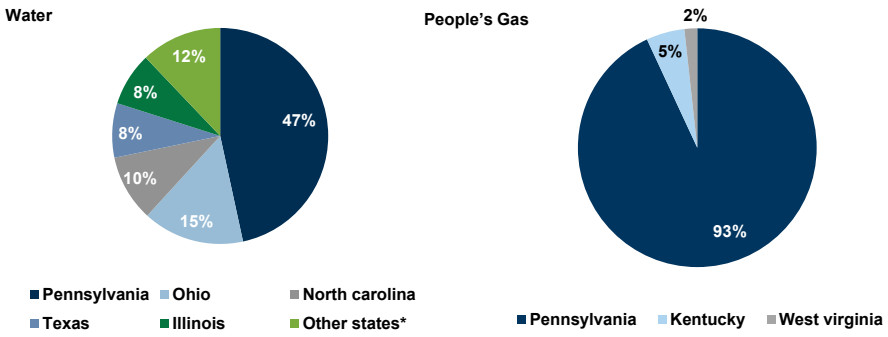
Exhibit 51: Essential Utilities is a Pennsylvania-based water and natural gas infrastructure company with a 10 state footprint...
Water + People's Gas Operating states for combined Essential Utilities



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 52: ... with combined 1.7 million regulated customers (1mn - water + 0.7mn gas), with PA as the biggest jurisdiction
Customer distribution across states Aqua + People's Gas



* Other states include New Jersey, West Virginia and Indiana

Source: Company data, Goldman Sachs Global Investment Research

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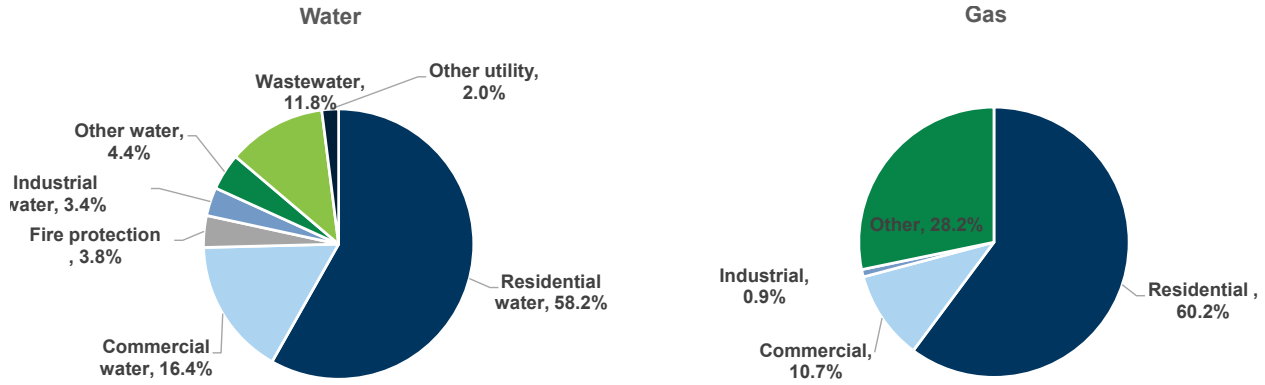
Exhibit 53: Residential revenues make up the bulk of both water and gas revenues...
Operating Revenue (2019) mix at the water/gas business by customer type



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 54: ... situated largely in constructive or balanced regulatory jurisdictions, especially its largest utility in PA.
State utility commission regulatory snapshot

WTRG Regulatory Profile							
	Pennsylvania	**Ohio**	**Illinois**	**Texas**	**North Carolina**	**Kentucky**	**West Virginia**
Commission Name	Pennsylvania Public Utility Commission	Public Service Commission of Ohio	Illinois Commerce Commission	Public Service Commission of Texas	North Carolina Utilities Commission	Kentucky Public Service Commission	Public Service Commission of West Virginia
No. of Commissioners	5 of 5 (3 D, 2 R)	5 of 5 (1 D, 2 R, 2 Non-Partisan)	5 of 5 (1 D, 2 R, 2 Non-Partisan)	3 of 3 (3 R)	4 of 7 (3 D, 1 R)	3 of 3 (3 R)	3 of 3 (2 R, 1 D)
Test year for Rate Case	Future test year	Historical test year	Future test year	Historical test year	Historical test year	Historical test year	Historical test year
Infrastructure replacement surcharges	Yes	Yes	Yes	No	Yes	Yes	Yes
Revenue Stability mechanisms	No	No	Yes	No	No	No	No
Expense mechanisms	Yes	Yes	Yes	Yes	Yes	Yes	No
Utility plant recovery mechanisms	Yes	No	Yes	No	No	Yes	No
DSIC Mechanism (applicable to Gas business)	Yes	NA	NA	NA	NA	Yes**	No
GS view on Regulation	Constructive	Balanced	Constructive	Somewhat Restrictive	Balanced	Balanced	Restrictive
Fair Market Legislation (FMV)	Yes	Yes	Yes	Yes	Yes	No	No
Company 2018 Revenue Exposure *% of total cutomers	**Water-53%; Peoples Gas*-93%**	**Water-13%**	**Water-9%**	**Water-9%**	**Water-7%**	**Peoples Gas*- 5%**	**Peoples Gas*- 2%**

Infrastructure Replacement surcharges: Allows rates to change periodically, outside a general rate case proceeding, to reflect recovery of capital investments made to replace infrastructure necessary to sustain safe, reliable services for our customers. These mechanisms typically involve periodic filings and reviews to ensure transparency.
Utility plant recovery mechanisms: Allows recovery of the full return on utility plant costs during the construction period, instead of capitalizing an allowance for funds used during construction. In addition, some states allow the utility to seek pre-approval of certain capital projects and associated costs. In this pre-approval process, the PUC may assess the prudency of such projects.
Expense mechanisms: Allows changes in certain operating expenses, which may fluctuate based on conditions beyond the utility's control, to be recovered outside of a general rate case proceeding or deferred until the next general rate case proceeding.
Revenue stability mechanisms: Separates a utility's cost recovery from the amount of water it sells to recover its fixed costs and ongoing infrastructure investment needs. Such a mechanism adjusts rates periodically to ensure that a utility's revenue will be sufficient to cover its costs, regardless of sales volume, including recognition of declining sales resulting from reduced consumption, while providing an incentive for customers to use water more efficiently.
Future test year: A test period used for setting rates, which begins with the date new rates are effective. This allows current or projected revenues, expenses and capital investments to be collected on a timelier basis.
Distribution System mprovement Charge ("DSIC") mechanism: Utilities are allowed to recover costs related to repair, replacement or improvement of eligible distribution property that has not previously been reflected in rates or rate base. Through a DSIC, subject to an earnings test, a utility may recover the fixed costs of eligible infrastructure incurred during the three months ended one month prior to the effective date of the charge, thereby reducing the historical regulatory lag associated with cost recovery through the traditional rate-making process.
Fair Market Legislation(FMV): Allows regulated water companies to pay a fair market value for the purchase of water and wastewater systems. Before these changes, system values were determined by their depreciated original cost, which generally did not reflect a reasonable market value for those assets and became a barrier to a sale.
**In Kentucky, Delta has a pipe replacement program tariff, which allows adjustment of regulated rates annually to earn a return on capital expenditures incurred subsequent to Delta's last rate case which are associated with the replacement of bare steel and vintage plastic pipe.

Source: SNL Financial, Company reports, Goldman Sachs Global Investment Research

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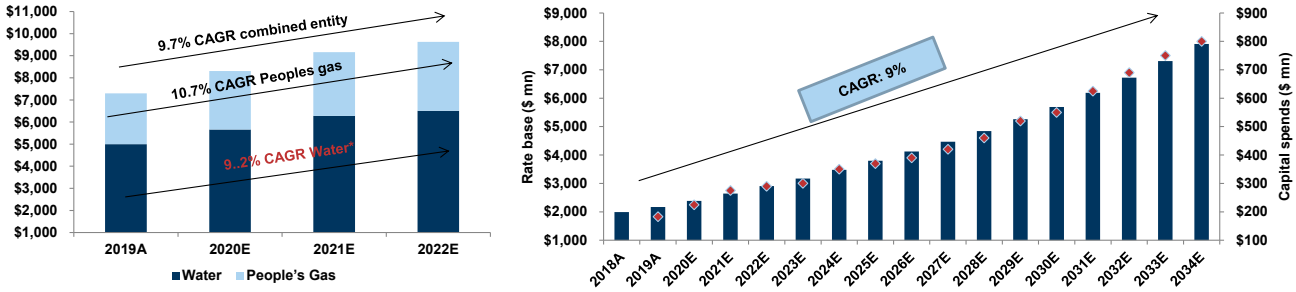
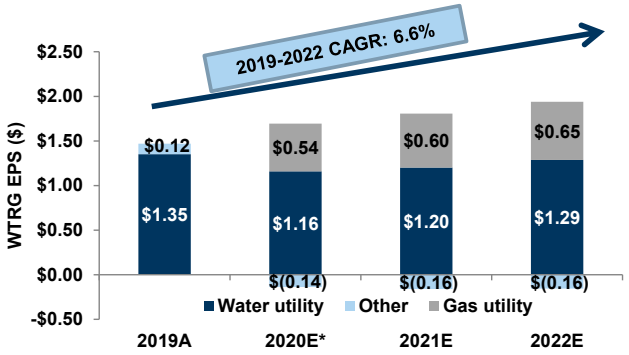
Exhibit 55: We expect WTRG to achieve 9.7% rate base CAGR from 2019-2022E across its utilities, with potential to sustain this level over the next 15 years based on organic investments and municipal acquisitions...
Rate base ($mn) 2019A-2022E



*includes $50mn/$75mn of capital in 2021/2022 at DELCORA

Source: Company data, Goldman Sachs Global Investment Research

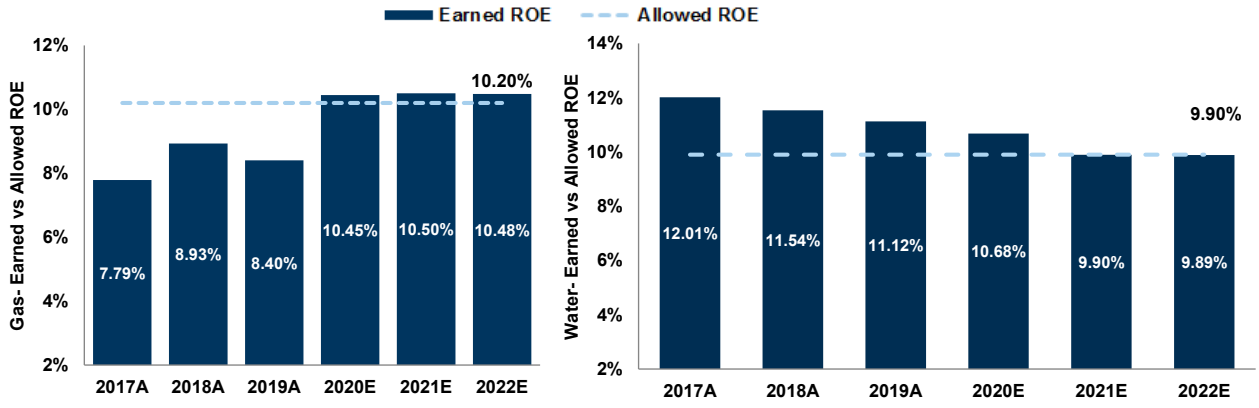
Exhibit 56: ...although we expect earnings growth to lag rate base growth at a larger rate through 2022 given acquisition earnings lag and water utilities transisiton away from tax repairs...
EPS 2019A-2022E



*2020 incorporates full-year of Peoples Gas earnings, comparable versus adjusted proforma company guidance ; 2021 summation for WTRG off by $0.01 due to rounding issue

Source: Goldman Sachs Global Investment Research, Company data

Exhibit 57: We model modest over-earning at gas utilities from expected PA tax repair benefits, versus closed to allowed ROE for water utilities after transitioning to more traditional ratemaking...
Water & Gas Utility Earned vs Allowed ROE



Source: Company data, Goldman Sachs Global Investment Research

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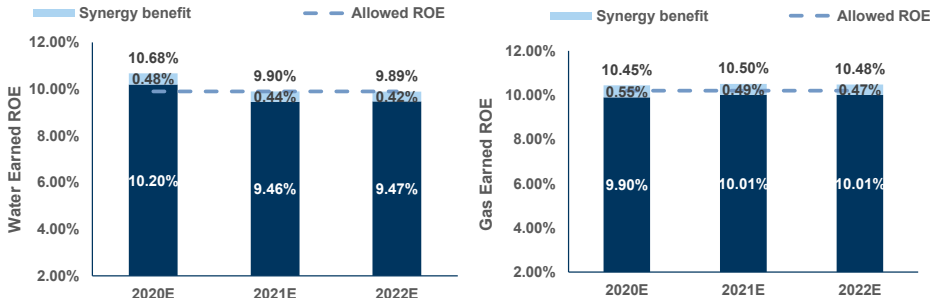
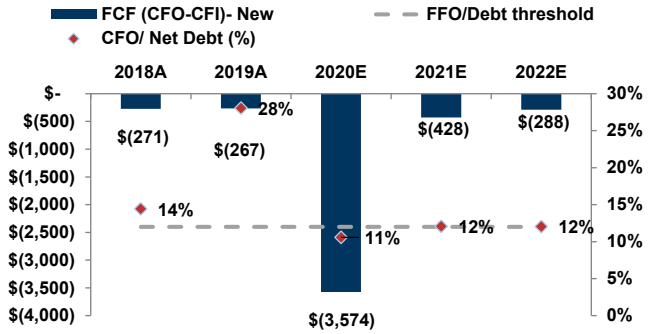
Exhibit 58: ...also supported by assumed Aqua-Peoples acquisition synergies.
Earned ROEs including and excluding merger synergies 2020E-2022E



Source: Goldman Sachs Global Investment Research

Exhibit 59: We expect FCF levels to improveing post acquisition financing, with FFO/debt near target threshold levels for its "A" rating by S&P
FCF (CFO-CFI $mn) & CFO/Net Debt (%)



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 60: Our EPS estimates are largely in line with consensus through 2022...
GS New vs Consensus

EPS Estimates			% Difference
	New	Consensus	vs Consensus
2019A	$1.47	$1.47	0%
2020E	$1.56	$1.57	-1%
2021E	$1.65	$1.65	0%
2022E	$1.78	$1.77	1%

Source: Goldman Sachs Global Investment Research, FactSet

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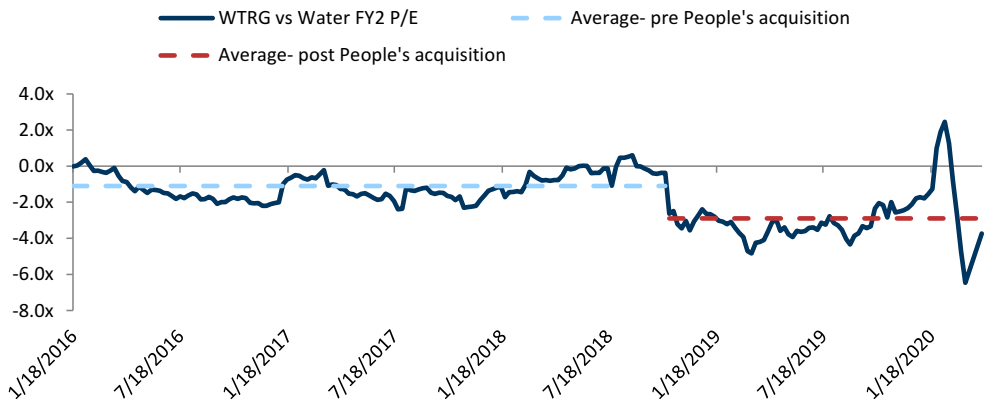
Exhibit 61: Our SOTP-based $45 price target reflects a 7% total return versus 15% for Regulated Utilities...
WTRG SOTP Valuation

VALUATION	
Water utility EPS 2021	**1.20**
Water utility multiple	30.00x
Assumed premium	0.00x
Adjusted P/E	30.0x
Water utility valuation	**36.08**
Gas utility EPS 2021	**0.60**
Gas utility multiple	20.00x
Assumed premium	2.00x
Adjusted P/E	22.0x
Gas utility valuation	**13.26**
Valuation - Other	**(0.16)**
2020 Blended multiple	27.33x
Other valuation	**(4.36)**
Total valuation	**45.00**
Current price per share	$42.80
Return potential	**5.14%**
Dividend yield	2.19%
Total return potential	**7%**

Source: Goldman Sachs Global Investment Research

Exhibit 62: ...and see WTRG's ~3-4x relative discount to pure-play water utilities as justified given its new gas utility exposure, which could affect ESG comparability
WTRG vs Regulated FY2 P/E



Source: Goldman Sachs Global Investment Research, FactSet

Company Overview

Essential Utilities Inc. (WTRG) formed from Aqua America's acquisition of privately owned Peoples Gas, completed on March 16, 2020. Essential's common stock

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began trading under the NYSE ticker symbol (WTRG) in early February. WTRG, with a market cap of $9.6 bn (as of 13th Apr close) market cap, serves more than 1 million water customers in 8 states and more than 740,000 gas customers in 3 states. WTRG projects 6-7% (ex. acquisitions) and 8-10% rate base growth for its water/gas utilities based on 2019 projected rate base of $5 billion and $2.3 billion, respectively. The key states served by WTRG are summarized in the Exhibit 52. The company operates through the following segments:

- **Regulated Water** (~70% of total operating revenues):
  - 2018 operating revenues were derived principally from the following states: ~53% in Pennsylvania, 9% in Ohio, 9% in Texas, 9% in Illinois, and 6% in North Carolina
  - The company's municipal growth strategy has accelerated significantly, largely due to the passage of Fair Market Value legislation(FMV) in several of its states. Aqua has added more than 33,000 new customers from 10 closed or signed municipal acquisitions in 2018
- **Regulated Gas** (~30% of total operating revenues):
  - The regulated gas business consists of 4 utility companies - Peoples Natural, and Peoples Gas (Formerly Peoples TWP) are regulated by the Pennsylvania Public Utility Commission. Peoples Gas – West Virginia is regulated by the West Virginia Public Service Commission. Peoples Gas – Kentucky is regulated by the Kentucky Public Service Commission
  - ~740,000 customers and 1,500 employees in western Pennsylvania, Kentucky and West Virginia
- **Market based business** (<1% of total operating revenues):
  - **Aqua Infrastructure**- provides non-utility raw water supply services for firms in the natural gas drilling industry
  - **Aqua Resources**- provides water service through O&M contracts with a municipal authority and another party close to utility companies' service territory; and offers, through a third-party, water and sewer line protection solutions and repair services to households

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Disclosure Appendix

Reg AC

I, Insoo Kim, CFA, hereby certify that all of the views expressed in this report accurately reflect my personal views about the subject company or companies and its or their securities. I also certify that no part of my compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

Unless otherwise stated, the individuals listed on the cover page of this report are analysts in Goldman Sachs' Global Investment Research division.

GS Factor Profile

The Goldman Sachs Factor Profile provides investment context for a stock by comparing key attributes to the market (i.e. our coverage universe) and its sector peers. The four key attributes depicted are: Growth, Financial Returns, Multiple (e.g. valuation) and Integrated (a composite of Growth, Financial Returns and Multiple). Growth, Financial Returns and Multiple are calculated by using normalized ranks for specific metrics for each stock. The normalized ranks for the metrics are then averaged and converted into percentiles for the relevant attribute. The precise calculation of each metric may vary depending on the fiscal year, industry and region, but the standard approach is as follows:

Growth is based on a stock's forward-looking sales growth, EBITDA growth and EPS growth (for financial stocks, only EPS and sales growth), with a higher percentile indicating a higher growth company. **Financial Returns** is based on a stock's forward-looking ROE, ROCE and CROCI (for financial stocks, only ROE), with a higher percentile indicating a company with higher financial returns. **Multiple** is based on a stock's forward-looking P/E, P/B, price/dividend (P/D), EV/EBITDA, EV/FCF and EV/Debt Adjusted Cash Flow (DACF) (for financial stocks, only P/E, P/B and P/D), with a higher percentile indicating a stock trading at a higher multiple. The **Integrated** percentile is calculated as the average of the Growth percentile, Financial Returns percentile and (100% - Multiple percentile).

Financial Returns and Multiple use the Goldman Sachs analyst forecasts at the fiscal year-end at least three quarters in the future. Growth uses inputs for the fiscal year at least seven quarters in the future compared with the year at least three quarters in the future (on a per-share basis for all metrics).

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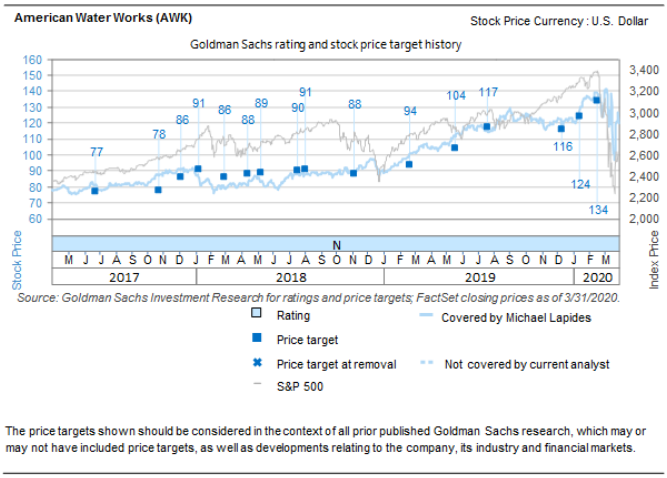

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HSBC Global Research

26 April 2021

UK and US Water

New growth opportunities vs same old bond proxies

Equities
Utilities

UK and US

- Federal Water rehabilitation plans in the US and the Green Recovery scheme in the UK are new opportunities for growth
- US stocks are best placed for growth. Pennon may provide the M&A blueprint for the UK
- Downgrade UU to Reduce from Hold, Pennon to Hold from Buy; American Water and Essential, both Buy, offer more growth; Severn Trent remains Hold

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New opportunities for growth: Despite their ESG credentials, regulated UK and US utilities have performed less well than energy transition-focused stocks because of their status as bond proxies. The water proposals set out by the US government for accelerated investment and the UK's Green Recovery proposals show policy-makers are waking up to the need to improve resilience in water and waste water provision.

Opportunities from Federal Water spending plans: The US administration has proposed a USD111bn budget, of which USD10bn is for monitoring and cleaning up toxic (per and polyfluoroalkyl substances) and investing in rural water systems, household wells, and septic units. USD56bn is proposed for modernising drinking water, wastewater, and storm water conveyance and treatment. The remaining USD45bn will be used to remove lead drinking water pipes. We raise our target prices for both US water companies we cover, which are well placed to benefit from the focus on asset rehabilitation and their expertise in removing water contaminants to address historical municipal underinvestment.

UK has insufficient investment – M&A could be the way to grow: In contrast, Ofwat's PR19 price control focused on reducing customer bills rather than allowing RCV growth for the listed companies, except for Severn Trent. An announcement is due in May on whether it will allow the Green Recovery investment proposed by the companies or if it will be scaled back. We increase our risk-free rate in line with HSBC's new UK bond yield assumption, which reduces our DCF valuation for UU (UU/ LN, 968p, TP 910p vs 960p, downgrade to Reduce from Hold). We assume Pennon and Severn Trent can deliver higher long-term growth from their more ambitious Green Recovery plans. Severn Trent (SVT LN, 2,447p, TP 2,570p vs 2,450p) remains Hold but we downgrade Pennon (PNN LN, 1,030p, TP 1,090p) to Hold from Buy after its strong recent performance.

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Summary of rating and target price changes

Company	Ticker	Currency	Current price	TP Old	TP New	Rating Old	Rating New	Upside/ downside	Premium to RCV (%) (P/Bx) 2022e	Yield 2022e
Pennon	PNN LN	GBPp	1,030	1,090	1,090	Buy	Hold	5.9%	16.2%	2.3%
Severn Trent	SVT LN	GBPp	2,447	2,450	2,570	Hold	Hold	5.0%	21.0%	4.3%
United Utilities	UU/ LN	GBPp	968	960	910	Hold	Reduce	-6.0%	17.2%	4.6%
American Water	AWK US	USD	161.4	175	183	Buy	Buy	13.4%	3.9x	1.6%
Essential	WTRG US	USD	47.9	55	57	Buy	Buy	19.0%	1.9x	2.4%

Source: HSBC estimates, priced as at close on 22 April 2021

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Executive summary

- New growth opportunities in the US from USD111bn water system improvements
- UK's Green Recovery proposals not sufficient to avoid bond proxy status for stocks; M&A needed to accelerate growth
- US water stocks AWK and WTRG, both rated Buy, offer growth potential; in the UK, we downgrade PNN to Hold from Buy after a strong performance, SVT remains Hold, UU offers limited growth potential and we downgrade to Reduce from Hold

New growth opportunities in UK and US water

The water proposals set out by the US government and the UK's Green Recovery proposals show governments are waking up to the need to improve resilience in water

Regulated UK and US utilities have not performed as strongly as energy transition stocks, because of their perceived status as bond proxies. UK water stocks are down 21.6% over 12 months relative to the FTSE Utilities Europe index compared with Drax (DRX LN, 412p, Buy) up 40.3%. However, they too have strong ESG credentials. The water proposals set out by the US government for accelerated investment and the UK government's Green Recovery proposals show policy-makers are waking up to the need to improve resilience in water and waste water provision.

The UK water companies have bond proxy status unless accelerated growth can be proven. In HSBC's report *The Price is right*, 14 April 2021, our Fixed Income strategists increased their 10- year RfR assumptions. "We move our 10-year gilt year-end forecast to 50bp (from 30bp) because some MPC members are concerned about the risk of inflation proving more persistent than elsewhere, and we fear market expectations could overshoot". We increase our risk-free rate used in our UK water company valuations in line with HSBC's new bond yield assumption. This reduces our DCF valuation for United Utilities and leads us to downgrade our rating to Reduce from Hold. We assume that Pennon and Severn Trent can deliver higher long-term growth from their more ambitious Green Recovery plans, which offset the higher WACCs we calculate for each company. We retain our Hold rating on Severn Trent but downgrade Pennon to Hold from Buy after its strong recent share price performance.

The UK

DEFRA and Ofwat likely to provide preliminary guidance on the Green Recovery Initiative in May

We expect the Department for Environment, Food and Rural Affairs (DEFRA) and the water industry regulator Ofwat to provide preliminary guidance on the projects submitted by the water companies under the Green Recovery Initiative in May. For the three UK water companies under our coverage this will accelerate their regulated asset growth. Severn Trent has the largest Green Recovery proposal of GBP730m as a percentage of its current five-year investment programme among the listed UK water companies, which if approved would lead to a rise of 24% in its existing capex plans of cGBP3bn for the current AMP (alternative

performance measures). Pennon has a capex plan of GBP1bn for the current AMP and has submitted proposals for GBP92m worth of plans under the Green Recovery initiative to the regulator; if approved it would increase capex by c9%. United Utilities has proposed GBP135m of additional capex, marking a c7% increase in its existing plan of GBP2bn for the current AMP.

Downgrade Pennon to Hold after strong recent performance, TP of 1,090p unchanged; better to travel than to arrive

The ability to create value through M&A, as Pennon did with Bournemouth Water, is a much more arduous task

Pennon has had a strong share price performance recently, driven by M&A expectations and strong initial regulatory performance. Its reinvestment decisions will provide an interesting regulatory precedent depending on where it chooses to invest its waste proceeds for growth. It could be bold and buy a large water company and plan ambitious expansion or look at a smaller water-only company and give the proceeds back to shareholders. As the sector resilience needs are significant, we assume management may think big. The case for paying a premium to Regulatory Capital Value (RCV) – the regulated asset base has been strengthened by National Grid's (NG/ LN, 915p, Buy) premium paid in March 2021 for WPD (a fast-tracked sector leader). Many of Pennon's unlisted water potential targets have a combination of complicated (with derivatives) balance sheets with higher leverage, or significant operational challenges. The ability to create value as it did with Bournemouth Water is a much more arduous task.

Severn Trent remains Hold, raise TP to 2,570p from 2,450p on higher longer term growth and higher performance rewards

Severn Trent continues to set itself out as an innovator with underlying growth and ideas for green investment

Severn Trent has applied for a cGBP730m package under the Green Recovery initiative. This investment plan is above its base capex plan of GBP3bn for the period 2021-25 (on top of the 4% RCV growth target for AMP7, the highest of its peers). Severn Trent continues to set itself out as an innovator with underlying growth and ideas for green investment. Management said in 2020 that M&A was not part of its strategy. It still has much work to do on Hafren Dyfrdwy, the small water company it owns. Management said in its pre-close statement at the end of March that Severn Trent remains on or ahead of target for almost 80% of its customer performance measures and has increased its guidance for outperformance on customer performance incentives (ODIs) this year from 'at least GBP25m' to 'at least GBP50m'. Pennon and UU shares have outperformed Severn Trent but in our view both have had a higher profile: Pennon through M&A and United Utilities at its CMD. However, Severn Trent consistently trades at a premium to RCV to the other two listed stocks, currently at c20%, and therefore we do not see sufficient additional value to justify a Buy rating.

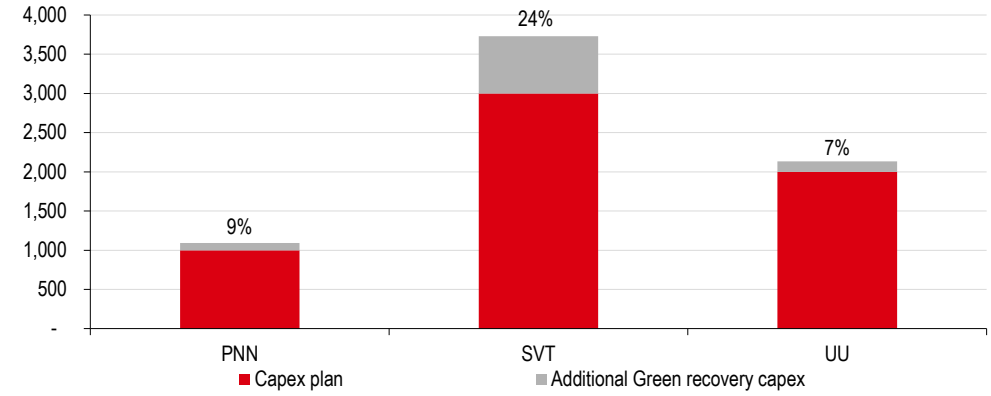
Downgrade United Utilities to Reduce from Hold, cut TP to 910p from 960p on higher gilt yield assumptions and brought forward phasing of investment

UU still struggles to avoid its bond proxy status. Of all the water stocks under our coverage it has the highest dividend yield and the lowest Green Recovery list of potential projects compared to its current investment. It continues to bring forward investment to drive ODI performance but management seems to have backtracked on exploring M&A opportunities in UK water despite a significant operational improvement.

Despite UU's significant operational improvements, its asset base is shrinking

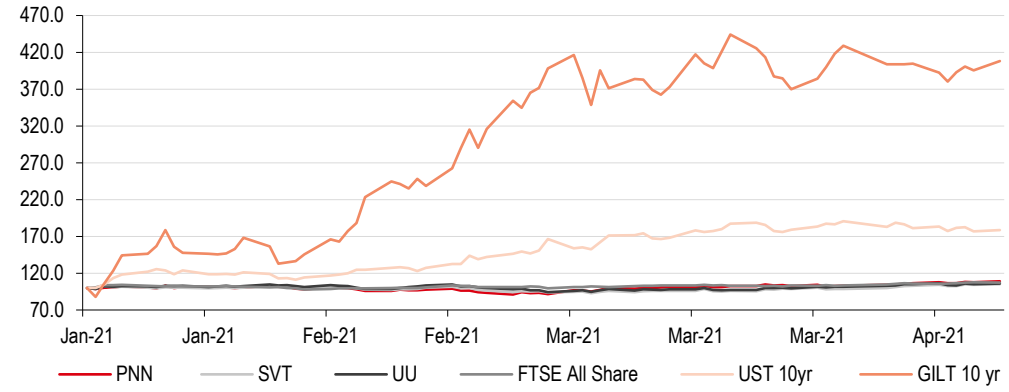
Despite UU's significant operational improvements, its asset base is shrinking. Ofwat is looking at the Haweswater Aqueduct Resilience Programme (HARP) project as a blueprint for attracting additional capital for major projects to the sector but it will have to prove convincingly that project finance without government guarantees with the additional cost of finance, lawyers, and cost duplication will deliver better value to shareholders. HARP in particular is a risky project because of the tunnelling required through hills in the Lake District, which is not a core competence for UU. We remain sceptical that it can be delivered at a lower cost to UU's customers bearing in mind that Thames Tideway, another significant project (Thames Water), needed a government guarantee. If HARP could be delivered more cheaply by United Utilities' management team it would form part of its regulatory asset growth post 2025.

Green Recovery capex acceleration (GBPm)



Source: Company data

Performance of AWK vs WTRG vs UST 10-year vs FTSE USA Growth Index vs S&P 500



Source: Refinitiv Datastream

The US

Federal proposal for USD111bn for water system improvements, most notably replacing lead pipes in drinking water systems

The US government set out its proposal, the 'American Jobs Plan', on 31 March 2021, which is a wide-ranging job creation and infrastructure rehabilitation plan. Among its many parts, it includes a proposal to allocate USD111bn for water system improvements, most notably replacing lead pipes in drinking water systems.

The larger privately held and investor-owned (IOU) water utilities including American Water Works and Essential Utilities, the two largest under our coverage, have the technological expertise to test and treat drinking water as additional federal and/or state contaminant levels are adopted. They also have the expertise in project management to rehabilitate waste water systems, which arguably have been neglected even more than the clean water network.

Funding aside, regulatory mechanisms such as Fair Market Value and the use of infrastructure charges have been major growth drivers for these listed companies

Funding aside, regulatory mechanisms such as Fair Market Value and the use of infrastructure charges have been a major growth driver for these listed companies. This has enabled them to:

- purchase regulated water systems at a premium to rate base (the appraised value),
- pay a premium for the municipality to redeploy the proceeds for other priorities,
- increase water rates incrementally each year in order to replace pipes.

The costs and risks of expansion within the states in which these two companies operate, has delivered savings through economies of scale and have also spread the cost of asset rehabilitation, especially for poor communities across the entire state rate base. US water assets are significantly underinvested compared to the UK. This underpins the mid-single digit earnings growth expected by the listed utilities.

Latest developments

HSBC's US Economics team on 15 April 2021 published *US Fiscal Policy*, updating on the Biden administration's latest proposals for spending on infrastructure and other areas of over USD2bn. We extract from this report below.

"Republican senators have indicated that they are preparing a smaller, counterproposal that would be focused on a narrower set of infrastructure investments compared to the American Jobs Plan. Republican Senator Shelley Moore Capito said on 14 April that the budgetary cost of such a plan could be in the range of USD600bn to USD800bn.

President Joe Biden is scheduled to address a joint session of Congress on 28 April. At that point, markets will be looking for some clarity about whether bipartisan discussions on infrastructure have yielded any progress or whether Democrats are likely to pursue enactment of American Jobs Plan proposals via budget reconciliation, relying on support strictly from Democratic lawmakers. In either case, it will be important to monitor the momentum of the discussions over the course of the early summer given that Congress typically goes on recess during the month of August".

American Water remains Buy, raise TP to USD183 from USD175 on higher growth

American Water plans to spend USD22-25bn over the next ten years on water quality, essential infrastructure replacement and regulated customer growth. This underpins regulated future revenue growth.

Its medium-term aim is for an EPS CAGR of 7-10% in 2021-2025. 1-2% growth is to come from Market-Based Businesses, 1-2% growth from Regulated Acquisitions and 5-7% growth from Regulated Investment (capex). Dividend growth is targeted at the high end of 7-10% while maintaining a payout ratio of 50-60% of earnings.

American plans to invest USD22-25bn of capital over the next ten years

It plans to maintain a predominantly regulated risk profile with capital-light, cash-generating Market-Based Businesses representing 12% of EPS in 2024.

Essential targets investment of USD3bn from 2021 to 2023 to maintain a 70/30 water to gas mix of business

Essential remains Buy, raise TP to USD57 from USD55 on higher growth

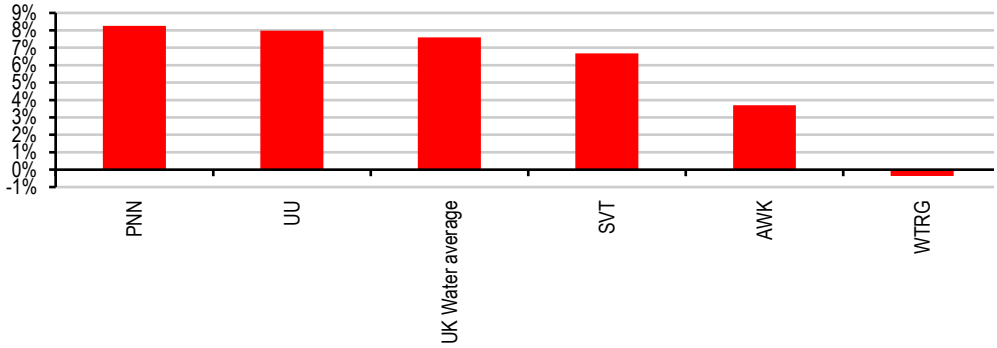
Essential Utilities' management targets investment of USD3bn from 2021 to 2023 to maintain a 70/30 water to gas mix of business measured by size of regulated rate base. To complement its infrastructure rehabilitation, Essential is also investing in municipal acquisitions in the US states in which it operates. We believe its recent performance has been muted because it remains embroiled in the political complexities of its Delcora acquisition, despite the legality of the contract. We think this could continue to depress its share price performance. Ultimately customers in Delaware will have to pay for asset rehabilitation even if Essential is not successful. There are other opportunities for expansion in water. In gas it has clear visibility for enhanced asset rehabilitation, which will also reduce carbon emissions.

Stock metrics

Company	Rating	PE			EV/EBITDA			Yield			FCF yield		
		2021e	2022e	2023e	2021e	2022e	2023e	2021e	2022e	2023e	2021e	2022e	2023e
PNN	Buy	35.6x	33.6x	30.6x	12.9x	12.6x	12.0x	2.1%	2.2%	2.3%	39.6%	2.2%	1.4%
SVT	Hold	23.2x	18.7x	15.8x	14.1x	13.1x	12.0x	4.1%	4.2%	4.3%	3.4%	1.3%	1.7%
UU	Reduce	17.6x	17.2x	15.9x	13.8x	13.7x	13.1x	4.4%	4.5%	4.6%	2.3%	3.9%	5.7%
WTRG	Buy	29.2x	26.7x	24.6x	19.1x	18.2x	16.5x	2.2%	2.4%	2.6%	-2.2%	-1.9%	0.8%
AWK	Buy	38.4x	35.3x	31.3x	18.8x	17.7x	17.0x	1.5%	1.6%	1.8%	-0.4%	-1.4%	-1.0%
UK average		**25.8x**	**23.3x**	**21.5x**	**13.6x**	**13.1x**	**12.4x**	**3.5%**	**3.6%**	**3.7%**	**15.1%**	**2.5%**	**2.9%**
Average		**28.8x**	**26.3x**	**23.6x**	**15.7x**	**15.1x**	**14.1x**	**2.9%**	**3.0%**	**3.1%**	**8.5%**	**0.8%**	**1.7%**

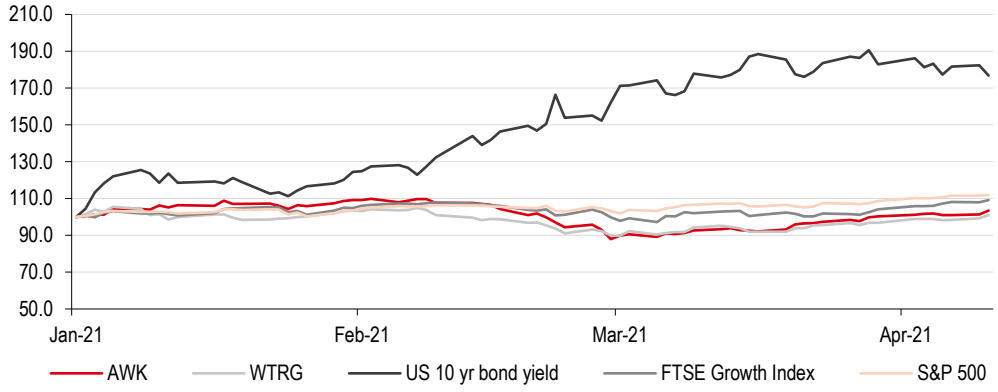
Source: HSBC estimates

Year-to-date share price performance



Source: Refinitiv Datastream

Performance of AWK vs WTRG vs UST 10yr vs FTSE USA Growth Index vs S&P 500



Source: Refinitiv Datastream

Opportunities from Federal Water spending plans

- The challenge of US water provision
- Lead pipe replacement and water contaminants removal are opportunities
- US water companies benefit from a highly fragmented, underinvested market

The challenge of US water provision

Clean water

Renewal and replacement of ageing water and wastewater infrastructure, as well as the financing for capital improvements, the top two issues facing the US water industry

Renewal and replacement of ageing water and wastewater infrastructure, as well as the financing for capital improvements, are the top two issues facing the US water industry according to the 2021 Infrastructure Report Card.

Funding for drinking water infrastructure has not kept pace with the growing need to address ageing infrastructure systems, and current funding sources do not meet the total needs. Since 2017, there have been signs of improvement with the modest expansion of federal financing programmes and water utilities are raising water rates to fund network investment.

The US Environmental Protection Agency's (EPA) drinking Water State Revolving Fund (DWSRF) provides low-interest loans to state and local drinking water infrastructure projects. The DWSRF programme grew from USD2bn in 2013 to nearly USD3bn in 2018. The EPA's Water Infrastructure Finance & Innovation Act (WIFIA) programme offers the sponsors of large projects (over USD20m) a new financing tool to leverage limited federal resources; stimulate additional investment in drinking water, wastewater, and stormwater infrastructure; and encourage greater private sector participation. By 2019, prospective borrowers had submitted letters of interest requesting over USD21bn in WIFIA loans, including USD3.9bn for drinking water projects. The US government increased its lending capacity from USD2.5bn in 2017 to USD6bn in 2019.

According to an American Society of Civil Engineers' (ASCE) 2020 economic study, the annual drinking water and wastewater investment gap will grow to USD434bn by 2029

US water customers have not paid tariffs, in our view, that allow the cost of infrastructure rehabilitation (in addition to water service provision) compared to markets such as France and the UK. The average nationwide monthly drinking water rate has increased 31% from 2012 to 2018 but more is needed. According to an American Society of Civil Engineers' (ASCE) 2020 economic study, the annual drinking water and wastewater investment gap will grow to USD434bn by 2029.

Wastewater

The majority of the nation's Wastewater Treatment Plants (WWTPs) were designed with an average lifespan of 40 to 50 years. Since the systems were constructed in the 1970s, around the passing of the Clean Water Act in 1972, they are reaching the end of their service lives.

Moreover, utilities face the challenge of meeting increasingly stringent surface water quality regulations for rivers and lakes. Significant infrastructure replacement is needed but clean water investment has tended to be prioritised compared to wastewater. Investor-owned utilities are experts in resilience-related planning and using technological and scientific innovations that produce profitable by-products such as sludge. They can also deliver cost savings from wastewater treatment relative to legacy plant. Today's waste water can be tomorrow's clean water in areas of water stress. In 2019, the federal government invited more than a dozen wastewater and water reuse projects to apply for over USD2.3bn in loans.

Federal Water spending plans

The US government set out its proposal, the 'American Jobs Plan', on 31 March 2021, which is a wide-ranging job creation and infrastructure rehabilitation plan. Among its many parts it includes a proposal to allocate USD111bn for water system improvements, most notably replacing lead pipes in drinking water systems.

The plan offers USD10bn for monitoring and cleaning up toxic (per and polyfluoroalkyl substances), a particular competence of the companies under our coverage

The plan offers USD10bn for monitoring and cleaning up toxic (per and polyfluoroalkyl substances or PFAS) and investing in rural water systems, household wells, and septic units. This is a major focus for US investors. A sum of USD56bn is proposed for modernising drinking water, wastewater, and storm water conveyance and treatment. The remaining USD45bn will be used to remove all of the country's estimated 6-10m lead drinking water pipes. Additionally, the plan provides funding for the 'western drought crisis' by investing in water efficiency and recycling programmes.

Where do the investor-owned utilities fit into these plans?
We look at what has happened historically when large Federal financial resources have been available. Federal money is expected to provide some support, but funding may not be available to all the municipalities in need.

Federal money is expected to provide some support, but funding may not be available to all the municipalities in need

Financially, municipal systems have been facing challenges with limited government funding and competing needs for other services. Operationally, due to a lack of expertise, smaller systems will find it difficult to keep up with increasingly stringent water quality standards over the medium term, even if they have money to replace their lead pipes in the short term. Municipal systems in the medium term will continue to weigh up the advantages of divesting assets for ongoing asset replacement needs and when the expense of testing and treating for higher standards of water is overly burdensome. This will continue to drive acquisition opportunities for the listed water stocks under our coverage.

The larger privately held and investor-owned (IOU) water utilities have the technological expertise to test and treat drinking water as additional federal and/or state contaminant levels are adopted. They also have the expertise in project management to rehabilitate waste water systems, which arguably have been neglected even more than the clean water network.

UK Water

- Announcement to deliver accelerated environmental growth expected next month
- Pennon – premium precedent by National Grid for regulated assets and CMA green light on increased leverage
- HSBC Fixed Income expects an increase in short-term gilt yields

Accelerated environmental growth through Green Recovery

DEFRA and Ofwat will provide preliminary guidance on the projects submitted by the water companies under the Green Recovery Initiative, we believe in May

DEFRA and Ofwat will provide preliminary guidance on the projects submitted by the water companies under the Green Recovery Initiative we believe in May. For all the companies under our coverage this will accelerate regulated asset growth. The UK water sector has lagged the performance of its UK electricity peers. The prospect of more growth and the strong ESG credentials of the listed water companies may lead to a better performance in calendar Q2.

M&A update – Pennon management could be tempted to pay up

M&A: Two recent events may encourage Pennon to pay up: National Grid's 60% premium payment for WPD; and the CMA's lack of endorsement for capital structure sharing with customers

The market is waiting for Pennon to conclude its strategic review on where to redeploy the GBP2.7bn of net proceeds from its waste sale. The easy option would be to enhance earnings through a share buyback and return the proceeds to shareholders. In our experience, water companies under our coverage have always found something to invest in. This is a once-in-a-lifetime to invest for environmental performance and growth. Two recent events may encourage Pennon to pay up:

- National Grid's 60% premium payment for WPD
- The CMA's lack of endorsement for capital structure sharing with customers.

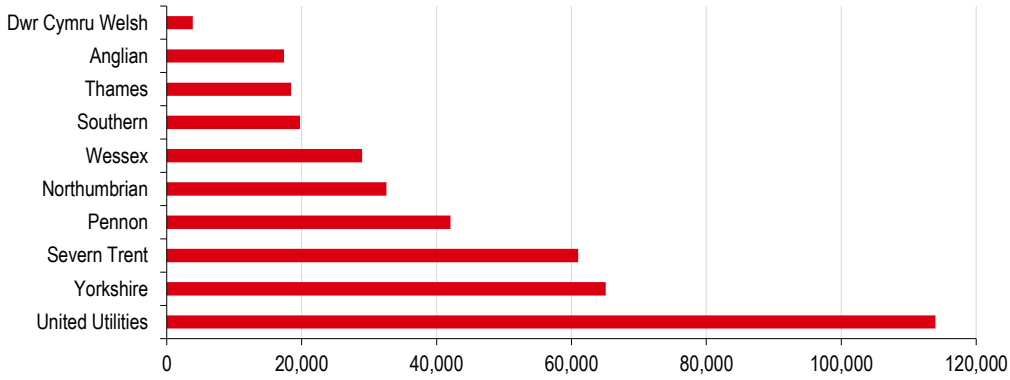
Both suggest that Pennon could pay more for one of the four companies that went to the CMA (Competition and Markets Authority) as it would not have to share the benefits of taking on more debt (to drive down the WACC) with shareholders.

Plenty of assets need accelerated investment – the UK's multiple sewage overflow numbers

According to an investigative report by the BBC's Panorama broadcast on 13 April, UK water companies have been illegally dumping untreated sewage into rivers. Panorama gathered detailed data from ten water companies in England and Wales through environmental information requests. The data suggests seven of the ten companies had treatment works that were breaching their permits by dumping sewage before they were treating the specified volumes. Water companies discharged untreated sewage into rivers more than 400,000 times lasting more than 3m hours last year.

To protect properties from flooding and prevent sewage from backing, treatment works are allowed to release sewage into rivers and streams after extreme weather, such as torrential rain, and when they are operating close to full capacity. This untreated sewage is normally screened and passed through storage tanks before it is dumped. Discharge permits issued by the Environment Agency specify the level of sewage each works has to treat before it can dump untreated sewage. But Panorama's report found some companies are discharging without a permit and/or providing incorrect information to the agency.

Number of storm water overflows, 2020



Source: Environment Agency

This is more an indication that even though the UK's water infrastructure has benefited from significant investment, more is needed

This chart does not imply that UU is exceeding its permitted discharge limits and this absolute chart does not reflect the size or geography of the companies. However, it does reflect that all the overflows were without permit. It merely demonstrates that further resilience investment is needed to reduce these numbers. This is more an indication that even though the UK's water infrastructure has benefited from significant investment, more is needed.

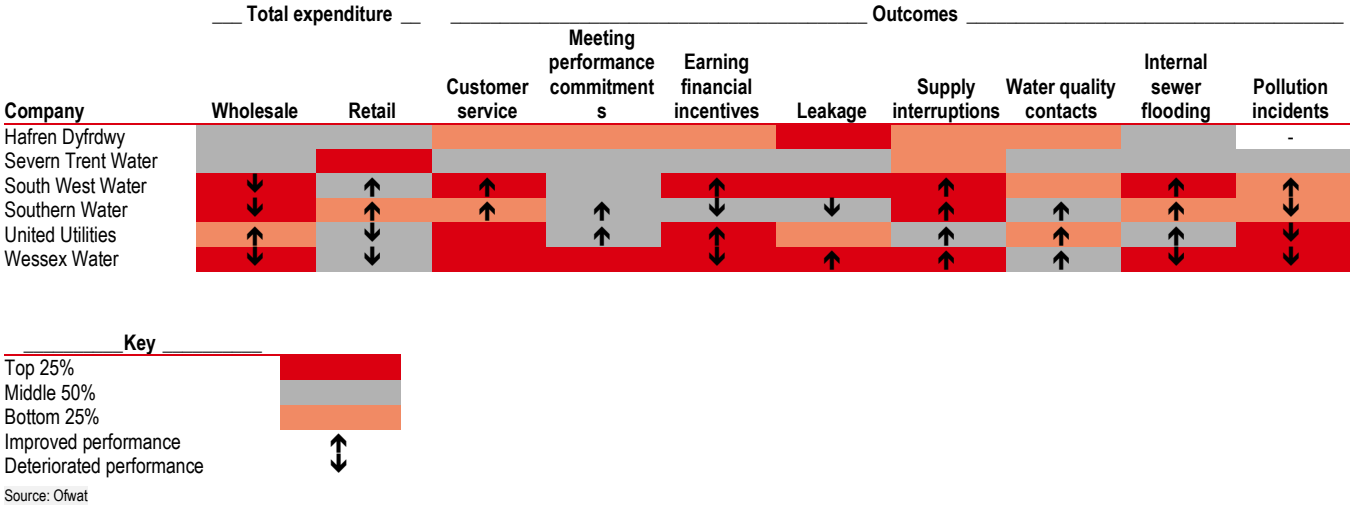
Customers may need to be prepared to accept increases in bills to ensure that less untreated sewage is released into rivers.

Bond proxy status unless accelerated growth can be proven

In HSBC Fixed Income's report *The Price is Right* published on 14 April 2021, the team increased its 10-year RfR assumptions. "We move our 10-year gilt year-end forecast to 50bp (from 30bp) because some MPC members are concerned about the risk of inflation proving more persistent than elsewhere, and we fear market expectations could overshoot".

We increase our RfR in line with HSBC's new UK bond yield assumption (we take an average of short and long-term gilt yields). This leads us to reduce our DCF valuation for United Utilities and we downgrade our rating to Reduce from Hold. We assume that Pennon and Severn Trent can deliver higher long-term growth from their more ambitious Green Recovery plans, which offset the higher WACC we now calculate for each company. We retain our Hold rating on Severn Trent but downgrade Pennon to Hold from Buy after its strong recent share price performance. United Utilities' RCV growth excludes the Haweswater Aqueduct project, which Ofwat is testing to see whether it can be financed more cheaply by project finance. This means its asset base is shrinking and it is hard to see how it will not continue to be seen as a bond proxy and command a yield premium to its peers. We downgrade United Utilities to Reduce from Hold on our higher RfR assumptions, not offset by significant Green Recovery Investment.

Overall Service Performance: Ofwat 2019-2020



Source: Ofwat

We reproduce above Ofwat's overall service performance table for 2019 to assess the task in hand for key companies in the sector. In terms of overall performance:

- Hafren Dyfrdwy, despite being owned by Severn Trent, is still a relatively poor performer on many measures.
- Severn Trent remains in the middle of the pack with an average performance but we know from its H1 presentation that it is working hard to alleviate its long-term weakness in supply interruptions.
- Southern Water is making progress but still has much work to do across many areas.
- South West Water still has to make better progress with water customer contacts, which was meant to be an area where its acquisition of Bournemouth Water was beneficial. It is already making improvements in reduction in pollution incidents.
- Wessex Water remains best in class across more measures than its peers.

Companies

American Water

- Acquisition-led growth accelerating
- Environmental credentials, especially in regard to removal of water contaminants
- Reiterate Buy rating, raise TP to USD183 from USD175

Investment thesis

American Water plans to spend USD22-25bn over the next ten years. This underpins its regulated future revenue growth.

Medium-term aims are for an EPS CAGR of 7-10% 2021-2025

The company's medium-term aims for an EPS CAGR of 7-10% from 2021-2025. adjusted EPS. 1-2% growth is to come from Market-Based Businesses, 1-2% growth from Regulated Acquisitions and 5-7% growth from Regulated Investment (capex). Dividend growth is targeted at the high end of a 7-10% range while maintaining a payout ratio of 50-60% of earnings.

It plans to maintain a predominantly regulated risk profile with capital-light, cash-generating Market-Based Businesses representing 12% of EPS in 2024. The company also plans to invest USD20-22bn of capital over the next ten years for water quality, needed infrastructure replacement and regulated customer growth.

Similarly, rate base growth of CAGR 7-8% is targeted for 2021-2025.

American is seen as one of the few regulated utilities with accelerated growth, which means it has not suffered as much as its peers from a bond proxy negative correlation with rising bond yields

Together this means American Water is regarded as one of the few regulated utilities with accelerated growth, which means it has not suffered as much as its peers from a bond proxy negative correlation with rising bond yields. Recent acquisitions have further underpinned its growth status.

2021 outlook

The outlook for 2021 was set out at the FY 2020 results on 25 February:

- 2021 earnings guidance range of USD4.18 to USD4.28 per diluted share.
- AWK has 44,000 customers in its pipeline through signed acquisitions following regulatory approval, which it expects to complete.
- The company is awaiting final orders for general rate cases in three states and filed for infrastructure surcharges in one state for a total annualised revenue request of USD126m.

Recent M&A activities underpin growth

American Water announced the acquisition of City of York wastewater systems in the state of Pennsylvania, through its subsidiary Pennsylvania American Water, for USD235m on 7 April. This acquisition will add roughly 45,000 connections. The agreement has received approval from York City Council and American Water plans to close the transaction by the end of 2021, assuming it receives the necessary approvals from the regulators. As part of the agreement, it will preserve current wastewater rates for a minimum of three years, offer employment to all of the city's wastewater system employees, establish an in-person customer service centre in

York, provide an upfront deposit of USD20m, and contribute at least USD50,000 in donations to non-profit organisations serving the city and its residents.

In another deal, American Water acquired the wastewater assets of Egg Harbour City in New Jersey for USD21.8m on 30 March. Under the terms of the deal, American Water will invest USD14m in the first ten years for necessary upgrades, including the construction of an emergency interconnection with the subsidiary's regional system. The deal is expected to be completed in the second half of the year, pending approval from the New Jersey Department of Community Affairs and the New Jersey Board of Public Utilities.

Performance against peers

The stock has underperformed the S&P 500 index by 8.5% and underperformed the FTSE USA growth index by 5.7% since 1 January 2021. In the same period, Essential Water's stock underperformed the S&P 500 index by 10.9% and FTSE USA growth index by 8.1%. Both American Water and Essential have performed as bond proxies since the start of the year. American Water appears to have a much greater correlation with the S&P 500 index than an inverse correlation with the US 10-year bond yield. As it accelerates its investment for growth, we expect the shares to continue to move in tandem with the FTSE USA Growth Index peers. This is in marked contrast to its regulated UK water peers, which have performed as bond proxies.

However, a falling UST 10-year yield has helped American Water's share price to move higher recently as it is the largest pure-play water company in the US with a clear growth trajectory and strong pipeline of acquisitive growth planned for the next few years.

Change in estimates

We update our model for the FY2020 results and introduce our 2023 estimates.

Change in estimates, introducing 2023e

	2021e	2022e	2023e
Revenues (USDm)			
Revised	3,942	4,193	4,456
Previous	3,957	4,203	-
Change	-0.4%	-0.2%	-
EBITDA (USDm)			
Revised	2,131	2,279	2,414
Previous	2,120	2,263	-
Change	0.5%	0.7%	-
EBIT (USDm)			
Revised	1,419	1,566	1,690
Previous	1,436	1,563	-
Change	-1.2%	0.2%	-
PBT (USDm)			
Revised	994	1,097	1,213
Previous	1,037	1,124	-
Change	-4.2%	-2.4%	-
Net income (USDm)			
Revised	763	842	958
Previous	778	843	-
Change	-2.0%	-0.1%	-
EPS (USD)			
Revised	4.20	4.58	5.15
Previous	4.21	4.57	-
Change	-0.2%	0.2%	-
DPS (USD)			
Revised	2.39	2.60	2.84
Previous	2.39	2.60	-
Change	0.0%	0.0%	-

Source: HSBC estimates

Valuation and risks

We value American Water via three approaches: DCF, target dividend yield, and sum of the parts (using the average of our rate base valuation and peer multiple valuation). Taking the average of the three fair values, which we update, we raise our target price to USD183 from USD175.

- **DCF:** We change our observed Bloomberg five-year beta to 0.79 from 0.5, reflecting volatility relating to interest rate rises in the US. We use a risk-free rate of 2.5%, equity risk premium of 3.0% and a cost of equity of 4.9%, resulting in a higher WACC of 4.2% (previously 3.7%). We update our earnings estimates. Despite the increased beta, recent deals mean we increase our terminal value growth rate by 50bp to 3.5%. This increases our DCF fair value to USD204.4 from USD175.5.
- **Target PE multiple and dividend yield:** We use the weighted average of the US water peer group (70%) and FTSE USA Growth index constituents (30%) to arrive at our PE multiple and target dividend yield. US water peers are now trading at a PE multiple of 36x with a yield of 1.45%, whereas the FTSE growth index is trading at a PE of 36x and yield of 1.25%. Hence, we use a 36x (unchanged) water peer multiple (for our SOTP valuation; see below) and a target dividend yield of 1.4% (unchanged in line with water peers), both in line with the above-mentioned methodology. The fair value from our yield approach is unchanged at USD170.9.
- **Sum of the parts:** In our SOTP approach, we continue to use the 2021e rate base to reflect the company's current growth trajectory (based on 2020e rate base numbers). In this we assume 8% annual growth of the rate base to 2021e. We then use the average of the sum-of-the-parts valuation based on the rate base with a small non-regulated element, and our peer multiple-based valuation of 3.5x price to regulated rate base (proxy for price to book in line with peers). Our new fair value from this method is USD173.3, down from USD179.9.

Our higher target price of USD183 implies upside of 13.4%. We retain our Buy rating as the company has a strong pipeline of accretive acquisitions to be completed in the next few years, which we expect to drive higher rate base growth than previously.

Summary of valuation

USD	New	Previous
Current price as on 22-Apr-21	**161.4**	**NA**
DCF	204.4	175.5
Yield 1.4% (unchanged)	170.9	170.9
Peer multiple	173.3	177.9
Target price (average rounded)	**183.0**	**175.0**
Implied upside to target price	13.4%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity valuation	USDm
Cost of debt		+ DCF value	46,361
Pre-tax cost of debt	3.1%	+ ST marketable assets	0
Marginal tax rate	23.3%	+ Value of associates	0
Cost of equity		+ Other assets	1,525
Risk-free rate	2.5%	**EV (asset side)**	47,886
Equity risk	3.0%	- Net debt (+ if net cash)	(10,368)
Additional risk	-	- Quasi debt (pension)	(388)
Beta (previously 0.5)	0.79	- Value of minorities	0
Debt - 28%	2.4%	**Total non-equity claims**	(10,756)
Equity - 72%	4.9%	Value of equity	37,130
Cost of capital	4.2%	**Value per share (USD)**	**204.4**

Source: HSBC estimates

SOTP valuation

Regulated rate base	2021e rate base USDm
California	581
Illinois	1,030
Indiana	1,238
Kentucky	517
Missouri	1,457
New Jersey	3,441
New York	321
Penn	3,689
Virginia	182
W Virginia	762
Total	**13,219**
Price to rate base valuation	46,265
Non-regulated 2020 (PE based valuation)	522
Net debt 2020e, pensions & Minority	-11,293
Total	**35,494**
NoS (m)	182
Value per share	**195**
2020 earnings (USD)	4.20
2020 PE sector average	36.0x
Value per share (USD)	**151**
Average of rate base and PE multiple (USD)	**173.3**

Source: HSBC estimates

Downside risks

If American Water fails to achieve the desired rate case revisions, this could impact its revenue and profit margins. The company may also fail to deliver organic growth. If it fails to keep its momentum in acquiring water systems or gaining O&M efficiency, it may not achieve our forecasts.

Financials & valuation: American Water Works

Buy

Financial statements

Year to	12/2020a	12/2021e	12/2022e	12/2023e
Profit & loss summary (USDm)				
Revenue	3,777	3,942	4,193	4,456
EBITDA	1,852	2,131	2,279	2,414
Depreciation & amortisation	-604	-712	-713	-724
Operating profit/EBIT	1,248	1,419	1,566	1,690
Net interest	-395	-425	-469	-477
PBT	924	994	1,097	1,213
Taxation	-215	-231	-255	-255
Net profit	709	763	842	958
Cash flow summary (USDm)				
Cash flow from operations	1,426	1,496	1,588	1,718
Capex	-1,822	-1,600	-2,000	-2,000
Cash flow from investment	-2,061	-1,600	-2,000	-2,000
Dividends	-389	-434	-478	-528
Change in net debt	999	537	190	810
FCF pre dividends	-396	-104	-412	-282
Balance sheet summary (USDm)				
Intangible fixed assets	1,559	1,559	1,559	1,559
Tangible fixed assets	20,837	21,725	23,013	24,289
Current assets	1,248	1,273	1,311	1,351
Cash & others	547	547	547	547
Total assets	24,137	25,051	26,376	27,692
Operating liabilities	3,097	3,144	3,216	3,292
Financial liabilities	10,944	11,481	11,671	12,481
Total liabilities	18,312	18,896	19,159	20,044
Net debt	10,397	10,934	11,124	11,934
Shareholders' funds	6,454	6,783	7,847	8,277

Ratio, growth and per share analysis

Year to	12/2020a	12/2021e	12/2022e	12/2023e
Y-o-y % change				
Revenue	4.6	4.4	6.4	6.3
EBITDA	5.7	15.0	6.9	6.0
Operating profit	6.7	13.7	10.4	7.9
PBT	10.9	7.6	10.4	10.6
HSBC EPS	7.8	7.8	9.0	12.5
Ratios (%)				
ROE	11.3	11.5	11.5	11.9
ROCE	6.1	6.1	6.4	6.6
EBITDA margin	49.0	54.0	54.3	54.2
Operating profit margin	33.0	36.0	37.3	37.9
Net debt/equity	161.1	161.2	141.8	144.2
CF from operations/net debt	13.7	13.7	14.3	14.4
Per share data (USD)				
EPS reported (diluted)	3.90	4.20	4.58	5.15
HSBC EPS (diluted)	3.90	4.20	4.58	5.15
DPS	2.19	2.39	2.60	2.84
Gross CFPS	8.40	8.12	8.46	9.04

Valuation data

Year to	12/2020a	12/2021e	12/2022e	12/2023e
EV/sales	10.5	10.2	9.6	9.2
EV/EBITDA	21.3	18.8	17.7	17.0
P/CF	19.2	19.9	19.1	17.8
PE*	41.4	38.4	35.3	31.3
FCF yield (pre div) (%)	-1.4	-0.4	-1.4	-1.0
Dividend yield (%)	1.4	1.5	1.6	1.8

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2019a
GHG emission intensity*	n/a
Energy intensity*	377.6
CO_2 reduction policy	Yes
Social Indicators	**12/2019a**
Employee costs as % of revenues	12.8
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	12/2020a
No. of board members	11
Average board tenure (years)	5.5
Female board members (%)	45.5
Board members independence (%)	45.5

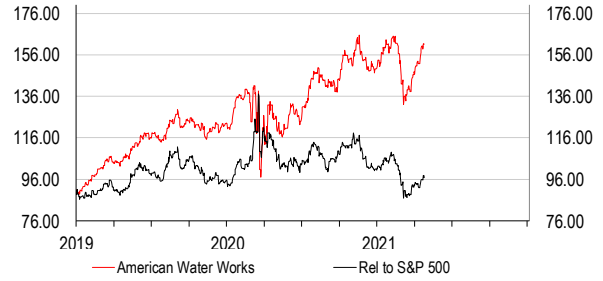
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	161.43	Free float	100%
Target price (USD)	183.00	Sector	Water Utilities
RIC (Equity)	AWK.N	Country/Region	United States
Bloomberg (Equity)	AWK US	Analyst	Verity Mitchell
Market cap (USDm)	29,294	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 22 Apr 2021

Essential Utilities

- The growth proposition with gas decarbonisation investment
- Next catalysts in the regulatory processes, Delcora uncertainty discount should unwind in 2021
- Reiterate Buy rating, raise TP to USD57 from USD55

Investment thesis

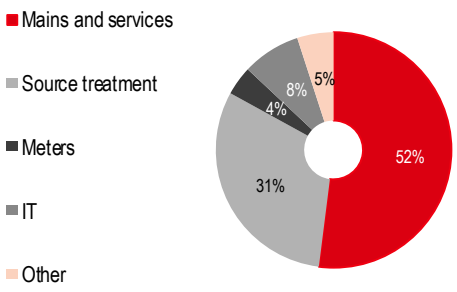
Essential Utilities' management set out its outlook for the period 2021-23 on 11 January, and confirmed it its FY2020 results on 24 February. It targets investment of USD3bn from 2021 to 2023 to maintain a 70/30 water (Aqua) to gas (Peoples) mix of business measured by size of regulated rate base. To complement its infrastructure rehabilitation, Essential is also investing in municipal acquisitions in the US states in which it operates. It has a pipeline of water acquisitions in these states and its accelerated investment programme in gas means it has not suffered as a bond proxy as much as some of its regulated peers. It has underperformed recently because of the well-publicised challenges to its acquisition of Delcora. We believe once either of these is resolved or indeed Essential walks away from the deal, this uncertainty discount should unwind.

2021 outlook

Management targets a range for 2021 EPS of USD1.64-1.69 with growth of 5-7% through to 2023. It will invest USD550m in regulated water and USD450m in its regulated gas segments.

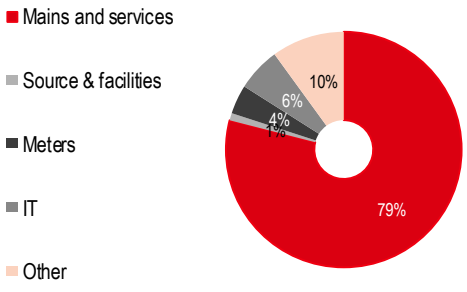
We discussed both its growth and this guidance in our report of 14 January: *Guidance update; ESG acceleration*. Management sees opportunities to add USD500m of rate base growth from a number of acquisition targets but the largest of these, Delcora, has faced a number of headwinds, as we discuss below.

Water segment capex plan through to 2023e



Source: Essential Utilities: Investors presentation – 11 January 2021

Gas segment capex plan through to 2023e



Source: Essential Utilities: Investors presentation – 11 January 2021

Caveat – why growth may not be linear

As with all regulated utilities under our coverage, it is important to note that asset and earnings growth should not be expected to be linear.

For example, Essential Utilities' management pointed out that this year, the company is preparing a water three-year rate case filing in Pennsylvania for its Aqua PA unit. Because the majority of Aqua's rate base is from Pennsylvania, this will result in a short-term earnings lag until it can recover the revenues at the new rates. Indeed, under- or over-recovery of revenues means adjustments are needed in subsequent years. However, M&A does provide some short-term support for earnings growth. Municipal acquisitions generally create a short-term earnings lag as these acquisitions rarely, if ever, earn a full return until they are included in a rate case.

Delcora – getting it done

In the light of uncertainty around the Delcora acquisition, Essential has excluded Delcora contributions from its 2021 guidance

In the light of the uncertainty around the Delcora acquisition, Essential has excluded Delcora contributions from its 2021 guidance. Post the ruling by a judge in favour of Essential's claims of legality of the purchase contract, the county has appealed to the Commonwealth Court. According to management, the ruling may take about six months. In a bid to make a better case for the deal, Essential says it will submit a rate stabilisation plan. Essential further updated that it will not delay the Aqua Pennsylvania rate case due to the pending Delcora deal.

Peoples Gas

According to management guidance, the rate base of gas segment will increase 8-10% pa to 2023

During its investor presentation in February, Essential disclosed an investment plan of USD3bn from 2021 to 2023, with USD1bn being invested in the current year to rehabilitate and strengthen water, wastewater and natural gas systems. According to the management guidance, the rate base of gas segment will increase at 8-10% per year to 2023. For the year 2021, Essential is planning to invest USD450m. Essential management hoped to used tax optimisation (using capital allowances on the balance sheet) to stay out of rates. It seems likely that this option may not be utilised for Peoples Gas. This suggests it will file for rate increases earlier. This will have no effect on earnings from an investor perspective but means customers will pay for the asset rehabilitation earlier than using balance sheet resources.

Performance against peers

Essential's stock has underperformed the S&P 500 index by 10.9% and FTSE USA growth index by 8.1% year-to-date. In our view, this is because of the newsflow on the regulatory and legal challenges to the Delcora acquisition. We believe that some of the issues have been resolved but there are still uncertainties. Essential raised 6,700,000 shares of equity in August 2020 on a forward sale basis which must be exercised by 10 August 2021. The proceeds from this equity raise was primarily for Delcora but also Essential management said, for general corporate purposes, including for water and wastewater utility acquisitions, working capital and capital expenditures.

Feedback from some investors is that the equity raise of USD300m on a deferred basis might still be drawn down even if the acquisition doesn't proceed. Essential management says it is confident there are other acquisition targets that could be funded by equity but a smaller amount of equity might be deployed. Investors need to be reassured that only the appropriate level of equity is raised for the investment needs of the business and Essential is not overcapitalised.

We believe certainty either of the success or failure of the Delcora deal should lead to the unwinding of the current uncertainty discount.

Change in estimates

We have updated our estimates post the company's FY2020 results and introduce our 2023 estimates.

Change in estimates, introducing 2023e

	2021e	2022e	2023e
EBIT (USDm)			
Revised	623	685	759
Previous	649	697	-
Change	-4%	-2%	-
Net income (USDm)			
Revised	428	467	519
Previous	420	456	-
Change	2%	2%	-
EPS (USD)			
Revised	1.64	1.79	1.94
Previous	1.67	1.81	-
Change	-2%	-1%	-
DPS (USD)			
Revised	1.07	1.15	1.23
Previous	1.07	1.15	-
Change	0%	0%	-

Source: HSBC estimates

Valuation and risks

We value Essential Utilities using the average of three approaches: DCF, dividend yield and the average of our PE multiple and rate-base valuations. After updating our earnings estimates and assumptions, we raise our target price to USD57 from USD55.

- In our DCF, we increase our Bloomberg observed five-year beta to 0.89 from 0.6. This reflects, we believe, the market volatility of interest rate rises in the US. This is the primary driver of the reduction in our DCF value to USD45.8 per share from USD56.5.
- For our yield-based valuation, we cut our target average yield to 1.64% from 2.25% in line with the water (70% of water peers' yield) and gas-related utilities peers (30% of gas peers' yield. This reflects Essential's business mix and leads us to increase our yield valuation to USD65.0 from USD47.7. This reflects the movement in peer group multiples as water and gas is seen as having more of a growth status compared to that of bond proxy stocks.
- For our approach using the average of our PE multiple and rate-base valuations, we keep our target multiple unchanged at 33.5x, in line with that of peers. We use a water and gas peer group PB average of 2.6x as a proxy for a rate-base valuation. This is consistent with all US utilities under our coverage and is a proxy for EV. Our new SOP and peer multiple value is USD58.7, down from USD61.4.

We increase our target price to USD57 from USD55, which implies 19.0% upside. We reiterate our Buy rating as we believe the combination of regulated investment growth and earnings growth remains attractive and there is scope for the current uncertainty discount to unwind.

Summary of valuation

USD	New	Previous
Current price as on 22-Apr-21	**47.9**	**NA**
DCF	45.8	56.5
Yield 1.64% (previously 2.25%)	65.0	47.7
SOP & peer multiple	58.7	61.4
Target price (average rounded)	**57.0**	**55.0**
Implied upside to target price	19%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity valuation	USDm
Cost of debt		+ DCF value	16,158
Pre-tax cost of debt	3.6%	+ ST marketable assets	0
Marginal tax rate	10.0%	+ Value of associates	0
Cost of equity		+ Other assets	1,369
Risk-free rate	2.5%	EV (asset side)	17,527
Equity risk premium	3.0%	- Net debt (+ if net cash)	(5,587)
Additional risk		- Quasi debt (pension)	0
Beta (previously 0.6)	0.89	- Value of minorities	0
Debt - 31%	3.2%	Total non-equity claims	(5,587)
Equity - 69%	5.2%	Value of equity	11,940
Cost of capital	5.2%	**Value per share (USD)**	**45.8**

Source: HSBC estimates

Average of rate base and peer multiple valuations

	2021e rate base USDm
Regulated water	
Pennsylvania	3,954
Ohio	393
Illinois	409
Texas	342
New Jersey	229
North Carolina	263
Indiana	96
Virginia	89
Regulated gas	2,634
Total	**8,409**
Price to rate base	21,864
Non-regulated 2020 PE multiple	10
Net debt 2021e, pensions & minority	(5,551)
Estimated equity value	16,323
Estimated equity value per share (USD)	**62.5**
PE multiple valuation	
2021e yield (%)	1.64
2021e PE sector average (USD)	33.5
Value per share (USD)	**54.9**
Average of rate base valuation and PE multiple valuation (USD)	**58.7**

Source: HSBC estimates

Downside risks

Essential Utilities failing to achieve the desired rate case upwards revisions and infrastructure surcharges; lacking organic growth from asset replacement; inability to take advantage of the Fair Market Value legislation opportunity; dividend growth at a lower rate than we assume; and inability to conclude the Delcora acquisition in 2021.

Financials & valuation: Essential Utilities

Buy

Financial statements

Year to	12/2020a	12/2021e	12/2022e	12/2023e
Profit & loss summary (USDm)				
Revenue	1,467	1,962	2,088	2,224
EBITDA	692	909	984	1,079
Depreciation & amortisation	-257	-286	-299	-320
Operating profit/EBIT	435	623	685	759
Net interest	-166	-168	-183	-201
PBT	265	455	502	558
HSBC PBT	268	455	502	558
Taxation	20	-27	-35	-39
Net profit	285	428	467	519
HSBC net profit	285	428	467	519
Cash flow summary (USDm)				
Cash flow from operations	508	740	773	847
Capex	-836	-1,000	-1,000	-750
Cash flow from investment	-4,334	-724	-1,000	-750
Dividends	-233	-280	-300	-328
Change in net debt	4,417	-36	526	-69
FCF equity	-328	-260	-227	97
Balance sheet summary (USDm)				
Intangible fixed assets	2,332	2,332	2,332	2,332
Tangible fixed assets	10,881	11,319	12,020	12,450
Current assets	375	449	476	504
Cash & others	5	5	5	5
Total assets	13,705	14,218	14,945	15,403
Operating liabilities	2,041	2,141	2,175	2,211
Gross debt	5,630	5,594	6,121	6,052
Net debt	5,625	5,589	6,116	6,047
Shareholders' funds	4,684	5,132	5,299	5,790
Invested capital	11,542	11,954	12,648	13,070

Ratio, growth and per share analysis

Year to	12/2020a	12/2021e	12/2022e	12/2023e
Y-o-y % change				
Revenue	64.9	33.7	6.4	6.5
EBITDA	39.2	31.4	8.3	9.6
Operating profit	27.8	43.3	10.0	10.7
PBT	25.3	71.9	10.2	11.2
HSBC EPS	7.6	46.7	9.1	8.6
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	5.3	5.0	5.2	5.5
ROE	6.7	8.7	9.0	9.4
ROA	4.2	4.2	4.4	4.7
EBITDA margin	47.2	46.3	47.1	48.5
Operating profit margin	29.6	31.8	32.8	34.1
EBITDA/net interest (x)	4.2	5.4	5.4	5.4
Net debt/equity	120.1	108.9	115.4	104.4
Net debt/EBITDA (x)	8.1	6.2	6.2	5.6
CF from operations/net debt	9.0	13.2	12.6	14.0
Per share data (USD)				
EPS Rep (diluted)	1.12	1.64	1.79	1.94
HSBC EPS (diluted)	1.12	1.64	1.79	1.94
DPS	1.00	1.07	1.15	1.23
Book value	18.39	19.67	20.31	21.67

Valuation data

Year to	12/2020a	12/2021e	12/2022e	12/2023e
EV/sales	11.8	8.8	8.6	8.0
EV/EBITDA	25.1	19.1	18.2	16.5
EV/IC	1.5	1.5	1.4	1.4
PE*	42.8	29.2	26.7	24.6
PB	2.6	2.4	2.4	2.2
FCF yield (%)	-2.8	-2.2	-1.9	0.8
Dividend yield (%)	2.1	2.2	2.4	2.6

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2019a
GHG emission intensity*	n/a
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social Indicators	**12/2019a**
Employee costs as % of revenues	n/a
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	12/2020a
No. of board members	8
Average board tenure (years)	7.0
Female board members (%)	25
Board members independence (%)	87.5

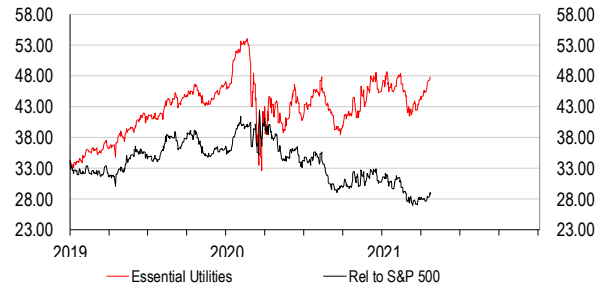
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	47.9	Free float	100%
Target price (USD)	57.00	Sector	Water Utilities
RIC (Equity)	WTRG.N	Country/Region	United States
Bloomberg (Equity)	WTRG US	Analyst	Verity Mitchell
Market cap (USDm)	11,751	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 22 Apr 2021

Pennon

- Trading update, positive FY21 guidance, possible news on cash deployment by June results
- Green Recovery push potential for cGBP92m of additional investment
- Downgrade to Hold from Buy with unchanged TP of 1,090p after strong performance; better to travel than to arrive

Investment thesis

The case for paying a premium to RCV has been strengthened by NG's premium paid for WPD (a fast-tracked sector leader). Many of Pennon's unlisted water potential targets have a combination of complicated (with derivatives) balance sheets with higher leverage, or significant operational challenges

Pennon shares have had a strong recent performance driven by M&A expectations and strong initial regulatory performance. Its reinvestment decisions will provide an interesting regulatory precedent depending on where it chooses to invest its waste proceeds for growth. It could be bold and buy a large water company and plan ambitious expansion or look for a smaller water-only company and give the proceeds back to shareholders. As the sector resilience needs are significant, we think management may think big. The case for paying a premium to RCV has been strengthened by National Grid's premium paid in March 2020 for WPD (a fast-tracked sector leader). Many of Pennon's unlisted water potential targets have a combination of complicated (with derivatives) balance sheets with higher leverage, or significant operational challenges as can be seen from the table on page 12 above. The ability to create value, as it did with Bournemouth Water, is a much more arduous task.

Trading update: growing regulatory return, M&A clarity in June

Pennon confirmed its FY2020/21 performance is in line with management expectations. It continues to expect a doubling of base RORE of 3.9% from total expenditure and financial outperformance, which remains in line with the H1 (April-September) number of 8%. The company anticipates a net ODI penalty (despite 80% ODIs on or ahead of targets) position for the year due to underperformance associated with pollution incidents. However, a COVID-19 financial impact is as anticipated. Pennon further suggested that cash collections in H2 have been robust and no new debtors provisions are added.

It confirmed that if a major deal is not completed, a substantial return of capital to shareholders will be made

There was no update on capital allocation plans, with clarity now expected at the FY2020/21 results in June. With GBP3bn cash and committed facilities, PNN is in a good financial position to carry out M&A. Pennon's management believes there is significant potential in the UK water sector and it continues to narrow down its review of potential growth opportunities to reinvest the proceeds from the Viridor sale in 2020. Moreover, Pennon has confirmed that if a major M&A opportunity is not available, a substantial return of capital to shareholders will be made.

Green Recovery initiative

Pennon has proposed a GBP92m Green Recovery investment for the period to 2025, which will mark a 10% increase in its existing GBP1bn investment programme for the period. It has proposed six projects focused on improving public health, protecting the environment and addressing climate change. Pennon has suggested that the impact on customer bills be paused until 2025. Ofwat will announce its preliminary views on the proposals in May.

Performance against peers

Pennon shares have underperformed the FTSE All share index by 19.4% year-to-date and underperformed other listed UK water companies. Lack of visibility on the deployment of cash may be driving this. It has announced it is evaluating M&A options in the UK water space and an update is expected during its full-year results in June. The current lack of visibility may hinder its performance in the short term, but management has confirmed a return of value is possible either through M&A or a share buyback in the medium term. It still appears to have some inverse correlation to gilt yields.

Change in estimates

We update our estimates post the trading update to reflect a slightly higher interest charge than we had assumed previously.

Change in estimates

GBPm	2021e	2022e	2023e
EBITDA			
Revised	327	336	355
Previous	327	336	355
Change	0%	0%	0%
EBIT			
Revised	205	218	233
Previous	205	221	235
Change	0%	-1%	-1%
PBT			
Revised	144	153	168
Previous	151	153	165
Change	-4%	0%	2%
Net income (continuing)			
Revised	121	128	141
Previous	127	128	139
Change	-4%	0%	1%
EPS (continuing, p)			
Revised	28.8	30.5	33.5
Previous	30.2	30.4	32.8
Change	-5%	0%	2%
DPS (p)			
Revised	21.7	22.5	23.4
Previous	21.8	22.6	23.5
Change	-0.5%	-0.5%	-0.5%

Source: HSBC estimates

Valuation and risks

We value Pennon shares using three valuation approaches: DCF, dividend yield and sum-of the-parts. We assign a 50% weight to yield and 25% each to DCF and SOTP, rounded, to arrive at our target price of 1,090p (unchanged).

- In the DCF valuation, we change our forward estimates for 2021 and onwards to reflect the guidance by management during the trading update for FY2020/21. We also update our tax rate and interest rate as per company guidance. We take the five-year Bloomberg observed beta of 0.70 (unchanged). We revise our RfR to reflect the HSBC Fixed Income team view of 10-year gilt rates to 50bp from 30bp previously. To this we add a 150bp premium. This increases our RfR to 2.0% from 1.83% previously. This increases our WACC to 3.8% from 3.6%. Because of the Green Recovery potential additional growth, we increase our terminal growth value in our DCF to 1.25% from 1.0%. We also update the pension deficit for the H1 results. These changes lead to a net increase in our DCF valuation to 1,439p from 1,249p.
- In the yield valuation, we add an unchanged premium of 0.25% to our revised RfR, increasing our yield to 2.55% from 2.08%. This reduces our yield value to 1,001p from 1,088p.
- In the SOTP valuation, we continue to assume net proceeds of GBP2.7bn from the sale of Viridor. We use South West Water's RCV to March 2022 for the basis of our SOTP. The higher WACC leads to a lower value creation assumption than previously but is offset by the assumption that Pennon is able to earn a 10% return on the Green Recovery investment (the same proportion we calculate for our value creation relative to its RCV) which we add to our value creation assumption. These changes lead us to increase in our SOTP valuation to 928p from 925p.

Our target price of 1,090p is unchanged and implies upside of 5.9%. We downgrade our rating to Hold from Reduce reflecting the strong recent share price performance.

Summary of valuation (p)

	New	Previous
Current price as on 22-Apr-21	**1,030**	**NA**
DCF	1,439	1,249
Yield 2.55% (vs 2.08%)	1,001	1,088
SOP	928	925
Target price (average rounded)	**1,090**	**1,090**
Implied upside to our TP	5.9%	NA
Rating	**Hold**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity valuation	GBPm
Cost of debt		**DCF value**	**5,996**
Pre-tax cost of debt	2.5%	Viridor net assets	0
Marginal tax rate	19.0%	**EV (asset side)**	**5,996**
Cost of equity		- Net debt (+ if net cash)	101
Risk-free rate (previously 1.83%)	2.0%	- Quasi debt (pension)	(52)
Equity risk premium	4.0%	- Value of minorities	(0)
Beta (unchanged)	**0.70**	- hybrid	0
Cost of debt - 37%	2.0%	Total non-equity claims	48
Cost of equity - 63%	4.9%	Value of Equity	6,045
Cost of capital	**3.8%**	**Value per share (p)**	**1,439**

Source: HSBC estimates

SOP valuation

	GBPm	EV RCV (combined)	GBPm
South West Water RCV 2022e	3,493	Net debt	2,612
Allowed return	355	Market cap	4,377
Total SWW	**3,848**	Less non-regulated	(2,700)
Total Viridor		Market implied utility value	4,289
PNN enterprise value	**3,848**	**Premium**	**22.8%**
Net debt 2022e, pensions & minority	52		
Estimated equity value	3,900		
Equity value per share (p)	**928**		

Source: HSBC estimates

Upside risks

- Pennon acquires a regulated water company that demonstrates a clear value creation proposition to shareholders
- Pennon cannot create shareholder value through acquisition and returns the proceeds to shareholders, enhancing earnings and yield through a share consolidation.

Downside risks

- For SWB, not being able to achieve the efficiency challenges in its business plan for 2020-25 and not being able to achieve the ODI rewards needed to support the dividend policy.
- Bad debts may continue to rise in SWB and Pennon Water Services from the current challenging economic conditions.
- Pennon is unable to expand profitably in UK water from a lack of opportunities that create value.
- It provides no clarity on its reinvestment strategy of return of proceeds by the time of the FY 2021 results in May.

Financials & valuation: Pennon Group

Hold

Financial statements

Year to	03/2020a	03/2021e	03/2022e	03/2023e
Profit & loss summary (GBPm)				
Revenue	637	603	615	633
EBITDA	365	327	336	355
Depreciation & amortisation	-120	-122	-118	-122
Operating profit/EBIT	246	205	218	233
Net interest	-63	-60	-65	-65
PBT	277	144	153	168
Taxation	-71	-14	-24	-27
Net profit	206	1,793	128	141
Cash flow summary (GBPm)				
Cash flow from operations	366	1,856	293	260
Capex	-323	-145	-198	-201
Cash flow from investment	-323	1,774	-198	-201
Dividends	-173	-184	-91	-95
Change in net debt	-31	-3,149	-3	36
FCF pre dividends	43	1,711	95	59
Balance sheet summary (GBPm)				
Intangible fixed assets	44	44	44	44
Tangible fixed assets	3,172	3,194	3,274	3,353
Current assets	861	2,979	2,938	2,909
Cash & others	666	2,712	2,715	2,680
Total assets	4,081	6,220	6,260	6,310
Operating liabilities	1,073	328	331	335
Financial liabilities	3,715	2,612	2,612	2,612
Total liabilities	5,050	3,202	3,205	3,208
Net debt	3,049	-101	-104	-68
Shareholders' funds	1,712	3,025	3,062	3,108

Ratio, growth and per share analysis

Year to	03/2020a	03/2021e	03/2022e	03/2023e
Y-o-y % change				
Revenue	-56.9	-5.4	2.0	2.9
EBITDA	-29.8	-10.5	2.8	5.6
Operating profit	-24.5	-16.7	6.7	6.8
PBT	6.4	-47.8	5.9	9.7
HSBC EPS	-32.5	-18.1	5.9	9.7
Ratios (%)				
ROE	8.7	5.1	4.2	4.6
ROCE	4.7	33.4	3.2	3.4
EBITDA margin	57.4	54.3	54.7	56.1
Operating profit margin	38.6	33.9	35.5	36.8
Net debt/equity	178.1	-3.3	-3.4	-2.2
CF from operations/net debt	12.0			
Per share data (GBPp)				
EPS reported (diluted)	61.71	28.20	30.50	33.46
HSBC EPS (diluted)	35.17	28.80	30.50	33.46
DPS	43.77	21.70	22.52	23.44
Gross CFPS	0.99	4.55	0.58	0.62

Valuation data

Year to	03/2020a	03/2021e	03/2022e	03/2023e
EV/sales	11.6	7.0	6.9	6.7
EV/EBITDA	20.2	12.9	12.6	12.0
P/CF	10.4	2.3	17.5	16.4
PE*	29.1	35.6	33.6	30.6
FCF yield (pre div) (%)	1.0	39.6	2.2	1.4
Dividend yield (%)	4.3	2.1	2.2	2.3

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	03/2020a
GHG emission intensity*	2,644.9
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social Indicators	**03/2020a**
Employee costs as % of revenues	13.5
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	03/2021a
No. of board members	7
Average board tenure (years)	5.6
Female board members (%)	42.9
Board members independence (%)	57.1

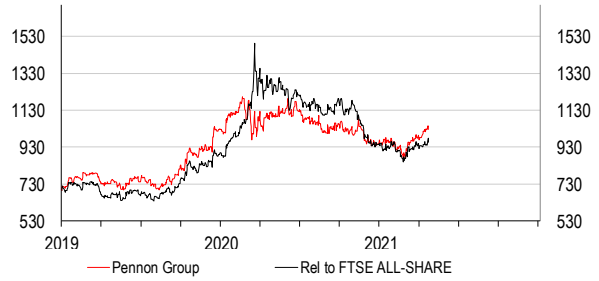
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (GBPp)	1,030	Free float	100%
Target price (GBPp)	1,090	Sector	Water Utilities
RIC (Equity)	PNN.L	Country/Region	United Kingdom
Bloomberg (Equity)	PNN LN	Analyst	Verity Mitchell
Market cap (USDm)	6,025	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 22 Apr 2021

Severn Trent

- Analysing the trading update, Green Recovery capex plans
- Still commands RCV premium relative to peers, despite Hafren Dyfrdwy performance and lack of M&A aspirations
- Retain Hold rating and raise TP to 2,570p from 2,450p on higher growth potential from Green Recovery

Investment thesis

Severn Trent continues to set itself out as an innovator with underlying growth and ideas for green investment. Management said in 2020 that M&A was not part of its strategy. It still has much work to do on Hafren Dyfrdwy, the water company it owns. We understand from the pre-close statement that management is focused on improvement in many areas. Severn Trent consistently trades at a premium to RCV to the other two UK listed stocks, currently at c20%, reflecting its higher RCV growth and recently its significant Green Recovery investment plans. We do not see therefore sufficient additional value to justify a Buy rating and remain at Hold.

Trading update for FY21

Company increased guidance for outperformance on Customer ODIs this year from GBP25m to at least GBP50m

SVT said at its trading update on 4 February 2021 that it remained on or ahead of its target for almost 80% of its customer performance measures. The company has therefore increased its guidance for outperformance on Customer ODIs this year from GBP25m to at least GBP50m.

Green Recovery initiative

SVT has applied for a cGBP730m package under Green Recovery

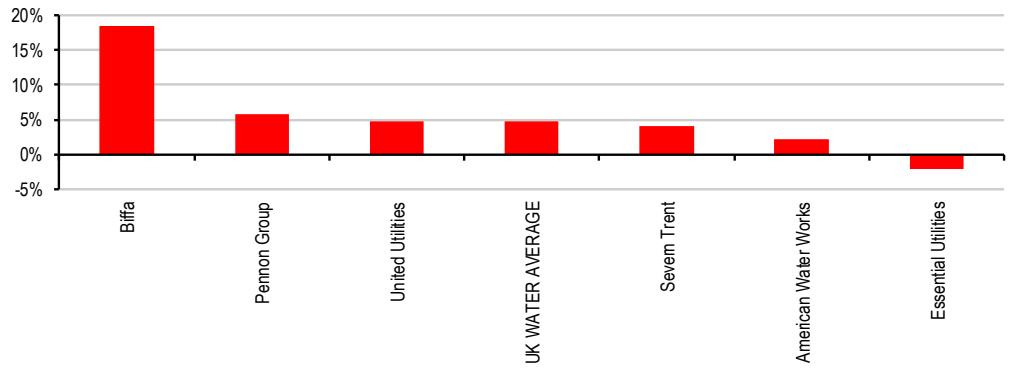
Severn Trent has applied for a cGBP730m package under Green Recovery. This investment plan is above the base capex plan of GBP3bn for the period 2021-25 (which would have delivered 4% RCV growth target for AMP7, the highest of its peers).

The water company said that only 15% of the cost would go directly onto customers' bills – Severn Trent will provide 85% of the funding needed upfront by raising new finance, which will then be recovered over a longer time period. Severn Trent estimates the extra cost to customers will be GBP6 per year on average.

Performance against peers

Pennon and UU shares have outperformed Severn Trent but in our view both have had a higher profile: Pennon through M&A and United Utilities at its CMD. However, Severn Trent consistently trades at a premium to RCV to the other two listed stocks, currently at c20%, and so we do not see sufficient additional value to justify a Buy rating. Our higher target price of 2,570p implies 5.0% upside and we maintain our Hold rating.

Relative return vs sector benchmark index y-t-d



Source: Refinitiv Datastream

Change in estimates

We update our estimates post trading update for FY2020/21.

Change in estimates

GBPm	2021e	2022e	2023e
EBIT			
Revised	476	548	625
Previous	492	546	607
Change	-3%	0%	3%
PBT			
Revised	279	352	422
Previous	289	350	404
Change	-3%	1%	4%
EPS (p)			
Revised	105.5	131.0	154.6
Previous	109.3	131.6	151.4
Change	-3%	0%	2%
DPS (p)			
Revised	100.58	102.38	104.50
Previous	100.71	102.51	104.63
Change	-0.1%	-0.1%	-0.1%

Source: HSBC estimates

Valuation and risks

We value Severn Trent shares using three valuation approaches: DCF, dividend yield and sum of the parts. We assign a 50% weight to yield and 25% each to DCF and SOTP, rounded to arrive at our new target price of 2,570p from 2,450p, after adjusting our earnings estimates and assumptions.

- In the DCF valuation, we change our forward estimates for 2021 and onwards to reflect the guidance given by management during the trading update for FY2020/21. We also update our tax rate as well as interest rate as per company guidance. We take an observed Bloomberg five-year beta of 0.71 (changed from 0.75 from the previous Bloomberg estimates used in December 2020). We revise our RfR to reflect the HSBC Fixed Income view of 10-year gilt rates to 50bp from 30bp previously. To this we add at 150bp premium. This increases our RfR to 2.0% from 1.83% previously. This increases our WACC to 3.9% from 3.8%. Because of the Green Recovery potential additional growth, we increase the

terminal growth value in our DCF to 1.5% from 1.0%. We also update the pension deficit for the H1 results. This increases our DCF to 3,190p from 2,452p.

- In the yield valuation, a premium of 1.75% is added to our revised RfR (2%) resulting in a yield of 3.75% (previously 3.58%). The higher RfR reduces our yield valuation to 2,730p from 2,860p.
- In our sum of the parts we assume that Severn Trent is able to earn a 6% return on the Green Recovery investment (the same proportion we calculate for our value creation relative to its RCV) which we add to our value creation assumption. This increases the SoP value to 1,637p from 1,625p.

Our new target price of 2,570p implies upside of 5.0%. We maintain our Hold rating as we think the accelerated Green Recovery potential and underlying RCV growth are fully reflected in its price. We also note the relatively weaker financial profile of Severn Trent vs peers.

Summary of valuation (p)

	New	Previous
Current price as on 22-Apr-21	**2,447**	**NA**
DCF	3,190	2,452
SOP	1,637	1,625
Yield 3.75% (previously 3.58%)	2,730	2,860
Target price (average rounded)	**2,570**	**2,450**
Implied upside to target price	5.0%	NA
Rating	**Hold**	**Hold**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity valuation	GBP m
Cost of debt		**+ DCF value**	**14,590**
Pre-tax cost of debt	3.3%	+ ST marketable assets	0
Marginal tax rate	11.0%	+ Value of associates	0
Cost of equity		+ Other assets	0
Risk-free rate (previously 1.83%)	2.0%	**EV (asset side)**	**14,590**
Equity risk	4.0%	- Net debt (+ if net cash)	(6,378)
Additional risk	0.00	- Quasi debt (pension)	(613)
Beta (vs 0.75)	**0.71**	- Value of minorities	0
Debt - 53%	2.9%	Total non-equity claims	(6,992)
Equity - 47%	4.9%	Value of Equity	7,598
Cost of capital	3.9%	**Value per share (p)**	**3,190**

Source: HSBC estimates

SOP valuation

	GBPm	EV RCV	GBPm
2021e RCV	9,730	Net debt	6,598
Value creation	611	Market cap	5,860
Total	10,478	Less non reg	(624)
Business Services	624	Market implied utility RCV	11,834
EV	11,100	RCV	9,730
Other assets	0	RCV premium	21.6%
Net debt 2021e, pensions & minority	(6,598)		
Total estimated equity value	3,899		
Equity value per share (p)	1,637		

Source: HSBC estimates

Upside risks

Severn Trent delivers additional operational total expenditure (totex) and ODI savings, driving higher EPS for FY 2020/21; property disposals above Severn Trent's GBP100m commitment; and growth in its Business Services division above our assumption.

Downside risks

Severn Trent faces higher costs than we assume, driving lower EPS for 2020/21; it may need to take remedial efforts to strengthen its balance sheet towards the end of the five-year period, which would be dilutive to shareholders.

Financials & valuation: Severn Trent

Hold

Financial statements

Year to	03/2020a	03/2021e	03/2022e	03/2023e
Profit & loss summary (GBPm)				
Revenue	1,741	1,786	1,797	1,904
EBITDA	908	860	940	1,041
Depreciation & amortisation	-367	-385	-392	-416
Operating profit/EBIT	541	476	548	625
Net interest	-206	-187	-198	-205
PBT	284	279	352	422
HSBC PBT	284	279	352	422
Taxation	-152	-55	-69	-83
Net profit	132	251	313	371
HSBC net profit	132	251	313	371
Cash flow summary (GBPm)				
Cash flow from operations	865	776	692	745
Capex	-804	-577	-614	-644
Cash flow from investment	-802	-633	-669	-699
Dividends	-228	-239	-243	-249
Change in net debt	371	154	220	203
FCF equity	61	198	78	101
Balance sheet summary (GBPm)				
Intangible fixed assets	245	245	245	245
Tangible fixed assets	9,581	9,774	9,995	10,223
Current assets	760	832	819	864
Cash & others	49	49	49	49
Total assets	10,780	11,100	11,364	11,693
Operating liabilities	1,925	1,939	1,943	1,978
Gross debt	6,433	6,587	6,807	7,010
Net debt	6,224	6,378	6,598	6,801
Shareholders' funds	1,244	1,171	1,212	1,303
Invested capital	8,613	8,863	9,067	9,306

Ratio, growth and per share analysis

Year to	03/2020a	03/2021e	03/2022e	03/2023e
Y-o-y % change				
Revenue	4.3	2.6	0.6	6.0
EBITDA	5.6	-5.2	9.2	10.7
Operating profit	-0.6	-12.0	15.1	14.0
PBT	-22.4	-1.5	26.1	19.9
HSBC EPS	-56.1	91.9	24.2	18.1
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	3.0	4.4	4.9	5.5
ROE	10.9	20.8	26.3	29.5
ROA	2.1	3.7	4.2	4.6
EBITDA margin	52.1	48.2	52.3	54.7
Operating profit margin	31.1	26.7	30.5	32.8
EBITDA/net interest (x)	4.4	4.6	4.8	5.1
Net debt/equity	500.5	544.8	544.9	522.6
Net debt/EBITDA (x)	6.9	7.4	7.0	6.5
CF from operations/net debt	13.9	12.2	10.5	11.0
Per share data (GBPp)				
EPS Rep (diluted)	54.97	105.49	130.98	154.63
HSBC EPS (diluted)	54.97	105.49	130.98	154.63
DPS	100.08	100.58	102.38	104.50
Book value	522.56	491.78	506.77	542.57

Valuation data

Year to	03/2020a	03/2021e	03/2022e	03/2023e
EV/sales	6.9	6.8	6.9	6.6
EV/EBITDA	13.3	14.1	13.1	12.0
EV/IC	1.4	1.4	1.4	1.3
PE*	44.5	23.2	18.7	15.8
PB	4.7	5.0	4.8	4.5
FCF yield (%)	1.1	3.4	1.3	1.7
Dividend yield (%)	4.1	4.1	4.2	4.3

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	03/2020a
GHG emission intensity*	160.8
Energy intensity*	920.9
CO_2 reduction policy	Yes
Social Indicators	**03/2020a**
Employee costs as % of revenues	19.8
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	03/2021a
No. of board members	9
Average board tenure (years)	4.1
Female board members (%)	55.6
Board members independence (%)	66.7

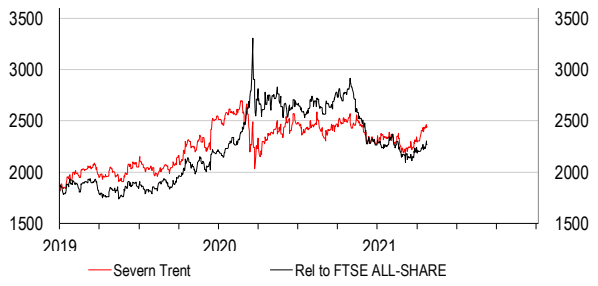
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (GBPp)	2,447	Free float	100%
Target price (GBPp)	2,570	Sector	Water Utilities
RIC (Equity)	SVT.L	Country/Region	United Kingdom
Bloomberg (Equity)	SVT LN	Analyst	Verity Mitchell
Market cap (USDm)	8,093	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 22 Apr 2021

United Utilities

- Trading update: FY21 revenue 3% lower, earnings 10% higher due to lower finance costs, Tallinn sale impact moves to next year
- Technology-driven GBP20m ODI outperformance, still ex-growth – most at risk of bond proxy correlation
- Downgrade to Reduce from Hold and cut TP to 910p from 960p on higher RfR assumption

Investment thesis

It has the highest dividend yield and the lowest Green Recovery list of potential projects compared to its current investment

United Utilities still struggles to avoid its bond proxy status. Of all the water stocks under our coverage it has the highest dividend yield and the lowest Green Recovery list of potential projects compared to its current investment. It continues to bring forward investment to drive ODI performance but management seems to have backtracked on exploring M&A opportunities in UK water despite a significant operational improvement.

Despite UU's significant operational improvements, its asset base is shrinking

Despite UU's significant operational improvements, its asset base is shrinking. Ofwat is looking at the Haweswater Aqueduct Resilience Programme (HARP) project as a blueprint for attracting additional capital for major projects to the sector but it will have to prove convincingly that project finance without government guarantees with the additional cost of finance, lawyers, and cost duplication will deliver better value to shareholders. HARP in particular is a risky project. We remain sceptical that it can be delivered at a lower cost to UU's customers, bearing in mind that Thames Tideway, another significant project (Thames Water), needed a government guarantee.

Trading update for FY21

UU issued a trading update on 25 March 2021. Management expects 3% lower revenue for FY 2020/21. Volumes have recovered in H2, compared to an H1 decline of 5%. Underlying operating profit for FY2020/21 is expected to be lower than in FY2019/20, largely reflecting the lower revenue and an increase in infrastructure renewals expenditure (IRE). The company expects its finance expenses to be cGBP100m lower than last year due to lower inflation applied to the group's index-linked debt. It has now adopted alternative performance measures (APMs) excluding what it says are non-core finance charges such as interest related to pensions. The recovery in H2 has also led to no extra provisions for bad debt, with only GBP17m bad debts aged more than a year. UU updated on its stake sale in Tallinn for EUR100m. The deal is pending regulatory clearance and realisation will move to next year.

Technology-driven GBP20m ODI outperformance

UU reiterated its ODI guidance of GBP20m announced during the capital markets day in early March

United Utilities reiterated its ODI guidance of GBP20m announced during the capital markets day in early March. The rewards are a result of accelerated investments in technology, automation and machine intelligence developed over the last five years. Moreover, UU recorded the lowest ever level of leakage and interruptions to water supply, which more than halved in the last 12 months.

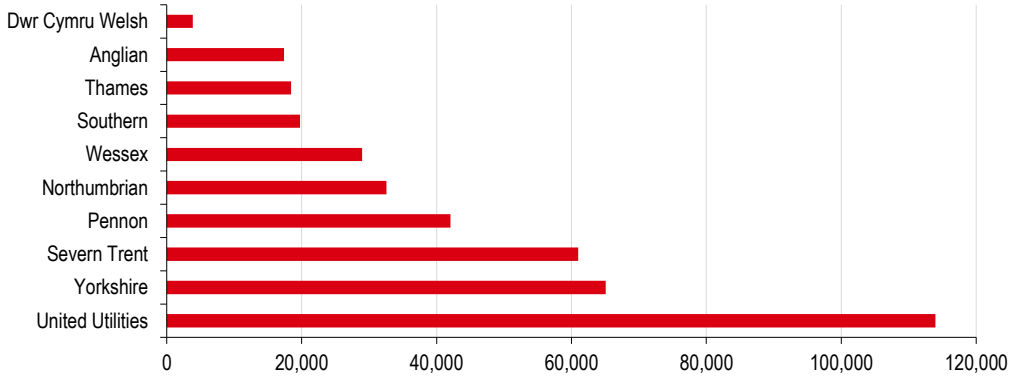
Green Economic Recovery spend

UU has proposed to DEFRA and Ofwat a total of a further GBP135m investment in AMP7 (2020-2025) pending regulatory approval as part of the Green Economic Recovery. Of this GBP135m, GBP119m is enhancement expenditure, which UU is proposing to bring forward from future AMP8 plans into AMP7. The proposal also includes delaying the recovery through customer bills until 2025-2030.

Panorama investigation highlights a continuing weakness in UU's infrastructure

Although the BBC Panorama broadcast on 13 April highlighting UK water companies have been illegally dumping untreated sewage into rivers is arguably investigative journalism of an emotive nature, United Utilities remains a significant outlier. Whether this is from the nature of its Lake District geography or insufficient funding provided in price reviews, it still detracts from its reputation as an environmental company. Unlike Pennon, which has made very public statements about the focus from top management on reducing pollution incidents, UU has said little about this publicly.

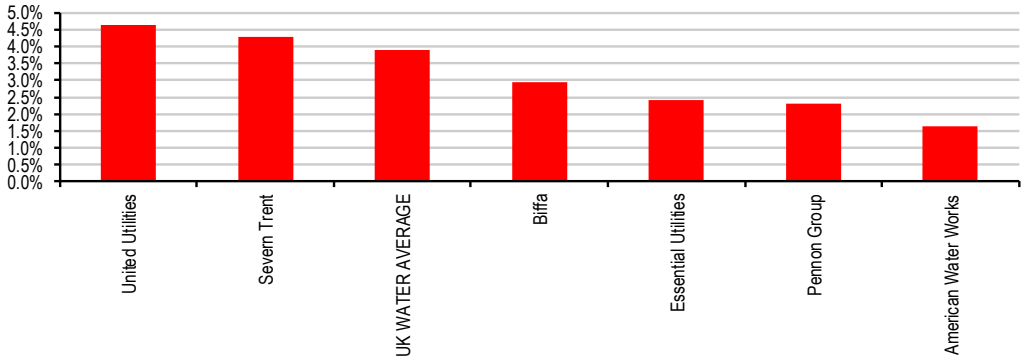
Number of storm water overflows, 2020



Source: Environment Agency

Performance against peers

2022e dividend yield for UK water and waste companies under our coverage



Source: HSBC estimates

Change in estimates

We update our estimates post trading update for FY2020/21.

Change in estimates

GBPm	2021e	2022e	2023e
EBITDA			
Revised	1,017	1,032	1,067
Previous	998	1,018	1,051
Change	*1.9%*	*1.4%*	*1.5%*
EBIT			
Revised	596	603	634
Previous	565	582	612
Change	*5.5%*	*3.7%*	*3.5%*
EPS (new method - pre deferred tax)			
Revised	55.3	56.6	61.3
Previous	45.5	46.5	49.2
Change	*21.6%*	*21.8%*	*24.5%*
DPS			
Revised	42.93	43.70	44.60
Previous	42.87	43.63	44.54
Change	*0.1%*	*0.2%*	*0.1%*

Source: HSBC estimates

Valuation and risks

We value United Utilities shares using three valuation approaches: DCF, dividend yield and sum of the parts. We assign a 50% weight to yield and 25% each to DCF and SOTP, rounded, to arrive at our lower target price of 910p from 960p.

- In our DCF valuation, we revise our RfR to reflect the new HSBC Fixed Income team view of 10-year gilt rates to 50bp from 33bp previously. To this we add a 150bp premium. This increases our RfR to 20% from 1.83% previously. We change our five-year Bloomberg observed beta to 0.73 from 0.75 because of share price movements since our last update in December 2020. We update our DCF estimates to reflect the phasing of capex that UU has brought forward in order to drive more ODI rewards. We increase our terminal value by 10bp to 1.10% because of the additional Green Recovery investment. This together reduces our DCF value to 939p from 1,064p.

- In our yield valuation we have updated our yield assumption to 4.25% from 4.58% based on higher RfR the premium of 2.25% remains unchanged. This reduces our valuation to 971p from 1,098p.
- In our SOP valuation, we assume that UU is able to earn a 4% return on the Green Recovery investment (the same proportion we calculate for our value creation relative to its RCV) which we add to our value creation assumption. This leads to an increase in our SOP valuation to 770p from 751p.

Overall, we reduce our target price to 910p from 960p, implying 6.0% downside from the current share price. We downgrade to Reduce from a Hold rating. We believe as a bond proxy with the most limited scope for Green Recovery of its peers, it is most at risk from rate increases.

Summary of valuation

	New	Previous
Current price on 22-Apr-21	**968**	**NA**
DCF (updated estimates)	939	1,064
Yield 4.25% (vs 4.58%)	971	1,098
SoP (updated estimates)	770	751
Target price (average rounded)	**910**	**950**
Implied downside to target price	-6.0%	NA
Rating	**Reduce**	**Hold**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs	`	Equity valuation	GBP m
Cost of debt		**+ DCF value**	13,870
Pre-tax cost of debt	3.2%	+ ST marketable assets	-
Marginal tax rate	18.0%	+ Value of associates	0
Cost of equity		+ Other assets	0
Risk-free rate (previously 1.83%)	2.0%	**EV (asset side)**	13,870
Equity risk premium	4.0%	- Net debt (+ if net cash)	(7,464)
Additional risk	0.0	- Quasi debt (pension)	0
Beta (previously 0.75)	0.73	- Value of minorities	-
Debt - 56%	2.6%	Total non-equity claims	(7,464)
Equity - 44%	5.0%	Value of Equity	6,406
Cost of capital	3.6%	**Value per share (GBp)**	939

Source: HSBC estimates

SOP valuation

	GBPm	EV RCV	GBPm
2021e RCV	12,073	Net debt	7,497
NPV of spread between achieved return and WACC	518	Market cap	6,635
Total	12,591	Less non-regulated	-
		Market implied utility value	14,132
Extra capex (not included in RCV)	100	Premium	17.1%
United Utilities EV	**12,691**	**Utility equity value**	**671**
Net debt 2021e, pensions & Minority	(7,497)		
Total estimated equity value	5,250		
Equity value per share (p)	**770**		

Source: HSBC estimates

Upside risks

(1) UU may reduce its bad debt provision potentially because better debt management at the end of the furlough scheme having not increased it at the H1; (2) UU delivers operational savings, decreasing its total expenditure (totex) over the five-year period relative to its regulatory allowances and increasing its ODI net rewards; and (3) in the medium term the HARP project is considered not to be achievable on a competitively tendered basis at a lower cost and risk to customers and the investment is then added back to UU's RCV, delivering accelerated growth from 2025 onwards.

Financials & valuation: United Utilities

Reduce

Financial statements

Year to	03/2020a	03/2021e	03/2022e	03/2023e
Profit & loss summary (GBPm)				
Revenue	1,859	1,802	1,793	1,813
EBITDA	1,113	1,017	1,032	1,067
Depreciation & amortisation	-483	-421	-429	-433
Operating profit/EBIT	630	596	603	634
Net interest	-284	-147	-149	-150
PBT	341	439	449	486
Taxation	-235	-70	-72	-78
Net profit	107	373	382	413
Cash flow summary (GBPm)				
Cash flow from operations	810	781	815	851
Capex	-680	-629	-554	-471
Cash flow from investment	-594	-629	-466	-471
Dividends	-285	-290	-293	-298
Change in net debt	294	103	32	-83
FCF pre dividends	130	152	260	381
Balance sheet summary (GBPm)				
Intangible fixed assets	189	189	189	189
Tangible fixed assets	11,511	11,719	11,844	11,882
Current assets	828	872	871	874
Cash & others	528	528	528	528
Total assets	13,290	13,542	13,578	13,619
Operating liabilities	1,240	1,266	1,264	1,268
Financial liabilities	8,507	8,610	8,555	8,472
Total liabilities	11,082	11,215	11,162	11,088
Net debt	7,361	7,464	7,497	7,414
Shareholders' funds	2,962	2,980	3,069	3,184

Ratio, growth and per share analysis

Year to	03/2020a	03/2021e	03/2022e	03/2023e
Y-o-y % change				
Revenue	2.2	-3.1	-0.5	1.1
EBITDA	8.0	-8.6	1.5	3.4
Operating profit	-0.7	-5.5	1.3	5.0
PBT	-20.5	28.5	2.4	8.1
HSBC EPS	-16.8	25.0	2.4	8.1
Ratios (%)				
ROE	10.0	12.5	12.6	13.2
ROCE	1.8	4.4	4.4	4.7
EBITDA margin	59.9	56.4	57.6	58.8
Operating profit margin	33.9	33.1	33.7	35.0
Net debt/equity	248.5	250.4	244.2	232.8
CF from operations/net debt	11.0	10.5	10.9	11.5
Per share data (GBPp)				
EPS reported (diluted)	44.24	54.67	55.98	60.54
HSBC EPS (diluted)	44.24	55.31	56.64	61.25
DPS	42.60	42.93	43.70	44.60
Gross CFPS	1.35	1.17	1.20	1.25

Valuation data

Year to	03/2020a	03/2021e	03/2022e	03/2023e
EV/sales	7.5	7.8	7.9	7.7
EV/EBITDA	12.5	13.8	13.7	13.1
P/CF	7.2	8.3	8.1	7.8
PE*	22.0	17.6	17.2	15.9
FCF yield (pre div) (%)	2.0	2.3	3.9	5.7
Dividend yield (%)	4.4	4.4	4.5	4.6

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	03/2020a
GHG emission intensity*	119.1
Energy intensity*	416.6
CO_2 reduction policy	Yes
Social Indicators	**03/2020a**
Employee costs as % of revenues	15.5
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	03/2021a
No. of board members	11
Average board tenure (years)	6.2
Female board members (%)	27.3
Board members independence (%)	72.7

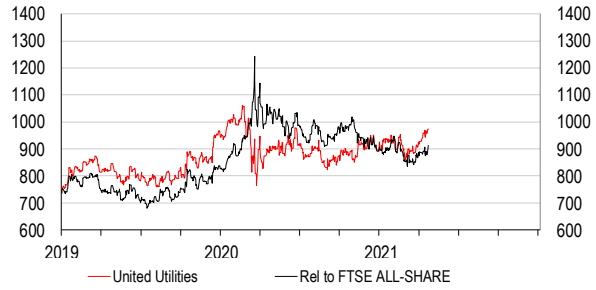
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (GBPp)	968	Free float	100%
Target price (GBPp)	910	Sector	Multi-Utilities
RIC (Equity)	UU.L	Country/Region	United Kingdom
Bloomberg (Equity)	UU/ LN	Analyst	Verity Mitchell
Market cap (USDm)	9,264	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 22 Apr 2021

Disclosure appendix

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Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

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For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

As of 23 April 2021, the distribution of all independent ratings published by HSBC is as follows:

Buy	58%	(29% of these provided with Investment Banking Services)
Hold	34%	(28% of these provided with Investment Banking Services)
Sell	8%	(25% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

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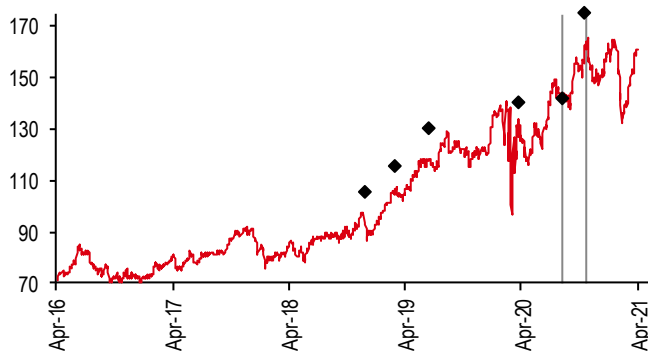
Share price and rating changes for long-term investment opportunities

American Water Works (AWK.N) share price performance USD Vs HSBC rating history



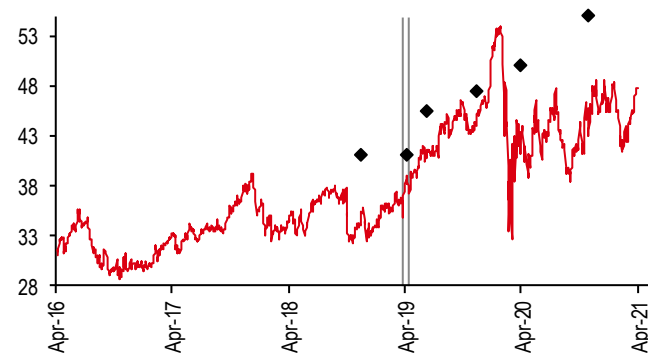
Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Hold	28 Aug 2020	Verity Mitchell
Hold	Buy	09 Nov 2020	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	105.00	17 Dec 2018	Verity Mitchell
Price 2	115.00	22 Mar 2019	Verity Mitchell
Price 3	130.00	08 Jul 2019	Verity Mitchell
Price 4	140.00	14 Apr 2020	Verity Mitchell
Price 5	142.00	28 Aug 2020	Verity Mitchell
Price 6	175.00	09 Nov 2020	Verity Mitchell

Source: HSBC

Essential Utilities (WTRG.N) share price performance USD Vs HSBC rating history



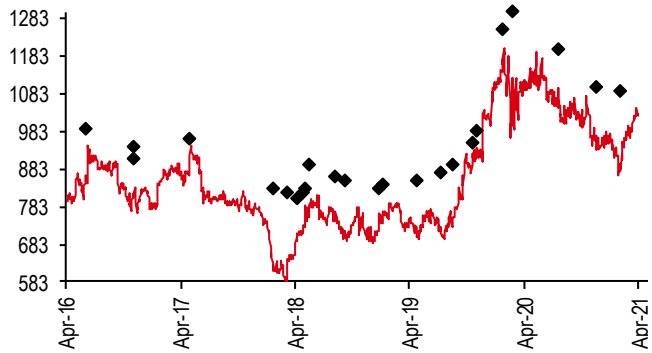
Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	41.00	06 Dec 2018	Verity Mitchell
Price 2	Restricted	15 Apr 2019	
Price 3	41.00	30 Apr 2019	Verity Mitchell
Price 4	45.50	28 Jun 2019	Verity Mitchell
Price 5	47.50	06 Dec 2019	Verity Mitchell
Price 6	50.00	22 Apr 2020	Verity Mitchell
Price 7	55.00	16 Nov 2020	Verity Mitchell

Source: HSBC

Pennon Group (PNN.L) share price performance GBp Vs HSBC rating history



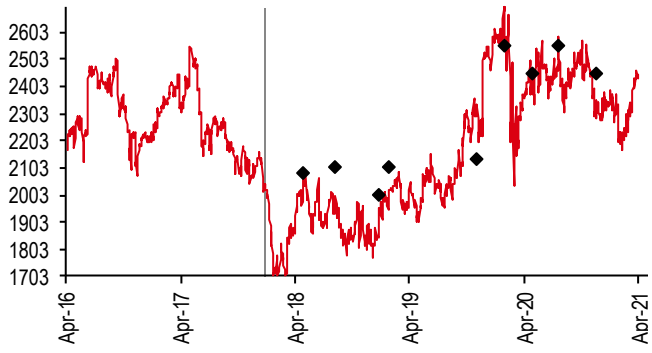
Source: HSBC

Rating & target price history

From	To	Date	Analyst
Overweight	Buy	31 Mar 2015	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	970	17 Apr 2015	Verity Mitchell
Price 2	950	06 Jul 2015	Verity Mitchell
Price 3	915	22 Oct 2015	Verity Mitchell
Price 4	950	15 Jan 2016	Verity Mitchell
Price 5	990	24 Jun 2016	Verity Mitchell
Price 6	910	21 Nov 2016	Verity Mitchell
Price 7	940	25 Nov 2016	Verity Mitchell
Price 8	960	24 May 2017	Verity Mitchell
Price 9	830	12 Feb 2018	Verity Mitchell
Price 10	820	26 Mar 2018	Verity Mitchell
Price 11	800	27 Apr 2018	Verity Mitchell
Price 12	820	17 May 2018	Verity Mitchell
Price 13	830	25 May 2018	Verity Mitchell
Price 14	890	08 Jun 2018	Verity Mitchell
Price 15	860	28 Aug 2018	Verity Mitchell
Price 16	850	28 Sep 2018	Verity Mitchell
Price 17	830	18 Jan 2019	Verity Mitchell
Price 18	840	31 Jan 2019	Verity Mitchell
Price 19	850	20 May 2019	Verity Mitchell
Price 20	870	31 Jul 2019	Verity Mitchell
Price 21	890	10 Sep 2019	Verity Mitchell
Price 22	950	12 Nov 2019	Verity Mitchell
Price 23	980	26 Nov 2019	Verity Mitchell
Price 24	1250	14 Feb 2020	Verity Mitchell
Price 25	1300	20 Mar 2020	Verity Mitchell
Price 26	1200	13 Aug 2020	Verity Mitchell
Price 27	1100	14 Dec 2020	Verity Mitchell
Price 28	1090	23 Feb 2021	Verity Mitchell

Source: HSBC

Severn Trent (SVT.L) share price performance GBp Vs HSBC rating history



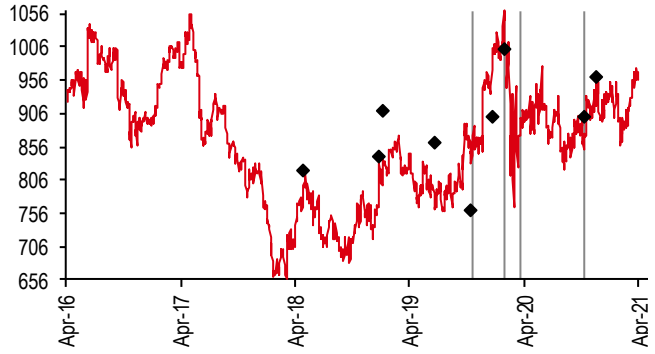
Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Hold	17 Jan 2018	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	2080	17 May 2018	Verity Mitchell
Price 2	2100	28 Aug 2018	Verity Mitchell
Price 3	2000	18 Jan 2019	Verity Mitchell
Price 4	2100	20 Feb 2019	Verity Mitchell
Price 5	2130	25 Nov 2019	Verity Mitchell
Price 6	2550	20 Feb 2020	Verity Mitchell
Price 7	2450	18 May 2020	Verity Mitchell
Price 8	2550	13 Aug 2020	Verity Mitchell
Price 9	2450	14 Dec 2020	Verity Mitchell

Source: HSBC

United Utilities (UU.L) share price performance GBp Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Hold	Reduce	07 Nov 2019	Verity Mitchell
Reduce	Hold	20 Feb 2020	Verity Mitchell
Hold	Buy	08 Apr 2020	Verity Mitchell
Buy	Hold	02 Nov 2020	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	820	17 May 2018	Verity Mitchell
Price 2	840	18 Jan 2019	Verity Mitchell
Price 3	910	01 Feb 2019	Verity Mitchell
Price 4	860	12 Jul 2019	Verity Mitchell
Price 5	760	07 Nov 2019	Verity Mitchell
Price 6	900	15 Jan 2020	Verity Mitchell
Price 7	1000	20 Feb 2020	Verity Mitchell
Price 8	900	02 Nov 2020	Verity Mitchell
Price 9	960	14 Dec 2020	Verity Mitchell

Source: HSBC

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Company	Ticker	Recent price	Price date	Disclosure
AMERICAN WATER WORKS	AWK.N	161.43	22 Apr 2021	6
ESSENTIAL UTILITIES	WTRG.N	47.88	22 Apr 2021	6
PENNON GROUP	PNN.L	10.29	22 Apr 2021	6, 7
SEVERN TRENT	SVT.L	24.47	22 Apr 2021	6, 7
UNITED UTILITIES	UU.L	9.68	22 Apr 2021	1, 4, 5, 6, 7

Source: HSBC

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AQUA AMERICA INC

Aqua America, Inc. is a publicly traded water and wastewater utility holding company with operating subsidiaries serving approximately three million people in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana, and Virginia. It has recently purchased Peoples, a natural gas distribution utility, which will diversify Aqua America's income.

Analyst's Notes

Analysis by Jacob Kilstein, CFA, and Justin Giacobbe, June 4, 2019

ARGUS RATING: BUY

- Raising target by $2 to $43 on relative valuation
- WTR shares trade at 27.1-times our 2019 EPS estimate, below the peer average P/E of 29.5. Our revised target values the stock in line with peers, which makes sense given WTR's above-average profitability.
- We think that Aqua America will continue to provide shareholders with solid risk-adjusted returns as it stands to benefit from an expected investment of more than $700 billion in the nation's water and wastewater infrastructure over the next two decades.
- On May 2, Aqua America reported 1Q19 adjusted income of $50 million, a 2% decline from 1Q18, partly due to higher operating and maintenance expenses. EPS of $0.28 missed our estimate of $0.29 and the consensus of $0.30.
- In October, the company announced that it would acquire Peoples, a natural gas distribution utility, for $4.3 billion in cash. The acquisition will diversify the company away from water distribution and is expected to close mid-2019.

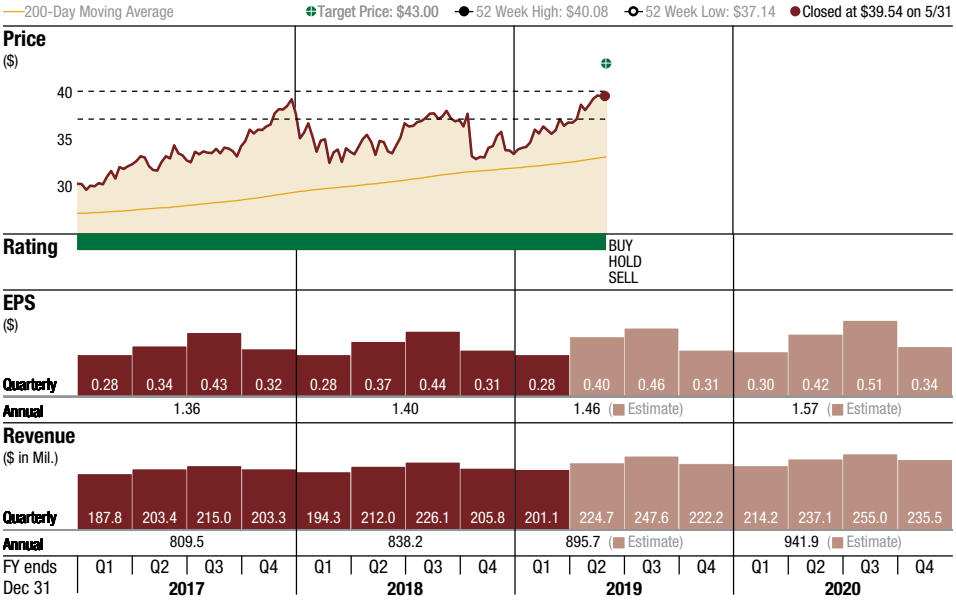
INVESTMENT THESIS

BUY-rated Aqua America Inc. (NYSE: WTR) has a solid business model, a history of steady earnings growth, and a growing dividend. We think the company will continue to provide shareholders with solid risk-adjusted returns as it stands to benefit from an expected investment of more than $700 billion in the nation's water and wastewater infrastructure recommended by the EPA over the next two decades. The company expects to grow its customer base not only through acquisitions but also organically, as it is well positioned in states such as North Carolina and Texas, where population growth is above the national average. The company also benefits from an experienced management team and balanced rate regulation. Lastly, we like the company's consistent earnings and rising dividend. We are increasing our 12-month price target to $43 from $41, which values the stock's P/E in line with its less profitable peers.

RECENT DEVELOPMENTS

Market Data

Pricing reflects previous trading week's closing price.



Argus Recommendations

Twelve Month Rating	SELL	HOLD	**BUY**
Five Year Rating	SELL	HOLD	**BUY**
Sector Rating	**Under Weight**	Market Weight	Over Weight

Argus assigns a 12-month BUY, HOLD, or SELL rating to each stock under coverage.

- BUY-rated stocks are expected to outperform the market (the benchmark S&P 500 Index) on a risk-adjusted basis over the next year.
- HOLD-rated stocks are expected to perform in line with the market.
- SELL-rated stocks are expected to underperform the market on a risk-adjusted basis.

The distribution of ratings across Argus' entire company universe is: 65% Buy, 34% Hold, 1% Sell.

Key Statistics

Key Statistics pricing data reflects previous trading day's closing price. Other applicable data are trailing 12-months unless otherwise specified

Market Overview

Price	**$39.82**
Target Price	**$43.00**
52 Week Price Range	**$32.09 to $40.08**
Shares Outstanding	**215.74 Million**
Dividend	**$0.88**

Sector Overview

Sector	**Utility**
Sector Rating	**UNDER WEIGHT**
Total % of S&P 500 Market Cap.	**3.00%**

Financial Strength

Financial Strength Rating	**MEDIUM**
Debt/Capital Ratio	**56.1%**
Return on Equity	**13.1%**
Net Margin	**18.7%**
Payout Ratio	**0.62**
Current Ratio	**0.37**
Revenue	**$844.88 Million**
After-Tax Income	**$158.07 Million**

Valuation

Current FY P/E	**27.27**
Prior FY P/E	**28.44**
Price/Sales	**10.17**
Price/Book	**3.56**
Book Value/Share	**$11.17**
Market Capitalization	**$8.59 Billion**

Forecasted Growth

1 Year EPS Growth Forecast
4.29%
5 Year EPS Growth Forecast
9.00%
1 Year Dividend Growth Forecast
7.06%

Risk

Beta	**0.62**
Institutional Ownership	**48.14%**

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Analyst's Notes...Continued

WTR shares have outperformed the S&P MidCap 400 over the last quarter, rising 9% compared to a 3% loss for the index. The shares have also outperformed over the past year, rising 13%, compared to a gain of less than 1% for the S&P MidCap 400 and a loss of 6% for the index. WTR shares have a beta of 0.62, in line with peers.

On May 2, Aqua America reported 1Q net income of $17 million or $0.09 per share, compared to $51 million or $0.29 per share in the prior-year period. The decrease was driven by losses on interest rate swaps and expenses related to WTR's acquisition of Peoples, a natural gas distribution utility. Adjusted income fell 2% to $50 million, or $0.28 per share, which missed our estimate of $0.29 and the consensus forecast of $0.30. Revenue rose 4% to $201 million, below our estimate of $202 million but in line with the consensus.

Operations and maintenance expenses rose 7% to $79 million. As such, the operating margin narrowed to 33.5% from 35.7% in 1Q18.

Along with the 1Q earnings release, management reiterated its 2019 EPS guidance of $1.45-$1.50, excluding transaction costs for the Peoples acquisition. Management's guidance assumes total customer growth of 2.0%-3.0%, in line with last year, and $550 million in capital spending. Management expects to spend $1.4 billion on capital projects through 2021.

In October, the company announced that it would acquire Peoples, a natural gas distribution utility, for $4.2 billion in cash, including the assumption of $1.3 billion in debt. Peoples serves about 740,000 customers in Pennsylvania, Kentucky, and West Virginia. The combined company's stock will trade under a new name. Management expects earnings accretion in the first full year after the closing and looks for 7% annual rate base growth in its water business and 8%-10% in natural gas through 2021. The Peoples deal is expected to close in mid-2019. Aqua America's revenue will still be 99% regulated following the acquisition.

WTR expects to spend an additional $50 million on system upgrades over the next 10 years. It expects to add 16,750 customers through the end of 2019 through additional acquisitions.

EARNINGS & GROWTH ANALYSIS

To date in 2019, WTR obtained rate increases or imposed surcharges in Ohio, Illinois and Pennsylvania, providing $5 million in revenue. Pending rate cases in New Jersey, Ohio, and North Carolina are seeking an additional $6 million of revenue.

During 1Q19, the company completed three acquisitions of water and wastewater systems, which added 572 customer connections. WTR financed those acquisitions with debt.

We are maintaining our 2019 EPS estimate of $1.46, which implies 4% growth and assumes higher rates in the company's regulated operations. We are also maintaining our 2020 estimate of $1.57.

We think the company will control costs and improve the

Growth & Valuation Analysis

GROWTH ANALYSIS

($ in Millions, except per share data)	2014	2015	2016	2017	2018
Revenue	780	814	820	810	838
COGS	289	309	305	287	308
Gross Profit	491	505	515	522	530
SG&A	—	—	—	—	—
R&D	—	—	—	—	—
Operating Income	314	321	326	329	323
Interest Expense	76	77	81	88	99
Pretax Income	239	217	255	257	178
Income Taxes	25	15	21	17	-14
Tax Rate (%)	11	7	8	7	—
Net Income	233	202	234	240	192
Diluted Shares Outstanding	178	178	178	178	178
EPS	1.31	1.14	1.32	1.35	1.08
Dividend	0.63	0.69	0.74	0.79	0.85
GROWTH RATES (%)					
Revenue	2.4	4.4	0.7	-1.3	3.5
Operating Income	4.2	2.1	3.8	0.2	-3.2
Net Income	5.4	-13.5	16.1	2.4	-19.9
EPS	4.3	-5.0	15.8	2.3	-20.0
Dividend	8.6	8.2	7.7	7.2	7.0
Sustainable Growth Rate	6.9	6.6	4.7	5.2	5.1
VALUATION ANALYSIS					
Price: High	$28.22	$31.09	$35.83	$39.55	$39.38
Price: Low	$22.40	$24.40	$28.03	$29.41	$32.09
Price/Sales: High-Low	6.4 - 5.1	6.8 - 5.3	7.8 - 6.1	8.7 - 6.5	8.4 - 6.8
P/E: High-Low	21.5 - 17.1	27.3 - 21.4	27.1 - 21.2	29.3 - 21.8	36.5 - 29.7
Price/Cash Flow: High-Low	13.8 - 11.0	14.9 - 11.7	16.9 - 13.2	18.1 - 13.5	18.0 - 14.7

Financial & Risk Analysis

FINANCIAL STRENGTH	2016	2017	2018
Cash ($ in Millions)	4	4	4
Working Capital ($ in Millions)	-173	-153	-252
Current Ratio	0.43	0.46	0.37
LT Debt/Equity Ratio (%)	93.9	102.6	119.4
Total Debt/Equity Ratio (%)	103.1	109.7	127.8
RATIOS (%)			
Gross Profit Margin	63.8	65.1	63.2
Operating Margin	40.7	41.2	38.6
Net Margin	28.6	29.6	22.9
Return On Assets	3.9	3.8	2.9
Return On Equity	13.1	12.6	9.7
RISK ANALYSIS			
Cash Cycle (days)	-21.3	-22.0	-33.7
Cash Flow/Cap Ex	1.0	0.8	0.7
Oper. Income/Int. Exp. (ratio)	—	—	—
Payout Ratio	53.8	60.4	58.5

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Analyst's Notes...Continued

efficiency of acquired assets, invest in infrastructure projects, and grow its customer base both organically and through acquisitions. The company plans to invest $550 million in infrastructure in 2019, following subsequent record investments of $478 million in 2017 and $500 million in 2018. WTR will use the funds to replace pipes, enhance water quality, and strengthen service reliability.

FINANCIAL STRENGTH & DIVIDEND

Our financial strength rating for Aqua America is Medium, the midpoint on our five-point scale. Our three main criteria include debt levels, fixed-cost coverage and profitability.

The company's total debt/total capitalization ratio was 57% at the end of 1Q, above the peer average of 55%. EBITDA covered interest expense by a factor of 5.5 in 1Q, below the peer average of 5.7. The 1Q adjusted net margin of 24.6% was well above the peer average of 12.3%. As of May 2, WTR had $4 million in cash and $2.7 billion in debt.

WTR pays a quarterly dividend of $0.219, or $0.876 annually, for a yield of about 2.3%, above the peer average of 1.8%. WTR has grown its dividend at a 7.6% average annual rate over the last five years. It has paid consecutive quarterly dividends for 74 years, and has raised the dividend 28 times in the past 27 years. Our 2019 dividend estimate is $0.91 per share and our 2020 estimate is $0.99.

MANAGEMENT & RISKS

Christopher Franklin has been CEO since July 2015. Mr. Franklin is a 25-year veteran of the company, and previously served as president and chief operating officer of its regulated operations.

The U.S. water industry is fragmented, with more than 53,000 individual water systems. Many of these systems cannot afford to meet the EPA's increasingly stringent standards, and have put themselves up for sale. In fact, several companies have sought to be acquired by Aqua America. The range of acquisition targets has also grown as cash-strapped municipalities look to monetize their utility assets. We believe that WTR will be able to acquire additional municipal water systems in the coming years at attractive prices.

Key risks for water utilities include the effect of adverse weather on revenues, regulatory issues (especially related to construction cost recovery), and potential environmental and safety-related liabilities. In addition, the utility's heavy capital needs create ongoing liquidity risk.

COMPANY DESCRIPTION

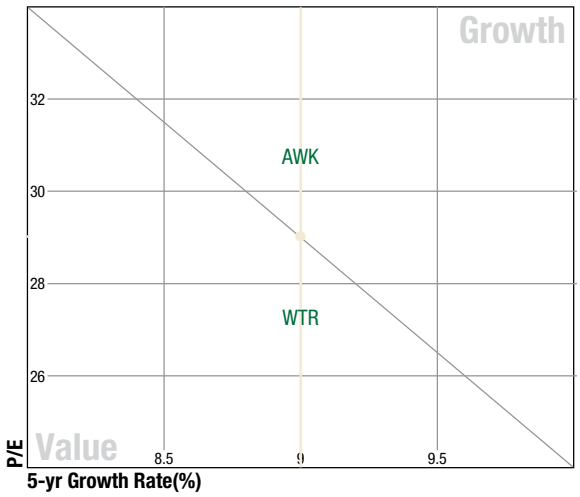
Aqua America, Inc. is a publicly traded water and wastewater utility holding company with operating subsidiaries serving approximately three million people in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana, and Virginia. It has recently purchased Peoples, a natural gas distribution utility, which will diversify Aqua America's income.

VALUATION

Peer & Industry Analysis

The graphics in this section are designed to allow investors to compare WTR versus its industry peers, the broader sector, and the market as a whole, as defined by the Argus Universe of Coverage.

- **The scatterplot shows how WTR stacks up versus its peers on two key characteristics: long-term growth and value. In general, companies in the lower left-hand corner are more value-oriented, while those in the upper right-hand corner are more growth-oriented.**
- **The table builds on the scatterplot by displaying more financial information.**
- **The bar charts on the right take the analysis two steps further, by broadening the comparison groups into the sector level and the market as a whole. This tool is designed to help investors understand how WTR might fit into or modify a diversified portfolio.**



Ticker	Company	Market Cap ($ in Millions)	5-yr Growth Rate (%)	Current FY P/E	Net Margin (%)	1-yr EPS Growth (%)	Argus Rating
AWK	American Water Works Co. Inc.	20,547	9.0	30.8	16.4	7.0	BUY
WTR	Aqua America Inc.	8,591	9.0	27.3	18.7	7.5	BUY
Peer Average		**14,569**	**9.0**	**29.0**	**17.6**	**7.3**	

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Analyst's Notes...Continued

WTR shares appear attractively valued at current prices near $39. Over the past 52 weeks, the shares have traded between $32 and $40.

WTR shares are trading at a discount to peers on a P/E basis, but at a premium based on price/book and price/sales, which we feel is justified by the company's solid long-term fundamentals. The shares trade at 27.1-times our 2019 EPS estimate which is below the peer average of 29.5. In our view, the company's financial strength, favorable risk profile, visible forward earnings stream and attractive integrated structure make WTR a compelling investment. We are increasing our 12-month price target to $43, which values the stock's P/E in line with less profitable peers.

On June 4, BUY-rated WTR closed at $39.82, down $0.22.

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About Argus

Argus Research, founded by Economist Harold Dorsey in 1934, has built a top-down, fundamental system that is used by Argus analysts. This six-point system includes Industry Analysis, Growth Analysis, Financial Strength Analysis, Management Assessment, Risk Analysis and Valuation Analysis.

Utilizing forecasts from Argus' Economist, the Industry Analysis identifies industries expected to perform well over the next one-to-two years.

The Growth Analysis generates proprietary estimates for companies under coverage.

In the Financial Strength Analysis, analysts study ratios to understand profitability, liquidity and capital structure.

During the Management Assessment, analysts meet with and familiarize themselves with the processes of corporate management teams.

Quantitative trends and qualitative threats are assessed under the Risk Analysis.

And finally, Argus' Valuation Analysis model integrates a historical ratio matrix, discounted cash flow modeling, and peer comparison.

THE ARGUS RESEARCH RATING SYSTEM

Argus uses three ratings for stocks: BUY, HOLD, and SELL. Stocks are rated relative to a benchmark, the S&P 500.

- A BUY-rated stock is expected to outperform the S&P 500 on a risk-adjusted basis over a 12-month period. To make this determination, Argus Analysts set target prices, use beta as the measure of risk, and compare expected risk-adjusted stock returns to the S&P 500 forecasts set by the Argus Market Strategist.
- A HOLD-rated stock is expected to perform in line with the S&P 500.
- A SELL-rated stock is expected to underperform the S&P 500.

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ESSENTIAL UTILITIES INC

Essential Utilities Inc., formerly Aqua America, Inc. is a publicly traded water and wastewater utility holding company with operating subsidiaries serving approximately five million people in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana, Kentucky, West Virginia and Virginia. In addition to its water/wastewater utilities, the company purchased the Peoples natural gas distribution utility in March 2020. The combined company has roughly 2,000 employees.

Analyst's Notes

Analysis by Angus Kelleher-Ferguson, June 18, 2021

ARGUS RATING: BUY

- Reiterating BUY and $55 price target
- Essential Utilities recently reported first-quarter results that exceeded analyst's expectations. On May 6, the company reported GAAP and non-GAAP EPS of $0.72 per share, up from non-GAAP EPS of $0.60 in 1Q20. The stronger results reflected contributions from Peoples, the natural gas utility that was acquired in March 2020.
- We are maintaining our 2021 EPS forecast of $1.68 from $1.66, implying 6% growth this year. We are maintaining our 2021 EPS forecast of $1.68. We look for continued gains in 2022 and are also reiterating our estimate of $1.80 per share, which assumes 7% growth from our 2021 forecast.
- The company has a long record - 75 years - of paying dividends. The current yield is about 2.1%.

INVESTMENT THESIS

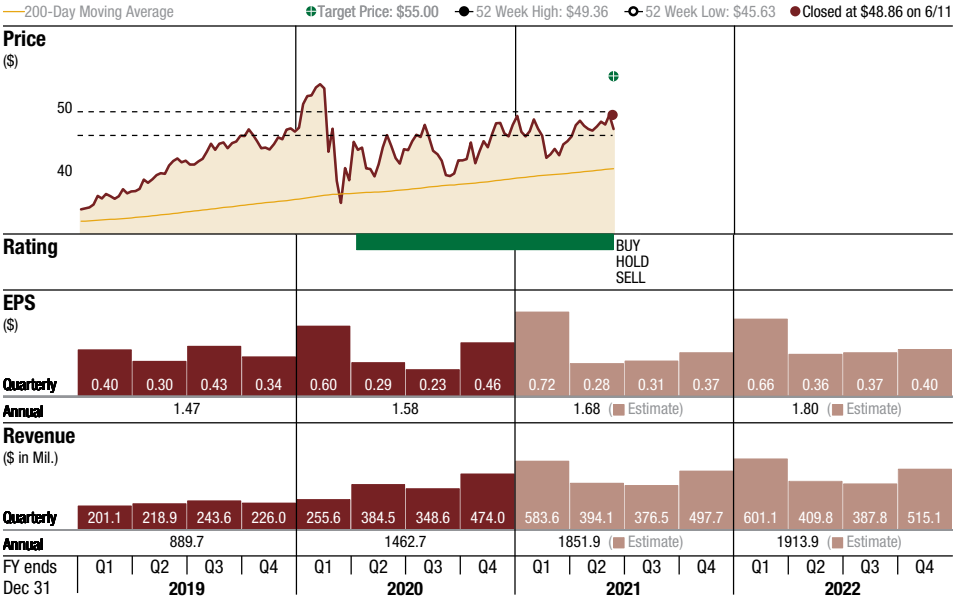
BUY-rated Essential Utilities Inc. (NYSE: WTRG) has a solid business model, a history of steady earnings growth, and a growing dividend. We think the company will continue to provide shareholders with solid risk-adjusted returns. Essential stands to benefit from aging water infrastructure that, according to industry observers, will soon require substantial investment to upgrade to safe levels. We also expect increased revenue and earnings following the March 2020 acquisition of Peoples, a gas distribution utility. We note that Essential has operations in states such as North Carolina and Texas, where population growth is above the national average. The company also benefits from an experienced management team and balanced rate regulation. Our 12-month price target is $55.

RECENT DEVELOPMENTS

WTRG shares have outperformed the S&P over the last three months, climbing 12% while the index has climbed 7%. The stock has underperformed over the past year, however, with a gain of 11% compared to a 35% increase for the market. The shares have roughly matched the performance of the Utility industry ETF IDU over the past year, but

Market Data

Pricing reflects previous trading week's closing price.



Argus Recommendations

Twelve Month Rating	SELL	HOLD	**BUY**
Five Year Rating	SELL	HOLD	**BUY**
Sector Rating	Under Weight	**Market Weight**	Over Weight

Argus assigns a 12-month BUY, HOLD, or SELL rating to each stock under coverage.

- BUY-rated stocks are expected to outperform the market (the benchmark S&P 500 Index) on a risk-adjusted basis over the next year.
- HOLD-rated stocks are expected to perform in line with the market.
- SELL-rated stocks are expected to underperform the market on a risk-adjusted basis.

The distribution of ratings across Argus' entire company universe is: 72% Buy, 28% Hold.

Key Statistics

Key Statistics pricing data reflects previous trading day's closing price. Other applicable data are trailing 12-months unless otherwise specified

Market Overview

Price	**$46.63**
Target Price	**$55.00**
52 Week Price Range	**$38.28 to $49.36**
Shares Outstanding	**245.64 Million**
Dividend	**$1.00**

Sector Overview

Sector	**Utility**
Sector Rating	**MARKET WEIGHT**
Total % of S&P 500 Market Cap.	**2.00%**

Financial Strength

Financial Strength Rating	**MEDIUM**
Debt/Capital Ratio	**55.2%**
Return on Equity	**8.6%**
Net Margin	**23.3%**
Payout Ratio	**0.62**
Current Ratio	**0.63**
Revenue	**$1.79 Billion**
After-Tax Income	**$416.76 Million**

Valuation

Current FY P/E	**27.76**
Prior FY P/E	**29.51**
Price/Sales	**6.40**
Price/Book	**2.38**
Book Value/Share	**$19.58**
Market Capitalization	**$11.45 Billion**

Forecasted Growth

1 Year EPS Growth Forecast	**6.33%**
5 Year EPS Growth Forecast	**6.00%**
1 Year Dividend Growth Forecast	**7.22%**

Risk

Beta	**1.05**
Institutional Ownership	**72.61%**

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Analyst's Notes...Continued

have outperformed over longer time horizons. The beta on WTRG shares is 0.53.

Essential Utilities recently reported first-quarter results that exceeded analyst's expectations. On May 6, the company reported GAAP and non-GAAP EPS of $0.72 per share, up from non-GAAP EPS of $0.60 in 1Q20. The stronger results reflected contributions from Peoples, the natural gas utility that was acquired in March 2020. Higher volume and favorable rates were secondary drivers, with an increase in Other expenses partially offsetting the strength. Revenue rose 128% to $586 million, with Peoples accounting for substantially all of this growth. Water usage per customer increased a modest 2% year-over-year as customers spent more time at home.

In March 2020, the company closed on the acquisition of Peoples Natural Gas for $4.3 billion in cash, including the assumption of $1.1 billion in debt. (The Canada Pension Plan invested $750 million into the company to help it close the deal.) Peoples serves about 740,000 customers in Pennsylvania, Kentucky, and West Virginia. The deal is partly synergistic, given that Essential was already providing water service to Peoples. Additionally, Peoples and Essential Water are the largest players in their respective industries in Pennsylvania, which is the company's biggest market.

Essential stands to benefit from aging water infrastructure that, according to industry observers, will soon require substantial investment. In August 2020, the American Society of Civil Engineers released a report detailing chronic underinvestment in drinking water and wastewater systems. The report highlighted the difficulties plaguing legacy systems, with many treatment facilities nearing the end of their design lives of 75-100 years. More recently, the $2.3 trillion Biden infrastructure bill earmarked roughly $111 billion over the next ten years to modernize water infrastructure. The bill still has a long way to go, and a size reduction looks increasingly more likely, but it remains a positive in any event. Looking ahead, we expect Essential to benefit from both new investment in water infrastructure and upgrades of existing systems.

Along with the 1Q21 earnings release, management reiterated its 2021 guidance calling for EPS of $1.64-$1.69. Management also stated that it expects compound annual earnings growth of 5%-7% through 2023.

EARNINGS & GROWTH ANALYSIS

The company's top-line growth is driven by acquisitions, organic customer count increases, volume increases, and rate increases. In 1Q21, revenue was up substantially due to inorganic growth from the March 2020 acquisition of Peoples. Excluding the impact of Peoples, revenue rose 4.7%. The growth in organic water utility revenue reflected better rates and higher volume.

We note that 2Q21 earnings will offer an appropriate year-over-year comp, as the Peoples acquisition will be fully annualized.

On growth, the company pursues a blended strategy of growth

Growth & Valuation Analysis

GROWTH ANALYSIS

($ in Millions, except per share data)	2016	2017	2018	2019	2020
Revenue	820	810	838	890	1,463
COGS	297	282	308	333	694
Gross Profit	523	527	530	557	768
SG&A	—	—	—	—	—
R&D	—	—	—	—	—
Operating Income	333	334	323	340	435
Interest Expense	81	88	99	100	183
Pretax Income	255	257	178	212	265
Income Taxes	21	17	-14	-13	-20
Tax Rate (%)	8	7	—	—	—
Net Income	234	240	192	225	285
Diluted Shares Outstanding	178	178	178	216	255
EPS	1.32	1.35	1.08	1.04	1.12
Dividend	0.74	0.79	0.85	0.91	0.97
GROWTH RATES (%)					
Revenue	0.7	-1.3	3.5	6.2	64.4
Operating Income	3.8	0.2	-3.2	5.3	27.8
Net Income	16.1	2.4	-19.9	17.0	26.9
EPS	15.8	2.3	-20.0	-3.7	7.7
Dividend	7.7	7.2	7.0	7.0	7.0
Sustainable Growth Rate	4.7	5.2	5.1	-1.1	0.2
VALUATION ANALYSIS					
Price: High	$35.83	$39.55	$39.38	$47.33	$54.52
Price: Low	$28.03	$29.41	$32.09	$32.70	$30.40
Price/Sales: High-Low	7.8 - 6.1	8.7 - 6.5	8.4 - 6.8	11.5 - 7.9	9.5 - 5.3
P/E: High-Low	27.1 - 21.2	29.3 - 21.8	36.5 - 29.7	45.5 - 31.4	48.7 - 27.1
Price/Cash Flow: High-Low	16.9 - 13.2	18.1 - 13.5	18.0 - 14.7	31.3 - 21.6	25.6 - 14.3

Financial & Risk Analysis

FINANCIAL STRENGTH	2018	2019	2020
Cash ($ in Millions)	4	1,869	5
Working Capital ($ in Millions)	-252	1,692	-224
Current Ratio	0.37	6.23	0.63
LT Debt/Equity Ratio (%)	119.4	76.1	118.8
Total Debt/Equity Ratio (%)	127.8	79.8	123.2
RATIOS (%)			
Gross Profit Margin	63.2	62.6	52.5
Operating Margin	38.6	38.2	29.7
Net Margin	22.9	25.2	19.5
Return On Assets	2.9	2.8	2.5
Return On Equity	9.7	7.6	6.7
RISK ANALYSIS			
Cash Cycle (days)	-33.7	-36.4	-13.9
Cash Flow/Cap Ex	0.7	0.6	0.6
Oper. Income/Int. Exp. (ratio)	2.8	2.7	2.4
Payout Ratio	58.5	59.5	120.5

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Analyst's Notes...Continued

through acquisitions and organic growth from its core operations (core ops include its regulated water utility and, more recently, a gas utility.) A key aspect of its acquisition strategy involves purchasing municipal water or wastewater utility assets. As of quarter end, there were seven pending acquisitions underway mixed between water and wastewater. Across the seven pending acquisitions, total purchase price came to $450.5 million and customer count totaled 231,000 dwelling units.

In 2020, Essential posted adjusted EPS of $1.58, up from $1.47 in 2019. Revenue of $1.46 billion rose from $890 million in 2019.

We are maintaining our 2021 EPS forecast of $1.68. We look for continued gains in 2022 and are also reiterating our estimate of $1.80 per share, which assumes 7% growth from our 2021 forecast. Our long-term earnings growth rate forecast is 6%.

FINANCIAL STRENGTH & DIVIDEND

Our financial strength rating for Essential Utilities is Medium, the midpoint on our five-point scale. Our three main criteria are debt levels, fixed-cost coverage, and profitability. Moody's rates the company's debt at Baa2 with a stable outlook and S&P rates it as A.

At the end of the quarter, WTRG had $18 million in cash and cash equivalents, up from $5 million at the end of 2020. The company had $5.8 billion in debt, up from $5.7 billion at the end of 2020. The total debt/total capitalization ratio was 54%, below the peer average of 58%. During the trailing twelve months, the interest coverage ratio was 4.4-times, below the peer average of 6.2. The company has $724 million in borrowing capacity on various credit facilities.

In August 2020, the Essential Utilities board approved a dividend hike. The quarterly cash dividend is now $0.2507, up from $0.2343. The annual distribution of roughly $1.00 yields about 2.1%. WTRG has grown its dividend at a 7% average annual rate over the last five years. It has paid consecutive quarterly dividends for 75 years, and has raised the dividend 30 times in the past 29 years. Our 2021 dividend estimate is $1.04 and our 2022 estimate is $1.12.

MANAGEMENT & RISKS

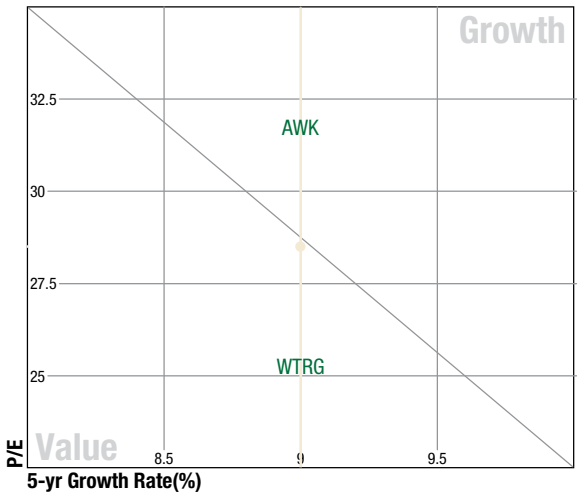
Christopher Franklin has been the company's CEO since July 2015, and is also chairman of the board. Mr. Franklin is a 25-year company veteran, and previously served as president and COO of its regulated operations. The COO is Richard Fox, who has served in the role since 2015, and the CFO is Daniel J. Schuller, who has been in the position since 2018. In August 2020, management announced that Mike Huwar would succeed Joe Gregorini as president of Peoples. Mr. Huwar has more than 30 years of industry experience and an established reputation with Pennsylvania regulators.

The U.S. water industry is fragmented, with more than 53,000 individual water systems. Many of these systems cannot afford to meet the EPA's increasingly stringent standards, and have put

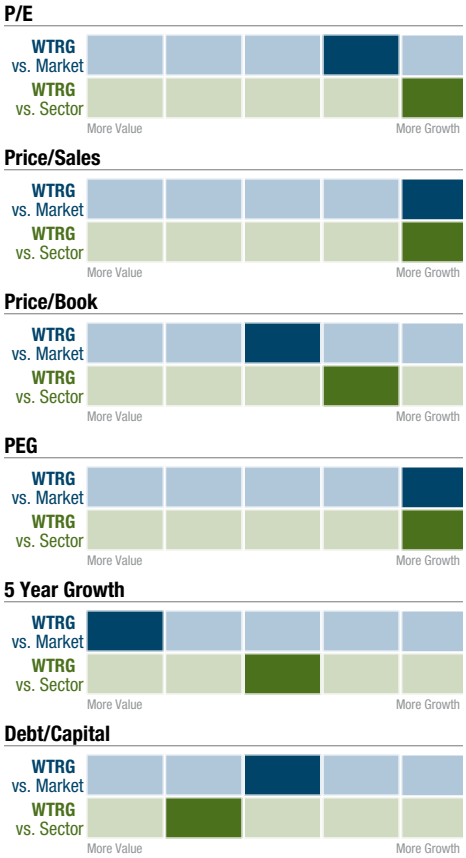
Peer & Industry Analysis

The graphics in this section are designed to allow investors to compare WTRG versus its industry peers, the broader sector, and the market as a whole, as defined by the Argus Universe of Coverage.

- **The scatterplot shows how WTRG stacks up versus its peers on two key characteristics: long-term growth and value. In general, companies in the lower left-hand corner are more value-oriented, while those in the upper right-hand corner are more growth-oriented.**
- **The table builds on the scatterplot by displaying more financial information.**
- **The bar charts on the right take the analysis two steps further, by broadening the comparison groups into the sector level and the market as a whole. This tool is designed to help investors understand how WTRG might fit into or modify a diversified portfolio.**



Ticker	Company	Market Cap ($ in Millions)	5-yr Growth Rate (%)	Current FY P/E	Net Margin (%)	1-yr EPS Growth (%)	Argus Rating
AWK	American Water Works Co. Inc.	25,104	9.0	31.7	18.8	10.1	BUY
WTRG	Essential Utilities Inc	10,417	9.0	25.3	19.5	7.1	BUY
Peer Average		**17,760**	**9.0**	**28.5**	**19.1**	**8.6**	



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Analyst's Notes...Continued

themselves up for sale. Several companies have even sought to be acquired by Essential Utilities. The range of acquisition targets has also grown as cash-strapped municipalities look to monetize their utility assets. We believe that WTRG will be able to acquire additional municipal water systems in the coming years as cities look to raise cash to deal with the impact of the pandemic.

Key risks for water utilities include the effect of adverse weather on revenues, regulatory issues (especially related to construction cost recovery), and potential environmental and safety-related liabilities. In addition, the utility's heavy capital needs create ongoing liquidity risk.

COMPANY DESCRIPTION

Essential Utilities Inc., formerly Aqua America, Inc. is a publicly traded water and wastewater utility holding company with operating subsidiaries serving approximately five million people in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana, Kentucky, West Virginia and Virginia. In addition to its water/wastewater utilities, the company purchased the Peoples natural gas distribution utility in March 2020. The combined company has roughly 2,000 employees.

VALUATION

WTRG shares appear attractively valued at current prices near $49. Over the past 52 weeks, the shares have traded between $38 and $49. WTRG trades at 29.0-times our 2021 EPS estimate and at 27.1-times our 2022 forecast. The shares are trading at premiums to electric and gas distribution peers on P/E, price/sales, and price/book, but in line on PEG, reflecting the company' stronger-than-average growth outlook. Compared to a basket of water utility peers, the shares trade at a discount versus the peer average of 33.2. We believe that premiums to electric utility peers are justified by the company's solid long-term fundamentals, and that WTRG shares should trade closer to the peer average of water utility peers. In our view, the company's financial strength, favorable risk profile, visible forward earnings stream, and attractive integrated structure make WTRG a compelling investment. Our target price is $55, implying a reasonable 2021 PE multiple of 32.7 - still below the water utility peer average.

On June 18, BUY-rated WTRG closed at $46.63, down $2.14.

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About Argus

Argus Research, founded by Economist Harold Dorsey in 1934, has built a top-down, fundamental system that is used by Argus analysts. This six-point system includes Industry Analysis, Growth Analysis, Financial Strength Analysis, Management Assessment, Risk Analysis and Valuation Analysis.

Utilizing forecasts from Argus' Economist, the Industry Analysis identifies industries expected to perform well over the next one-to-two years.

The Growth Analysis generates proprietary estimates for companies under coverage.

In the Financial Strength Analysis, analysts study ratios to understand profitability, liquidity and capital structure.

During the Management Assessment, analysts meet with and familiarize themselves with the processes of corporate management teams.

Quantitative trends and qualitative threats are assessed under the Risk Analysis.

And finally, Argus' Valuation Analysis model integrates a historical ratio matrix, discounted cash flow modeling, and peer comparison.

THE ARGUS RESEARCH RATING SYSTEM

Argus uses three ratings for stocks: BUY, HOLD, and SELL. Stocks are rated relative to a benchmark, the S&P 500.

- A BUY-rated stock is expected to outperform the S&P 500 on a risk-adjusted basis over a 12-month period. To make this determination, Argus Analysts set target prices, use beta as the measure of risk, and compare expected risk-adjusted stock returns to the S&P 500 forecasts set by the Argus Market Strategist.
- A HOLD-rated stock is expected to perform in line with the S&P 500.
- A SELL-rated stock is expected to underperform the S&P 500.

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Analyst's Notes

Analysis by Angus Kelleher-Ferguson, October 13, 2020

ARGUS RATING: BUY

- Reiterating BUY with target of $50
- WTRG shares remain 23% below their all-time high and currently offer investors a favorable entry point.
- In a transformative deal, the company recently acquired Peoples, a natural gas utility, for $4.2 billion in cash. It has also received regulatory approval for rate hikes and infrastructure surcharges in a range of states.
- The company has a long record - 75 years - of paying dividends. The current yield is about 2.4%.

INVESTMENT THESIS

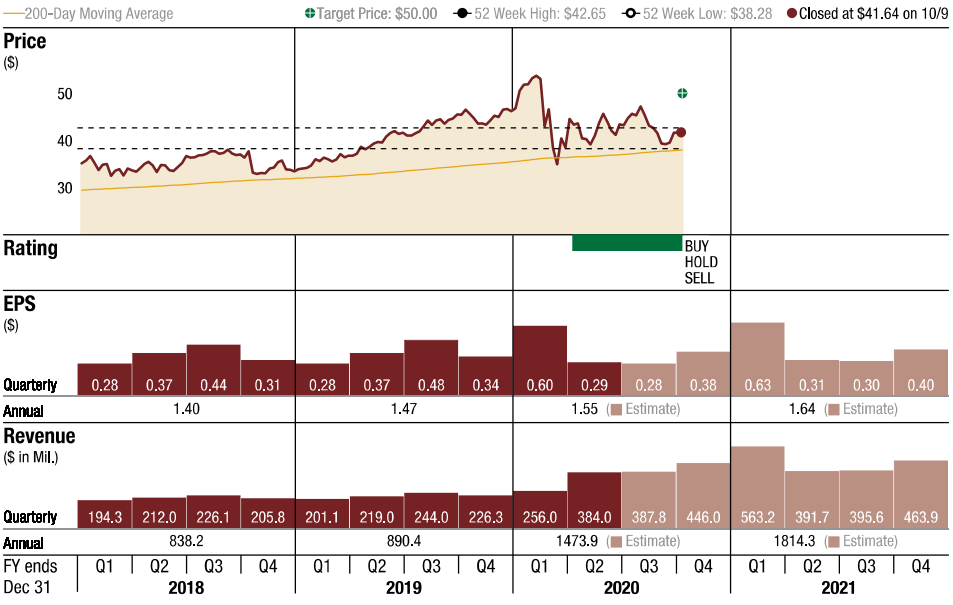
BUY-rated Essential Utilities Inc. (NYSE: WTRG) has a solid business model, a history of steady earnings growth, and a growing dividend. We think the company will continue to provide shareholders with solid risk-adjusted returns. Essential stands to benefit from aging water infrastructure that, according to many industry observers, will soon require substantial investment. In 2019, EPA Chief Andrew Wheeler projected that $700 billion would be needed over the next 20 years to upgrade/overhaul U.S. water infrastructure. Similarly, in August 2020, the American Society of Civil Engineers released a report detailing chronic underinvestment in drinking water & wastewater systems. The report highlighted the difficulties plaguing legacy systems, with many treatment facilities nearing the end of their design lives of 75-100 years. Looking ahead, we expect Essential Utilities to benefit from both new investment in water infrastructure and upgrades of existing systems.

In addition, Essential expects to grow its customer base, helped by operations in states such as North Carolina and Texas, where population growth is above the national average. The company also benefits from an experienced management team and balanced rate regulation. Our 12-month price target is $50.

RECENT DEVELOPMENTS

Market Data

Pricing reflects previous trading week's closing price.



Argus Recommendations

Twelve Month Rating	SELL	HOLD	**BUY**
Five Year Rating	SELL	HOLD	**BUY**
Sector Rating	Under Weight	Market Weight	**Over Weight**

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- BUY-rated stocks are expected to outperform the market (the benchmark S&P 500 Index) on a risk-adjusted basis over the next year.
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- SELL-rated stocks are expected to underperform the market on a risk-adjusted basis.

The distribution of ratings across Argus' entire company universe is: 63% Buy, 36% Hold, 1% Sell.

Key Statistics

Key Statistics pricing data reflects previous trading day's closing price. Other applicable data are trailing 12-months unless otherwise specified

Market Overview

Price	**$42.25**
Target Price	**$50.00**
52 Week Price Range	**$30.40 to $54.52**
Shares Outstanding	**245.15 Million**
Dividend	**$1.00**

Sector Overview

Sector	**Utility**
Sector Rating	**OVER WEIGHT**
Total % of S&P 500 Market Cap.	**3.00%**

Financial Strength

Financial Strength Rating	**MEDIUM**
Debt/Capital Ratio	**44.4%**
Return on Equity	**8.2%**
Net Margin	**25.2%**
Payout Ratio	**0.63**
Current Ratio	**6.31**
Revenue	**$1.11 Billion**
After-Tax Income	**$279.13 Million**

Valuation

Current FY P/E	**27.26**
Prior FY P/E	**28.74**
Price/Sales	**9.33**
Price/Book	**2.23**
Book Value/Share	**$18.91**
Market Capitalization	**$10.36 Billion**

Forecasted Growth

1 Year EPS Growth Forecast	**5.44%**
5 Year EPS Growth Forecast	**9.00%**
1 Year Dividend Growth Forecast	**6.59%**

Risk

Beta	**0.97**
Institutional Ownership	**67.73%**

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Analyst's Notes...Continued

WTRG shares have underperformed the S&P over the last quarter, falling 2% while the S&P 500 has climbed 9%. The stock has also underperformed over the past year, with a decline of 7% compared to a 17% advance for the broad market. The shares have outperformed the Utility industry ETF IDU over the past year. The beta on WTRG shares is 0.47.

On August 5, the company reported 2Q adjusted EPS of $0.29, above the consensus forecast of $0.24 but down from $0.37 in 2Q19. On a GAAP basis, EPS rose to $0.29 from $0.25 in 2Q19. Revenue rose 76% to $384 million, primarily reflecting contributions from Peoples, a natural gas utility acquired in March.

The company acquired Peoples for $4.2 billion in cash, including the assumption of $1.3 billion in debt. Peoples serves about 740,000 customers in Pennsylvania, Kentucky, and West Virginia. During Essential's second-quarter conference call, management announced that Mike Huwar would succeed Joe Gregorini as president of Peoples. Mr. Huwar has over 30 years of industry experience and is well regarded by Pennsylvania regulators.

Along with its 2Q earnings, management reiterated its 2020 guidance calling for adjusted EPS of $1.53-$1.58. The guidance assumes compound annual earnings growth of 5%-7% through 2022, infrastructure investments of $2.8 billion through 2022, and customer growth of 2%-3% per year in the regulated water segment.

EARNINGS & GROWTH ANALYSIS

The company's top-line growth is driven by acquisitions, volume increases and rate increases. In 2Q20, revenue rose significantly due to the Peoples acquisition. Excluding the acquisition, revenue still rose an impressive 9%, reflecting increased residential water usage, partially offset by lower usage from commercial and industrial customers.

On the regulatory front, to date in 2020, Essential's regulated water segment has received approval for higher rates or infrastructure surcharges in Illinois, Indiana, North Carolina, Ohio, Virginia and Pennsylvania. The changes will provide an estimated $10.2 million in additional annualized revenue. The company has additional proceedings pending in Indiana, New Jersey, Virginia and Ohio for its regulated water segment, which could provide another $5.2 million in revenue. Essential's regulated natural gas segment has also received approval for higher rates or infrastructure surcharges in Kentucky and Pennsylvania that will generate approximately $1 million in annualized revenue.

Below the top line, O&M expense rose 49% from 2Q19 due to new Peoples O&M, partially offset by merger-related synergies.

Turning to our estimates, we are maintaining our 2020 non-GAAP EPS estimate of $1.55, near the midpoint of management's guidance range and implying growth of 5% this year. We think the company will control costs and improve the efficiency of acquired assets, invest in infrastructure projects, and grow its customer base both organically and through acquisitions. The company plans to invest $950 million in gas and water

Growth & Valuation Analysis

GROWTH ANALYSIS

($ in Millions, except per share data)	2015	2016	2017	2018	2019
Revenue	814	820	810	838	890
COGS	309	297	282	308	333
Gross Profit	505	523	527	530	557
SG&A	—	—	—	—	—
R&D	—	—	—	—	—
Operating Income	321	333	334	323	340
Interest Expense	77	81	88	99	100
Pretax Income	217	255	257	178	212
Income Taxes	15	21	17	-14	-13
Tax Rate (%)	7	8	7	—	—
Net Income	202	234	240	192	225
Diluted Shares Outstanding	178	178	178	178	216
EPS	1.14	1.32	1.35	1.08	1.04
Dividend	0.69	0.74	0.79	0.85	0.91
GROWTH RATES (%)					
Revenue	4.4	0.7	-1.3	3.5	6.2
Operating Income	2.1	3.8	0.2	-3.2	5.3
Net Income	-13.5	16.1	2.4	-19.9	17.0
EPS	-5.0	15.8	2.3	-20.0	-3.7
Dividend	8.2	7.7	7.2	7.0	7.0
Sustainable Growth Rate	6.6	4.7	5.2	5.1	-1.1
VALUATION ANALYSIS					
Price: High	$31.09	$35.83	$39.55	$39.38	$47.33
Price: Low	$24.40	$28.03	$29.41	$32.09	$32.70
Price/Sales: High-Low	6.8 - 5.3	7.8 - 6.1	8.7 - 6.5	8.4 - 6.8	11.5 - 7.9
P/E: High-Low	27.3 - 21.4	27.1 - 21.2	29.3 - 21.8	36.5 - 29.7	45.5 - 31.4
Price/Cash Flow: High-Low	14.9 - 11.7	16.9 - 13.2	18.1 - 13.5	18.0 - 14.7	31.3 - 21.6

Financial & Risk Analysis

FINANCIAL STRENGTH	2017	2018	2019
Cash ($ in Millions)	4	4	1,869
Working Capital ($ in Millions)	-153	-252	1,694
Current Ratio	0.46	0.37	6.31
LT Debt/Equity Ratio (%)	102.6	119.4	76.1
Total Debt/Equity Ratio (%)	109.7	127.8	79.8
RATIOS (%)			
Gross Profit Margin	65.1	63.2	62.6
Operating Margin	41.2	38.6	38.2
Net Margin	29.6	22.9	25.2
Return On Assets	3.8	2.9	2.8
Return On Equity	12.6	9.7	7.6
RISK ANALYSIS			
Cash Cycle (days)	-22.0	-33.7	-36.4
Cash Flow/Cap Ex	0.8	0.7	0.6
Oper. Income/Int. Exp. (ratio)	3.9	2.8	2.7
Payout Ratio	60.4	58.5	59.5

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Analyst's Notes...Continued

infrastructure in 2020, following investments of $550 million in water infrastructure in 2019. WTRG will use the funds to replace pipes and strengthen service reliability, among other projects. We look for continued growth in 2021 and are maintaining our EPS forecast of $1.64.

FINANCIAL STRENGTH & DIVIDEND

Our financial strength rating for Essential Utilities is Medium, the midpoint on our five-point scale. Our three main financial strength criteria are debt levels, fixed-cost coverage, and profitability. Moody's rates the company's debt at Baa2 with a stable outlook. S&P's rating is A.

WTRG had $7 million in cash and $5.2 billion in debt at the end of 2Q20. The company's total debt/capitalization ratio was 53%. On April 13, the company completed a $1.1 billion public debt offering, with $500 million of 10-year 2.7% notes and $600 million of 30-year 3.3% notes, for a weighted-average maturity of 20.9 years and a weighted-average coupon of 3.0%. On April 14, the company priced $175 million of first mortgage bonds for Aqua Pennsylvania. The proceeds were used to pay off short-term borrowings and to fund an acquisition. As of May 1, after considering the effects of these financings, the company had $1.1 billion in borrowing capacity on various credit facilities.

On August 4, the Essential Utilities board approved a dividend hike. The quarterly cash dividend is now $0.2507, up from $0.2343. The annual distribution of roughly $1.00 yields about 2.4%. WTRG has grown its dividend at a 7% average annual rate over the last five years. It has paid consecutive quarterly dividends for 75 years, and has raised the dividend 30 times in the past 29 years. Our 2020 dividend estimate is $0.97, down from $0.98, and our 2021 estimate is $1.04, up from $1.02.

MANAGEMENT & RISKS

Christopher Franklin has been CEO since July 2015. Mr. Franklin is a 25-year veteran of the company, and previously served as president and COO of its regulated operations. The current COO is Richard Fox, who has served in the role since 2015, and the CFO is Daniel J. Schuller, who has been in the position since 2018.

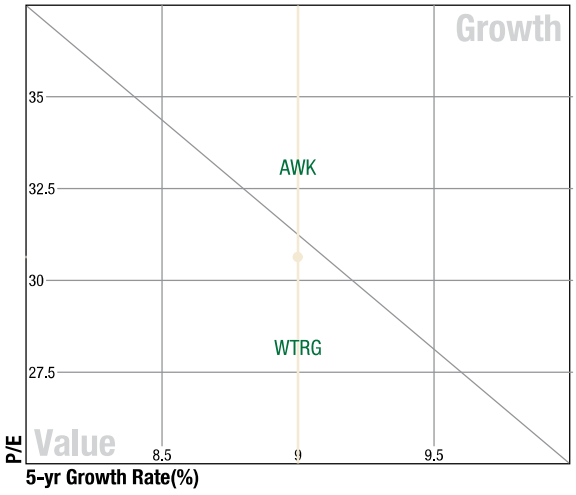
The U.S. water industry is fragmented, with more than 53,000 individual water systems. Many of these systems cannot afford to meet the EPA's increasingly stringent standards, and have put themselves up for sale. Several companies have even sought to be acquired by Essential Utilities. The range of acquisition targets has also grown as cash-strapped municipalities look to monetize their utility assets. We believe that WTRG will be able to acquire additional municipal water systems in the coming years as cities look to raise cash amid rising pandemic-related costs.

Key risks for water utilities include the effect of adverse weather on revenues, regulatory issues (especially related to construction cost recovery), and potential environmental and safety-related liabilities. In addition, the utility's heavy capital needs create

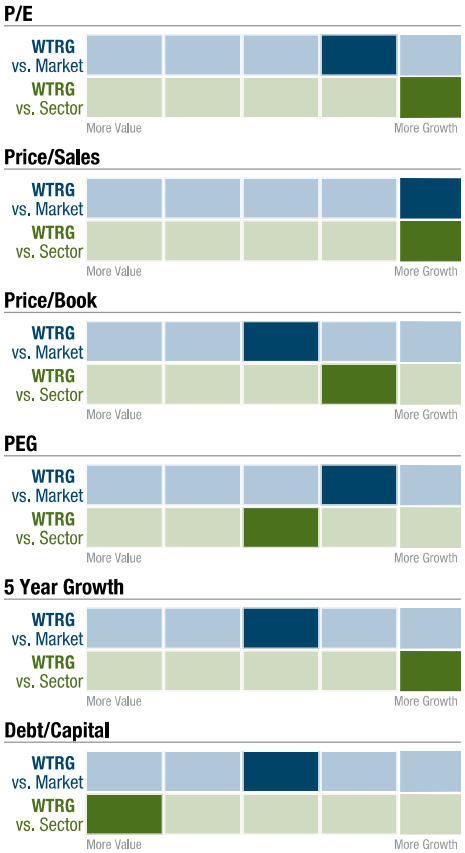
Peer & Industry Analysis

The graphics in this section are designed to allow investors to compare WTRG versus its industry peers, the broader sector, and the market as a whole, as defined by the Argus Universe of Coverage.

- **The scatterplot shows how WTRG stacks up versus its peers on two key characteristics: long-term growth and value. In general, companies in the lower left-hand corner are more value-oriented, while those in the upper right-hand corner are more growth-oriented.**
- **The table builds on the scatterplot by displaying more financial information.**
- **The bar charts on the right take the analysis two steps further, by broadening the comparison groups into the sector level and the market as a whole. This tool is designed to help investors understand how WTRG might fit into or modify a diversified portfolio.**



Ticker	Company	Market Cap ($ in Millions)	5-yr Growth Rate (%)	Current FY P/E	Net Margin (%)	1-yr EPS Growth (%)	Argus Rating
AWK	American Water Works Co. Inc.	23,721	9.0	33.1	17.4	10.1	BUY
WTRG	Essential Utilities Inc	10,703	9.0	28.2	27.5	5.8	BUY
Peer Average		**17,212**	**9.0**	**30.6**	**22.4**	**8.0**	



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Analyst's Notes...Continued

ongoing liquidity risk.

COMPANY DESCRIPTION

Essential Utilities Inc., formerly Aqua America Inc., is a publicly traded water and wastewater utility holding company with operating subsidiaries serving approximately five million people in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana, Kentucky, West Virginia and Virginia. In addition to its water/wastewater utilities, the company purchased a natural gas utility in March 2020. The combined company has roughly 2,000 employees.

VALUATION

WTRG shares appear attractively valued at current prices near $42. Over the past 52 weeks, the shares have traded between $30 and $55. They are currently about 23% below their all-time high.

WTRG shares are trading at a discount to peers on P/E and price/book, but at a premium based on price/sales, which we feel is justified by the company's solid long-term fundamentals. The shares trade at 27.3-times our 2020 EPS estimate, below the peer average of 32.2. In our view, the company's financial strength, favorable risk profile, visible forward earnings stream and attractive integrated structure make WTRG a compelling investment. Our target price is $50.

On October 13 at midday, BUY-rated WTRG traded at $41.99, down $0.26.

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About Argus

Argus Research, founded by Economist Harold Dorsey in 1934, has built a top-down, fundamental system that is used by Argus analysts. This six-point system includes Industry Analysis, Growth Analysis, Financial Strength Analysis, Management Assessment, Risk Analysis and Valuation Analysis.

Utilizing forecasts from Argus' Economist, the Industry Analysis identifies industries expected to perform well over the next one-to-two years.

The Growth Analysis generates proprietary estimates for companies under coverage.

In the Financial Strength Analysis, analysts study ratios to understand profitability, liquidity and capital structure.

During the Management Assessment, analysts meet with and familiarize themselves with the processes of corporate management teams.

Quantitative trends and qualitative threats are assessed under the Risk Analysis.

And finally, Argus' Valuation Analysis model integrates a historical ratio matrix, discounted cash flow modeling, and peer comparison.

THE ARGUS RESEARCH RATING SYSTEM

Argus uses three ratings for stocks: BUY, HOLD, and SELL. Stocks are rated relative to a benchmark, the S&P 500.

- A BUY-rated stock is expected to outperform the S&P 500 on a risk-adjusted basis over a 12-month period. To make this determination, Argus Analysts set target prices, use beta as the measure of risk, and compare expected risk-adjusted stock returns to the S&P 500 forecasts set by the Argus Market Strategist.
- A HOLD-rated stock is expected to perform in line with the S&P 500.
- A SELL-rated stock is expected to underperform the S&P 500.

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February 28, 2020

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	**Outperform/Moderate**
Price:	$46.34
Target Price ($US):	$50.00
Market Cap ($US millions):	$10,002
ADTV (US$ millions):	$67.5

Price as-of Prior Day Close

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2018A	$1.08	-	$838.1	-	42.9x
2019A	$1.00	-	$889.7	-	46.3x
2020E*	$1.10	$1.56	$1,384	$1,871	42.2x
2021E	$1.65	$1.70	$1,662	$2,086	28.0x

FYE 12/30; Revenue in USD millions.

*Assumes 3/16/2020 closing for Peoples acquisition.

Source: Capital IQ, B&S Estimates

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Analyst Day Highlights: 2020 guidance just OK, but M&A, three-year growth targets affirm thesis.

Essential Utilities hosted an analyst day at the NYSE, the company's first high-profile public appearance since receiving key PA regulatory approval for the impending acquisition of Peoples Gas. Major topics included the Peoples transaction (reaffirmation of strategic rationale and progress update), municipal acquisition pipeline, 4Q19 earnings, and forward guidance and growth targets. Overall, we came away reinforced in our favorable view of the fundamental story.

With the critical Pennsylvania regulatory approval now secured, the acquisition of Peoples is set to close on 16 March. The regulatory approval process took longer than expected due to the Goodwin-Tombaugh situation (see prior research), and as a result the first full quarter with Peoples on the P&L will be 2Q20. Still, we continue to view the addition of Peoples, which buttresses Essential's already robust regulatory presence in PA and enhances consolidated rate base growth, as a major strategic differentiator vs. peers.

Essential continues to shine on the municipal deal front not only in absolute terms, but also in terms of moving the needle relative to its size. Notable deals include the purchase of Cheltenham WW for $50 million and the pending acquisition of DELCORA for $276 million, which together with several smaller deals provide a material tailwind to customer growth. We expect Essential to remain highly active on municipal M&A, with deals outside PA likely to accelerate.

Essential issued 2020 EPS guidance of $1.53-$1.58, although given the later than expected Peoples closing, it is on an "illustrative pro forma adjusted" basis (i.e as if Peoples were in for a full 1Q, which it is not). While this means incoming 2020 consensus of $1.56 could come down, the run-rate pro forma guidance reflects the sustainable go-forward earnings power of the combined enterprise.

Essential initiated three-year growth targets for EPS (5%-7%) and rate base (6%-7% for Aqua, 8%-10% for Peoples). We see these as highly credible targets that Essential can achieve without sowing the seeds of longer-term problems in terms of regulatory/OCA relations, ratepayer affordability in acquired territories, and long-term customer growth. Importantly, Essential's long-term growth targets do NOT include acquisitions, which represent potential upside.

We reiterate our Outperform rating for Essential, which we see as a best-of-breed player in the regulated water utility space with notable catalysts. Our price target of $50 reflects a forward P/E multiple of 30.5 times, in-line with the current peer group average.

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Disclosure Appendix

Rating and Price Target History:

Risk Factors

The realization of any or all of the following risk factors, among others, may adversely affect the company's stock price and prevent it from reaching our price target: the economic cycle, concentration in energy sector, foreign currency exposure, and client concentration.

Analyst Certification:

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Boenning & Scattergood has managed a public offering and received compensation from the subject company within the past 12 months.

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Our three-tier investment ratings are based on a stock's return potential relative to a broad market index:

- ***Outperform (Buy):*** The security's total return over the year or longer is expected to exceed the total return of the S&P 500™ over the identical period.
- ***Neutral (Hold):*** The security's total return over the next year or longer is expected to be roughly equivalent to the total return of the S&P 500™ over the identical period.
- ***Underperform (Sell):*** The security's total return over the next year or longer is expected to be less than the total return of the S&P 500™ over the identical period.

Our four-tier risk ratings are based on a mix of price volatility and fundamental factors relative to the market and peer group.

- ***Low:*** The security has higher-than-average fundamental predictability and/or lower-than-average price volatility.
- ***Moderate:*** The security has average fundamental predictability and/or average price volatility.
- ***High:*** The security has lower-than-average fundamental predictability and/or higher-than-average price volatility.
- ***Speculative:*** The security has very inconsistent fundamental predictability and/or very high relative price volatility.

Ratings Distribution (12/31/19):

Coverage Universe (a)	% of Universe
Outperform (Buy)	29%
Neutral (Hold)	58%
Underperform (Sell)	0%
Not Rated	12%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	14%
Neutral (Hold)	21%
Underperform (Sell)	0%
Not Rated	10%

(a) Related to services provided within the past 12 months.

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Aqua America, Inc.

(WTR-NYSE)

June 12, 2019

Water | Environment

Rating/Risk:	Outperform/Low
Price:	$40.58
Target Price:	$43.00

Aqua/Peoples regulatory process enters litigation in PA, but last-minute (non-unanimous) settlement reached; We expect PUC approval despite I&E objection.

Summary: Yesterday, we were in Harrisburg to attend evidentiary hearings for the Aqua/Peoples deal, which entered formal litigation in PA this week due to disagreement among key parties to the case regarding how to deal with certain high-risk gas gathering systems. While the unexpected delay in the regulatory approval process is by no means a positive, yesterday's hearing began with the news that terms of a non-unanimous settlement have been agreed to, with the formal settlement agreement to be filed with the PUC by June 26. We expect the PA PUC to approve the Peoples acquisition, and maintain our Outperform rating for WTR, with our $43 target price based on our proprietary regulation-weighted valuation model (click HERE for rankings and model).

Key Points:

- **PA regulatory approval dragging out, but settlement reached.** The Pennsylvania regulatory approval process for Aqua/Peoples is taking longer than initially expected, with actual litigation beginning with yesterday's hearings in Harrisburg. There appears to be light at the end of the tunnel, however, with parties telling the ALJ yesterday that terms have been reached on a non-unanimous settlement. The proposed timeline calls for a formal settlement agreement filing by June 26, with opposing party briefs due July 11 (the next two PUC Public Meetings are July 11 and August 8). The PUC's Bureau of Investigation and Enforcement (I&E) and the PA Office of the Small Business Advocate (OSBA) are opposing the non-unanimous settlement.
- **Handling of Equitable gas gathering assets the sticking point.** The main issue of contention is how to handle certain gas gathering assets acquired by Peoples as part of the 2013 Equitable deal – specifically the "Goodwin and Tombaugh" system. This gathering system serves roughly 1,600 customers, but has very high leakage rates and is a non-regulated asset that has been the subject of ongoing controversy since the Equitable acquisition (it was noted during yesterday's hearing that Aqua factored this issue into its negotiated purchase price). Fixing the G&T system would cost $122 million (or $75,000 per customer), and the non-unanimous settlement (which includes OCA) would allow Aqua/Peoples single-tariff rate recovery on this investment.
- **I&E opposes settlement, prefers abandonment of G&T system.** As it has since the Peoples/Equitable merger in 2013, I&E continues to strongly oppose allowing the sizable per customer investments to fix G&T into rate base, on the basis that this is not in the public interest and that it would amount to excessive subsidization by existing Peoples customers. Instead, I&E prefers abandoning the G&T system and moving these customers to propane, noting that Peoples CEO Morgan O'Brien has indicated that in some cases abandonment is in the public interest (for his part, O'Brien stressed he said *in some cases*, and this may not be one of those cases). Discussion of rate recovery vs. abandonment of the G&T system dominated yesterday's hearing.
- **PUC approval likely, clearing the way for closing.** We anticipate the PUC approving the non-unanimous settlement despite I&E's opposition. G&T is a problem asset that must be addressed regardless of owner, and the settlement lays out clear plan with a defined timeline (7 years), to be executed by a credible counterparty in Aqua with manageable impact on existing ratepayers (a 1% bill increase). In our view, a PUC rejection of the settlement would represent a de facto endorsement of abandoning the G&T customers, which would be unpopular politically, further tipping the scales toward approval. Of note, I&E lacks the ability to appeal a PUC ruling, so approval by the PUC would likely stand (OSBA can appeal, but rarely does), clearing the way for the Aqua/Peoples deal to close according to the existing "midyear" timetable.

EPS

Current	Q1	Q2	Q3	Q4	FY
2018A	$0.29	$0.37	$0.44	($0.02)	$1.08
2019E*	$0.09	$0.40	$0.50	$0.28	$1.28
Prior	**Q1**	**Q2**	**Q3**	**Q4**	**FY**
2019	$0.09	$0.40	$0.50	$0.28	$1.28
Consensus	**Q1**	**Q2**	**Q3**	**Q4**	**FY**
2018	$0.29	$0.36	$0.43	$0.31	$1.41
2019	$0.30	$0.39	$0.46	$0.32	$1.44
2020	$0.31	$0.42	$0.50	$0.33	$1.56

**1Q represents actual results.*

Revenue	Current	Prior	Consensus
2018A	$838	$838	$847
2019E	$894	$894	$900

Market Data	
Current Price	$40.58
52-Week Range:	$32.09 - $41.51
Market Cap. (M)	$8,755
Shares Out. (M):	215.7
Float Shs. (M):	215.2
Inst. Ownership:	49%
Short Interest (M)	10.4
Avg. Daily Vol. (Shs.Th.):	967.8
ADTV (M):	$39.27
Valuation	
P/E 2019E	31.8x
Capitalization	
Book Value / Share:	$9.37
Net Cash / Shares:	$0.02
Enterprise Value (M):	$11,515.3
Dividend / Share:	$0.88
Dividend Yield:	2.2%

Note: All estimates reflect stand-alone Aqua. We have discontinued stand-alone Aqua estimates for 2020 given our expectation of the Peoples acquisition closing in 2019.

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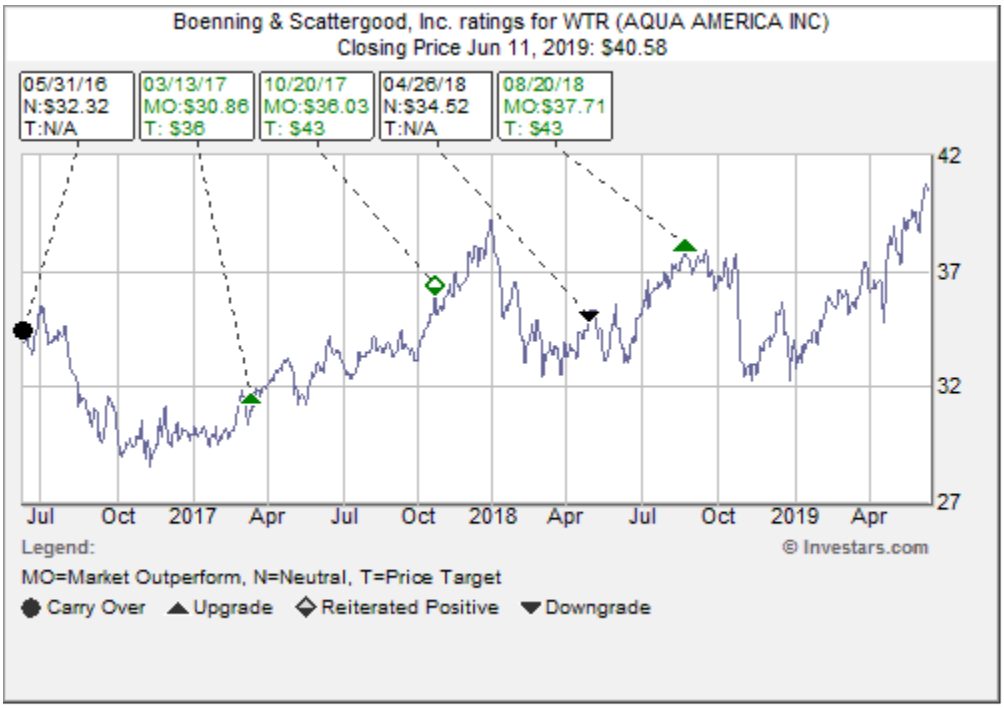
Disclosure Appendix

Rating and Price Target History:



Risk Factors:

The realization of any or all of the following risk factors, among others, may adversely affect the company's stock and prevent it from reaching our target price: regulatory lag; economic regulation; environmental law; water availability; weather; funding; and inputs.

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- ***Neutral (Hold):*** The security's total return over the next year or longer is expected to be roughly equivalent to the total return of the S&P 500™ over the identical period.
- ***Underperform (Sell):*** The security's total return over the next year or longer is expected to be less than the total return of the S&P 500™ over the identical period.

Our four-tier risk ratings are based on a mix of price volatility and fundamental factors relative to the market and peer group:

- ***Low:*** The security has higher-than-average fundamental predictability and/or lower-than-average price volatility.
- ***Moderate:*** The security has average fundamental predictability and/or average price volatility.
- ***High:*** The security has lower-than-average fundamental predictability and/or higher-than-average price volatility.
- ***Speculative:*** The security has very inconsistent fundamental predictability and/or very high relative price volatility.

Ratings Distribution (3/31/19):

Coverage Universe (a)	% of Universe
Outperform (Buy)	43%
Neutral (Hold)	48%
Underperform (Sell)	0%
Not Rated	9%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	13%
Neutral (Hold)	18%
Underperform (Sell)	0%
Not Rated	13%

(a) Total may not add up to 100% due to rounding.
(b) Related to services provided within the past 12 months.

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July 1, 2019

Heads Up

Research Flash Update

Aqua America, Inc.
(WTR/NYSE)

Rating/Risk:	Outperform/Moderate
Price*:	$41.37
Target Price ($US):	$43.00
Market Cap ($US millions):	$8,925
ADTV (US$ millions):	$4.6

Price as-of Prior Day Close

*Target Price and Rating are for 12 months.

EPS	Q1	Q2	Q3	Q4	FY	P/E
2018A	$0.29	$0.37	$0.44	($0.02)	$1.08	38.3x
2019E	$0.09	$0.40	$0.50	$0.28	$1.28	32.4x
2020E	$0.25	$0.41	$0.52	$0.30	$1.49	27.8x

FYE 12/31; Q1-19 represents actual EPS.

Source: Capital IQ, B&S Estimates

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PA-PUC approval of Peoples deal inches closer; Peoples rate case settlement appears imminent.

Last week, Aqua formally filed the non-unanimous settlement agreement with the PA-PUC for its pending acquisition of Peoples Natural Gas, and overall the terms include no major incremental surprises and read favorably from a shareholder perspective.

Notable provisions include:

- A 7-year, $120 million plan to rehabilitate the Goodwin/Tombaugh gas gathering assets, to be recovered via base rates (not DSIC).
- $23 million in rate credits shared across Peoples and Aqua water/WW customers, to be applied by year-end 2019. This is below the $30-$40 million typical in such cases, and keeps the EPS impact within 2019, which is rife with deal-related noise anyway.
- Plans to accelerate replacement of gas distribution pipe within the Peoples system by $30 million a year (which translates into an enhanced rate base growth opportunity).

Based upon statutory timing parameters and precedent, we expect the ALJ to render a proposed decision within 3-4 weeks and for the settlement to come before the PUC for a vote in the September-October timeframe (of note, we believe the potential still exists for a unanimous settlement, which would accelerate this timing).

Separately, evidentiary hearings for the Peoples Gas rate case were abruptly cancelled, suggesting a settlement agreement is imminent. We expect a settlement to be announced in the days/weeks ahead, creating a positive catalyst for WTR shares.

With the Peoples close likely slipping into the fall, visibility on 2020 earnings is likely to remain extremely limited into late 2019. Repair tax treatment is a key variable impacting 2020 expectations, and it remains to be seen how this will affect earnings over the next 12-18 months. Aqua's 2012 adoption of flow-through accounting for repairs on the water side created an immediate and sizable earnings boost, but the company may take a different approach on Peoples.

Overall, WTR remains our top idea in the water utility space due to the combination of discount valuation and fundamental catalysts. We rate WTR shares Outperform, with our $43 target price based on our proprietary regulation-weighted relative valuation model (click HERE for RCI rankings report and valuation model).

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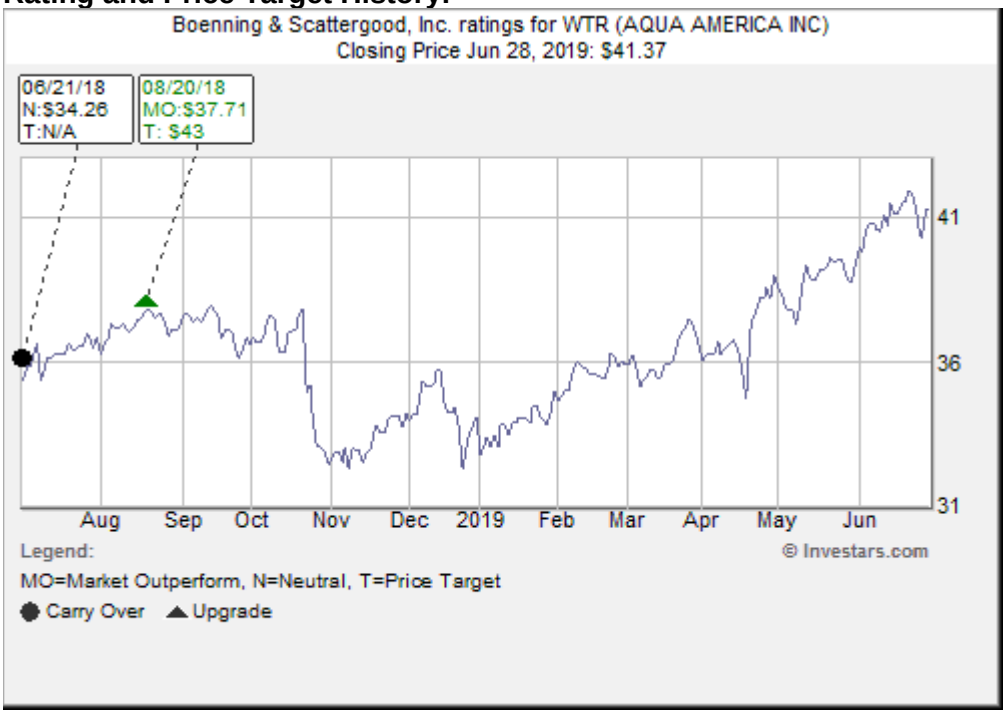

Risk Factors

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Top 10 Ideas: 3Q19

July 24, 2019

A look at our Top Ten picks for 3Q19 and the investment thesis behind each.

- **Aqua America (WTR): Top-flight utility with catalysts, at a discount.** With 85% of revenue coming from the attractive regulatory jurisdictions of Pennsylvania, Ohio, and Illinois, Aqua is well positioned to deliver consistent growth in its core regulated water business. Meanwhile, management is pursuing a compelling strategy of doubling-down on these favorable regulatory areas with the pending acquisition of PA-based gas LDC Peoples. The result is a combination of stable underlying growth and compelling catalysts, with the impending regulatory approval of the Peoples deal likely to drive the stock higher in our view. Like most utilities, Aqua has seen its P/E multiple rise of late, but the stock trades at a ~10% discount to peers (our $43 target price based on our proprietary regulation-weighted relative valuation model (click HERE for RCI rankings report and valuation model). B&S Analyst: Ryan M. Connors.
- **Argo International (ARGO): Strong growth and execution, attractive valuation.** ARGO produced strong operating results in 1Q19, including solid premium growth and improved core loss and expense ratios. Management continues to enhance ARGO's operations via investments in technology and people, and we believe the company's operating performance is poised to further benefit from these investments. We compare ARGO to a peer group of 12 specialty insurers. The peer group is trading at a higher price-to-book multiple than ARGO (1.6x vs. 1.3x), but peers have generated only modestly stronger returns. ARGO's shares have returned 20% since mid-2018 but, relative to expected ROE, the shares still appear undervalued. Our $82 target is 1.4 times our forward BVPS estimate. B&S Analyst: Bob Farnam.
- **Bridge Bancorp (BDGE): A differentiated strategic model in an attractive area.** In a region (Long Island, NY) full of banks with high loan-to-deposit ratios and compressing net interest margins, Bridge Bancorp stands out as a differentiated model with a 91% L/D and expanding NIM. Combined with an attractive footprint, a long runway for above-average organic growth, and the ability to grow tangible book value 10% annually, we believe the risk/reward profile is favorable today, with shares trading at a discount to peers on a P/E basis (10.3x 2019E vs. 11.9x). Our $34 target price incorporates a forward (2020) P/E multiple of approximately 11.3 times. B&S Analyst: Erik Zwick.
- **Ecolab: Margin tailwinds set stage for upward revision cycle.** After battling higher oil-based raw material costs for years, Ecolab is finally seeing the price/cost situation turn in its favor, and we expect margin expansion to drive solid bottom-line growth in 2H19 and into 2020. Ecolab also represents a compelling "offense plus defense" story: top-line growth and margin expansion set the stage for the company to thrive if the economy continues to expand, while the "razor/razor-blade" nature of the company's consumables chemistry business makes the story low-beta to a potential recession scenario over the next 12-18 months. Our $210 target price for ECL reflects an Economic Value Added (EVA) yield of 1.3%, roughly in-line with the water infrastructure peer group average. B&S Analyst: Ryan M. Connors.
- **Employers Holdings (EIG): Compelling pure-play on workers' comp.** Employers booked favorable loss reserve development in each of the last eight quarters and, based on our review of the company's loss reserves at YE18, we believe the company will continue to recognize prior year reserve redundancies near-term. Given ongoing initiatives to improve efficiency and expand distribution capabilities, we also expect the company to gradually grow its top line (despite pricing headwinds) and maintain strong underwriting margins (although initiative-related expenses will be higher in the near-term). Loss trends remain favorable in the workers' compensation market. EIG's shares appear attractively priced trading at 1.1 times adjusted BVPS versus a median of 1.6x for a peer group of other specialty insurers. Our target price of $50 reflects a forward price/adjusted BVPS multiple of 1.25 times. B&S Analyst: Bob Farnam.

Boenning & Scattergood

Top 10 Best Ideas: 3Q19
(In alphabetical order)

Aqua America, Inc.
WTR-$41.12-Outperform; TP: $43.00

Argo Group International
ARGO-$70.30-Outperform; TP: $82.00

Bridge Bancorp
BDGE-$28.58- Outperform; TP: $34.00

Ecolab, Inc.
ECL-$197.24-Outperform; TP: $210.00

Employers Holdings
EIG-$42.84-Outperform; TP: $50.00

Flagstar Bancorp
FBC-$33.17-Outperform; TP: $39.00

Kingstone Companies
KINS-$8.37-Outperform; TP: $13.00

Middlefield Bancorp
MBCN-$41.16-Outperform; TP: $51.50

SB One Bancorp
SBBX-$22.44-Outperform; TP: $28.00

Xylem Inc.
XYL-$80.33-Outperform; TP: $90.00

*In alphabetical order.

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- **Flagstar Bancorp (FBC): Credit hiccup creates buying opportunity.** Flagstar disclosed an isolated credit issue that we expect to result in sizeable losses in 2Q, which partially explains the stock's steep discount. The situation involved a commercial loan to a reverse mortgage lender that declared bankruptcy, which we do not believe is indicative of larger problems with the loan portfolio or underwriting standards. Mortgage revenue comprises ~50% of earnings and given our more optimistic outlook for origination activity via lower market interest rates, we believe there is upside potential to current estimates. FBC trades at 10.5x our 2019 estimate and 132% of tangible book value. Our $39 target is based on a takeout-based valuation and peer multiples using a blend of banks and mortgage lenders. B&S Analyst: Scott Beury.
- **Kingstone (KINS): Solid insurer oversold after modest reserve charge.** Kingstone's shares are down 35% since late April when the company preannounced 1Q catastrophe losses ($0.37/share after tax) and a claims department restructuring/reserve charge ($0.37/share after tax). The stock price has declined 50% YTD, with the P/B multiple contracting to 1.1x from 2.1x – the dividend yield is 4.5% at the current price. We believe the shares have been oversold and think the market has overreacted to the company needing to boost reserves after seeing deteriorating trends in a handful of older liability claims, mostly in the company's small commercial lines book rather than in its core personal lines book. In our view, Kingstone remains one of the industry's top underwriters and we believe the company's long-term story remains intact (although results may continue to be pressured in the near-term until the commercial lines book is cleaned up). Our $13 target is 1.6 times our forward BVPS estimate. B&S Analyst: Bob Farnam.
- **Middlefield Banc Corp. (MBCN): Russell sell-off creates opportunity.** Middlefield was removed from the Russell 2000 index last month, which was preceded by a sustained sell-off in the shares, resulting in a discounted valuation. We believe the company is capable of generating consistent mid-single digit loan growth while maintaining stable credit metrics, and modest margin compression. The stock currently trades at 10x 2019e EPS and 114% of tangible book value, both representing a sizeable discount to peer multiples (11.5x, 155%). We believe this is unwarranted given the company's fundamental trends and expect the stock to drift higher through the remainder of the year. Our $51.50 target price is based on a blended valuation of peer multiples and a discounted acquisition analysis. B&S Analyst: Scott Beury.
- **SB One Bancorp (SBBX): Strong management team, winning culture.** SB One is a $1.9 billion community bank lead by a talented management team with big bank pedigrees. They operate the bank with a pervasive entrepreneurial spirit aimed at enhancing franchise value. We continue to see multiple catalysts for the stock to close the valuation gap with peers, including: 1) successful execution of acquisition-related cost saves, 2) improving profitability, and 3) above-peer organic balance sheet growth. We believe the risk/reward profile is favorable today, with shares trading at a discount to peers on both, P/E (8.9x 2019E vs. 11.9x peers) and P/TBV (1.3x vs. 1.4x peers) basis. Our $28 target price reflects a multiple of 10.2 times our current 2020 EPS estimate. B&S Analyst: Erik Zwick.
- **Xylem (XYL): Secular drivers create long-tailed growth story.** A water sector bellwether, Xylem boasts the water sector's most comprehensive solutions portfolio, offering a wide range of water treatment, transport, test, and metering/AMI solutions for customers in the municipal, industrial, and construction channels. The company has an established track record of organic growth and compelling acquisitions, and recently removed a key tactical risk from the equation by pushing its ambitious long-term operating margin target to the right. Our recent checks suggest Xylem's recent product launches are gaining strong pricing traction, setting up a strong second half for the company. Our $90 target reflects a forward P/E of 24.5x times, in-line with the water infrastructure peer group average. B&S Analyst: Ryan M. Connors.

Disclosure Appendix

Rating and Price Target History:

Note: Please refer to http://www.boenninginc.com/research/disclosures/ for analyst certifications, important disclosures regarding possible conflicts of interest, ratings definitions, ratings distribution, recommendation histories, and other disclosures concerning the recommendations referenced herein. Alternatively, call 800-883-1212 or write to Boenning & Scattergood, Inc. at Four Tower Bridge, 200 Barr-Harbor Drive, West Conshohocken, PA 19428 to the attention of the analyst listed on the front page of this report.

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November 5, 2019

Heads Up

Research Flash Update

Aqua America, Inc.
(WTR/NYSE)

Rating/Risk:	**Outperform/Moderate**
Price:	$43.56
Target Price ($US):	$50.00
Market Cap ($US millions):	$9,829
ADTV (US$ millions):	$39.7

Price as-of Prior Day Close

Target Price and Rating are for 12 months.

EPS	Q1	Q2	Q3	Q4	FY	P/E
2018A	$0.29	$0.37	$0.44	($0.02)	$1.08	40.3x
2019E	$0.09	$0.25	$0.38	$0.24	$0.96	45.2x

FYE 12/31; Q1-Q3 2019 represent actual EPS.

Source: Capital IQ, B&S Estimates

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Third quarter report contains no big surprises; Peoples, DELCORA key growth catalysts.

Aqua America posted 3Q EPS of $0.38, a penny below our estimate of $0.39, as stronger than expected revenue growth was offset by higher O&M expenses. Revenue increased 7.7% year/year in the third quarter, above our model at +5%, with new base rates, organic customer growth, and acquisitions all contributing. O&M expenses rose 19.5% year/year, driven by Peoples-related merger costs and a tough comp (management notes core expense growth was in-line with the historic run-rate).Overall, it was a solid operating quarter for Aqua, with the robust top-line growth encouraging.

The ALJ handling the Aqua/Peoples merger application in PA issued a favorable recommended decision last week, paving the way for the PUC to issue a final ruling (potentially on December 5 or 19). We expect the Peoples acquisition to close in January 2020, providing a notable catalyst for Aqua that will set the company apart from peers. As we've written consistently since Aqua sought to acquire electric transmission utility ITC in 2016 (and again when Eversource (ES-$81.42-Not Rated) acquired water utility Aquarion in 2017), we are big believers in the multi-utility concept. We envision Aqua/Peoples evolving into a powerful regulated infrastructure growth platform once the two companies have been successfully integrated.

In addition, Aqua signed an agreement to acquire DELCORA in 3Q, setting the stage for one of the industry's largest municipal deals in years. DELCORA is a regional WW system serving 500,000 people (or roughly 165,000 connections) in the southwestern Philadelphia suburbs, and Aqua will pay $277 million for the system. Aqua also has an additional 22,600 customers in the near-term acquisition pipeline. Headlined by DELCORA, Aqua continues to execute well on its municipal acquisition program, a key growth driver.

Aqua's combination of organic rate base growth, steady pipeline of municipal deals, and addition of a Pennsylvania gas platform provide a strong mix of fundamental catalysts that we believe set the stage for strong shareholder value generation in the years ahead. WTR shares remain our top idea in the utility space due to a mix of valuation and these fundamental catalysts. We rate WTR shares Outperform, with our $50 target price based on our regulation-driven valuation model and the stock's premium dividend yield.

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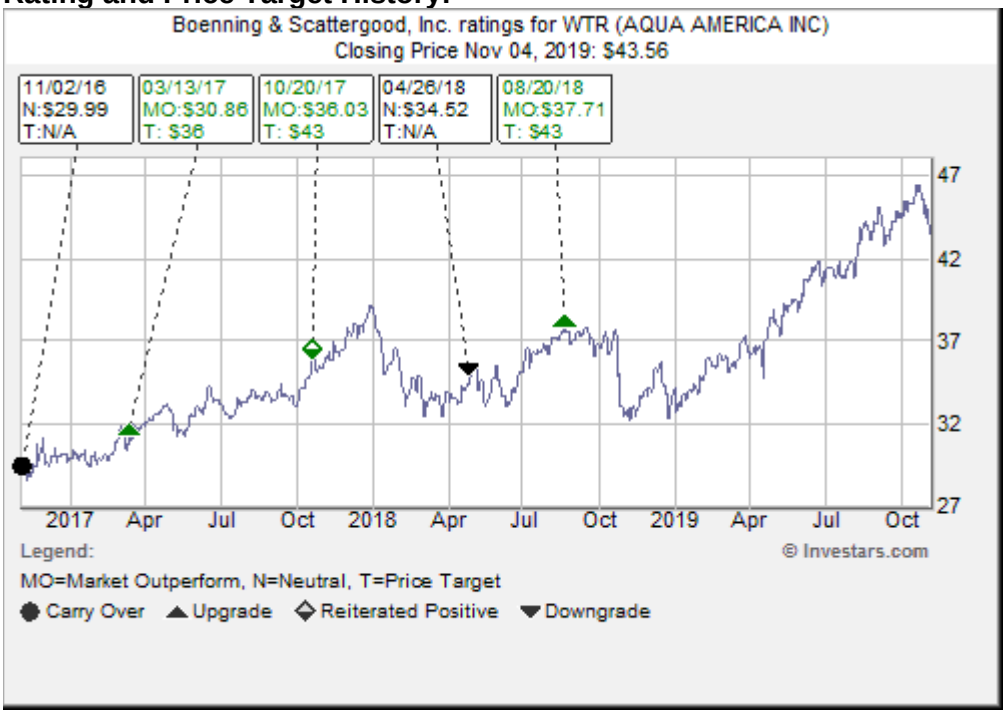

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- ***Underperform (Sell):*** The security's total return over the next year or longer is expected to be less than the total return of the S&P 500™ over the identical period.

Our four-tier risk ratings are based on a mix of price volatility and fundamental factors relative to the market and peer group.

- ***Low:*** The security has higher-than-average fundamental predictability and/or lower-than-average price volatility.
- ***Moderate:*** The security has average fundamental predictability and/or average price volatility.
- ***High:*** The security has lower-than-average fundamental predictability and/or higher-than-average price volatility.
- ***Speculative:*** The security has very inconsistent fundamental predictability and/or very high relative price volatility.

Ratings Distribution (9/30/19):

Coverage Universe (a)	% of Universe
Outperform (Buy)	33%
Neutral (Hold)	56%
Underperform (Sell)	0%
Not Rated	11%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	19%
Neutral (Hold)	20%
Underperform (Sell)	0%
Not Rated	22%

(a) Related to services provided within the past 12 months.

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October 7, 2019

Heads Up

Research Flash Update

Aqua America, Inc.
(WTR/NYSE)

Rating/Risk:	Outperform/Moderate
Price*:	$45.55
Target Price ($US):	$50.00
Market Cap ($US millions):	$9,829
ADTV (US$ millions):	$39.7

Price as-of Prior Day Close

*Target Price and Rating are for 12 months.

EPS	Q1	Q2	Q3	Q4	FY	P/E
2018A	$0.29	$0.37	$0.44	($0.02)	$1.08	42.2x
2019E	$0.09	$0.25	$0.39	$0.22	$0.95	47.9x

FYE 12/31; Q1 and Q2 2019 represent actual EPS.

Source: Capital IQ, B&S Estimates

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PA PUC approves Peoples rate case settlement, but silence deafening on merger application.

Update: Peoples Rate Case (Docket R-2018-3006818):

Last week, the Pennsylvania Public Utilities Commission approved the settlement agreement in the Peoples rate case by a vote of 4-0. The company receives $59.5 million in new revenue, or 63% of the $94.9 million requested, a solid outcome relative to other recent cases. The new rates represent a 9% increase over Peoples' current PA regulated revenue, and will take effect on October 29.

Of note, the PUC ruled in Peoples' favor on the sole remaining issue of contention in the case (the proposed main line extension policy), overriding objections raised by the Office of the Small Business Advocate. We view the Peoples rate case settlement approval as a positive development for Aqua America, as it improves the returns and earnings power of a potential combined Aqua/Peoples entity.

Update: Aqua/Peoples Merger Application (A-2018-3006061):

While the Peoples rate case settlement approval is a clear positive, the Aqua/Peoples 's merger application continues to drag on longer than initially expected. We had expected an ALJ decision to come before the PUC as early as August, so the delay is significant, but it is difficult to interpret what the holdup means.

The "glass half empty" interpretation is that the delay suggests that the ALJ is leaning toward a negative ruling, with the rationale being that a denial of the merger would be highly controversial and therefore require an extremely high level of diligence and detail given the inevitable scrutiny and pushback it would trigger. Upgrade vs. abandonment of the Goodwin/Tombaugh gas gathering system is the key sticking point (see our June 20 note for details).

The "glass half full" read is that the PUC has finite resources, and the Peoples rate case was seen as the more urgent matter to be dealt with first. With the rate case resolved, the PUC will now move ahead with addressing the merger settlement agreement. In our view, the Peoples acquisition remains likely to close by year-end, creating a notable positive catalyst for WTR shares.

WTR remains our top idea in the water utility space due to a mix of discount valuation and fundamental catalysts. We rate WTR shares Outperform, with our $50 target price based on our regulation-driven valuation model and the stock's premium dividend yield.

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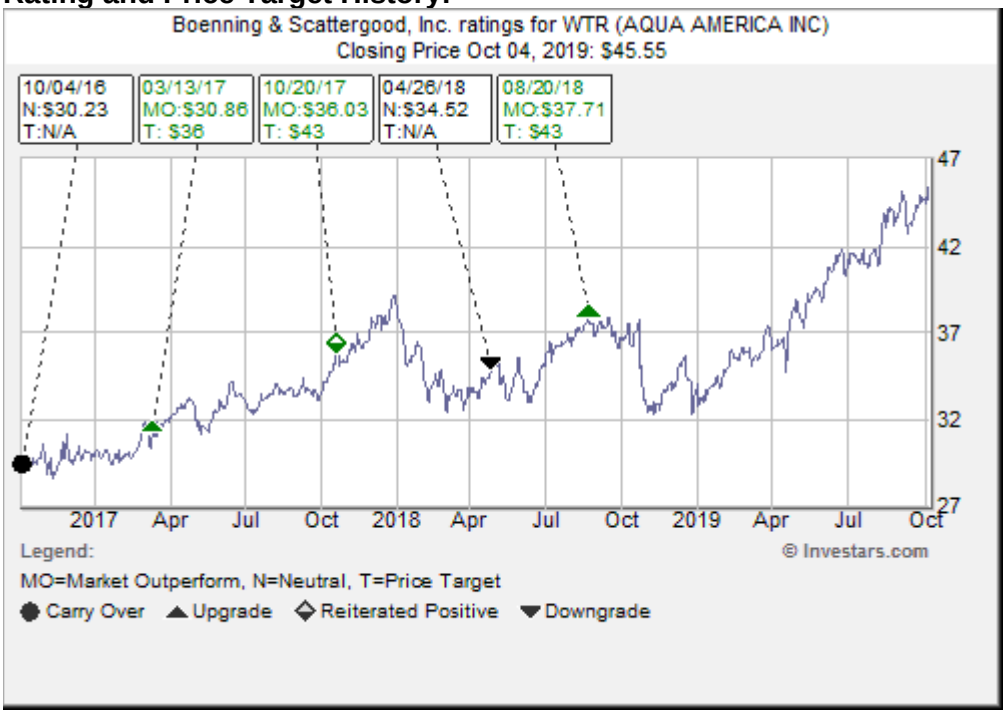

Risk Factors

The realization of any or all of the following risk factors, among others, may adversely affect the company's stock price and prevent it from reaching our price target: the economic cycle, concentration in energy sector, foreign currency exposure, and client concentration.

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- ***Speculative:*** The security has very inconsistent fundamental predictability and/or very high relative price volatility.

Ratings Distribution (6/30/19):

Coverage Universe (a)	% of Universe
Outperform (Buy)	32%
Neutral (Hold)	56%
Underperform (Sell)	0%
Not Rated	13%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	20%
Neutral (Hold)	20%
Underperform (Sell)	0%
Not Rated	20%

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January 14, 2021

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	Outperform/Moderate
Price:	$46.88
Target Price ($US):	$54.00
Market Cap ($US millions):	$11,550
ADTV (US$ millions):	$61.0

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2018A	$1.08	-	$838.1	-	43.4x
2019A	$1.00	-	$889.7	-	46.8x
2020E*	$1.15	$1.59	$1,396	$1,639	40.8x
2021E	$1.68	$1.67	$1,625	$1,819	27.9x

FYE 12/30; Revenue in USD millions.

All historical EPS and B&S EPS estimates GAAP.

*Guidance: $1.53-$1.58 ("adjusted") reflects full year of Peoples.

Source: Capital IQ, B&S Estimates

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Surprise ALJ decision a setback, but DELCORA acquisition remains likely to move forward.

Yesterday, the administrative law judges dealing with Essential/Aqua acquisition of DELCORA issued a proposed decision recommending that the PUC reject the deal. The surprise decision comes just days after the Delaware County of Common Pleas issued a distinctly one-sided ruling in Essential/DELCORA's favor. While the recommended ALJ decision is tactical setback for the transaction, we continue to believe that the deal will ultimately move forward to a 2021 close.

There appear to be three primary points on which the ALJ bases the adverse recommendation, and we believe that all three issues are manageable and will ultimately turn in Essential's favor.

Rate Stabilization Fund. The ALJ decision notes that the novel rate stabilization trust that is part of the DELCORA deal is not included in the PUC application. Since the ultimate ratemaking details stemming from the trust remain to be determined in future rate cases, it is not surprising that this was left out, but this is an easy fix, as there are a number of ways to ensure that ratepayers are made whole.

Local Municipality Protests. The recommended decision also says that protest from some local municipalities is a problem, but sources close to the situation suggest that many are open to settling and on the path to doing so. Based on the players involved, this pushback appears driven in part by local politics/personalities rather than the public interest, a dynamic that will not escape the commission.

Potential DelCo ruling appeal. The ALJ cites "ongoing litigation" as an issue, since Delaware County is believed to be mulling an appeal despite the judge ruling in Aqua's favor. Our read of the DelCo ruling suggests it is very unlikely to be overturned, and there also remains the possibility of a settlement. The bottom-line is that whatever the ALJ says, the DelCo lawsuit has been going Essential's way.

While there have been adverse ALJ recommendations in the past, it is rare for the commission to actually rule against an acquisition between two willing parties. This is particularly the case when the acquirer is a well-known, established, and respected in-state player such as Essential/Aqua. As a result, we believe the DELCORA deal will ultimately move forward despite the ALJ recommendation.

WTRG and its peers have performed respectably on a risk-adjusted basis, but have lagged the broader market (S&P 500 +17% TTM) and the huge gains in the water industrial sector (+33% TTM). We believe that WTRG offers compelling reward/risk, with our $54 target price reflecting a P/E of 32 times, in-line with the peer group.

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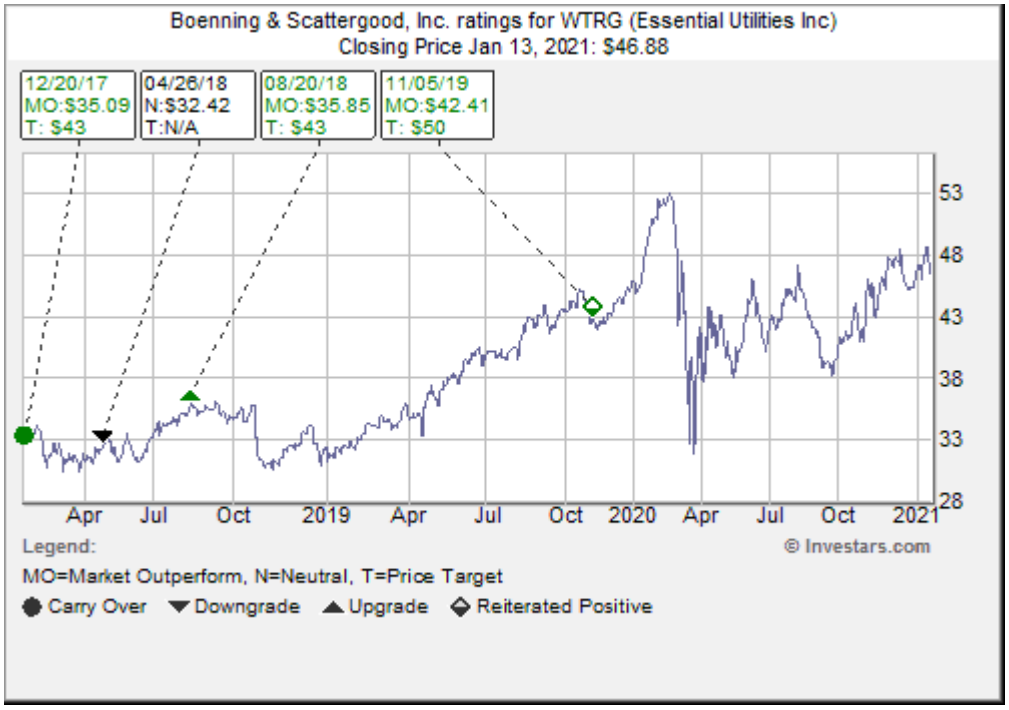

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Ratings Distribution (9/30/20):

Coverage Universe (a)	% of Universe
Outperform (Buy)	32%
Neutral (Hold)	46%
Underperform (Sell)	1%
Not Rated	20%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	21%
Neutral (Hold)	9%
Underperform (Sell)	100%
Not Rated	7%

(a) Related to services provided within the past 12 months.

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February 25, 2021

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	Outperform/Moderate
Price:	$44.09
Target Price ($US):	$54.00
Market Cap ($US millions):	$11,550
ADTV (US$ millions):	$61.0

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2019A	$1.00	-	$889.7	-	44.0x
2020A	$1.12	-	$1,463	-	39.4x
2021E	$1.68	$1.68	$1,877	$1,983	26.3x
2022E	$1.80	$1.81	$1,952	$2,163	24.4x

FYE 12/30; Revenue in USD millions.

All historical EPS and B&S EPS estimates GAAP.

Source: Capital IQ, B&S Estimates

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4Q solid yet anti-climactic after guidance update call; All eyes on PUC as DELCORA ruling looms.

Essential posted 4Q20 EPS of $0.40, up from $0.28 a year ago, with the upside driven by the addition of Peoples and organic growth also contributing. Revenue more than doubled year/year (+109.7%), with Peoples adding $240 million, or 106.4%. Ex-Peoples, revenue rose 3.3% on a combination of higher volumetric sales, rates/surcharges, and acquisitions. Seasonally high purchased gas costs ($93 million, or 20% of sales vs. 7% in 1Q-3Q) pressured margins, with operating margin down 220 bps sequentially to 28%. Of note, one-time credits to gas customers related to the Peoples deal hit EPS by $0.06.

Essential acquired six water/WW systems totaling 12,000 customers for $63 million in 2020, and currently has APAs in place for a further 227,000 in connections. The largest is the $276 million acquisition of DELCORA, which was dealt an adverse ALJ ruling last month. Still, we see the three major issues raised by the ALJ (rate stabilization fund, local municipality protests, and potential appeal of a favorable DelCo Ct. of Common Pleas ruling) ultimately turning in Essential's favor. Essential expects a PA PUC decision by March 2021.

Essential was awarded $21 million in base rates and surcharges in 2020, including in Illinois, Indiana, Kentucky, North Carolina, Ohio, Pennsylvania, and Virginia. Year-to-date, the company has received $8.5 in rates/surcharges across New Jersey, NC, OH, and PA, and has $1.8 million pending in IN and VA. Though not immaterial, this pipeline of rate activity is light by the company's historical standards, which we see as timely. Essential had just completed a number of major rate cases before COVID-19, and therefore does not have to seek major rate hikes during these difficult times for customers.

Essential's fourth quarter report is somewhat of a non-event, as the company stole its own thunder with its January 11 guidance release and conference call. Predictably, management reiterated the 2021 guidance of $1.64-$1.69 issued last month (one wildcard 2021 issue to watch is the EPS impact of the Texas situation). Essential also reiterated its 5%-7% EPS CAGR target through 2023, and we see the company as well positioned to deliver the top growth rate across the regulated water/multi-utility peer group over this timeframe.

WTRG and peers have underperformed notably in recent days due in part to rising inflation concerns, despite the fact that the data show utilities outperform the broader market during inflationary periods (for details, see our industry report today). We believe WTRG shares offer a compelling reward/risk equation, with our $54 target reflecting a P/E of 32 times, in-line with the water utility peer group.

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Ratings Distribution (12/31/20):

Coverage Universe (a)	% of Universe
Outperform (Buy)	38%
Neutral (Hold)	49%
Underperform (Sell)	1%
Not Rated	13%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	22%
Neutral (Hold)	3%
Underperform (Sell)	100%
Not Rated	0%

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May 7, 2020

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	**Outperform/Moderate**
Price:	$40.67
Target Price ($US):	$50.00
Market Cap ($US millions):	$9,965
ADTV (US$ millions):	$30.1

Price as-of Prior Day Close

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2018A	$1.08	-	$838.1	-	37.7x
2019A	$1.00	-	$889.7	-	40.6x
2020E*	$1.10	$1.46	$1,384	$1,655	37.0x
2021E	$1.65	$1.65	$1,662	$1,970	24.6x

FYE 12/30; Revenue in USD millions.

All historical EPS and B&S EPS estimates GAAP.

*Adjusted guidance of $1.53-$1.58 reflects full year of Peoples.

Source: Capital IQ, B&S Estimates

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*

Keep Calm, Carry On: Guidance, growth targets reaffirmed as regulated model shines amid crisis.

Essential Utilities posted 1Q EPS of $0.20, which include two weeks of the Peoples Gas acquisition which closed on March 16 (assuming a full quarter of Peoples, EPS would have been $0.60). In addition to the Peoples deal, Essential filed paperwork with the PUC in 1Q for the acquisition of the DELCORA regional wastewater system, which will be the largest municipal acquisition in the company's 134-year history as well as the biggest ever in the state of Pennsylvania.

In light of the solid first quarter report, Essential reiterated both its indicative (i.e. adjusted to include a full year of Peoples) 2020 EPS guidance of $1.53-$1.58 and its 5%-7% earnings CAGR through 2022. Given the strong organic growth dynamics and active M&A cadence, we believe Essential has the most compelling, sustainable growth story in the regulated environmental utility peer group.

Importantly for the intermediate-term outlook, Essential continues to move forward with its capital improvement program. Maintaining a robust capital investment level is key to sustaining rate base growth, which in turn is key to driving earnings and shareholder value. While affordability is a near-term concern, there is so far no evidence that COVID-19 is leading PUCs to lean on IOUs to cut capex to forestall future rate impacts. We believe that this is in part because regulated utilities provide timely offsetting infrastructure spending/stimulus at a time when state and local governments will be cutting budgets.

Like peers, Essential has suspended shut-offs during the COVID-19 crisis. This industry issue has been cited as a risk in the financial press, including a Wall Street Journal article this week (link HERE) saying households will "prioritize bills causing immediate disruptions to their lives if left unpaid. Cable TV and internet, which can still be cut off, are likely to rank higher on the payment hierarchy than electricity, gas and water". Such views misunderstand/ overstate the collection risks facing IOUs. Bills are being generated and will come due as the crisis stabilizes, and liabilities for basic utility services are unlikely to be forgiven except in cases of true financial hardship.

Essential's solid 1Q, guidance/growth target affirmation, active M&A pipeline, and continued execution on its capital investment program amid the huge COVID-19 economic shock epitomize the resilience of the regulated utility business model. We reiterate our Outperform rating for Essential, which we see as a best-of-breed player in the regulated utility space with notable near-term growth catalysts.

Our price target of $50 reflects a forward P/E multiple of 30.3 times, ~in-line with the current peer group average of 30.2 times.

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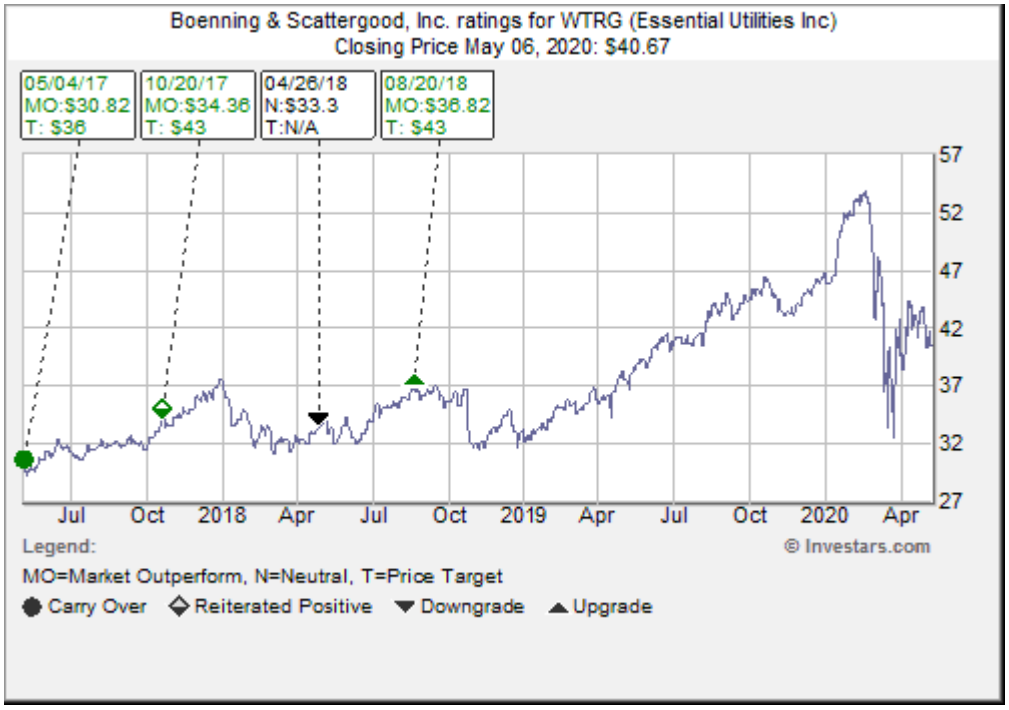
Disclosure Appendix

Rating and Price Target History:



Risk Factors

The realization of any or all of the following risk factors, among others, may adversely affect the company's stock price and prevent it from reaching our price target: the economic cycle, concentration in energy sector, foreign currency exposure, and client concentration.

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Ratings Distribution (3/31/20):

Coverage Universe (a)	% of Universe
Outperform (Buy)	28%
Neutral (Hold)	61%
Underperform (Sell)	0%
Not Rated	11%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	27%
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Essential Utilities, Inc.

(WTRG-NYSE)

June 18, 2020

Water | Environment

Rating/Risk:	Outperform/Low
Price:	$43.14 (intra-day; 1:46pm)
Target Price:	$50.00

County of Delaware vs. DELCORA: Initial hearing suggests acquisition likely to close in 2020 despite shrill rhetoric, legal maneuvering by local officials.

Summary: We attended today's Delaware County Court of Common Pleas hearing in the County of Delaware (aka DelCo) vs. DELCORA, which has major ramifications on whether Essential's acquisition of DELCORA will go forward (and if so under what terms). Contrary to rhetoric from county officials assailing any deal and privatization generally, the county's legal positions focused primarily on the structure of the ratepayer stabilization fund, leaving us with the clear impression that the case is really about who gets the money and not an effort to block the deal altogether. The attorneys agreed on a path forward that includes follow-up hearings in July-August, with hopes to conclude in the fall, and we came away believing the acquisition is likely to close in 2020.

Key Points:

- **County walks back attack on sale, focuses on ratepayer trust.** Told by the judge that he read the initial complaint as an attack on the sale of DELCORA and the ratepayer stabilization fund, DelCo lawyers seemed to backpedal, saying the complaint is meant to attack the trust and that at this time it has no issue with the sale of DELCORA per se. DelCo also seemed to walk back the immediacy of its June 3 ordinance to dissolve DELCORA, saying the authority can only be terminated once key impediments are removed, which could take months. While a lot can still happen, DelCo's legal stance on the Aqua/DELCORA deal appears far less nuclear than recent rhetoric in the local press suggests, substantially increasing the odds of the deal going.
- **DELCORA: County must honor deal even if authority terminated.** DELCORA attorneys made a persuasive argument that while DelCo does have the ability to dissolve the authority, it can only do so after honoring all contracts, which in this case encompasses the sale agreement with Aqua. DelCo's lawyers did not appear to have a ready answer to this, and the issue did not engender much further discussion with the judge, suggesting that public statements from Aqua and DELCORA that the merger agreement and rate stabilization fund are enforceable no matter who owns DELCORA are on solid legal ground. This is key, since it would render draconian press reports on the ramifications of the termination of DELCORA essentially moot.
- **Judge steering parties toward agreeing on modifications to trust.** The judge acknowledged that the structure of the ratepayer stabilization fund, and not DELCORA's sale or termination, is the key issue, noting at one point that "we don't deal with rhetoric in the newspaper, we deal with representations in court". A key point came when, at the judge's prodding, DelCo attorneys said they would be amenable to opening discussions about how to improve upon the structure of the trust. In our view, this was the clearest evidence yet that the county's opposition is really about the money trail rather than the deal itself. We believe Aqua would be open to reasonable modifications of the trust, provided they do not result in a negative financial impact.
- **Deal looks more likely to close, creating positive EPS/stock catalyst.** The key take-away is that the hearing indicated a much less extreme position on the part of DelCo than suggested by recent public meeting comments and quotes in the press. In addition to appearing to back off of attacks on the sale itself and the immediate termination of DELCORA, the county did not raise any concerns regarding the sale process itself. As a result, we now believe the DELCORA deal is likely to close in 2020, giving Essential critical mass to go after additional WW deals in PA and creating a positive earnings tailwind for 2021. We reiterate our Outperform rating for shares of WTRG, with our $50 target price applying a P/E of 30 times, in-line with peers.

EPS	2018A	2019A	2020E	2021E	2022E
Current	$1.08	$1.00	$1.10	$1.65	$1.85
Prior	-	-	$1.10	$1.65	$1.85
Consensus	-	-	$1.38	$1.67	$1.79
Guidance*			$1.53-$1.58		

Revenue	Current	Prior	Consensus
2018A	$838	-	-
2019A	$881	-	-
2020E	$1,488	$1,488	$1,658
2021E	$1,668	$1,668	$1,948
2022E	$1,835	$1,835	$2,098

Market Data	
Current Price*:	$43.14
52-Week Range:	$30.40 - $54.52
Market Cap. (M)	$10,570
Shares Out. (M):	245.0
Float Shs. (M):	244.3
Inst. Ownership:	70%
Short Interest (M)	4.6
Avg. Daily Vol. (Shs.Th.):	383.9
ADTV (M):	$16.6
Valuation (Cons.)	
P/E 2020E	31.3x
P/E 2021E	25.8x
P/E 2022E	24.1x
Capitalization	
Book Value / Share:	$9.37
Net Cash / Shares:	$0.13
Enterprise Value (M):	$15,935.5
Dividend / Share:	$0.94
Dividend Yield:	2.2%

*Price as-of Prior Day Close
Target Price and Rating are for 12 months.
FYE 12/30; Revenue in USD millions.
Historical and B&S EPS estimates U.S. GAAP.
*Adj. 2020 guidance reflects full year of Peoples.
Source: Capital IQ, B&S Estimates

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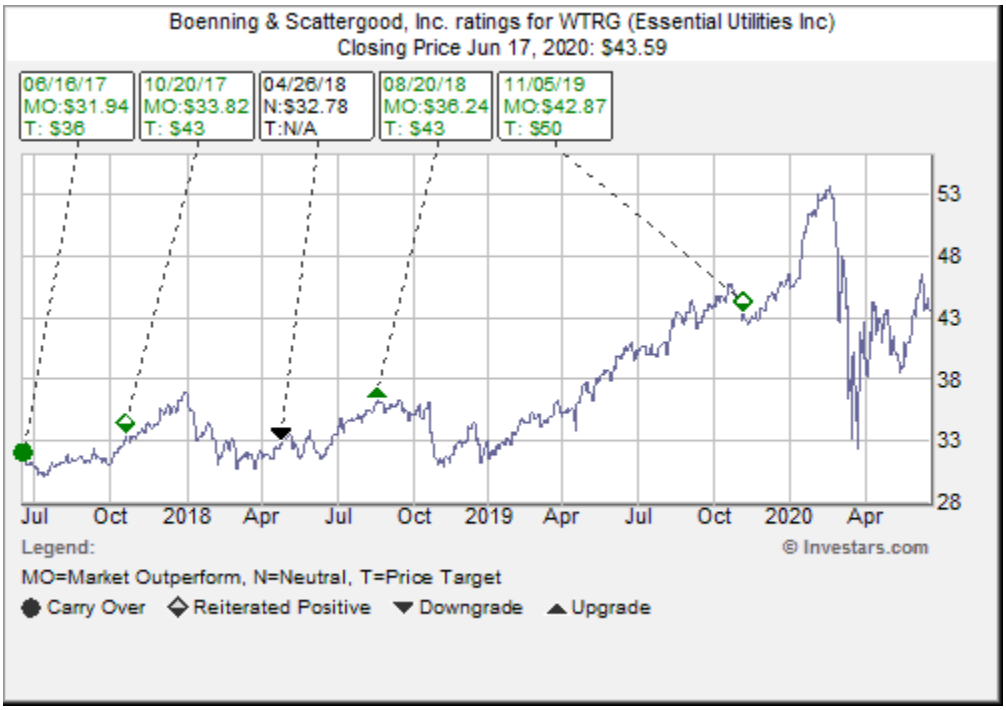

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June 21, 2021

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	Outperform/Low
Price:	$46.63
Target Price ($US):	$54.00
Market Cap ($US millions):	$11,740
ADTV (US$ millions):	$63.0

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2019A	$1.00	-	$889.7	-	46.6x
2020A	$1.12	-	$1,463	-	41.7x
2021E	$1.68	$1.67	$1,839	$1,908	27.8x
2022E	$1.82	$1.80	$1,955	$2,010	25.6x

FYE 12/30; Revenue in USD millions.

All historical EPS and B&S EPS estimates GAAP.

Source: Capital IQ, B&S Estimates

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Tour of Aqua's state-of-the-art environmental lab affirms thesis as PA's teethier WQAA advances.

We toured Aqua's recently completed 14,700 sq. foot environmental lab, located at Essential's corporate headquarters in Bryn Mawr, PA. Led by Chief Environmental, Safety, and Sustainability Officer Chris Crockett, our tour affirmed several key aspects of the investment thesis for WTRG. In particular, the lab's opening is timely given the likely imminent passage of PA 597, PA's water quality accountability legislation (unlike in NJ, where WQAA is still not being enforced due to DEP foot-dragging, the PA law will be implemented by the PUC, which aims to enforce it vigorously). The Bryn Mawr lab positions Aqua well as a partner for local water systems as they struggle to meet WQAA testing and compliance reporting requirements.

While it's predictable that Essential itself touts the new lab, our in-person tour independently confirms that the lab is in fact impressive. We've toured environmental labs for peer companies and major, big city municipal water/WW utilities, and Aqua's is the largest and most advanced environmental water testing facility we've seen yet.

Below are some of the key attributes of the new facility:

- Certified for environmental compliance reporting in five states (Ohio, Pennsylvania, New Jersey, North Carolina, Virginia).
- Equipped for 300,000 tests annually on 30,000 water samples.
- Comprehensive microbiological, organic, and inorganic analysis.
- Liquid Chromotography tandem Mass Spectrometry (LC-MS-MS) capabilities test for PFAS at demanding parts per trillion levels.
- Dedicated space for piloting cutting-edge analytical technologies.
- 20 employees; room to expand as organization grows.

WTRG trades at a discount to water utility peers, and a trite refrain is that Essential's foray into gas makes the company "less sustainable" and inhibits a full "ESG multiple". We don't buy this, seeing Essential as among the most sustainable companies in the space, and the state-of-the-art Bryn Mawr lab affirms this, highlighting that this is not only still very much a water company, but one at the forefront of addressing difficult issues like PFAS. Meanwhile, environmentally sound natural gas is crucial to Western PA's energy mix, and years of observing the industry from the frontlines (not puffy ESG reports) inform our view of Essential's sound corporate governance and excellent employee/customer/community/regulatory relations.

Our $54 target reflects a P/E of 32 times, in-line with water peers.

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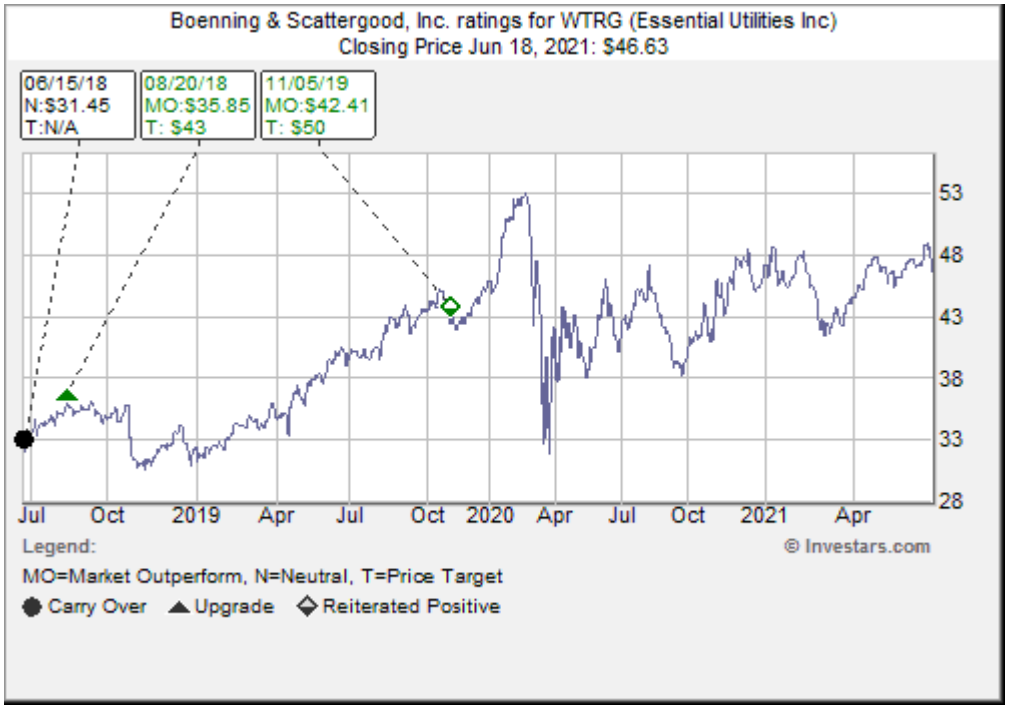

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Ratings Distribution (3/31/21):

Coverage Universe (a)	% of Universe
Outperform (Buy)	38%
Neutral (Hold)	47%
Underperform (Sell)	1%
Not Rated	14%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	7%
Neutral (Hold)	3%
Underperform (Sell)	100%
Not Rated	10%

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August 6, 2020

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	Outperform/Moderate
Price:	$44.69
Target Price ($US):	$50.00
Market Cap ($US millions):	$10,951
ADTV (US$ millions):	$46.6

Price as-of Prior Day Close

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2018A	$1.08	-	$838.1	-	41.4x
2019A	$1.00	-	$889.7	-	44.6x
2020E*	$1.40	$1.48	$1,485	$1,656	31.8x
2021E	$1.70	$1.66	$1,658	$1,813	26.3x

FYE 12/30; Revenue in USD millions.

All historical EPS and B&S EPS estimates GAAP.

*MOAP guidance of $1.53-$1.58 reflects full year of Peoples.

Source: Capital IQ, B&S Estimates

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EPS surge 17% as lockdowns drive residential demand; Growth outlook robust, highly visible.

Essential Utilities reported 2Q EPS of $0.29, up 17% year/year, with solid organic growth in the core water business and the addition of Peoples Gas driving a strong quarter, and management affirming its 2020 EPS guidance of $1.53-$1.58 (MOAP-basis). Excluding $150 million from Peoples, revenue rose 7.3% year/year in the core water business. Management says that higher residential demand due to COVID-19 quarantining more than offset the negative impact of the recession on commercial and industrial demand in the quarter.

An active rate pipeline is a usually a good thing for a regulated utility, but in the current environment, where rate increases are even more politically fraught than normal due to the impact of the COVID-19 recession on households, it pays to be off the radar. With just $5.2 million pending vs. annual revenue ~$1.5 billion, Essential's current rate pipeline is light. This is more a matter of being lucky than good (both Peoples and Aqua Pennsylvania recently wrapped up major rate cases), but either way it positions the company well to ride out the recession avoiding what could be meaningful regulatory lag.

Essential's $276 million DELCORA acquisition has seen unexpected delays due to a local legal challenge, but we believe the deal will close in 2020, creating a notable growth catalyst (see our June 18 note for details). Meanwhile, the municipal deal pipeline continues to expand, with Pennsylvania leading the way. In June, the city council in Norristown (pop. 35,000) approved the sale of the WW system to Aqua for $82 million. In addition to its size, Norristown is strategic because, with DELCORA, it would create a large PA WW ratepayer base, enabling future bolt-ons. Also, as the county seat in populous Montgomery County, Norristown is an anchor for peripheral deals.

After a brief lull at the onset of the COVID-19 pandemic, Essential is fully back up and running on its capital investment program, with the current 2020 capex target at $950 million (Aqua + Peoples). Early on in the pandemic, there were fears that rate base growth could slow (sapping future earnings growth), but this has not transpired.

Essential's solid 2Q, guidance/growth target affirmation, active M&A pipeline, and continued execution on its capital investment program amid the huge COVID-19 economic shock epitomize the resilience of the regulated utility business model. We reiterate our Outperform rating for Essential, which we see as a best-of-breed player in the regulated utility space with notable near-term growth catalysts.

Our price target of $50 reflects a forward P/E multiple of 30.1 times, ~in-line with the current peer group average of 29.5 times.

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Disclosure Appendix

Rating and Price Target History:

Risk Factors

The realization of any or all of the following risk factors, among others, may adversely affect the company's stock price and prevent it from reaching our price target: the economic cycle, concentration in energy sector, foreign currency exposure, and client concentration.

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Our three-tier investment ratings are based on a stock's return potential relative to a broad market index:

- ***Outperform (Buy):*** The security's total return over the year or longer is expected to exceed the total return of the S&P 500™ over the identical period.
- ***Neutral (Hold):*** The security's total return over the next year or longer is expected to be roughly equivalent to the total return of the S&P 500™ over the identical period.
- ***Underperform (Sell):*** The security's total return over the next year or longer is expected to be less than the total return of the S&P 500™ over the identical period.

Our four-tier risk ratings are based on a mix of price volatility and fundamental factors relative to the market and peer group.

- ***Low:*** The security has higher-than-average fundamental predictability and/or lower-than-average price volatility.
- ***Moderate:*** The security has average fundamental predictability and/or average price volatility.
- ***High:*** The security has lower-than-average fundamental predictability and/or higher-than-average price volatility.
- ***Speculative:*** The security has very inconsistent fundamental predictability and/or very high relative price volatility.

Ratings Distribution (6/30/20):

Coverage Universe (a)	% of Universe
Outperform (Buy)	22%
Neutral (Hold)	40%
Underperform (Sell)	0%
Not Rated	38%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	24%
Neutral (Hold)	6%
Underperform (Sell)	0%
Not Rated	21%

(a) Related to services provided within the past 12 months.

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Aqua America, Inc. (WTR)

First Look at Q2 Results

Reiterate Outperform rating after Q2 earnings release. WTR reported results which were in line with consensus estimates, and the company reaffirmed adj. EPS guidance of $1.45 to $1.50 (excluding impacts of Peoples acquisition). Importantly, Peoples appears on track to close this fall (settlement filed in July), which we believe is the most important driver of the stock. Additionally, WTR has received $57.5M in annualized revenue increases YTD ($47M in Pennsylvania). We will look for additional information on the conference call.

- **Q2 results were in line with consensus EPS estimates due to rate increases and new customers from acquisitions and organic growth.** Q2 revenue was ~$218.9M vs. our/consensus estimates of $225M/$220M, as additional revenue from infrastructure surcharges contributed to ~3.3% growth y/y. Non-GAAP net income (excluding impacts of Peoples transaction-related expenses) was $66.8M vs. $70M/$66M, and EPS was $0.37 vs. $0.40/$0.37, respectively, due to rate increases and regulated growth.
- **WTR reaffirmed 2019 guidance.** WTR continues to expect $1.45 to $1.50 in EPS in 2019 (excluding impacts of Peoples transaction), total customer growth of ~2%-3%, and ~$550M in infrastructure investments.
- **Peoples appears on track to close in the fall.** Kentucky and West Virginia approved the Peoples acquisition in March and April, respectively, and WTR filed a settlement agreement in Pennsylvania which all but two intervenors chose not to oppose. The commission is expected to issue an order this fall.
- **Acquisition activity should continue to drive customer growth in the water business.** WTR has signed purchase agreements which are expected to add ~22.6k customer connections over the next two years (~$100M in rate base, on aggregate). Additionally, the company has a pipeline of ~400k water and wastewater customer connections it is actively pursuing across four states, which should help drive growth over time.
- **Rate increases and surcharges continue to contribute to revenue growth.** WTR has received $57.5M in annualized revenue increases thus far in 2019 due to favorable decisions in rate cases and infrastructure charges in five states, including ~$47M in Aqua Pennsylvania. Additionally, a decision on a total of ~$2.3M in annualized revenue increase is pending in Ohio, although the timing of potential regulatory approval remains unclear.
- **WTR's Q2 earnings call will be held today at 10:00 a.m. CT.** The call can be accessed at www.ir.aquaamerica.com.

RESEARCH UPDATE

1-Year Price Chart

Stock Data

Rating:	Outperform
Suitability:	Lower Risk
Price Target:	$44
Price (8/6/19):	$41.15
Market Cap (mil):	$7,341
Shares Out (mil):	178.4
Average Daily Vol (mil):	1.01
Dividend Yield:	2.1%

Estimates

FY Dec	2018A	2019E	2020E
Q1	0.29 A	0.28 A	
Q2	0.37 A	0.37 A	
Q3	0.44 A	0.47 E	
Q4	0.31 A	0.33 E	
Fiscal EPS	**1.41 A**	**1.48 E**	**1.57 E**
Fiscal P/E	29.2x	27.8x	26.2x

Chart/Table Sources: FactSet and Baird Data. Price chart reflects most recent closing price.

Please refer to Appendix - Important Disclosures and Analyst Certification

Aqua America is a holding company for numerous regulated water/waste water utilities serving almost 3.0 million people in the eastern half of the U.S.

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Investment Thesis

US water infrastructure needs should drive long-term earnings growth. The water infrastructure in the United States is in significant need of upgrade and expansion. We believe a significant long-term earnings growth driver for WTR comes from substantial capital investment opportunities, which contribute to rate base growth, and in turn, drives earnings.

Peoples acquisition, a natural gas utility, should add another platform for organic growth. The combined entity is expected to have ~$10.8B in assets and a rate base of >$7.2B, 70% in water and wastewater and 30% in natural gas. We estimate WTR paid ~14.8x EV/EBITDA (based on an enterprise value of $4.275B and 2019E EBITDA of $289M) for the assets. The transaction is subject to regulatory approvals, including approval by public utility commissions in Pennsylvania, Kentucky, and West Virginia, and is expected to close in mid-2019.

Planned capital investment should expand rate base and generate growth for the company in the long run. We expect Aqua America's long-term EPS growth to be fueled in part by the company's ~$500 million annual capex investment. $1.4B is expected to be invested into system upgrades (main, pipes, hydrants, etc.) over the next three years, which provides direct value to customers. Discretionary system investments are typically targeted for states with enhanced recovery mechanisms which help stabilize margin and earnings consistencies despite accelerated investment.

The majority of WTR's regulatory operations are located in states that maintain enhanced regulatory recovery mechanisms. The majority of WTR's current operating system employs infrastructure mechanisms, which allow a return on investment outside of a full rate case, substantially reducing regulatory lag time and minimizing rate case activity. These regulatory mechanisms include infrastructure investment riders, statewide rates and incentive mechanisms for acquisitions of troubled water systems. We believe such mechanisms provide a constructive regulatory environment in which to make capital investments, enabling improved and more consistent earned returns, which should lead to a premium peer valuation.

Continued municipal water acquisitions should help customer growth. The company targets 2-3% customer growth in 2019 driven by acquisitions of municipal utilities. Aqua has successfully acquired numerous water and waste water systems in the past decade to supplement its internal growth. Acquisitions also provide significant follow-on investment opportunities as WTR improves the quality of an acquired water system. The company is expected to be a key player in consolidating some of the 53,000 private water systems in the U.S., and rehabilitating those systems to improve water quality and drive investment growth.

Raising price target to $44. Our price target is based on a ~28x P/E multiple on our 2020 EPS estimate, which is in line with comps which are currently trading at a ~24x-31x multiple. We believe this is justified as WTR integrates the Peoples acquisition.

Risks & Caveats

Our suitability rating on Aqua America is Lower Risk. Key risks include the following.

Regulation. Regulated operations are subject to local, state and federal regulations. Changes in the regulatory environment can affect WTR's near-term and long-term performance.

Weather. WTR's businesses are sensitive to fluctuations in the weather. Particularly wet or dry weather can impact near-term financial results.

Acquisition risk. WTR may have the opportunity to purchase assets or companies in the near future. Acquisitions carry risks related to personnel, expected-versus-actual growth and a myriad of unforeseen hurdles, all of which can negatively affect earnings.

Product quality. Unique among its sister regulated utility sectors, water utilities provide a product that is ingested. Despite robust mandated service quality standards that lower risk, a quality failure could materially impact the earnings and stock of WTR.

Company Description

Aqua America is a holding company for regulated utilities providing water and waste water services to nearly 3 million people located in the eastern half of the U.S. Over 50% of operating revenues and net income are derived from Pennsylvania.

Appendix - Important Disclosures and Analyst Certification

Approved on 06 August 2019 20:17EDT/ Published on 07 August 2019 01:02EDT.

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Aqua America, Inc. (WTR)

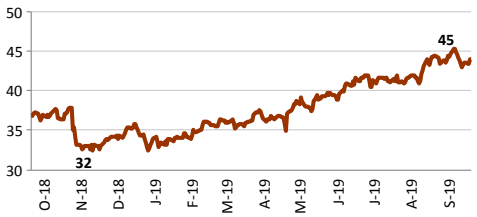
Announces Major Municipal Acquisition

Reiterate Outperform rating following acquisition announcement. WTR announced an agreement to acquire DELCORA's wastewater assets for $276.5M — the largest municipal acquisition in company and Pennsylvania history. With a prior estimated depreciated rate base of ~$240M, the acquired assets should drive significant rate base growth (~5%+ initially) with an opportunity for ~$1.2B of CapEx over the next 20 years. Financing will likely be the next questions for investors and we think WTR could look to issue an ATM to fund the deal. Remain buyers at current levels.

- **Last night, WTR announced an agreement to acquire DELCORA's wastewater assets for $276.5M, which will be the largest municipal acquisition in PA history.** Delaware Country Regional Water Quality Control Authority (DELCORA) serves ~500k people (estimated ~165k retail customers) in Southeast Pennsylvania; the acquisition is the largest ever municipal acquisition for WTR and the largest water/wastewater deal in Pennsylvania history. WTR previously announced it signed a letter of intent committing to exclusive discussions with DELCORA (see: Q2 Conference Call Highlights). The transaction is subject to approval by the Pennsylvania PUC.
- **Transaction significantly expands WTR's wastewater customer base; DELCORA assets to be aggregated into wastewater business.** For context, WTR serves ~3M people across its asset base— the DELCORA assets alone serve ~500k customers. The company currently has ~100k wastewater customers, so the addition of 165k new retail customers from acquired assets is significant. As part of the acquisition, Aqua will hire all 136 DELCORA employees and will aggregate all wastewater customers into what is effectively the company's new wastewater division.
- **DELCORA depreciated rate base previously forecast at ~$240M; should drive significant (~5%+) growth with an opportunity for further investment over time.** The depreciated rate base for the DELCORA assets was previously estimated at ~$240M and should immediately drive ~5% rate base growth (over YE:19 forecast of ~$5B in rate base for WTR's water assets). Additionally, WTR indicated CapEx need for the acquired assets is forecast at $1.2B through 2041, which should drive further rate base growth over time.
- **Financing likely next question for investors; we think it is possible WTR will look to issue an ATM to fund deal.** Particularly following the Peoples acquisition, we think investors will now focus on financing strategies for the large deal. Management previously indicated it could look to put out an at-the-market program to fund a municipal acquisition of this size, though we will look for more information on the Q3 conference call.

RESEARCH UPDATE

1-Year Price Chart



Stock Data

Rating:	Outperform
Suitability:	Lower Risk
Price Target:	$44
Price (9/17/19):	$43.90
Market Cap (mil):	$9,649
Shares Out (mil):	219.8
Average Daily Vol (mil):	1.03
Dividend Yield:	2.0%

Estimates

FY Dec	2018A	2019E	2020E
Q1	0.29 A	0.28 A	
Q2	0.37 A	0.37 A	
Q3	0.44 A	0.48 E	
Q4	0.31 A	0.35 E	
Fiscal EPS	**1.41 A**	**1.48 E**	**1.57 E**
Fiscal P/E	31.1x	29.7x	28.0x

Chart/Table Sources: FactSet and Baird Data. Price chart reflects most recent closing price.

Please refer to Appendix - Important Disclosures and Analyst Certification

Aqua America is a holding company for numerous regulated water/waste water utilities serving almost 3.0 million people in the eastern half of the U.S.

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Investment Thesis

US water infrastructure needs should drive long-term earnings growth. The water infrastructure in the United States is in significant need of upgrade and expansion. We believe a significant long-term earnings growth driver for WTR comes from substantial capital investment opportunities, which contribute to rate base growth, and in turn, drives earnings.

Peoples acquisition, a natural gas utility, should add another platform for organic growth. The combined entity is expected to have ~$10.8B in assets and a rate base of >$7.2B, 70% in water and wastewater and 30% in natural gas. We estimate WTR paid ~14.8x EV/EBITDA (based on an enterprise value of $4.275B and 2019E EBITDA of $289M) for the assets. The transaction is subject to regulatory approvals, including approval by public utility commissions in Pennsylvania, Kentucky, and West Virginia, and is expected to close in late-2019.

Planned capital investment should expand rate base and generate growth for the company in the long run. We expect Aqua America's long-term EPS growth to be fueled in part by the company's ~$500 million annual capex investment. $1.4B is expected to be invested into system upgrades (main, pipes, hydrants, etc.) over the next three years, which provides direct value to customers. Discretionary system investments are typically targeted for states with enhanced recovery mechanisms which help stabilize margin and earnings consistencies despite accelerated investment.

The majority of WTR's regulatory operations are located in states that maintain enhanced regulatory recovery mechanisms. The majority of WTR's current operating system employs infrastructure mechanisms, which allow a return on investment outside of a full rate case, substantially reducing regulatory lag time and minimizing rate case activity. These regulatory mechanisms include infrastructure investment riders, statewide rates and incentive mechanisms for acquisitions of troubled water systems. We believe such mechanisms provide a constructive regulatory environment in which to make capital investments, enabling improved and more consistent earned returns, which should lead to a premium peer valuation.

Continued municipal water acquisitions should help customer growth. The company targets 2-3% customer growth in 2019 driven by acquisitions of municipal utilities. Aqua has successfully acquired numerous water and waste water systems in the past decade to supplement its internal growth. Acquisitions also provide significant follow-on investment opportunities as WTR improves the quality of an acquired water system. The company is expected to be a key player in consolidating some of the 53,000 private water systems in the U.S., and rehabilitating those systems to improve water quality and drive investment growth.

Price target $44. Our price target is based on a ~28x P/E multiple on our 2020 EPS estimate, which is in line with comps which are currently trading at a ~24x-31x multiple. We believe this is justified as WTR integrates the Peoples acquisition.

Risks & Caveats

Our suitability rating on Aqua America is Lower Risk. Key risks include the following.

Regulation. Regulated operations are subject to local, state and federal regulations. Changes in the regulatory environment can affect WTR's near-term and long-term performance.

Weather. WTR's businesses are sensitive to fluctuations in the weather. Particularly wet or dry weather can impact near-term financial results.

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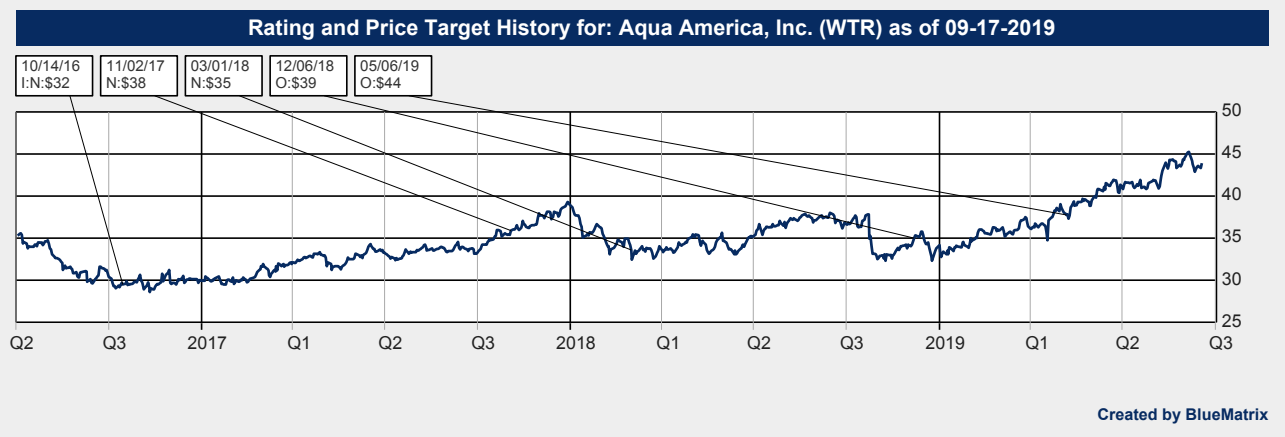
Company Description

Aqua America is a holding company for regulated utilities providing water and waste water services to nearly 3 million people located in the eastern half of the U.S. Over 50% of operating revenues and net income are derived from Pennsylvania.

Appendix - Important Disclosures and Analyst Certification

Approved on 18 September 2019 08:43EDT/ Published on 18 September 2019 08:48EDT.



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Aqua America, Inc. (WTR)

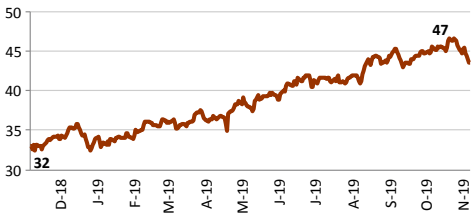
First Look at Q3 Results

Reiterate Outperform rating after Q3 earnings release. WTR reported results which were in line with consensus estimates, and the company reaffirmed adj. EPS guidance of $1.45 to $1.50 (excluding impact of Peoples acquisition). Importantly, the Peoples acquisition is now expected to close in late 2019 or early 2020 (vs. prior expectation of fall 2019), though WTR appears to be progressing through regulatory proceedings; we believe this is the most important driver of the stock. Additionally, WTR has received $59.8M in annualized revenue increases YTD.

- **Q3 results were in line with consensus EPS estimates due to rate increases and new customers from acquisitions and organic growth.** Q3 revenue was ~$243.6M vs. our/consensus estimates of $241M/$250M, as additional revenue from infrastructure surcharges contributed to ~7.7% growth y/y. Non-GAAP net income (excluding impacts of Peoples transaction-related expenses) was $85.6M vs. $86M/$88M, and EPS was $0.48 vs. $0.48/$0.44, respectively, due to rate increases and regulated growth.
- **WTR reaffirmed 2019 guidance, excluding impact of Peoples acquisition.** WTR continues to expect $1.45 to $1.50 in EPS in 2019 (excluding impacts of Peoples transaction), total customer growth of ~2%-3%, and ~$550M in infrastructure investments.
- **Peoples acquisition now expected to close in late 2019 or early 2020 (vs. prior expectation of fall 2019), though WTR appears to be progressing through regulatory proceedings.** Kentucky and West Virginia approved the Peoples acquisition in March and April, respectively. In Pennsylvania, the Administrative Law Judge issued a recommended decision determining WTR is fit to control Peoples and that the acquisition would be positive for the public; the Pennsylvania Utility Commission will now review the recommendation and issue a final order. WTR now expects the acquisition to close in late 2019 or early 2020.
- **Acquisition activity should continue to drive customer growth in the water business; WTR announced an agreement to acquire DELCORA's wastewater assets for ~$276.5M in Q3.** WTR has signed purchase agreements which are expected to add ~22.6k customer connections by early 2020 (~$110M in rate base, on aggregate). Additionally, WTR announced an agreement to acquire DELCORA's wastewater assets; the largest municipal acquisition in company and Pennsylvania history (see: Municipal Acquisition); we will look for more information on the conference call.
- **Rate increases and surcharges continue to contribute to revenue growth.** WTR has received $59.8M in annualized revenue increases thus far in 2019 due to favorable decisions in rate cases and infrastructure charges in five states.
- **WTR's Q3 earnings call will be held today at 10:00 a.m. CT.** The call can be accessed at www.ir.aquaamerica.com.

RESEARCH UPDATE

1-Year Price Chart



Stock Data

Rating:	Outperform
Suitability:	Lower Risk
Price Target:	$44
Price (11/4/19):	$43.56
Market Cap (mil):	$9,574
Shares Out (mil):	219.8
Average Daily Vol (mil):	1.15
Dividend Yield:	2.2%

Estimates

FY Dec	2018A	2019E	2020E
Q1	0.29 A	0.28 A	
Q2	0.37 A	0.37 A	
Q3	0.44 A	0.48 A	
Q4	0.31 A	0.35 E	
Fiscal EPS	**1.41 A**	**1.48 E**	**1.57 E**
Fiscal P/E	30.9x	29.4x	27.7x

Chart/Table Sources: FactSet and Baird Data. Price chart reflects most recent closing price.

Please refer to Appendix - Important Disclosures and Analyst Certification

Aqua America is a holding company for numerous regulated water/waste water utilities serving almost 3.0 million people in the eastern half of the U.S.

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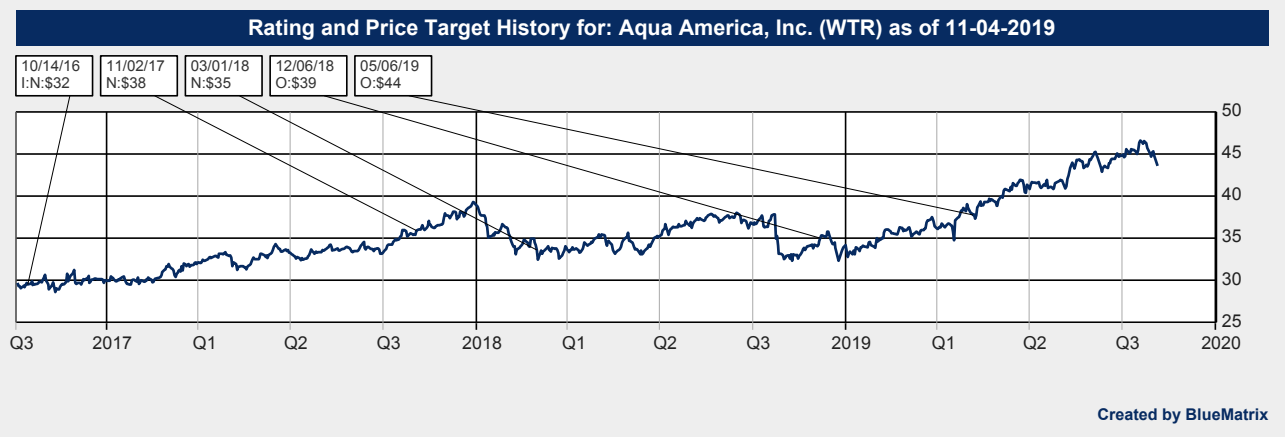

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Essential Utilities Inc., (WTRG)

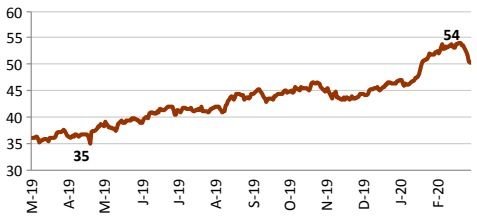
Brief Thoughts After Investor Day

Reiterate Outperform rating after investor day. WTRG issued 2020 and three-year EPS growth guidance which was largely in line with expectations and should help calibrate models following the close of the Peoples acquisition (expected mid-March). Importantly, we believe long-term growth drivers are on track: the accelerated pipeline replacement program and long-term water infrastructure need provides CapEx visibility and WTRG continues to execute on its municipal acquisition strategy. We think Essential Utilities is well-positioned for current market volatility, and remain buyers at current levels.

- **WTRG issued 2020 and three-year EPS growth guidance which was largely in line with expectations; EPS growth should align with rate base growth over the long run.** For 2020, WTRG guided to ~$1.53 - $1.58 of adj. EPS (largely in line with consensus of $1.58) and $1.05 - $1.10 of GAAP EPS (assuming 9.5 months of Peoples contribution and transaction expenses). EPS is expected to grow at a 5%-7% CAGR through 2022E, which compares favorably with water utility peers, and overtime management indicated EPS growth should mirror rate base growth (6%-7% growth for water, excluding acquisitions, 8%-10% for Gas).
- **Pipeline replacement at Peoples, along with substantial need for investment in water infrastructure, provides significant visibility on forward CapEx.** WTRG guided to ~$400M of annual CapEx for Peoples alone, as the company operates under an accelerated pipe replacement program; at ~189 miles replaced/year, the business has visibility on 15+ years of increased capital spending (recovered through DSIC). Separately, ongoing CapEx in the water business (~$550M expected in 2020) should drive rate base and earnings growth.
- **WTRG's municipal acquisition strategy is on track, and could help accelerate growth (particularly in the water business).** Since 2015, WTRG has added ~$237M of rate base through 57 acquisitions, and has signed municipal agreements (pending close) for ~$327M of aggregate purchase price, most significantly DELCORA (198k total customers, alone). Moving forward, the company has identified acquisition opportunities totaling ~320k customer additions (majority wastewater), which could contribute to rate base growth over time. As a reminder, every ~$100M of acquired rate base amounts to ~$5M of incremental annual earnings potential.
- **We think WTRG, and the other water utilities under our coverage, are well-positioned in the current macro environment and could be a safe haven during market volatility.** All four utilities under our coverage have significant growth visibility and little to no exposure to trade or the global economy, which we think is a key differentiating factor. Favorable regulatory dynamics, M&A activity and accelerating capital investment should continue to drive EPS growth regardless of broader macro uncertainty. We believe the space is well positioned to outperform the market if volatility and/or macro headwinds persist.

RAISING PRICE TARGET

1-Year Price Chart



Stock Data

Rating:	Outperform
Suitability:	Lower Risk
Price Target/Previous:	▲$50/$44
Price (2/27/20):	$46.34
Market Cap (mil):	$10,186
Shares Out (mil):	219.8
Average Daily Vol (mil):	1.36
Dividend Yield:	2.0%

Estimates

FY Dec	2019A	2020E	2021E
Q1	0.28 A	0.56 E	
Q2	0.37 A	0.19 E	
Q3	0.48 A	0.26 E	
Q4	0.34 A	0.53 E	
Fiscal EPS	**1.47 A**	**1.55 E**	**1.64 E**
Previous Est	1.48 A	1.57 E	
Fiscal P/E	31.5x	29.9x	28.3x

Chart/Table Sources: FactSet and Baird Data. Price chart reflects most recent closing price.

Please refer to Appendix - Important Disclosures and Analyst Certification

Essential Utilities is a holding company for numerous regulated water/waste water utilities serving almost 3.0 million people in the eastern half of the U.S.

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Investment Thesis

US water infrastructure needs should drive long-term earnings growth. The water infrastructure in the United States is in significant need of upgrade and expansion. We believe a significant long-term earnings growth driver for WTRG comes from substantial capital investment opportunities, which contribute to rate base growth, and in turn, drives earnings.

Peoples acquisition, a natural gas utility, should add another platform for organic growth. The combined entity is expected to have ~$10.8B in assets and a rate base of >$7.2B, 70% in water and wastewater and 30% in natural gas. We estimate WTR paid ~14.8x EV/EBITDA (based on an enterprise value of $4.275B and 2019E EBITDA of $289M) for the assets. The transaction is expected to close in mid-March.

Planned capital investment should expand rate base and generate growth for the company in the long run. We expect WTRG's long-term EPS growth to be fueled in part by the company's ~ $950M annual capex investment. Investments are typically targeted for states with enhanced recovery mechanisms which help stabilize margin and earnings consistencies despite accelerated investment.

The majority of WTRG's regulatory operations are located in states that maintain enhanced regulatory recovery mechanisms. The majority of WTRG's current operating system employs infrastructure mechanisms, which allow a return on investment outside of a full rate case, substantially reducing regulatory lag time and minimizing rate case activity. These regulatory mechanisms include infrastructure investment riders, statewide rates and incentive mechanisms for acquisitions of troubled water systems. We believe such mechanisms provide a constructive regulatory environment in which to make capital investments, enabling improved and more consistent earned returns, which should lead to a premium peer valuation.

Continued municipal water acquisitions should help customer growth. The company targets 2-3% customer growth in 2020 driven by acquisitions of municipal utilities. Aqua has successfully acquired numerous water and waste water systems in the past decade to supplement its internal growth. Acquisitions also provide significant follow-on investment opportunities as WTR improves the quality of an acquired water system. The company is expected to be a key player in consolidating some of the 53,000 private water systems in the U.S., and rehabilitating those systems to improve water quality and drive investment growth.

Raising price target to $50. Our price target is based on a ~29x P/E multiple on our 2022 EPS estimate, which is in line with comps which are currently trading at a ~24x-31x multiple. We believe this is justified as WTR integrates the Peoples acquisition.

Risks & Caveats

Our suitability rating on Essential Utilities is Lower Risk. Key risks include the following.

Regulation. Regulated operations are subject to local, state and federal regulations. Changes in the regulatory environment can affect WTRG's near-term and long-term performance.

Weather. WTRG's businesses are sensitive to fluctuations in the weather. Particularly wet or dry weather can impact near-term financial results.

Acquisition risk. WTRG may have the opportunity to purchase assets or companies in the near future. Acquisitions carry risks related to personnel, expected-versus-actual growth and a myriad of unforeseen hurdles, all of which can negatively affect earnings.

Product quality. Unique among its sister regulated utility sectors, water utilities provide a product that is ingested. Despite robust mandated service quality standards that lower risk, a quality failure could materially impact the earnings and stock of WTRG.

Company Description

Essential Utilities is a holding company for regulated utilities providing water and waste water services to nearly 3 million people located in the eastern half of the U.S. Over 50% of operating revenues and net income are derived from Pennsylvania.

Appendix - Important Disclosures and Analyst Certification

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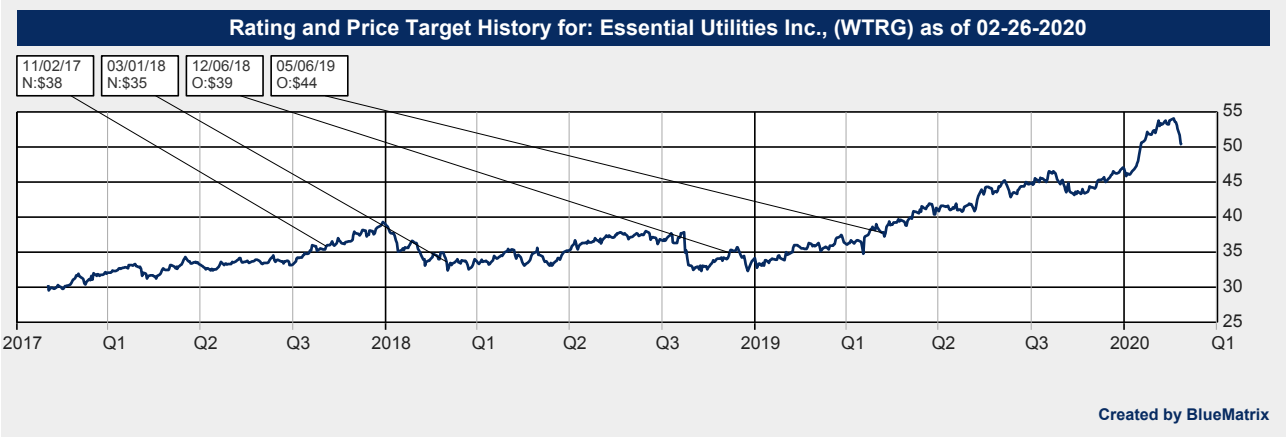

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Essential Utilities Inc., (WTRG)

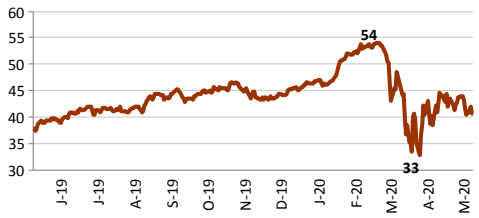
Solid First Quarter with Peoples, M&A Focus Now on DELCORA

Reiterate Outperform rating after Q1 earnings release. WTRG reported results which were slightly below our estimates, though the company reaffirmed 2020 adj. EPS guidance of $1.53 to $1.58 (excluding impact of Peoples acquisition). Following the close of Peoples on March 16, the M&A focus shifts to DELCORA wastewater assets, which is the largest municipal acquisition in company and Pennsylvania history. We will look for more information on the Q1 conference call, which will be held today at 10 a.m. CT.

- **Q1 results were slightly below our/consensus EPS estimates in the first quarter of Peoples contribution.** Q1 revenue was ~$255.6M vs. our/consensus estimates of $241M/$250M, driven by a $38.5M contribution from Peoples (from March 16 close to quarter end) and rate increases in the regulated water segment. Non-GAAP EPS (excluding contribution of Peoples and transaction-related expenses) was $0.60 vs. $0.65/$0.65, respectively, due to rate increases and regulated growth. On a GAAP basis, EPS of $0.20 exceeded our estimate of $0.08 on a larger Peoples contribution.
- **Importantly, WTRG reaffirmed 2020 guidance and continues to monitor potential impacts of COVID-19.** WTRG continues to expect $1.53 to $1.58 in adj. EPS in 2019 (excluding impacts of Peoples transaction, ~$1.05 - $1.10 on GAAP basis), total water customer growth of ~2%-3%, and ~$950M in infrastructure investments (~$550M in regulated water, ~$400M in natural gas).
- **Acquisition activity should continue to drive customer growth in the water business and WTRG filed the DECLORA wastewater acquisition request with the Pennsylvania PUC.** WTRG has signed purchase agreements which are expected to add ~205k customer connections by early 2020 (~$327M in rate base, on aggregate). These figures include the ~$276.5M (~198k retail customer) DELCORA acquisition, which is the largest municipal acquisition in company and Pennsylvania history.
- **Repair tax deduction for Peoples a ~$5.9M benefit in Q1; should enable further infrastructure investment and increase time between rate cases.** WTRG elected to employ the repair tax deduction for Peoples, which allows a tax deduction for qualifying infrastructure investments and reduces tax expense. The deduction allows WTRG to continue investing while increasing the time between rate cases and limiting the need for future rate increases.
- **Rate increases and surcharges continue to contribute to revenue growth.** The regulated water segment has received $5.2M in annualized revenue increases thus far in 2020 due to favorable decisions in rate cases and infrastructure charges in Illinois, North Carolina, Ohio, and Virginia. The gas segment has received ~$1M of annualized revenue increases.
- **WTRG's Q1 earnings call will be held today at 10:00 a.m. CT.** The call can be accessed at www.ir.aquaamerica.com.

ESTIMATE CHANGE

1-Year Price Chart



Stock Data

Rating:	Outperform
Suitability:	Lower Risk
Price Target:	$46
Price (5/6/20):	$40.67
Market Cap (mil):	$10,373
Shares Out (mil):	255.1
Average Daily Vol (mil):	1.38
Dividend Yield:	2.3%

Estimates

FY Dec	2019A	2020E	2021E
Q1	0.28 A	0.60 A	
Q2	0.37 A	0.20 E	
Q3	0.48 A	0.26 E	
Q4	0.34 A	0.49 E	
Fiscal EPS	**1.47 A**	**1.55 E**	**1.68 E**
Previous Est			1.64 E
Fiscal P/E	27.7x	26.2x	24.2x

Chart/Table Sources: FactSet and Baird Data. Price chart reflects most recent closing price.

Please refer to Appendix - Important Disclosures and Analyst Certification

Essential Utilities is a holding company for numerous regulated water/waste water utilities serving almost 3.0 million people in the eastern half of the U.S.

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Investment Thesis

US water infrastructure needs should drive long-term earnings growth. The water infrastructure in the United States is in significant need of upgrade and expansion. We believe a significant long-term earnings growth driver for WTRG comes from substantial capital investment opportunities, which contribute to rate base growth, and in turn, drives earnings.

Peoples acquisition, a natural gas utility, should add another platform for organic growth. The combined entity is expected to have ~$10.8B in assets and a rate base of >$7.2B, 70% in water and wastewater and 30% in natural gas. We estimate WTR paid ~14.8x EV/EBITDA (based on an enterprise value of $4.275B and 2019E EBITDA of $289M) for the assets. The transaction is expected to close in mid-March.

Planned capital investment should expand rate base and generate growth for the company in the long run. We expect WTRG's long-term EPS growth to be fueled in part by the company's ~ $950M annual capex investment. Investments are typically targeted for states with enhanced recovery mechanisms which help stabilize margin and earnings consistencies despite accelerated investment.

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Continued municipal water acquisitions should help customer growth. The company targets 2-3% customer growth in 2020 driven by acquisitions of municipal utilities. Aqua has successfully acquired numerous water and waste water systems in the past decade to supplement its internal growth. Acquisitions also provide significant follow-on investment opportunities as WTR improves the quality of an acquired water system. The company is expected to be a key player in consolidating some of the 53,000 private water systems in the U.S., and rehabilitating those systems to improve water quality and drive investment growth.

$46 price target. Our price target is based on a ~26x P/E multiple on our 2022 EPS estimate, which is in line with comps which are currently trading at a ~24x-31x multiple. We believe this is justified as WTR integrates the Peoples acquisition.

Risks & Caveats

Our suitability rating on Essential Utilities is Lower Risk. Key risks include the following.

Regulation. Regulated operations are subject to local, state and federal regulations. Changes in the regulatory environment can affect WTRG's near-term and long-term performance.

Weather. WTRG's businesses are sensitive to fluctuations in the weather. Particularly wet or dry weather can impact near-term financial results.

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Company Description

Essential Utilities is a holding company for regulated utilities providing water and waste water services to nearly 3 million people located in the eastern half of the U.S. Over 50% of operating revenues and net income are derived from Pennsylvania.

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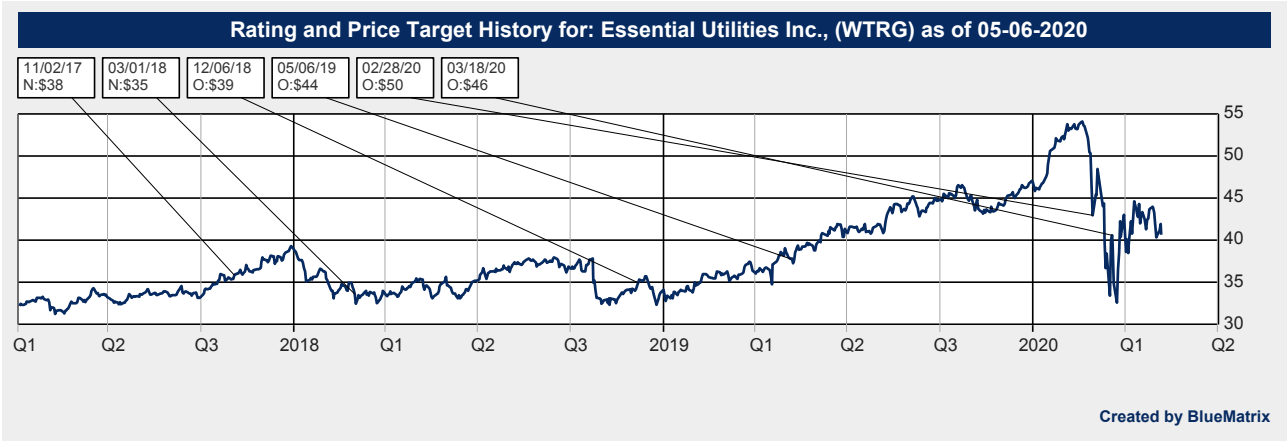
Approved on 06 May 2020 20:13EDT/ Published on 07 May 2020 01:05EDT.



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Essential Utilities Inc., (WTRG)

Strong Peoples Contribution Drives Earnings Beat

Reiterate Outperform rating after Q2 earnings release. WTRG reported results which exceeded our/consensus estimates driven by a better-than-expected contribution from Peoples. The company reaffirmed 2020 adj. EPS guidance, and continues to target ~$950M of regulated system investment for the year. We will look for an update on the DELCORA acquisition (transaction close previously expected early 2021), which should drive significant rate base and earnings growth, when completed. We will look for more information on the Q2 conference call, which will be held today at 10 a.m. CT.

- **Q2 results exceeded our/consensus EPS driven by a better-than-expected contribution from Peoples.** Q2 revenue was ~$384M vs. our/consensus estimates of $375M/$371M, driven by a $149.6M contribution from Peoples (we modeled $144M for the quarter) and rate increases & surcharges ($7.6M). EPS was $0.29 vs. $0.20/$0.23, largely related to lower-than-expected purchased gas costs ($43M in Q2, vs. our $60M estimate). We will look for more information on the Q2 earnings call.
- **Importantly, WTRG reaffirmed 2020 guidance; continuing to monitor COVID impacts, though volumes have been fairly resilient thus far.** WTRG continues to expect $1.53 to $1.58 in adj. EPS in 2020, ~$950M of regulated system investments ($550M in water, ~$400M in natural gas), and annual rate base growth of 6%-7% for water and 8%-10% for gas. Importantly, Q2 water sales increased 0.3% in Q2, as 10% growth in residential consumption (66% of quarterly consumption) more than offset the declines in commercial & industrial (-16% and -11%, respectively).
- **Substantial dividend increase (~7% annualized) highlights commitment to returning capital to shareholders and long-term value proposition.** WTRG recently increased its dividend ~7%; annualized dividend now amounts to a ~2.2% yield based on the August 5 closing price. WTRG has grown the dividend at a 7.2% CAGR since 2014, and we expect growth to continue, consistent with rate base and EPS growth.
- **Acquisition activity should continue to drive customer growth in the water business; will look for an update on DELCORA acquisition process (previously expected to close in early 2021).** WTRG has closed two acquisitions YTD (~$28.3M of cumulative rate base) and has signed purchase agreements totaling 203k customer connections (~$315M in rate base, on aggregate); we expect this will add ~$15M to annual earnings potential. These figures include the ~$276.5M (~198k retail customer) DELCORA acquisition, which is the largest municipal acquisition in company and Pennsylvania history; we will look for an update on potential transaction timing on the conference call.
- **WTRG's Q2 earnings call will be held today at 10:00 a.m. CT.** The call can be accessed at www.ir.aquaamerica.com.

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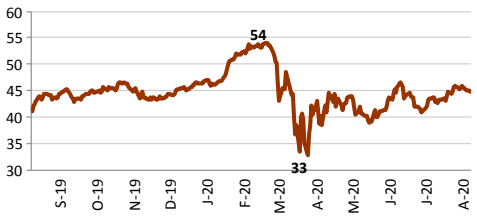

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Chart/Table Sources: FactSet and Baird Data. Price chart reflects most recent closing price.

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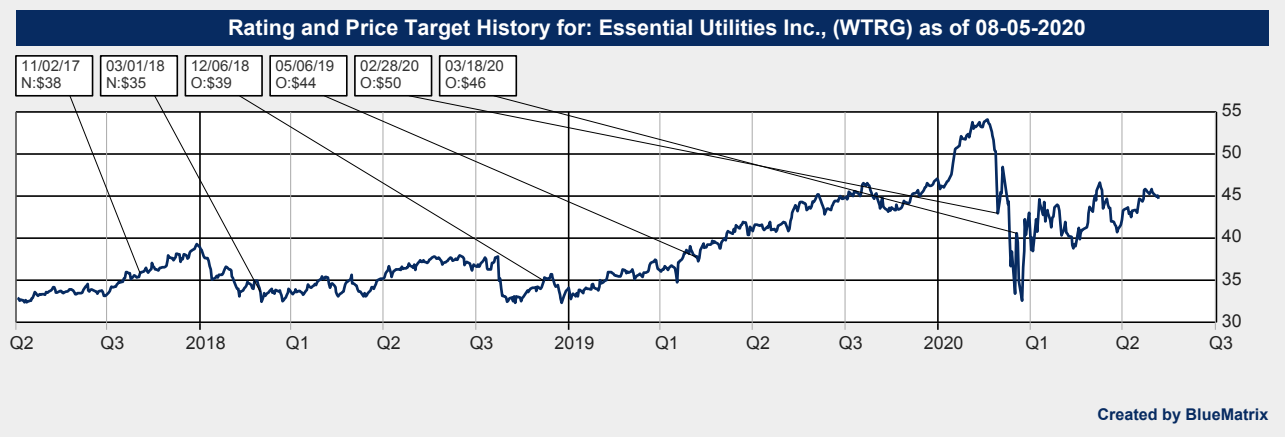

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Aqua America

Overflowing Interest: Downgrading to Neutral

Rating Change: NEUTRAL | PO: 52.00 USD | Price: 50.57 USD

Transaction Approval, New Branding & Leadership

Following the PA PUC's approval of WTR's pending Peoples Gas transaction on Thursday, we are downgrading shares to Neutral. After a rather protracted process since announcing the acquisition in 2018, the commission finally voted 4-1 in favor of the deal, with Commissioner Place the lone commissioner opting against it. Following approval, the company put out a press release mid-afternoon on Thursday announcing their new name, ticker, and executive leadership team ahead of the transaction close. The name will become 'Essential Utilities' on February 3rd (the ticker is also set to transition to WTRG), with Chris Franklin remaining CEO & Chairman of the Pro Forma entity. Since our launch in July, shares are up 23%, outperforming the XLU by 1300bps. While the final commission approval helps to de-risk the earnings profile going forward, we see a more balanced setup into the upcoming Analyst Day (February 27th) when the company lays out their long term guidance (potentially *more smoothed*). We have confidence in the mgmt. team in place and note their ability to effectively deploy their currency for the deal. We further highlight the shares' ability to re-rate higher into the deal - despite the foray into gas - as helping to mitigate ESG concerns around gas utes more broadly. Further, gas is additive.

Updating our Valuation & Moving to the Sidelines

Our estimates remain unchanged following our broader 4Q water preview published last week. While we remain above the street, we see shares as less attractive given elevated expectations into the Analyst Day and caution the lack of clarity around the ability to smooth earnings with implementation of the repairs tax benefit. With our latest valuation, we mark to market our above street estimates for the latest water and gas peer multiples of 28.1x and 19.6x (vs. 26.2x and 19.0x respectively just last week). Even after applying higher premiums to both the water and gas segments – which we see as worthwhile given the purer composition (vs. closest peer AWK with meaningful non-reg) and clear muni-driven EPS growth opportunities - our PO only shifts to $52, implying just 5% TSR. With water multiples overall still quite elevated vs. peer utility asset classes & risk that mgmt. may seek to moderate near-term EPS in favor of a 'trajectory' we d/g.

Estimates (Dec)

(US$)	2017A	2018A	2019E	2020E	2021E
EPS	1.36	1.41	1.47	1.70	1.72
GAAP EPS	1.36	1.41	1.47	1.70	1.72
EPS Change (YoY)	3.0%	3.7%	4.3%	15.6%	1.2%
Consensus EPS (Bloomberg)			1.44	1.56	1.67
DPS	0.81	0.86	0.92	0.99	1.06

Valuation (Dec)

	2017A	2018A	2019E	2020E	2021E
P/E	37.2x	35.9x	34.4x	29.7x	29.4x
GAAP P/E	37.2x	35.9x	34.4x	29.7x	29.4x
Dividend Yield	1.6%	1.7%	1.8%	2.0%	2.1%
EV / EBITDA*	1.2x	9.1x	29.9x	18.7x	17.8x
Free Cash Flow Yield*	-0.9%	-1.2%	-1.4%	-1.2%	-0.9%

* For full definitions of IQmethod℠ measures, see page 8.

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Refer to important disclosures on page 9 to 11. Analyst Certification on page 6. Price Objective Basis/Risk on page 6. 12085436

Timestamp: 21 January 2020 06:00AM EST

21 January 2020

Equity

Key Changes

(US$)	Previous	Current
Inv. Opinion	A-1-7	A-2-7
Inv. Rating	BUY	NEUTRAL
Price Obj.	47.00	52.00

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Stock Data

Price	50.57 USD
Price Objective	52.00 USD
Date Established	21-Jan-2020
Investment Opinion	A-2-7
52-Week Range	33.72 USD - 50.71 USD
Mrkt Val (mn) / Shares Out (mn)	10,915 USD / 215.8
Average Daily Value (mn)	57.60 USD
BofA Ticker / Exchange	WTR / NAS
Bloomberg / Reuters	WTR US / WTR.N
ROE (2019E)	8.4%
Net Dbt to Eqty (Dec-2018A)	127.1%

PUC: Public Utility Commission

TSR: Total Shareholder Return

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iQprofile℠ Aqua America

*iQ*method℠ – Bus Performance*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Return on Capital Employed	5.1%	3.9%	3.9%	5.1%	5.0%
Return on Equity	12.6%	9.7%	8.4%	8.3%	8.1%
Operating Margin	41.5%	38.7%	41.7%	68.9%	70.1%
Free Cash Flow	(97)	(127)	(154)	(135)	(95)

*iQ*method℠ – Quality of Earnings*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash Realization Ratio	1.6x	1.9x	1.7x	1.8x	1.9x
Asset Replacement Ratio	3.5x	3.4x	3.9x	2.6x	2.5x
Tax Rate	6.6%	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	108.3%	127.1%	95.9%	99.5%	102.6%
Interest Cover	3.9x	2.8x	3.4x	3.5x	3.3x

Income Statement Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Sales	805	835	902	949	966
% Change	0.6%	3.7%	8.0%	5.3%	1.7%
Gross Profit	810	838	905	1,572	1,638
% Change	-1.3%	3.5%	8.0%	73.7%	4.2%
EBITDA	14,226	1,941	590	942	990
% Change	-33.6%	-86.4%	-69.6%	59.7%	5.1%
Net Interest & Other Income	(88)	(99)	(115)	(193)	(210)
Net Income (Adjusted)	240	192	284	404	409
% Change	2.4%	-19.9%	48.1%	42.2%	1.2%

Free Cash Flow Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Net Income from Cont Operations (GAAP)	240	192	325	432	437
Depreciation & Amortization	137	147	163	330	356
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	14	(15)	0	0	0
Other Adjustments, Net	(9)	45	(3)	(32)	(3)
Capital Expenditure	(478)	(496)	(639)	(865)	(885)
Free Cash Flow	-97	-127	-154	-135	-95
% Change	NM	-31.5%	-21.4%	12.4%	29.6%

Balance Sheet Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash & Equivalents	4	4	3	5	5
Trade Receivables	99	101	109	190	198
Other Current Assets	28	42	44	56	57
Property, Plant & Equipment	5,400	5,930	9,132	9,667	10,196
Other Non-Current Assets	801	887	2,462	2,462	2,462
Total Assets	6,332	6,964	11,750	12,380	12,919
Short-Term Debt	117	160	287	310	332
Other Current Liabilities	167	239	245	307	313
Long-Term Debt	2,008	2,398	4,290	4,638	4,963
Other Non-Current Liabilities	2,083	2,158	2,158	2,158	2,158
Total Liabilities	4,375	4,955	6,979	7,412	7,765
Total Equity	1,958	2,009	4,771	4,968	5,154
Total Equity & Liabilities	6,332	6,964	11,750	12,380	12,919

* For full definitions of *iQmethod*℠ measures, see page 8.

Company Sector

Water Utilities

Company Description

Aqua America is a regulated water utility providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI. In Oct 2018, The company announced the acquisition of Peoples Gas in Oct 2018, which the PA PUC approved in January 2020. Peoples Gas is a gas utility providing distribution services to 740,000 customers in PA, WV, and KY.

Investment Rationale

We are Neutral rated on shares of WTR, seeing risk/reward as balanced at the current valuation. We have confidence in the mgmt. team in place and view the People's Gas deal constructively. The re- effective use of their currency can drive value, and the ability for shares to re-rate higher - despite the foray into gas - helps to mitigate ESG concerns around gas utilities more broadly.

Stock Data

Average Daily Volume	1,138,923

Quarterly Earnings Estimates

	2018	2019
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NA

Details of Pro Forma 'Essential Utilities' Revealed

Following approval from the Pennsylvania Public Utility Commission on Thursday for their pending acquisition of Peoples Gas, WTR put out a press release mid-afternoon announcing their new name, ticker and executive leadership team ahead of the close. The name will become "Essential Utilities" on Feb 3rd, with Chris Franklin remaining CEO and Chairman of the pro forma entity. The same day, the ticker is set to transition to WTRG. We include the full slate of leadership updates in the exhibit below. Mgmt. plans to host an Analyst Day in New York on February 27th with the release of full year results, which should provide an opportunity to interact and engage in Q&A with the newly introduced executive team.

Despite our more balanced view of shares, we have confidence in the mgmt. team in place and view the deal constructively; the re- effective use of their currency can drive value, and the ability for shares to re-rate higher - despite the foray into gas - helps to mitigate ESG concerns around gas utilities more broadly.

Table 1: WTR Leadership Team: Executives

'Essential Utilities' Executive Leadership Team	
Name	Title
Chris Franklin	Chairman, CEO
Richard Fox	EVP, COO
Christopher Luning	EVP, GC
Matthew Rhodes	EVP, Strategy and Corp Development
Dan Schuller	EVP, CFO
Ruth DeLost-Wylie	SVP, Business Transformation
Susan Haindl	SVP, Chief Administrative Officer
Christina Kelly	SVP, Chief HR Officer
Brian Dingerdissen	VP, Chief of Staff, IR & Communications
Kimberly Joyce	VP, Regulatory & Government Affairs

Source: BofA Global Research, company report

Table 2: WTR Leadership Team: Executives

'Essential Utilities' Operating Presidents	
Name	Title
Joseph Gregorini	President, Nat Gas Utilities
Colleen Arnold	President, Water & Wastewater Utilities

Source: BofA Global Research, company report

...but Repairs Tax Details Unaddressed

Despite the protracted timeline for the close of the transaction (we perceive around March 1st as a conservative expectation for final close), the company plans to elect to implement the repairs tax benefit in 2020. Under the strategy, earnings will see a large step up as the company expenses capital costs as opposed to depreciating them over a useful life for tax purposes. The magnitude of the initial increase will ultimately be determined by how much of the capital investment program qualifies for the treatment and whether the commission allows the company to use a catch up component for costs that are currently being depreciated. Our sense is that capital investments back to 2012 could potentially be privy to such treatment – albeit we perceive historical investment as likely more muted relative to future capital expenditures. With any approved catch up component, we also would expect the commission to be inclined to give at least part of the benefit back to customers.

While mgmt. has noted a desire to smooth out the impact from implementation as opposed to a large step up in '20 and minimal growth in future years, how they will approach this remains unclear. Bottom line, we see more execution risk to implementation given the elevated expectations implied by the current share price. Look for additional details at the upcoming Analyst Day on February 27th.

EPS Estimates

The exhibit below reflects our unchanged EPS estimates into the upcoming Analyst Day. We remain 3% above the street for '21 given what we perceive as strong earnings upside from the election of the Repairs Tax Benefit. That said, we perceive higher expectations from the buy side as largely priced in at the current valuation.

Table 1: EPS Estimates: still meaningfully above Street ests, but this moderates

EPS Estimates	2019E	2020E	2021E	2022E	2023E
PA	$1.05	$0.79	$0.77	$0.82	$0.86
OH	$0.09	$0.07	$0.07	$0.08	$0.08
IL	$0.10	$0.07	$0.08	$0.08	$0.09
TX	$0.08	$0.06	$0.06	$0.06	$0.06
NC	$0.05	$0.04	$0.04	$0.04	$0.05
Other States	$0.10	$0.08	$0.09	$0.09	$0.10
Water Utility	1.47	1.12	1.11	1.17	1.24
Peoples Gas		0.66	0.71	0.77	0.82
Parent & Other		*-0.08*	*-0.10*	*-0.12*	*-0.14*
EPS	1.47	1.70	1.72	1.82	1.92
YoY Growth		*16%*	*1%*	*6%*	*6%*
Guidance	1.45-1.50				
Shares O/S	*193*	*238*	*238*	*250*	*254*
Fully Diluted Shares O/S	*178*	*254*	*254*	*254*	*254*
Previous EPS		*$1.70*	*$1.72*	*$1.82*	
Consensus	1.44	1.56	1.67		

Source: BofA Global Research, Bloomberg

PO Shifts to $52: Downgrade to Neutral

The exhibit below reflects our latest SOTP. While our estimates remain unchanged, we mark to market for the latest utility peer multiples and update our premium/discount assumptions. Latest peer multiples shift to 28.1x and 19.6x for water and gas, respectively vs. 26.2x and 19.0x previously.

We now apply premiums to the water segment of 2x for PA (up from 1.5x previously), and add additional premiums of 2x, 3x, and 1x for OH, IL, and NC, respectively. We continue to highlight IL as a key state to watch for consolidation in the industry.

Following approval of the Peoples Gas transaction by the commission last week, we apply a 2x premium to the LDC peer group (compared to a -0.5x discount previously).

Despite the higher premiums ascribed in our valuation and our street-high estimates, our SOTP suggests limited upside after the latest run-up in share price. While our PO shifts to $52, we now see risk/reward as more fairly balanced at the current share price. Downgrade to Neutral.

We treat the blended entity with premium multiples still and see its fully regulated profile with sustained EPS growth as superior among water utility peers. We stress the ongoing municipal acquisition cycle appears to have accelerated of late (see our water preview) with datapoints suggesting this should indeed persist. We see the relative market cap size and breadth of state involvement as allowing larger market-cap companies to prove more nimble in pursuing municipal acquisitions.

Table 2: WTR SOTP

Water Utilities	2022 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*28.1x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		30.4x							
Water Utilities									
States	2022E EPS	ROE	embedded						
PA	$0.82	10.0%	2.0x	31.4x	32.4x	33.4x	$26	$27	$27
OH	$0.08	9.9%	2.0x	31.4x	32.4x	33.4x	$2	$3	$3
IL	$0.08	9.6%	3.0x	32.4x	33.4x	34.4x	$3	$3	$3
TX	$0.06	10.0%	0.0x	29.4x	30.4x	31.4x	$2	$2	$2
NC	$0.04	9.9%	1.0x	30.4x	31.4x	32.4x	$1	$1	$1
Other (including acquisitions)	$0.09	9.9%	0.0x	29.4x	30.4x	31.4x	$3	$3	$3
Water utilities total (ex-Peoples)	$1.17			*31.2x*	*32.2x*	*33.2x*	$37	$38	$39
Gas Utilities									
Peer Gas P/E		*19.6x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		20.7x							
	2022E EPS	ROE	embedded						
Peoples Gas	$0.77	13.5%	2.0x	21.7x	22.7x	23.7x	$17	$17	$18
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			-811	50%			($406)	($406)	($406)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($402)	($371)	($433)
50/50 Weighted Drag from HoldCo Drag							($808)	($777)	($839)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							$50.00	$52.00	$54.00
Current Price								$50.57	
Dividend Yield								2%	
Total Return								4.65%	

Source: BofA Global Research, Bloomberg

Price objective basis & risk

Aqua America (WTR)
Our price objective is $52 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 2.0x premium to Peoples Gas given the organic growth opportunities.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Risks to the upside include upward revisions to street estimates and further accretion from implementation of the Repairs Tax Benefit

Analyst Certification

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North American Utilities, Alternative Energy & LNG Coverage Cluster

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	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
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	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
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	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	AES	AES	AES US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Aqua America	WTR	WTR US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
RSTR				

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith
	Pattern Energy Group	PEGI	PEGI US	Julien Dumoulin-Smith

iQmethod℠ **Measures Definitions**

Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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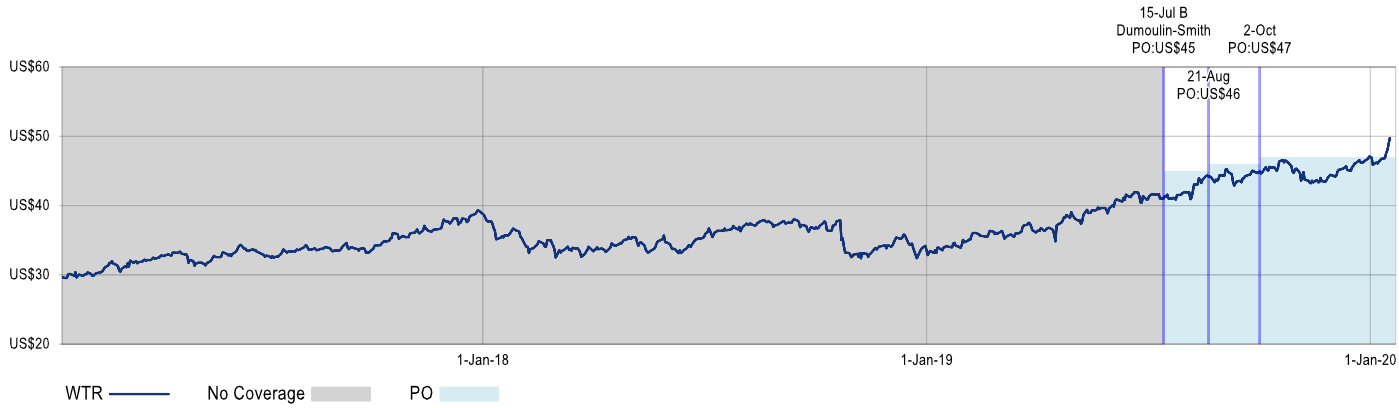
Aqua America (WTR) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Utilities Group (as of 31 Dec 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	63	44.06%	Buy	44	69.84%
Hold	43	30.07%	Hold	31	72.09%
Sell	37	25.87%	Sell	27	72.97%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1560	50.49%	Buy	991	63.53%
Hold	717	23.20%	Hold	461	64.30%
Sell	813	26.31%	Sell	415	51.05%

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Underperform	N/A	≥ 20%

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North American Utilities & IPPs

1Q20 Regulated Utility Preview: Who is key in COVID resiliency?

Price Objective Change

20 April 2020

Equity
North America
Utilities & IPPs

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Prospects for 1Q20: COVID, oil prices and mild weather

We present our 1Q20 regulated preview including LNT, AEE, AEP, AWK, ED, DTE, DUK, EIX, ETR, WTRG, EVRG, ES, FE, PNW, PPL, WEC, and XEL. Overall, we see the sector splitting into stocks well-suited to weather the storm that started in 1Q – and those that are less equipped. Key factors that distinguish between these include: Having decoupling and/or bad debt trackers to balance out decreases in demand from COVID, oil price, and mild weather pressures (**ES**, **ED**, **WEC**); revenues with a heftier reliance on resi or fixed-charges vs industrial or volumetric (**FE**, **AWK**, **WTRG**) strong FFO/debt metrics (**AEE**); and having room in original 2020 O&M projections for more savings given these pressures (both **LNT** and **XEL** had factored in increases YoY). We have updated our models and made a number of changes to our ests and POs using a 17.6x peer multiple for both electric and gas.

Key company views for 1Q

For 1Q, we expect **EIX** mgmt. to focus on wildfire mitigation execution as well as decoupling/other constructive regulatory mechanisms to offset COVID related pressures; focus remains on the equity overhang where mgmt. is likely to delay its '20 issuance into 2H - *'20* equity addresses mgmt.'s current expectations for wildfire related liabilities and timely recovery of memo accounts ($1.09bn in aggregate); we believe clarity on these outcome remain protracted and uncertain at best. For **DUK**, we see a weak 1Q with weather related headwinds; expect mgmt. to talk-up cost reductions up to $150mn to offset COVID related pressures (3-5% decline in load?); rate case risks in Carolinas remain with ROE and coal ash to be litigated with still wide bid-ask. Resi compositions of **AWK** and **WTRG** should help limit load degradation, they are largely not decoupled. LT, we would expect tailwinds for further industry consolidation as muni's face add'l budget pressure and see both base capital plans as intact over the forecast period with upside from tuck-ins. While **PPL** is decoupled in the UK, we stress a year two lag before true up and see the company as particularly exposed to load degradation in KY as near term rate relief seems less likely given the current rate paradigm and international crisis (albeit plans for timing not totally clear). UK risks appear to be improving but watch govt reactions to Covid on biz response. On top of O&M room (with -8c YoY), we see **LNT**'s Wisconsin regulatory env, confidence in getting renewables online (w/ two of four already commissioned), and credit metrics ($1.17bn of available liquidity) as strengths. **XEL** too could have more O&M savings and push out rate cases expected this year depending on if spend can be tracked. **AEP** is sensitive given it already factors in significant O&M savings in 2020 guide, but the company has noted it could bend the curve further to mitigate demand impacts from COVID and oil prices; some reprieve at Indiana (still underway) and confidence on North Central have us remain at Buy. **FE** is expected to have a quiet quarter as the Street awaits updates of the the New Jersey rate cases; the rest of the year is quiet on the reg front (a pos). For **AEE** we look for any sign of accelerated coal retirement given this fall's integrated resource plan (IRP) but note federal coal quality regulations have been eased of late. Finally, **ES** may start to give a (further) sense of incremental grid mod spend and is largely one of the lease impacted companies as it is almost fully decoupled. **Click for our other previews: SMID-cap (PacNW), SMID-cap (rest of country), PEG & EXC, AGR & NEE, Gas LDCs and Other Diversifieds**

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1Q Summary and PO Changes

We include a brief summary of our 1Q estimates compared vs Street as well as PO changes reflected in this report.

Table 1: PO Changes

Company	Ticker	New PO	Old PO
Alliant Energy Corp	LNT	$56.00	$58.00
Ameren Corp.	AEE	$85.00	$80.00
American Electric Power, Inc	AEP	$93.00	$89.00
American Water	AWK	$133.00	$128.00
Consolidated Edison	ED	$93.00	$100.00
DTE Energy Co.	DTE	$112.00	$116.00
Duke Energy	DUK	$93.00	$93.00
Edison International	EIX	$69.00	$61.00
Entergy Corp.	ETR	$122.00	$108.00
Essential Utilities	WTRG	$47.00	$50.00
Evergy, Inc	EVRG	$69.00	$70.00
Eversource Energy	ES	$83.00	$93.00
FirstEnergy Corp.	FE	$47.00	$47.00
Pinnacle West Capital Co.	PNW	$84.00	$105.00
PPL Corporation	PPL	$29.00	$36.00
WEC Energy Group Inc.	WEC	$85.00	$95.00
Xcel Energy Inc.	XEL	$66.00	$70.00

Source: BofA Global Research

Table 2: 1Q Estimate Summary: only significant beat remains Sempra

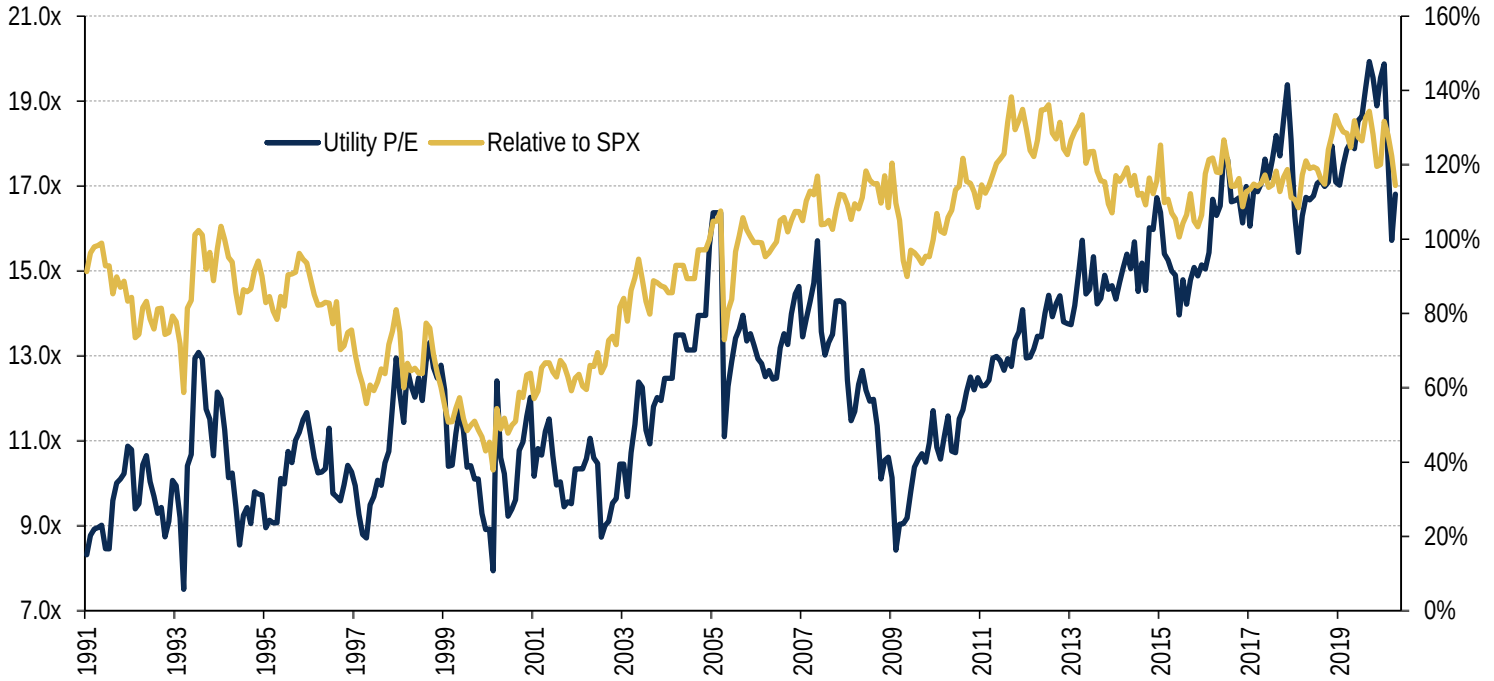
Diversified		1Q20 - BofAe	1Q20 - Cons	Delta
Avangrid Inc.	AGR	$0.71	$0.76	-7%
CenterPoint Energy Inc	CNP	$0.47	$0.46	2%
Dominion Resources	D	$1.11	$1.13	-2%
Exelon Corp.	EXC	$0.86	$0.85	1%
NextEra Energy	NEE	$2.24	$2.20	2%
Public Service Enterprise Group	PEG	$1.05	$1.06	-1%
Sempra Energy	SRE	$2.35	$1.97	19%
Southern Company	SO	$0.72	$0.73	-1%
Regulated		1Q20 - BofAe	1Q20 - Cons	Delta
Alliant Energy Corp	LNT	$0.55	$0.55	0%
Ameren Corp.	AEE	$0.67	$0.73	-8%
American Electric Power, Inc	AEP	$1.03	$1.15	-10%
American Water	AWK	$0.67	$0.67	0%
Consolidated Edison	ED	$1.33	$1.41	-6%
DTE Energy Co.	DTE	$1.80	$1.93	-7%
Duke Energy	DUK	$1.14	$1.23	-7%
Edison International	EIX	$0.81	$0.84	-4%
Entergy Corp.	ETR	$1.01	$1.01	0%
Essential Utilities	WTRG	$0.61	$0.58	5%
Evergy, Inc	EVRG	$0.40	$0.47	-15%
Eversource Energy	ES	$1.02	$1.02	0%
FirstEnergy Corp.	FE	$0.62	$0.63	-2%
Pinnacle West Capital Co.	PNW	$0.15	$0.16	-6%
PPL Corporation	PPL	$0.73	$0.72	1%
WEC Energy Group Inc.	WEC	$1.32	$1.32	0%
Xcel Energy Inc.	XEL	$0.53	$0.62	-15%
SMID		1Q20 - BofAe	1Q20 - Cons	Delta
Avista Corp	AVA	$0.62	$0.63	-2%
Black Hills Corp	BKH	$1.60	$1.66	-4%
CMS Energy	CMS	$0.79	$0.86	-8%
Hawaiian Electric Industries	HE	$0.42	$0.45	-7%
Idacorp, Inc	IDA	$0.77	$0.81	-5%
NorthWestern Corp	NWE	$1.23	$1.27	-3%
OGE Energy Corp	OGE	$0.18	$0.21	-14%
PNM Resources	PNM	$0.18	$0.36	-50%
Portland General Electric Company	POR	$0.90	$0.90	0%
Unitil Corp	UTL	$0.93	$1.05	-11%

Source: BofA Global Research, FactSet

Macro Backdrop

We believe investors are generally skeptical of current sector valuations – and see the continued upward trajectory of the sector as still showing an expensive backdrop from a high level perspective. The chart below shows the latest mark-to-market of the group on an absolute basis and against the SPX; utilities are now trading below their all-time highs on both a relative and absolute basis.

Chart 1: Utility PE vs SPX

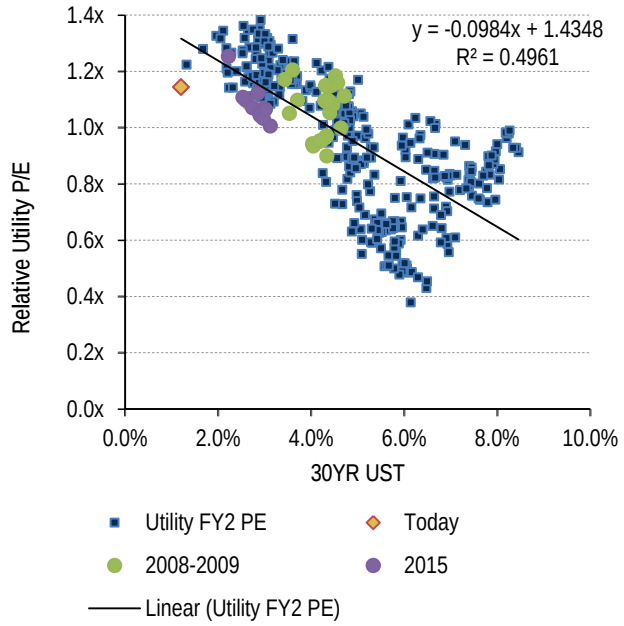


Source: BofA Global Research Estimates, company report, Bloomberg

When adjusting for the S&P itself *and* the treasury environment: different story

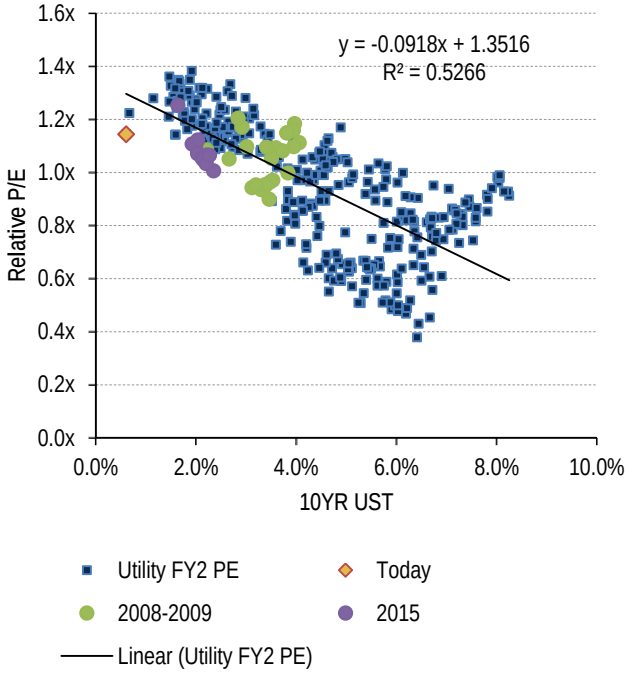
In the exhibits below, we show a time series of where the sector has traded relative to the linear regression on a relative and absolute basis for Treasuries to illustrate the premium; the group has started to trade more in line with its historical linear relationship with 10Yr and 30 Yr Treasuries on a relative basis and could argue somewhat cheap vs historical relationships.

Chart 2: Relative Utility PE vs. 30 YR UST



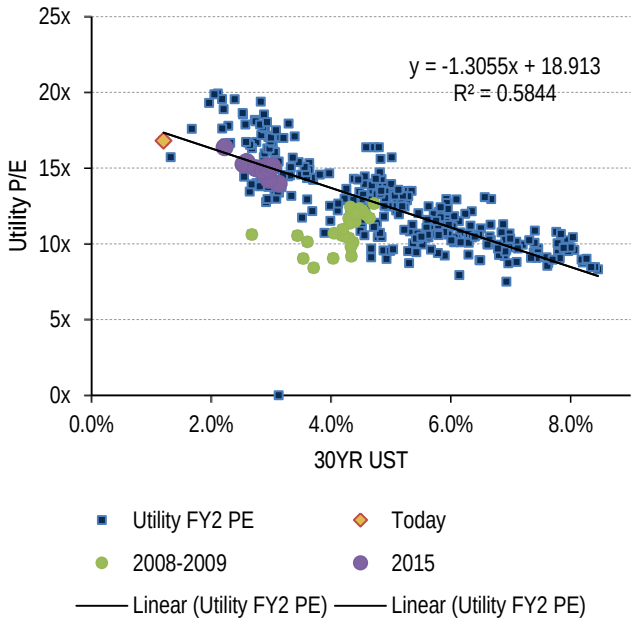
Source: BofA Global Research, Bloomberg

Chart 3: Relative Utility PE vs. 10 YR UST



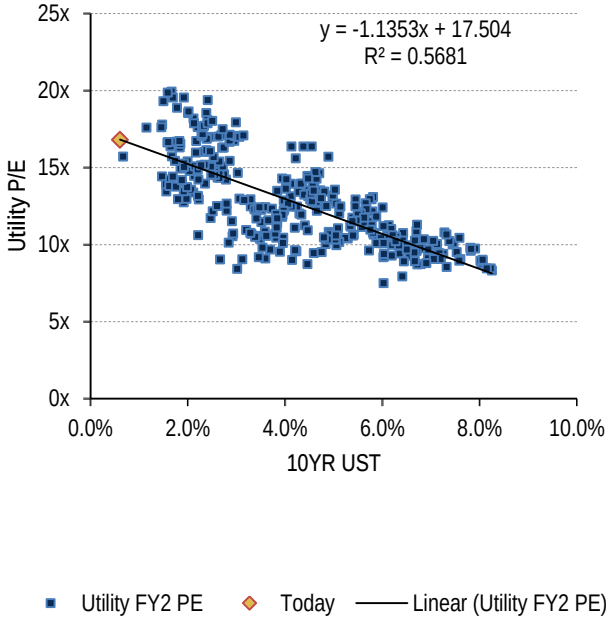
Source: BofA Global Research, Bloomberg

Chart 4: Absolute Utility PE vs. 30 YR UST



Source: BofA Global Research, Bloomberg

Chart 5: Absolute Utility PE vs. 10 YR UST

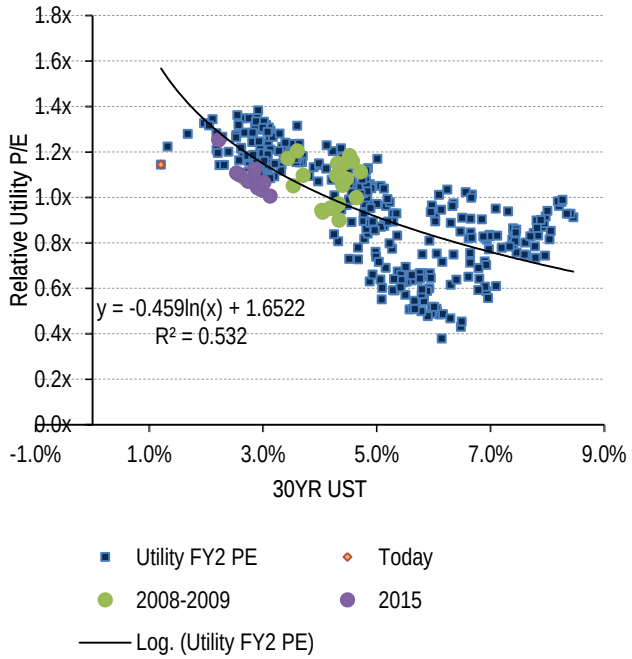


Source: BofA Global Research, Bloomberg

Non-linear makes more sense to us...

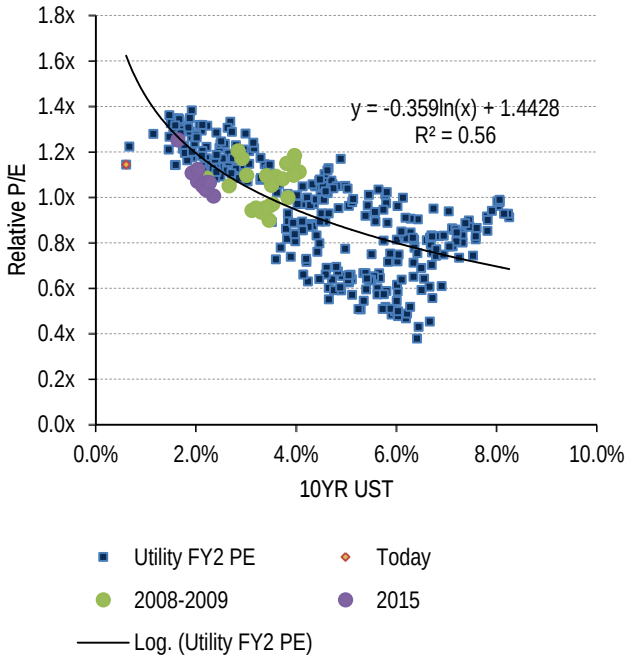
We provide the non-linear relationship below as well given the greater percent change on valuations for every 1% move. We emphasize the limited shift in authorized returns through the cycle also argues that value creation should accelerate with rates declining too. On this basis, the sector looks much less expensive.

Chart 6: Relative Utility PE vs. 30 YR UST



Source: BofA Global Research, Bloomberg

Chart 7: Relative Utility PE vs. 10 YR UST



Source: BofA Global Research, Bloomberg

Alliant (LNT)

We reiterate our Buy going into the 1Q20 call. We adjust down '20 and '21 ests -2c to reflect potential demand impacts from COVID, oil, and 1Q weather – balanced by our expectation that LNT has room for O&M savings as -8c YoY is included in the co's original '20 ests. This takes into account the co's recently disclosed electric sales sensitivity (1% change correlates with an EPS impact of 2c for resi, 1c for industrial, and 1c for commercial), the forecast of 1% sales increasing this yr, and the class breakdown ('19 margins 46% resi, 28% commercial, 26% industrial – with 30-40% of industrial demand fixed, and a hefty chunk agriculture focused that we see as more resilient). We see the company as having stronger credit metrics as well, with $1.17bn of available liquidity as of April 2, 2020. Also recall LNT executed on equity in March. We see other positives for the company including its regulatory relationship in Wisconsin (having deferral of bad debts approved), its ongoing renewable deliveries for the two wind projects to commission in 3Q-4Q (two already commissioned in 1Q), and West Riverside to commission next quarter. Finally, we anticipate the company discusses its forthcoming Wisconsin rate case and solar case. We forecast a 1Q20 estimate of $0.55/sh (the same as Consensus).

LNT 1Q20 Walk

Below we forecast a $0.55/sh 1Q20 EPS, compared to a $0.55/sh Consensus and a $0.53/sh 1Q19 EPS the prior year.

- **Drivers**: We expect about +19c of benefits from the IPL Gas and Electric base rate increases and WPL Electric's as well.
- **Other**: We expect a few of the drivers that LNT provided in its 2020 annual walk (e.g. depreciation, AFUDC, interest expense, other expenses) will be weighted to later quarters, meaning less of an impact of 1Q. Note LNT also has some equity dilution.
- **Wildcard**: As for most companies, the mild winter was noticeable for LNT. We note that 1Q19 saw a +5c benefit (to be reversed now) associated with 800 heating degree days more than average; as such, we expect a -3c hurt in 1Q20 from the mild winter that was 500 days below average. COVID shouldn't impact LNT in a big way yet, since stay at home started mid-March; we expect that the leap day benefit largely counter-balances demand impact since LNT doesn't have decoupling.

Table 3: LNT 1Q20 walk

1Q20 EPS Walk	Notes	EPS Impact
1Q19 Starting Point		$0.53
Weather impact 1Q19	*Had positive*	($0.05)
Weather impact 1Q20	*Very mild*	($0.03)
IPL Base rate increase	*IPL Electric effective 1/8/20; IPL Gas effective 12/18/19*	$0.10
WPL Electric	*New rates at WPL*	$0.09
Depreciation	*-$0.18/sh for full year; weighted more heavily later in yr*	($0.03)
AFUDC increases	*-$0.13/sh for full year*	($0.02)
Other items / O&M / ATC	*-$0.08/sh for full year*	($0.02)
Int Expense	*Debt issuance at WPL and IPL - less neg impact: some was later / intr rates better*	($0.01)
COVID	*Stay at home mid-March balanced by leap yr extra day*	$0.00
Dilution	*Incremental equity dilution*	($0.02)
1Q20 EPS		$0.55
Consensus		$0.55
2020 EPS		$2.44
2020 Consensus EPS		$2.41
2020 Guidance		2.34-2.48
1Q19 Sharecount		237
1Q20 Sharecount		245

Source: BofA Global Research estimates, company report, Bloomberg

Items to track going into 1Q20 call

Key COVID considerations

- **Retail electric margins and sensitivities**: LNT provided sales sensitivities in early April, indicating that a +1% change in electric sales in '20 correlates with a $0.02/sh resi impact, a $0.01/sh commercial impact, and a $0.01/sh industrial impact. It also shared that its 2019 retail electric margins were split such that 46% were resi, 28% commercial, and 26% industrial. Also importantly, LNT acknowledged that 40% of Iowa and 30% of Wisconsin C&I margins are demand-based charges.

- **Diverse industrial customers not all equally impacted**: LNT has a number of C&I customer types, diversifying demand impact. In Iowa, customers are particularly focused on food/agriculture – as well as some chemicals, and manufacturing. In Wisconsin, customers are focused on metals, chemicals, petroleum and plastics (i.e. biofuels), and food. We expect that ethanol has of course been pressured by oil and gas prices, but note that electric demand from farmers should still stays strong as it is too soon to decrease long-term food demand expectations (which would require decisions now to plant less crops for a lower yield this fall).

- **Not decoupled (*for now*) *but* Wisconsin grants bad debt mechanism**: LNT is not decoupled and in its original 2020 guidance expected about 1% sales growth; this included the leap year and industrial customers with operational issues in '19 coming back to normal in '20. Importantly, we see Wisconsin as a positive regulatory environment for LNT, particularly as the state regulators recently approved deferral of bad debts above the revenue requirement. We highlight that the state is evaluating how to proceed with impacts to demand, and we look for future commentary around decoupling in the future.

- **Space for more O&M cuts**: LNT has some room in its earnings for more O&M savings, particularly as it baked in -$0.08/sh YoY in its annual 2020 walk. We expect that the company has some leverage to increase O&M savings in 2020 making the company more resilient to COVID impacts.

- **We expect more demand data to come**: LNT has real-time demand data for resi and commercial customers since AMI exists in both WI & IA, but LNT has about a month lag for industrial data given the meter technology. We expect LNT to provide more customer class-specific impacts from COVID on demand during the 1Q call.

Wisconsin

- **Rate case**: LNT is still analyzing how to file its Wisconsin rate case during this sensitive time, such that it is mindful of its customers during the economic hardship COVID presents to many. We expect to hear more details on requests on the call.

- **Solar filing**: LNT continues to plan to file for about half of its targeted 1Q solar build in 2Q. The company is wrapping up development activity since Wisconsin requires exact sites pre-filing (Iowa allows the site to be named after). While details might be ready on the 1Q call, some more details might come after.

- **West Riverside Energy Center**: LNT's 730MW gas plant is still expected to commission next quarter (2Q20).

Iowa

- **Renewables on schedule**: Amidst the rush to commission wind by year-end to effortlessly qualify for the production tax credit (PTC), LNT is in good shape. Two IPL projects are already in service (201MW Whispering Willow North, and 200MW Golden Plains), and the remaining 130MW Richland project (expected in service 3Q20) is currently receiving timely equipment deliveries. This on time delivery applies for the Wisconsin wind farm too (150MW Kossuth expected in service 4Q20)

- **Multi-year cases**: We still think there's a potential for multi-year cases in the future, but doubt this will take up much of the conversation on the 1Q call.

Estimates

We include our latest EPS estimates and ROEs below by subsidiary. We tweak down our estimates by a few pennies in '20 and '21 to reflect how LNT is not decoupled and could see EPS impacts from lower demand – but with our expectation the company has some ability to ramp up O&M cuts. We are at the middle of the 5-7% guidance range for LNT looking at '18-'23 CAGR.

Table 4: LNT EPS Estimates

EPS by Segment	2017A	2018A	2019E	2020E	2021E	2022E	2023E
IPL	$0.94	$1.13	$1.19	$1.41	$1.47	$1.56	$1.58
WPL	$0.80	$0.89	$0.97	$0.98	$1.05	$1.11	$1.19
ATC	$0.11	$0.13	$0.13	$0.13	$0.14	$0.14	$0.15
Parent/Other	$0.09	$0.02	$0.01	-$0.08	-$0.08	-$0.07	-$0.07
Total	$1.93	$2.17	$2.31	$2.44	$2.59	$2.74	$2.85
Prior Estimates	$1.93	$2.17	$2.31	$2.46	$2.61	$2.74	$2.85
EPS Guidance							
IPL +WPL		*2.04 - 2.07*	*2.21 -2.23*				
ATC		*0.10 - 0.12*	*0.11 - 1.13*				
Parent/Other		*(0.01) - 0.00*	*(0.05) - (0.03)*				
Guidance	$1.89-$1.97	$2.13-$2.19	2.27-2.33	2.34-2.48			
Non-GAAP EPS Growth Off $2.26 in '19 (5-7%)				7.94%	6.97%	6.67%	5.96%
Consensus	$1.95	$2.16	$2.30	$2.41	$2.58	$2.72	$2.84
Consensus CAGR					6.88%		
Mid				$2.41	$2.56	$2.71	$2.87
High				$2.48	$2.65	$2.84	$3.04
Low				$2.34	$2.46	$2.58	$2.71
Model Embedded ROEs / Equity	2017A	2018A	2019E	2020E	2021E	2022E	2023E
IPL							
Regulatory ROE (Avg)	9.2%	9.8%	9.0%	9.2%	9.4%	9.7%	10.0%
GAAP ROE (AVG)	8.4%	8.9%	8.5%	9.6%	9.5%	9.6%	9.3%
WPL							
Regulatory ROE (Avg)	10.5%	10.1%	10.1%	9.9%	9.9%	9.6%	9.7%
GAAP ROE (AVG)	10.1%	10.3%	10.3%	9.9%	10.4%	10.7%	11.1%
ATC							
Earned ROE	10.5%	10.8%	10.5%	10.2%	10.2%	10.2%	10.2%

Source: BofA Global Research estimates, company report, Bloomberg

Valuation

We update the peer multiple to 17.6x for electric and update our WPL peer multiple to 3x (prev 2x) to reflect the regulatory ability to defer bad debt. We reiterate Buy with a $56/sh PO.

Table 5: LNT SOTP Valuation

2022E SotP Analysis - BofAe										
All figures in USD millions except per share										
Regulated Utilities	2022E Net Income	EPS	P/E Multiple					Equity Value		
			Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric			-	17.6x	-	-	-	-	-	-
Group EPS '18-'22 CAGR - Electric			-	5.00%	-	-	-	-	-	-
			-	-	-	-	-	-	-	-
Relative Utility Group P/E Multiple				18.5x						
IPL	$385	$1.56	19.5x	18.5x	2.0x	20.5x	21.5x	$7,500	$7,885	$8,270
WPL	$275	$1.11	20.5x	18.5x	3.0x	21.5x	22.5x	$5,636	$5,911	$6,186
ATC (LNT Share)	$36	$0.14	19.5x	18.5x	2.0x	20.5x	21.5x	$697	$732	$768
EPS (w/o Parent)	$696	$2.82						$13,832	$14,528	$15,224
Parent NI	-$18	-$0.07	18.5x	18.5x	1.0x	19.5x	20.5x	($330)	($348)	($366)
Add Back: Parent Interest Exp	$14	$0.06	18.5x	18.5x	1.0x	19.5x	20.5x	$252	$133	$279
Less: Parent Debt (Term Loan AEF)					*50% weighting*			($500)	($500)	($500)
								($578)	($715)	($587)
Total Implied			19.5x			20.4x	21.6x	$13,254	$13,813	$14,637
Shares Outstanding (2022E)								247	247	247
Total Equity Value Per Share								$54.00	$56.00	$59.00
Total Return Analysis										
Current Share Price									$51.61	
Price Objective									$56.00	
Implied Return									8.51%	
Dividend Yield									2.75%	
Total Return									11.26%	

Source: BofA Global Research estimates, company report, Bloomberg

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Alliant Energy Corporation: Our favorite defensive utility idea	Julien Dumoulin-Smith	11 March 2020
Alliant Energy Corporation: Watching the solar front with carbon goal announcements later this yr; reiterate Buy	Julien Dumoulin-Smith	25 February 2020
Alliant Energy Corporation: Constructive update with more strength ahead: Raise EPS & Reiterate Buy	Julien Dumoulin-Smith	08 November 2019
Alliant Energy Corporation: Iowa resolution, financing updates, and spend all coming up; Maintain Buy	Julien Dumoulin-Smith	05 August 2019

Ameren (AEE)

Our latest EPS projections of $3.43/sh (vs '20 guidance of $3.40-3.60/sh) factor in lower 30-year Treasury assumptions starting at 1.5% in 2020, a lower base ROE for FERC jurisdiction (10.38% with 50bps adder), and our expectation that there is room for cost savings since AEE in its 2020 guidance acknowledged O&M would be increasing at Missouri and Illinois Gas (the exact amount not disclosed). We note that AEE is decoupled in IL, which we think will be a clear benefit; note this leaves about ½ of ratebase (in MO) not decoupled. Although more exposed in MO, we view the company's low portion of industrial energy demand as a positive as well (class break down: 50% margins resi, 40% commercial, 10% industrial), and note that impact of commercial demand is typically more protracted given many billing cycles are 12-month trailing. More specifically, we would expect O&M savings balance out MO commercial sales impact for '20. This still leaves us at ~7% for '20-24 EPS CAGR. Outside of COVID and demand, we expect 1Q commentary to highlight the strong pipeline opportunities the company has outside of its five-year and ten-year capex projections. We specifically watch for any hinting toward potential accelerated retirement of unscrubbed coal, but note that with the outstanding 8th Circuit Case on EPA regulations and lack of securitization legislation will indicate a later update here. Finally, we note the company has strong FFO/debt metrics that sets it apart from peers. As for 1Q20, we expect a $0.67/sh quarter impacted by mild winter, limited COVID impact on demand (due to shoulder month), and lower energy efficiency benefits. Maintain Buy.

1Q20 Walk

We expect a $0.67/sh 1Q20 estimate, versus a Consensus of $0.74/sh and a prior year's 1Q19 est of $0.78/sh.

- **Drivers**: We expect the 1Q result of the Treasury will bring down Illinois Electric ROEs by -2c; this is largely counteracted by ratebase growth (balancing ROE revisions) in IL Electric, IL Growth, and Transmission (+2c).

- **Other**: Note that 1Q19 included $0.03/sh of weather and $0.06/sh of energy efficiency that need to be backed out. The 2019 spring Callaway outage mostly impacted 2Q19, and new rates in AEE Missouri will be a 2Q20 item as well. The company benefited from two refi's in 2019: One March 6th that replaced a $329mn 6.7% with a 450mn 3.5%, and one Oct 1st that replaced a $244mn 5.10% with a $330 3.25%. Lower tax benefits with share-base comp usually benefits 1Q (+3c) and dilution from the $100mn drip is nearly flat.

- **Wildcard**: We see 1Q20 as a mild winter. Looking at heating degree days (HDD) of 2019 and 2020 versus the 10-year average (2009-2018) in Saint Louis, we find 236 more days in 1Q19 and 202 less days in 1Q20. As 1Q19 benefited AEE by +3c, we adjust 1Q19 by -3c. O&M will be another wildcard: We factor in -1c compared to 2019. Finally, COVID impacts on demand are unknown but likely limited in 1Q given the shoulder month it would have impacted (i.e. March).

Table 6: AEE 1Q20 Walk

Ameren 1Q20 Earnings Walk	Notes	EPS
1Q19 EPS		$0.78
Return to normal weather	Cold	($0.03)
1Q20 weather impact	Mild	($0.03)
AEE Illinois		
IL Electric	2019 Average 30 YR UST was 2.58% vs. Current @ 1.368%	($0.02)
IL Gas		$0.01
IL Transmission/Dist./ATXI	Ratebase growth largely balanced by ROE change	$0.01
AEE Missouri		
New Rates	Effective 2Q20	$0.00
Callaway refueling	Roughly 9c for 2019, mostly in 2Q	$0.01
PISA Benefit	Depreciation exp and int exp typically balance out	$0.00
MEEIA Benefits	Lower energy efficiency performance incentive (-11c for 2019)	($0.06)
O&M, Other	Higher O&M over the year (no guide yet)	($0.01)
Interest Refinancings	Two 2019 refi's (March & Oct)	$0.01
Parent Company income tax exp	2020 lower tax benefits w/ share-base comp (3c in 2020 all 1Q)	$0.03
Dilution	Dividend reinvestment plan and employees - $100Mn/yr	($0.00)
COVID	Reduced demand (1Q shoulder months)	($0.01)

Table 6: AEE 1Q20 Walk

Ameren 1Q20 Earnings Walk	Notes	EPS
Other	Donations at AEE Parent more in line w/ normal level, some for COVID	$0.00
1Q20 BofA Adjusted EPS		$0.67
1Q20 BofA Modeled EPS		$0.67
1Q20 Consensus		$0.74
BofA 2020E EPS		$3.43
2020 Consensus		$3.46
1Q19 Shares outstanding		246
1Q20 Shares outstanding		248

Source: BofA Global Research estimates, company report, Bloomberg

Key considerations

We see AEE as well suited to recover on the rebound more than peers.

- **Strong growth yet to come**: AEE showed its growth strength at 4Q19 when it added $3bn to its five-year capex & disclosed a substantial 10-year $36bn runway of 'business as usual' investments. We perceive some slight risks to further acceleration previously contemplated this Fall with IRP update, but overall see among the best positioned longer-term ratebase growth stories. Bottom line we see capex backdorp as securing EPS growth of the 7-8% range (with DPS growth that should beat that given the lower payout ratio), but it will help AEE achieve of on the best 'rate of change' ESG stories in the sector to come. We acknowledge potential pressures on ’20 EPS guide from 30-year treasuries in tandem.

- **Potential accelerated coal retirements & rate-based replacements**: We note AEE might have the opportunity to accelerate its ratebase plan this fall with is integrated resource plan (IRP) filing. Note, though, that actual timing of MO coal retirement could depend on securitization legislation (in '21) as well as Sept resource filing: both key upsides on capex.

- **Illinois is likely later-dated**: While AEE might have upside via more renewables in IL, an extension of formula rates in IL at a higher auth ROE, and more transmission projects, it will likely be a challenge this year. We expect social distancing makes getting to all legislative decisions in the May session difficult, and we could see other issues fill up the November veto session as well. Based on our latest industry conversations, we are expecting a little more difficulty for a broad energy reform involving nukes in the near-term – and could see further out legislation that includes more folks (e.g. labor, environmental) in the future with perhaps more modest gains for utilities (e.g. just formula rates rather than ratebasing renewables).

- **Good balance sheet**: Finally, it would be remiss to ignore AEE's stronger FFO/debt metrics, with projected 19.2% in '19-'25 vs. credit rating 17% min and regulated avg of 16.5% (& larger caps even lower).

- **COVID impact**: AEE in the near-term faces a lower COVID impact given seasonality (i.e. shoulder months limit heating/cooling) and given half of its rate base has limited exposure (i.e. IL electric has full decoupling; IL gas has full decoupling for resi & small commercial & a bad debt expense tracker). AEE faces exposure in MO outside of its energy efficiency mechanism; with 50% of margins resi, 40% commercial, and 10% industrial, increase in resi may offset some drop in commercial but with billing cycles this will likely impact '21 as well.

Estimates

Our estimates remain largely the same as we already adjusted down our EPS expectations for ’20 and beyond given COVID impact on demand (no decoupling in MO) as well as lowered IL ROEs given where 30-year Treasuries have fared thus far. We continue to expect a 1.5% +580bps IL Electric earned ROE.

Table 7: AEE EPS Estimates: towards the bottom end of '20 with risk it could drop below; our focus remains on longer-term compounding outlook

Consolidated EPS Projections	2016A	2017A	2018A	2019E	2020E	2021E	2022E	2023E	2024E	2025E	Segment CAGR ('20-'24)
Ameren Missouri	$1.48	$1.48	$1.94	$1.72	$1.89	$2.04	$2.15	$2.28	$2.41	$2.49	6.26%
Ameren Illinois	$1.05	$1.10	$1.25	$1.39	$1.34	$1.46	$1.64	$1.80	$2.01	$2.22	10.58%
ATXI	$0.23	$0.27	$0.31	$0.32	$0.32	$0.31	$0.30	$0.29	$0.28	$0.28	-2.92%
Other	-$0.07	-$0.02	-$0.13	-$0.09	-$0.12	-$0.12	-$0.11	-$0.11	-$0.11	-$0.11	
Total EPS	$2.68	$2.83	$3.37	$3.35	$3.43	$3.69	$3.97	$4.26	$4.59	$4.88	7.03%
Guidance		*$2.70 - $2.90*	*$3.35-3.45*		*$3.40-3.60*						
EPS CAGR off 2018 ($3.05)				9.86%	6.11%	6.51%	6.83%	6.90%	7.06%	6.95%	
EPS CAGR off 2020 ($3.50)						5.30%	6.54%	6.76%	7.03%	6.88%	
YoY Growth		5.39%	19.14%	-0.53%	2.49%	7.31%	7.80%	7.19%	7.83%	6.29%	
Prior Estimates	*2.68*	*2.83*	*3.37*	*3.35*	*3.43*	*3.69*	*3.97*	*4.26*	*4.59*	*4.88*	
Consensus		$3.46	$3.40	$3.29	$3.46	$3.76	$4.03	$4.30	$4.46		6.25%
Average Earned ROE (Auth in parenthesis)											
Missouri (Auth: electric 9.4-9.8%, gas 9.4-9.95%)		9.5%	12.2%	10.3%	10.0%	9.7%	9.7%	9.8%	10.0%	9.9%	
Illinois (Auth: electric 580bps + 30yr T, gas 9.87%)		9.9%	10.0%	10.0%	8.8%	9.0%	9.2%	9.2%	9.4%	9.5%	
BofA 30-yr Treasury assumption					*1.50%*	*1.75%*	*2.00%*	*2.25%*	*2.50%*	*2.75%*	
ATXI (9.88% plus 50bps adder)		10.82%	10.82%	10.82%	10.38%	10.38%	10.38%	10.38%	10.38%	10.38%	
Consolidated FFO/Debt			23.8%	20.9%	18.1%	18.5%	18.5%	18.7%	19.1%	19.4%	
Guidance (6-8% '18-'23 off of $3.05) --> *Midpoint*				$3.26	$3.49	$3.74	$4.00	$4.28			
Low Implied				$3.23	$3.43	$3.63	$3.85	$4.08			
High Implied				$3.29	$3.56	$3.84	$4.15	$4.48			
Guidance (6-8% '20-'24 off of $3.50) --> *Midpoint*					$3.50	$3.75	$4.01	$4.29	$4.59	$4.91	
Low Implied					$3.50	$3.71	$3.93	$4.17	$4.42	$4.68	
High Implied					$3.50	$3.78	$4.08	$4.41	$4.76	$5.14	

Source: BofA Global Research estimates, company report, Bloomberg

Valuation

We MtM the peer multiple (now 17.6x) and come to a price objective of $85/sh using the same 3x premiums at Missouri and Illinois (not transmission or parent). We reiterate our Buy rating.

Table 8: AEE SOTP Valuation

Ameren Sum of the Parts Valuation - 2022E BofA

All figures in $Mn except per share

Regulated Utilities	2022E EPS	P/E Multiple					Equity Value		
		Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric			17.6x	-	-	-	-	-	-
Group EPS '18-'22 CAGR - Electric			5.00%	-	-	-	-	-	-
				-	-	-	-	-	-
			18.5x	-	-	-	-	-	-
Ameren Missouri	$2.15	20.5x		3.0x	21.5x	22.5x	$44.02	$46.17	$48.32
Ameren Illinois	$1.64	20.5x		3.0x	21.5x	22.5x	$33.56	$35.20	$36.84
Ameren Transmission (ATXI)	$0.30	17.5x		0.0x	18.5x	19.5x	$5.22	$5.52	$5.81
Parent/Unallocated Items	-$0.11	17.5x		0.0x	18.5x	19.5x	-$1.99	-$2.11	-$2.22
Total Implied Utilities	$3.97						$80.81	$84.78	$88.76
Shares outstanding	262								
Implied P/E		21.4x							
Valuation							$81.00	$85.00	$89.00
BofAe Implied Multiple								21.4x	
Current Price								$77.83	
PO								$85.00	
Upside/Downside								9.21%	
NTM Dividend Yield								2.54%	
Total Return								11.76%	

Source: BofA Global Research estimates, company report, Bloomberg

American Electric Power (AEP)

We see the 1Q20 call quite important as it will set the stage for FY20 guidance. It is clear AEP will be negatively impacted by very mild winter as it is not fully decoupled (we factor in -10c for 1Q20 given an even more mild winter than 1Q17, which was -8c YoY). Shares remain among the most controversial of large-cap peers. On top of this, we expect AEP to face lower electric demand from low oil prices' impact on industrial customers (O&G represent 30% of this class) as well as its outcome of its pending Indiana rehearing request. Even so, AEP has been clear that even though it already factors in 'bending the curve' O&M cost cuts, it could factor in more later this year to balance out some of these impacts. The degree to which is so far unclear, so we await commentary to provide a sense. We weigh in the full North Central Wind into our valuation as we see it proceeding forward in key states, but look for any commentary on financing the project (if the asset rotation is possible to pay for the equity check). Upside includes repowering opportunities from the SRE portfolio. We reiterate Buy at a $93/sh PO with an updated peer multiple of 17.6x. Finally, we forecast $1.03/sh for 1Q20 EPS – lower than a $1.15/sh Consensus and 1Q19 results of $1.19/sh.

1Q20 AEP EPS Walk

We estimate EPS of $1.03/sh for 1Q20. This compares to Consensus of $1.15/sh and last year's 1Q19 EPS of $1.19/sh.

- **Drivers**: Apart from weather, 1Q will be driven by a -9c Ohio regulatory provision, YoY wholesale rate changes (+6c for wholesale with Michigan going into effect in February, West Virginia, Arkansas, and Oklahoma last year), and some improvements in O&M (although many are planned for later this year)

- **Other**: A number of 2020 full year walk items are weighted heavier towards other quarters. This includes the -10c for 2020 wholesale load (mostly in 2-3Q), +19c for 2020 O&M (mostly after 1Q), -3c Texas carrying charges (a 2Q item), and a -9c Transmission HoldCo true-up (a 2Q item).

- **Wildcard**: The mild weather will likely account for around -10c YoY for 1Q given that a slightly less mild winter in 1Q17 represented -8c YoY. Note that AEP also has a +1c to return to normal from 1Q19.

Table 9: AEP 1Q20 EPS Walk: street still a bit too high on '20

American Electric Power 1Q20 Earnings Walk	EPS
1Q19 adjusted earnings	$1.19
Vertically Integrated Utilities	($0.11)
Wholesale/Normal Load	($0.02)
Rate Changes	$0.06
Weather	
Return to Normal	$0.01
Current Quarter	($0.10)
Transmission revenues	$0.02
O&M	$0.01
Depreciation and Other	($0.04)
Int/AFUDC	$0.00
Other	($0.01)
Trans./Dist. Utilities	($0.08)
Rate Changes (AEP Ohio, TX DCRF)	$0.01
OH Legacy Riders	($0.01)
OH Reg Prov	($0.09)
Weather	
Weather (Texas) Normalization	$0.00
Weather (Texas) Impact	$0.00
AEP TX transmission revenues (T-cost filings pre-ratecase)	$0.02
O&M	$0.04
TX Carrying Chgs	$0.00
Depreciation and Other	($0.02)
Other Taxes	($0.02)
Other/AFUDC	($0.00)

Table 9: AEP 1Q20 EPS Walk: street still a bit too high on '20

American Electric Power 1Q20 Earnings Walk	EPS
Transmission Holdco	$0.04
Investment growth (ahead of schedule)	$0.04
O&M	$0.00
True-Up	$0.00
Other	$0.01
Generation and Marketing	$0.02
Corporate/Other	($0.02)
Dilution	($0.00)
1Q20E Adjusted EPS	$1.03
1Q20 BofA EPS	$1.03
1Q20 Consensus	$1.15
2020 BofA EPS	$4.25
2020 Consensus	$4.30
2020 Guidance	4.25-4.45

Source: BofA Global Research estimates, company report, Bloomberg

Key items for the 1Q20 call

- **Indiana**: The final outcome for I&M's rate case in Indiana is still underway. Previously, we highlighted that it was possible AEP face a -7c impact from loss of wholesale revenues ($46mn) associated with the case (on top of the ROE result). We note that at the end of March, the Indiana regulatory commission gave the company results of a compliance filing that updated the net impact of the case from $8mn to $26mn. The outcome of the rehearing to recoop the remaining portion associated with wholesale revenues is due 60 days from 3/31. Stay tuned here.

- **Exposure to Covid**: We could see AEP towards the lower end of its guided '20 range based on its exposure to the industrial sales (and specifically Oil & Gas prone growth assumptions). Note that 30% of industrial sales is based on O&G – and that looking at 4Q19, AEP's Industrial GWh growth was 3.5% for the oil & gas related sectors but -6.1% for others. With sensitivity of $0.015/sh for every 1% change in industrial volume (the same for every 1% change in commercial volume as well), we expect the potential loss (vs. the company's originally projected 3.2% growth YoY in industrial GWh Sales) could be a significant driver for a '20 EPS reduction. Flat industrial growth in '20 would bring down '20 EPS by -$0.05/sh alone, and an actual drop in industrial volumes (which we see more likely due to its oil biz dependency) could mean a revision closer to -$0.10 or more. Here, we acknowledge AEP's less decouple profile (largely just Ohio and Texas through regular use of TCOS/DCOS riders) leaves some greater risk vs other more pre play utilities.

- **O&M and mitigating factors**: AEP factors in +19c of O&M cost savings YoY (equates to $200mn of savings established last Nov at EEI) into its 2020 walk already. While not commenting on flexibility, the company noted that it would be evaluating yet further reductions to bend the O&M curve even more this year in effort to balance some of the impacts of lower demand. We see O&M as a mitigating factor to COVID / oil price impacts on demand, Indiana's rate case outcome, and poor 1Q weather. Other ways to mitigate could include filing new rate cases. Finally, we continue to perceive mgmt. strategy as among the best positioned vs. peers between its largely transmission oriented growth strategy and nascent renewable build efforts.

- **Load loss**: As AEP experienced some load loss on the industrial side last year, it factored in some load loss assumptions for 2020 in the residential segment given the normal business cycle for the utility usually sees trends lead by industrial and then followed by resi 12 months later. AEP had factored in a resi decrease of 1.4%. We watch here as COVID work from home mandates could result in more residential use of electric.

- **Wind catcher**: With Louisiana filing its settlement, we await more official certainty before AEP announces how it plans to finance the project. Prior calls have identified 50% to two-thirds financed with equity. We look for whether the company is still able to pursue asset rotations in this environment.

- **Liquidity**: We highlight that AEP had $2.1bn in liquidity at the end of 2019 and that it signed a $1bn credit agreement several weeks ago as well. We expect that the company addresses liquidity and credit concerns as all companies in the utility space have looked to do. Finally, we note that Moody's previously placed AEP on negative outlook last November, but that credit rating agency is well aware of North Central Wind (and the equity associated with the project) as well as measures to reduce O&M at AEP. Note that our FFO/debt reconciliations are roughly around 15% (the company guides to mid-teens).

Estimates

Below we include our estimates largely unchanged from before – still at the bottom of 2020 guidance. We already factored in negative impacts expected from oil price impact as well as COVID impact on industrial demand and the cautious result at Indiana (although still could be mitigated). We note other moving pieces include a further O&M push and 1Q weather pressures.

Table 10: AEP EPS Estimates

EPS	2017A	2018A	2019E	2020E	2021E	2022E	2023E	2024E	2025E
APCo	$0.67	$0.73	$0.78	$0.79	$0.82	$0.84	$0.89	$0.93	$0.97
I&M	$0.38	$0.53	$0.51	$0.52	$0.55	$0.55	$0.57	$0.58	$0.60
SWEPCO	$0.25	$0.30	$0.37	$0.36	$0.38	$0.41	$0.45	$0.47	$0.49
PSO	$0.15	$0.17	$0.25	$0.24	$0.27	$0.30	$0.33	$0.35	$0.36
Other Utes (incl. KY)	$0.17	$0.27	$0.24	$0.24	$0.25	$0.25	$0.26	$0.26	$0.26
KY break out	$0.13	$0.14	$0.15	$0.16	$0.17	$0.17	$0.17	$0.17	$0.18
North Central Wind					$0.02	$0.18	$0.17	$0.17	$0.17
Vertically Integrated	$1.64	$2.00	$2.17	$2.14	$2.28	$2.36	$2.49	$2.58	$2.69
Guidance		$2.00	$2.17	$2.19					
Ohio	$0.66	$0.66	$0.67	$0.58	$0.63	$0.65	$0.69	$0.74	$0.80
Texas	$0.39	$0.41	$0.41	$0.44	$0.53	$0.60	$0.69	$0.76	$0.83
T&D	$1.01	$1.05	$1.00	$1.01	$1.15	$1.26	$1.38	$1.50	$1.62
Guidance		$1.05	$1.00	$1.03					
Transmission HoldCo	$0.72	$0.75	$1.05	$1.07	$1.18	$1.28	$1.38	$1.50	$1.66
Guidance		$0.75	$1.05	$1.08					
AEP Energy Supply	$0.30	$0.29	$0.30	$0.33	$0.23	$0.24	$0.26	$0.27	$0.30
Guidance		$0.29	$0.30	$0.35					
Corp & Eliminations	$0.01	($0.14)	($0.28)	($0.30)	($0.31)	($0.31)	($0.30)	($0.31)	($0.32)
Guidance		($0.14)	($0.28)	($0.30)					
Consolidated EPS without North Central	$3.68	$3.95	$4.24	$4.25	$4.53	$4.83	$5.20	$5.56	$5.94
CONSOLIDATED EPS with NORTH CENTRAL WIND	$3.68	$3.95	$4.24	$4.25	$4.56	$5.01	$5.38	$5.73	$6.11
EPS Growth (%)		*7.5%*	*7.3%*	*0.2%*	*7.3%*	*9.9%*	*7.3%*	*6.5%*	*6.7%*
Previous EPS (without North Central)	*$3.68*	*$3.95*	*$4.24*	*$4.25*	*$4.54*	*$4.84*	*$5.21*	*$5.56*	*$5.95*
Consensus		$3.93	$4.22	$4.30	$4.63	$4.97	$5.31	$5.58	
BofAe CAGR without North Central (vs '18 mid)			10.2%	5.0%	5.6%	5.9%	6.2%	6.3%	6.4%
BofAe CAGR with North Central (vs '18 mid)			10.2%	5.0%	5.8%	6.8%	6.9%	6.8%	6.8%
Annual Guidance	3.55-3.68	3.88-3.98	4.14-4.24	4.25-4.45					
Guidance: 5-7% EPS CAGR off of '18 (or '19 orig midpt)		$3.85	$4.19	$4.35	$4.59	$4.86	$5.15	$5.46	$5.82
Low			$4.14	$4.25	$4.46	$4.68	$4.91	$5.16	$5.42
High			$4.24	$4.45	$4.72	$5.05	$5.40	$5.78	$6.18
Share Count	492	493	494	496	497	511	515	519	522

Source: BofA Global Research estimates, company report, Bloomberg

Valuation

We MtM the peer multiple to 17.6x and derive a $93/sh PO with the same premiums awarded per subsidiary. We reiterate our Buy rating.

Table 11: AEP SOTP Valuation

AEP SoTP	2022E EPS			P/E Multiple	Premium/ Discount	Value ($mn)	Value ($/Sh)
Group Peer Multiple - Electric				17.6x			
Group EPS '18-'22 CAGR - Electric				5.00%			
Vertically Integrated Utilities (SWEPCO, PSO, APCo) excl KY	$2.19			18.5x	0.0x	$20,673	$40.5
Kentucky Power break out	$0.17			18.5x	0.0x	$1,612	$3.2
T&D Utilities (Principally D) - TNC/TCC, Ohio Power	$1.26			18.5x	1.0x	$12,502	$24.5
Transmission-Only Utilities - Mostly FERC	$1.28			18.5x	1.0x	$12,735	$24.9
Parent & Other - Principally HoldCo Debt	($0.31)			18.5x	0.0x	($2,904)	($5.7)
Total Regulated & HoldCo Value	$4.59					$44,618	$87.4
Renewables							
Legacy Energy Supply + Marketing/ Increasingly Renewables	$0.24			18.5x	-3.0x	$1,934	$3.8
Total AEP Equity Value - Existing Assets							$91.1
Upside	**2022E EPS (or discounted)**	**Capex**	**FFO**	**Earnings Impact (50% Equity)**	**P/E Multiple**	**Premium**	**Probability Weighted**	
SWEPCO 1200MW RFP filing - in service '21 (mostly 80% PTC)	0.09	1,089	$75		18.5x	0.0x	100%	$1.7
PSO 1000MW RFP filing - in service '21 (mostly 80% PTC)	0.07	908	$55		18.5x	0.0x	100%	$1.3
Total	0.17	1,997						3.1
Probability-Weighted EPS	0.17							
Discount Factor by year	10%							
Total Capex (probability weighted)				1,997				
Total Equity Needed ($M) (assuming 50%)				799				
Issuance Price (current price)				86.38				
Shares Issued (mn)				9				
Dilution %				2%				
Value Dilution				($808)			($808)	($1.6)
Shares Outstanding								511
Total Equity Value Per Share								$93
							Price Appreciation	7.7%
							+2020 Dividend Yield	3.2%
							Total Return	10.8%

Source: BofA Global Research estimates, company report, Bloomberg

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
American Electric Power: Starting from the Top: Breaking down the COVID Impact on C&I Sales	Julien Dumoulin-Smith	25 March 2020
American Electric Power: All on the same 5-7% page: North Central, financing, and rate cases	Julien Dumoulin-Smith	21 February 2020
American Electric Power: Adding to the US1 List: Key utility opportunity in 2020	Julien Dumoulin-Smith	22 January 2020
American Electric Power: Still confident on '20 & Awaiting critical updates with EEI; Reiterate Buy	Julien Dumoulin-Smith	25 October 2019

American Water Works (AWK)

Amid the escalation of the COVID pandemic, we expect continued execution by AWK with their inaugural ten year capital forecast of $20-22Bn intact and the company recently taking action to proactively address NT liquidity. We don't perceive any meaningful delays in spend or regulatory filings (albeit note the timing shift for new rates to take effect for NYAW) and with recent changes in mgmt. taking effect in the beginning of the month, we have confidence in the team's ability to navigate the crisis with potential for a further acceleration in muni acquisitions during any recovery period. While we appreciate the scarcity element and higher sustained investment trajectory for the subsector, we ultimately see the steep premium as unwarranted. We reiterate our Underperform rating.

AWK 1Q20 Earnings Walk

We forecast 1Q20 adjusted EPS of $0.67, in line with consensus and a $0.06 uptick from 1Q19 results of $0.61.

- **Key Drivers:** The primary positive drivers y/y are new rates implemented across a number of states in their footprint as well as various infrastructure surcharges. Partially offsetting results at the regulated segment includes higher D&A and O&M, as well as a bit of a drag at the parent level offsetting MBB contributions.

Table 12: AWK 1Q20 Walk

AWK 1Q20 Earnings Walk		EPS
AWK 1Q19 EPS	$	0.61
Regulated		0.06
Rate Cases & Step Increases		0.07
Infrastructure Charges		0.03
Depreciation		-0.02
O&M		-0.02
MBB		0.02
Parent		-0.02
Interest/Other Impact		-0.02
1Q20 BofAe Adjusted EPS	$	0.67
In Model	*$*	*0.67*
Consensus		$0.67
BofAe 2020 EPS	$	3.85
Guidance		3.79-3.89
2020 Consensus		$3.84
AWK 1Q20 Shares Outstanding		181
AWK 1Q19 Shares Outstanding		181

Source: BofA Global Research, Bloomberg

Predictable Execution Amid Unpredictable Crisis

Amid the escalating COVID crisis, mgmt. of AWK has maintained a clear focus on liquidity: in addition to their $2.25Bn revolver, the company entered into a $750Mn term loan, drawing $500Mn to hold in cash for add'l flexibility. The company has no near term debt maturities and remains confident in its ability to access both debt & equity markets (no equity needed in '20) as they still expect to fully execute on their capital investment plan of $20-$22Bn over the next ten years (any 2020 delays are expected to be made up later this year). To date, the company hasn't seen major disruptions to the supply chain: key distributors have indicated excess inventory, while chemical providers are meeting needs and reporting no shortages. On the margin, we sense commercial trucking capacity as mgmt's only potential concern for transport of chemicals or bottled water in the event of a major service outage – and the company said it has secured contracts with two suppliers with relationships with gov't agencies in any event.

Reg., Leg., and Muni Prospects

We further perceive regulatory filings as generally proceeding as planned – while remote - with no anticipation of a delay in their ongoing NJ rate case. That said, late last month, NYAW announced postponement of the rate increase and improvement charge. We could also see a further uptick in bad debt expense with no real time tracker for recovery. With resi composing 69% of revenue, we see load impact as likely more muted, however. Given the already longer process of engaging in municipal transactions, mgmt hasn't seen particular delays on the acquisition front and we perceive a potential for further acceleration in industry consolidation under a recovery scenario as munis focus on the small businesses. Meanwhile, the capital light MBB is continuing to generate cash with no impacts yet to Military and an expectation that the customer base in homeowners services will be maintained in any economic downturn.

EPS Estimates

The exhibit below reflects our latest EPS estimates with annuals remaining unchanged ahead of our 1Q preview and as we await additional data points. We continue to expect sustained long term growth within their 7-10% LT EPS CAGR and 7% rate base growth longer term.

Table 13: EPS Estimates

AWK	2019A	2020E	2021E	2022E	2023E	2024E
Earnings Metrics						
Regulated Water EPS	3.60	3.84	4.19	4.43	4.66	4.98
Market Based EPS	0.45	0.47	0.51	0.53	0.57	0.63
Parent and Other EPS	-0.44	-0.46	-0.43	-0.40	-0.36	-0.39
Adjusted EPS	3.61	3.85	4.27	4.56	4.87	5.21
Consensus	3.61	3.84	4.23	4.53	4.92	
Guidance	3.56-3.64	3.79-3.89				
Midpoint of Guidance	3.60	3.84				
Implied Guidance - 2020-2024 off 2018 EPS base						
High	3.64	3.89	4.39	4.83	5.31	5.85
Low	3.56	3.79	4.04	4.33	4.63	4.95
Mid	3.60	3.84	4.22	4.58	4.97	5.40
EPS CAGR - BofA off 2018 EPS base - 2020-2024	*7.9%*					

Source: BofA Global Research, Bloomberg

Valuation

The exhibit below reflects our latest valuation: We mark to market our valuation for the latest water utility multiple of 26.3x (vs. 25.2x), with our PO shifting to $133. We maintain our Underperform rating given the large premium vs. electric & gas peers, which we see as unjustified given its only modest relative growth premium.

Table 14: AWK SOTP

Water Utilities	2022E EPS	P/E Multiple					Equity Value		
		Peer	Prem/ Discount	Low	Base	High	Low	Base	High
AWK Earnings		26.3x							
Group EPS '18-'22 CAGR		8.30%							
Water Utilities		28.5x							
NJ	$1.12		3.0x	30.5x	31.5x	32.5x	$34.13	$35.25	$36.37
PA	$1.27		3.0x	30.5x	31.5x	32.5x	$38.81	$40.08	$41.35
IL	$0.35		3.0x	30.5x	31.5x	32.5x	$10.57	$10.92	$11.26
MO	$0.50		2.0x	29.5x	30.5x	31.5x	$14.64	$15.14	$15.63
IN	$0.29		1.0x	28.5x	29.5x	30.5x	$8.27	$8.56	$8.85
CA	$0.19		-1.0x	26.5x	27.5x	28.5x	$5.03	$5.22	$5.42
Other	$0.71		0.0x	27.5x	28.5x	29.5x	$19.50	$20.21	$20.92
Regulated Water EPS	$4.43						$130.95	$135.38	$139.80
Parent/Other Drag	-$0.40		0.0x	27.5x	28.5x	29.5x	-$11.03	-$11.43	-$11.83
Market Based Business									
Military (40%)	$0.21	26.3x	-3.0x	22.3x	23.3x	24.3x	$4.74	$4.95	$5.17
Non Military (60%)	$0.32			11.0x	12.0x	13.0x	$3.51	$3.83	$4.15
Total Market Based Business	$0.53						$8.25	$8.78	$9.31
Valuation	$4.56						$128.00	$133.00	$137.00
Current Price as of 04/19/20								*$131.76*	
Dividend Yield								1.5%	
Total Return							-1.35%	2.45%	5.48%

Source: BofA Global Research, Bloomberg

See our other recent reports on AWK:

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
American Water Works: Takeaways from our latest fireside chat	Julien Dumoulin-Smith	07 April 2020
American Water Works: Adding detail to our valuation approach: Underperform	Julien Dumoulin-Smith	09 March 2020
American Water Works: Analyst Day Redux: A Splash of Deleveraging & More	Julien Dumoulin-Smith	16 December 2019

Consolidated Edison (ED)

ED is expected to deliver Q1 results down slightly from the prior-year quarter. Our 1Q20 estimate of $1.33/sh compared to adjusted EPS of $1.39/sh in 1Q19 and Street consensus of $1.42/sh – we see downside here as effects of Covid-related slowdown are more fully reflected in consensus estimates. ED's main electric and gas business at the Con Edison Company of New York (CECONY) and Orange & Rockland (O&R) is fully decoupled leaving its earnings relatively defensive in the face of Covid-related slowdowns amid ongoing shut-in orders, with the Steam business being the only one exposed to weather and load factors. ED's non-regulated business should see a modest uplift in 2020 on higher earnings from the ongoing Mountain Valley Pipeline (MVP) project as well as the normalizing effect of weather-curtailed renewable production in the Clean Energy Business (CEB).

1Q20 Quarterly Walk

We see Q1 EPS at $1.33/sh, slightly below Street at $1.42 though we perceive downside to consensus ests after weather and demand considerations are more fully factored in to forecasts. Weather is expected to be a drag (we estimate 5 cents, see below) due to milder weather in Q1 2020 affecting principally the Steam business (CECONY and O&R are decoupled for Electric and Gas) offset partially by normalization of the negative effect from 1Q19. We expect a $0.12/sh uplift from new rates at the gas and electric utilities in effect since January with new rates in place following the approval of the joint settlement in the CECONY rate case, and modest uplift at CEB from improving wind resource in Q1 (ex HLBV impact). Key unknown is the drag from stock-based compensation (SBC) which becomes incrementally larger depending on the y/y share price return as of the end of the quarter – given market volatility in Q1 this item is particularly difficult to estimate, though we assume some drag given the share price was higher *on average* during 1Q20 as compared to the prior year.

Table 15: ED 1Q20 Earnings Walk

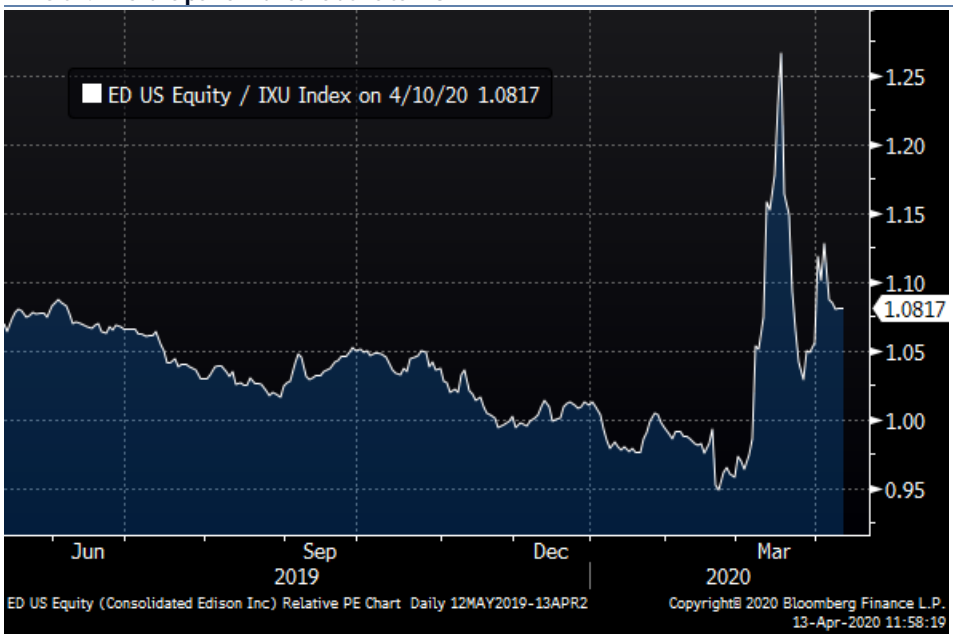
ConEd 1Q20 Earnings Walk		EPS
1Q19 Adjusted EPS	Notes	$1.39
Con Edison of New York (CECONY)		
Rate Changes		0.12
Gas	$84m increase effective Jan. 1, 2020	0.05
Electric	$113m increase effective Jan. 1, 2020	0.07
Impact of Steam 1Q19	Normalizing last year impact	0.01
Impact of Steam 1Q20	Warmer than normal weather; demand due to COVID	(0.05)
O&M		(0.03)
Stock based comp	Share price higher in Q1 2020 based on quarterly average	(0.03)
D&A / Property Taxes		(0.10)
Interest Expense		0.00
Orange & Rockland (O&R)		
Rate Changes		0.02
O&M		0.00
D&A / Property Taxes		(0.01)
Competitive Business		
CET	Flat y/y	0.00
CEB	Normalizing wind resource	0.04
Dilution		(0.03)
1Q20 Adjusted EPS		$1.33
1Q20 Consensus		$1.42
1Q20 in Model		$1.33
2020 BofAe		$4.38
2020 Consensus		$4.42
2020 Guidance		$4.30-$4.50
Share Count		
1Q19		323
1Q20		330

Source: BofA Global Research Estimates, company report, Bloomberg

Stock trading dynamics

Shares of ED have held up relatively well during the March market volatility which was kicked off by concerns about the economic effect of Covid. ED remains one of the more defensive names in our coverage owing to its largely decoupled business – both Electric and Gas distribution at CECONY and O&R are decoupled, leaving the much smaller Steam business along with the Rockland Electric Company (RECO) exposed to changes in load. The New York Independent System Operator (NYISO) has reported electricity demand in Zone J declining by as much as 18% during the weeks since the shut in orders began, largely driven by lower morning peaks as commercial customers are shut down and commuting has declined precipitously. While the timing of the Covid demand shock is more likely to impact Q2, we note that milder Q1 weather can be a negative driver for the steam business, though ED does not disclose sensitivities. ED has weather normalization at the CECONY and O&R gas businesses but not at the electric utility. While ED does not have a separate bad debt expense rider, each rate case creates an allocation for bad debt expense that is then recovered through rates. Nonetheless, on a 2-year forward PE relative to the IXU, ED shares continue to screen relatively expensive. Accordingly we remain comfortable with our Neutral rating, seeing risk and reward as largely balanced.

Exhibit 1: ED share performance relative to IXU



Source: Bloomberg

Weather should be more impactful than demand in Q1

We expect that despite ED's largely decoupled business, the impact of milder than normal weather in Q1 results will be more pronounced in 2020, on an order of magnitude more in line with Q1 2018. As measured by heating degree days at LaGuardia Airport, Q1 was 20% warmer than normal, a level of mild weather last approached in 2016 and 2017. ED's reported weather impact on the steam business includes both the normalization of the prior year's impact as well as that of the current year. As such it is more instructive to look at the total delta in deviation from normal from year to year – note that in 2016 HDDs swung from 18% above normal to 16% below normal, an aggregate change of -34% which resulted in a significant 12 cent impact on EPS. The change in 2020 is not as dramatic as 2019 was only slightly below normal in terms of HDDs, accordingly the total drop in HDDs including the impact of the current year is -18%. We therefore estimate that the impact on EPS from weather impacts on the Steam business is -$0.05. We not however that this impact is historically volatile and numerous factors affect the total EPS swing including the timing of when the biggest deltas from normal occur – HDDs in Jan-Feb are "worth more" in an EPS sense than

those in more shoulder months of Mar-Apr generally speaking. 2020 saw relatively consistent trends in weather, with each Q1 month recording double-digit percentage declines from normal including 20%/15% declines in Jan/Feb. In 2016 by contrast, Jan-Feb declines were approximately 10% while March HDDs were 30% below normal. Bottom line: we see weather as a likely negative driver in Q1 on an order of magnitude similar to 2018. We see this as a much more impactful Q1 event than Covid-related demand declines owing to the timing of state shut-in orders, though both will be Q1 headwinds with the mix shifting toward demand declines looking forward to Q2 and beyond.

Table 16: New York City HDD data

	Q1 2015	Q1 2016	Q1 2017	Q1 2018	Q1 2019	Q1 2020
NYC HDDs	3,057	2,171	2,132	2,406	2,530	2,062
Normal	2,582	2,582	2,582	2,582	2,582	2,582
% Above / Below	18%	-16%	-17%	-7%	-2%	-20%
% Delta		-34%	-2%	11%	5%	-18%
Steam impact ($/sh)		(0.12)	0.02	0.05	(0.01)	

Source: BofA Global Research Estimates, NYSERDA

Credit and financing update

ED's 3-year financing plan includes up to $1.8B of equity issuance in 2020-22. Needs in the current year are seen at up to $600m on top of $88m of equity forwards settled in January, while the forecast for the two following years calls for $1.1B. Street estimates were higher than our forecast. However, they still trail the announced issuance by ~$400m through 2022. On the credit side, Fitch lowered outlooks of ED and its subsidiaries CECONY and Orange and Rockland Utilities Inc. to negative from stable reflecting a weak financial profile associated with lower demand and higher than anticipated bad debt expense involving NY power market due to COVID 19. Admittedly, the companies have revenue recovery mechanisms in place to deal with such situations but Fitch expects those are not sufficient enough to protect the utilities. We continue to see ED's consolidated CFO pre-WC to net debt metric as bouncing back from the ~15% level at the end of 2019, increasing to 17-18% by 2024.

Table 17: ED credit update

Rating Agencies	2015A	2016A	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E	2025E
CFO		3,459	3,367	2,695	3,134	3,452	3,678	3,912	4,140	4,364	4,747
Add: Pensions		233	187	233	233	233	233	233	233	233	233
Add: Operating Leases		12	12	12	12	12	12	12	12	12	12
Less: Changes in WC		(150)	(83)	414	160	160	160	160	160	160	160
Adj CFO Pre-W/C	3,692	3,554	3,483	3,354	3,539	3,857	4,083	4,317	4,545	4,769	5,152
Long -Term Debt		14,774	16,029	18,970	19,973	20,484	20,989	21,222	21,731	22,103	22,182
Add: Short-Term Debt		1,054	577	1,741	1,692	1,692	1,692	1,692	1,692	1,692	1,692
Add: Pensions		1,623	1,262	1,262	999	999	999	999	999	999	999
Add: Operating Leases		180	180	180	880	880	880	880	880	880	880
Add: Non-Standard Adjustments			134	142	142	167	167	167	167	167	167
Adj Total Debt	17,170	17,765	18,190	22,295	23,711	24,222	24,727	24,960	25,469	25,841	25,920
(CFO Pre-W/C) / Debt	21.5%	20.0%	19.1%	15.0%	14.9%	15.9%	16.5%	17.3%	17.8%	18.5%	19.9%

Source: BofA Global Research estimates, company report, Bloomberg

EPS Estimates

We tweak our 2020 estimates lower on Covid and weather impact at the Steam business, reducing earned ROE to 8.8% (in line with authorized) from 8.9% while we continue to reflect 10 bps of over-earning at CECONY in 2021 and beyond. We also reflect a slight uptick in results at the CEB y/y as below-normal results from 2019 are normalized, though in the long-term growth in this business is expected to come principally via contractual escalators and investment in incremental projects. Our estimates are modestly below Street consensus in '20 and '22 and in-line in '21, reflecting a CAGR of ~4% over our 2019 estimate.

Table 18: ED updated estimates

EPS by Business	2019A	2020E	2021E	2022E	2023E	2024E	2025E
CECONY	$3.79	$3.71	$3.91	$4.07	$4.26	$4.51	$4.77
O&R	$0.21	$0.22	$0.22	$0.23	$0.24	$0.26	$0.27
Regulated	$4.01	$3.93	$4.14	$4.30	$4.50	$4.76	$5.04
Core Regulated Growth (Y/Y)	*-0.12%*	*-1.85%*	*5.22%*	*3.88%*	*4.71%*		
CED Development (Solar)	$0.21	$0.29	$0.31	$0.33	$0.35	$0.37	$0.39
CEE (Energy/Wholesale Marketing)	$0.02	$0.02	$0.02	$0.02	$0.02	$0.02	$0.02
CES (Solutions)	$0.01	$0.01	$0.01	$0.01	$0.01	$0.01	$0.01
Clean Energy Businesses	$0.24	$0.32	$0.34	$0.36	$0.38	$0.40	$0.42
Electric Transmission	$0.02	$0.03	$0.03	$0.03	$0.03	$0.03	$0.03
Midstream/Stagecoach	$0.08	$0.06	$0.06	$0.06	$0.06	$0.06	$0.06
MVP	$0.09	$0.11	$0.08	$0.05	$0.05	$0.05	$0.05
Consolidated Edison Transmission	$0.19	$0.20	$0.17	$0.13	$0.13	$0.13	$0.13
Parent	-$0.07	-$0.07	-$0.07	-$0.07	-$0.07	-$0.07	-$0.07
CONSOLIDATED EPS	$4.38	$4.38	$4.57	$4.72	$4.94	$5.22	$5.52
Prior EPS Estimates	$4.08	$4.49	$4.62	$4.78	$4.99		
Management guidance		$4.30-$4.50					
Midpoint		$4.40	$4.58	$4.76	$4.95	$5.15	$5.35
Long term CAGR (3-5% CAGR guide off 2020 guidance)			3.9%	3.6%	4.0%	4.4%	4.7%
Consensus	4.30	4.42	4.59	4.79			
BofAe CAGR '19 -'22	2.6%						
CECONY CAGR '19-22	2.4%						
O&R CAGR '19-22	2.3%						
Earned ROEs							
CECONY	9.2%	8.8%	8.9%	8.9%	8.9%	8.9%	8.9%
O&R	9.3%	9.1%	9.1%	9.1%	9.1%	9.1%	9.1%

Source: BofA Global Research Estimates, company report, Bloomberg

Valuation

We update our PO to $93 following mark to market of the latest peer group multiples of 17.6x for electric and 17.6x for gas. We remain Neutral on ED as the latest guidance provides a below-peer rate of return of 3-5% over a five year period based off 2020's guidance, which implies minimal growth over 2019 at the midpoint. While in our view shares are largely derisked in terms of rate case uncertainty with new rates in place for three years, we would expect the market to remain focused near-term impacts from warmer weather and Covid-related demand destruction in the near term along with a focus on the below-average growth trajectory and uncertain cadence of 2021-22 equity issuance in the medium term. Reiterate Neutral.

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Consolidated Edison: Cautious update as equity issuance exceeds expectations	Julien Dumoulin-Smith	21 February 2020
Consolidated Edison: Fine-tuning equity & renewable investments; reiterate Neutral	Julien Dumoulin-Smith	20 December 2019
Consolidated Edison: Moving to conservative ROE outlook following EEI; D/G to Neutral	Julien Dumoulin-Smith	14 November 2019
Consolidated Edison: '19 Narrowed Lower: Long-term still quite compelling despite NT Noise; Buy	Julien Dumoulin-Smith	05 November 2019

Table 19: ED SOTP

ConEd Valuation	Metric	Multiples				Equity Value		
	2022E EPS	Low	Prem/ Discount	Base	High	Bear	Base	Bull
	-	-	-	-	-	-	-	-
	-	-		-	-	-	-	-
Group Peer Multiple - Electric	-	-	17.6x	-	-	-	-	-
Group EPS '18-'22 CAGR - Electric	-	-	5.00%	-	-	-	-	-
	-	-		-	-	-	-	-
Group Peer Multiple - Gas	-	-	17.6x	-	-	-	-	-
Group EPS '18-'22 CAGR - Gas	-	-	5.10%	-	-	-	-	-
	-	-		-	-	-	-	-
Applied Multiple	-	-		-	-	-	-	-
Electric (& Steam)	-	-	18.5x	-	-	-	-	-
Gas	-	-	18.5x	-	-	-	-	-
Utilities		-	-	P/E	-	-	-	-
CECONY Electric	$2.85	18.5x	1.0x	19.5x	20.5x	$53	$56	$58
CECONY Steam	$0.19	18.5x	1.0x	19.5x	20.5x	$3	$4	$4
CECONY Gas	$1.03	18.5x	1.0x	19.5x	20.5x	$19	$20	$21
Total CECONY	$4.07					$75	$79	$83
O&R + RECO Electric	$0.16	18.5x	1.0x	19.5x	20.5x	$3	$3	$3
O&R Gas	$0.07	18.5x	1.0x	19.5x	20.5x	$1	$1	$1
Total O&R	$0.23					$4	$4	$5
Grand Total Utilities EPS	$4.30							
Competitive Businesses								
	2022E EPS			P/E				
CET Electric Transmission (NY Transco)	$0.03	15.5x	-2.0x	16.5x	17.5x	$0.40	$0.42	$0.45
CEE (Wholesale Energy)	$0.02	11.5x	-6.0x	12.5x	13.5x	$0.23	$0.25	$0.27
Infrastructure	2022E EPS			P/E				
Stagecoach Midstream	$0.06	15.5x	-2.0x	16.5x	17.5x	$0.89	$0.95	$1.01
	2022E EBITDA			Baseline	Adjusted			
Mountain Valley Pipeline (MVP)	$70	10.0x	-2.0x	11.0x	9.0x	$1.41	$1.81	$2.21
ConEd Development: Renewables	2022E EBITDA			EBITDA Multiple				
Legacy ED Portfolio	360	9.0x		10.0x	11.0x	3,240	3,599	3,959
Renewables Acquistion (60% of SRE portfolio)	211	9.0x		10.0x	11.0x	1,897	2,107	2,318
Total CEB EBITDA	571							
Less: CEB Project Level Debt						-2,806	-2,806	-2,806
Total Renewable Portfolio Equity Value						2,330	2,901	3,471
Implied Equity Value $/sh						$6.72	$8.36	$10.01
Parent + HoldCo Debt	2022E EPS							
Corp & Other Drag	-$0.07	17.5x	0.0x	18.5x	19.5x	-$1.18	-$1.25	-$1.32
Holding Company: 50% Weighting to Debt Subtraction & 50% Weighting to Interest Expense								
Current HoldCo Debt	-900					-450	-450	-450
Imputed MVP Debt @ 10% Ownership	-324					-324	-324	-324
Add Back: Interest expense (Tax effected)	41	17.5x	0.0x	18.5x	19.5x	361	382	403
Total Adjustment $/Sh						-$1.19	-$1.13	-$1.07
Shares Outstanding							347	
Total Equity Value						$87.00	$93.00	$100.00
Implied Consolidated P/E							19.7x	
Dividend Yield							3.31%	
Total Return						0.4%	7.1%	15.0%

Source: BofA Global Research Estimates, company report, Bloomberg

Duke Energy (DUK)

With DUK's upcoming 1Q call, we expect a sharp focus on cost reduction mitigation measures to offset in part COVID-19 related pressures. While mgmt. is still assessing the impact on load and delayed bad debt expense recovery, we could potentially see up to a -$0.14-16/sh headwind assuming just 2-3% load degradation (although could be materially higher than this) on C&I/wholesale customers and $20mn incremental bad debt similar to '09 levels if not for offsets. Specific details on cost cuts have yet to be delineated, although we look back to 2017 where weather was a significant headwind with mgmt. offsetting the impact through cost reductions of $100-150mn, which would translate to $0.11-$0.16/sh EPS benefit in 2020. Ability to bend the cost curve is notable and opportune following last year favorable weather and pull-ahead on O&M execution. Beyond 1Q details around load pressures and cost reduction, we look to discussions around the North Carolina rate cases where we remain cautious given litigated ROEs and coal ash pressures; perceive the risks of negative revisions to be largely known/priced-in. With potential for multi-year rates/ ROE banding in exchange for enhanced customer metrics the Carolina jurisdictions could be partially de-risked following rate case outcome. Longer-term, the NC IRP filing in Sept that could create additional opportunities for DUK in terms of clean energy and coal reduction opportunities, although we look for further discussion on natural gas build considerations given still uncertainty around ACP. Net-net, we maintain our Neutral rating.

DUK 1Q20 EPS walk

We forecast 1Q20 EPS of $1.14 compared to 1Q19 results of $1.24 and consensus estimates of $1.24. While our estimates are below consensus and down -3% YoY it includes -$0.08 of negative weather est in the quarter. With rate cases in the Carolinas/IN expected to be implemented in 2H and potential cost cuts upwards of $0.16/sh we see the ability to hold the line of 2020 guide.

- **Key drivers**: Positive YoY drivers include the implementation of rates and riders at the electric utilities (+$0.08), the wholesale contract moving to formula rates (+$0.01), new rates at Piedmont (+$0.04), AFUDC on Atlantic Coast Pipeline (+$0.01), other gas utility growth (+$0.01), Offsetting results are regulatory lag (-$0.04), impacts from COVID on load growth (-$0.02), the tax true-up reversal at the gas segment (-$0.06), higher interest expense (-$0.01), preferred coupon interest expense (-$0.04), share dilution (-$0.01), and increased O&M expense due to the Feb. storms in the Carolinas (-$0.03).

- **Unknowns**: Weather is expected to be unfavorable driver in the quarter with HDDs 20% below the norm and 15-18% below the prior year, although slightly offset by more favorable CDDS; the exact magnitude is unclear. Another unknown impact is the decline in load growth from COVID19; while mgmt. provides sensitivity that every 1% decline in load equates to a $0.15/sh impact with industrial load ~20% of retail sales, which has lower margins compared to the other customer classes and Commercial load ~30% of retail, and the ~15% from wholesale, the exact extent of the decline is difficult to discern in 1Q. Further, it remains unclear if the company was able to bend the cost curve on O&M costs, which could be a potential offset, although likely to show up in 2Q.

Table 20: DUK 1Q20 EPS walk

DUK 1Q20 Earnings Walk	EPS
DUK 1Q19 EPS	1.24
Weather - normalize from 1Q19	$0.06
Weather- 1Q20	-$0.11
Electric	$0.03
Rate implementation:	
DEC SC rates (full quarter)	$0.01
DEP SC rates (full quarter)	$0.01
Florida - multi-year plan	$0.01
SOBRA - FL	$0.01
Other Riders - IN and OH	$0.04
Regulatory lag	-$0.04
Load Growth - 1%	-$0.02
AFUDC equity	$0.00
Wholesale - fixed to formula rates	$0.01
Gas	$0.00
LDC Growth	$0.01
New Rates - PNY	$0.04
AFUDC for ACP	$0.01
Tax true-up reversal	-$0.06
Renewables	$0.00
Palmer (60MW) – 2Q in-service	$0.00
Other	-$0.08
O&M - Feb. storms	-$0.03
Interest expense	-$0.01
Other - preferred	-$0.04
Dilution	-$0.01
DUK 1Q BofAe Adjusted EPS	$1.14
Consensus	$1.25
BofAe 2020 EPS	5.21
Guidance	5.05-5.45
2020 Consensus	5.17
DUK 1Q20 Shares Outstanding	732
DUK 1Q19 Shares Outstanding	728
Tax Rate	12%

Source: BofA Global Research estimates, company report, Bloomberg

Bending the O&M cost curve

Given the potential implications from a decline in load with the electric utility largely exposed as several C&I customers have announced closures in its service territory (see further below), we expect mgmt. to look to mitigate these impacts through reductions in O&M. While the company has not yet announced these mitigating measures, we look back to 2017 where weather was a severe headwind with mgmt. able to offset that by $100-150mn in cost reductions. We could very well see mgmt. announce similar cost reductions (relative to flat growth yoy) that would result in a $0.11-$0.16/sh EPS benefit in 2020 to offset (or at least partially) the below headwinds to load. Additionally, mgmt. executed on pulling cost forward with favorable weather last year, including $0.04/sh for foundation giving that could be a benefit as well. While details on where these O&M levers are going to come from have yet to be disclosed, we look forward to additional commentary from mgmt. to see if these are more transitory (i.e. at the utility level) or through sustainable corp. overhead reductions. Net-net, we see this as a positive as it would be able to offset headwinds from load this year.

Load growth considerations and decoupling

DUK's electric utilities & infrastructure jurisdiction (~83% of 2020 adjusted EPS contribution according to guidance) does not have decoupling and is much more exposed to load. On a sensitivity basis, every +/- 1% change in electric load across all customer classes equates to +/- $0.15 change in EPS. Note DUK's industrial load is ~20% of its retail business, which has lower margins compared to the other customer classes driving a lower impact to EPS ($0.02/sh for every 1% change). Commercial load accounts for ~30% of retail, residential is ~35% and the remaining ~15% is wholesale. As we've mentioned before, the residential market may be set up to benefit from COVID-19 as people continue to self-quarantine in their homes (especially true as we enter peak

cooling demand with more residential customers utilizing air conditioning). We also highlight that wholesale represents 15% of its load with every 1% load loss in retail, equating to $0.02-0.03/sh impact to EPS; although this is likely overestimating the impact to some extent as its largest wholesale customers in the Carolinas are residential. Also, the impact for wholesale would only impact the current year as volumes get reset in the following year's rates automatically.

While mgmt. is still assessing the impacts to load, there have been several announced closures in DUK's service territory: BMW in NC and Fiat in IN announced closures in mid-march while many schools and small businesses have also announced closures. See our assumptions below for potential headwinds to EPS from a 2% decline in load (w/ a partial offset by 0.5% increase in residential load), although see this offset in part from increased O&M cost cuts.

Table 21: DUK EPS Load Sensitivity and Assumptions

DUK Load Sensitivity	Every 1% change	Assume 2% decline in load (ex-residential)
Industrial	$0.02	-$0.04
Commercial	$0.05	-$0.09
Residential	$0.09	$0.04
Wholesale	$0.03	-$0.05
Total Headwind		-$0.14

Source: BofA Global Research estimates, company report

Gas LDC's decoupled in NC with weather normalization in SC/TN

On the positive side, most of DUK's gas jurisdiction is decoupled or has weather normalization with only about 9% of total gas earnings exposed to load (~91% of Gas Utilities & Infrastructure business has mostly fixed margins). Piedmont is fully decoupled in North Carolina (75% of Piedmont gas business). South Carolina and Tennessee have weather protection only (25%). From an earnings contribution standpoint Gas Utilities & Infrastructure only accounts for ~12% of 2020 adj. EPS or ~10% excluding ACP's EPS per DUK's latest guidance.

Bad debt expense and recovery of COVID costs

DUK has a bad debt expense rider in Piedmont for fuel expenses (60% of the bill) and a full rider for all bad debt expense at Duke OH gas and electric. For Duke Ohio, bad debt expense is collected through annual uncollectible riders for both the gas and electric businesses, with true-ups. For the Piedmont businesses, these are collected in the fuel rider, and mgmt. can update the fuel costs as often as it needs, although tends to do it every six months driven by under or over-collection status as the cost of natural gas changes. For the other jurisdictions, mgmt. will be tracking incremental bad debt expenses and other COVID-19 related expenses, and if significant, would explore regulatory asset treatment similar to other extraordinary costs when material to the respective utility. *While the majority of the business does not have a bad debt expense rider/mechanism we continue to see a relatively minimal impact from incremental costs associated with bad debt: for context, the company experienced $20mn of incremental bad debt during the 2008/2009 financial recession, which would translate to $0.02-$0.03/sh today (assuming inflationary increase in today's dollars).*

NC rate cases remain key to watch: ROE and coal ash

We continue to expect DUK's rate case in the Carolinas to have a similar outcome to Dominion's coal ash order potentially further cautious for earned/recoverable ROEs where we already assume $0.10-$0.13/sh eventual drag. Further, we expect the ROE to be litigated in the Duke Energy Progress (DEP) case with intervenor testimony on April 13th likely to give further indication of staffs issue with ROE given the wide discrepancy between parties on the current interest rate environment and cost of capital (which has rebounded precipitously for DUK of late). Rate cases remain cautious although see risks of the negative revisions priced-in/largely known.

EPS estimates

We provide our EPS estimates below and see a 4.5% CAGR through '24 with estimates slightly below street and mgmt. guide for 5% growth at the mid-point. See headwinds in 2020 despite sizeable O&M reductions given weather headwinds and reduction in load. We don't expect a guidance cut to be clear with '20 despite 1Q pressures, particularly considering cost levers. DUK appears among the most confident in sourcing these offsets across the sector.

Table 22: DUK EPS Estimates: looking for consensus ests to come down a touch

EPS Estimates	2018A	2019A	2020E	2021E	2022E	2023E	2024E
Electric							
Carolinas	1.65	1.95	1.88	1.94	2.02	2.10	2.20
Indiana	0.57	0.60	0.61	0.62	0.65	0.67	0.69
Ohio - Electric	0.26	0.22	0.25	0.25	0.28	0.31	0.35
Progress- Carolinas	1.02	1.12	1.16	1.16	1.19	1.22	1.24
Progress- Florida	0.81	0.96	0.97	1.02	1.05	1.09	1.10
Commercial Transmission	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Eliminations	0.39	-0.04	0.00	0.00	0.00	0.00	0.00
Consolidated Earnings	4.70	4.81	4.86	4.99	5.19	5.38	5.58
Guidance		4.77	4.94				
Gas							
Ohio - Gas	0.13	0.12	0.14	0.16	0.19	0.20	0.21
Piedmont (PNY)	0.23	0.27	0.31	0.33	0.37	0.41	0.45
Midstream Pipelines	0.02	0.23	0.23	0.29	0.23	0.25	0.25
Eliminations	0.06	0.00	0.00	0.00	0.00	0.00	0.00
Consolidated Earnings	0.45	0.62	0.68	0.79	0.78	0.85	0.91
Guidance		0.51	0.72				
Commercial Renewables	0.14	0.27	0.33	0.33	0.30	0.28	0.29
Guidance		0.32	0.33				
Parent/Other	-0.57	-0.64	-0.73	-0.65	-0.60	-0.56	-0.53
Guidance		-0.60	-0.73				
Adjustments							
BofAe EPS	4.72	5.06	5.14	5.45	5.67	5.95	6.24
Previous Estimates		*5.06*	*5.21*	*5.45*	*5.67*	*5.95*	*6.24*
Guidance	4.65-4.85	*4.95-5.15*	*5.05-5.45*				
Consensus	4.76	5.02	5.16	5.47	5.70	5.97	
Mgmt EPS CAGR: 4-6% from 2019-2023E		5.00	5.25	5.51	5.79	6.08	6.39
Low End		4.80	5.05	5.41	5.62	5.85	6.08
High End		5.20	5.45	5.62	5.96	6.31	6.69
BofAe CAGR '19-'23e						4.5%	
BofAe CAGR '19-'24e							4.5%

Source: BofA Global Research estimates,, Bloomberg, company filings

Valuation: PO of $93

Our PO of $93 based on our latest EPS estimates and mark to market of peer utility multiples of 17.9x for gas and electric. Ability to turn the narrative in the NC jurisdiction would clearly help shares to re-rate on DUK shares although still look for execution.

Critically, the ability to implement PBR (Performance Based Rates) potentially in exchange for implementation of an ROE band/and or multi-year stay out of rate cases appears increasingly likely and among a handful of understated emerging positive trends for shares. We anticipate further discussion albeit beyond the scope of the near-term pressures and Covid related concerns.

Table 23: DUK SOTP Valuation

Duke Energy Sum of the Parts Valuation
2022E
All figures in $Mn except per share

	Metric	P/E Multiple						Equity Value	
	2022E EPS	Low	Peer	Prem/ Discount	Base	High		Low	Base	High
Group Peer Multiple - Electric	-	-	17.9x	-	-	-	-	-	-	-
Group EPS '18-'22 CAGR - Electric	-	-	5.00%	-	-	-	-	-	-	-
	-	-	-	-	-	-	-	-	-	-
Electric Utilities			18.8x							
Duke Energy Carolinas	$2.02	17.8x		0.0x	18.8x	19.8x		$36.02	$38.04	$40.07
Duke Energy Progress/Carolinas	$1.18	17.8x		0.0x	18.8x	19.8x		$21.07	$22.26	$23.44
Duke Energy Florida	$1.05	18.8x		1.0x	19.8x	20.8x		$19.80	$20.86	$21.91
Duke Energy Indiana	$0.65	18.8x		1.0x	19.8x	20.8x		$12.13	$12.77	$13.42
Duke Energy Ohio/Kentucky	$0.28	17.8x		0.0x	18.8x	19.8x		$4.98	$5.26	$5.54
Total Electric Utility Value	$5.19							$94.01	$99.19	$104.38
Group Peer Multiple - Gas			17.9x							
Group EPS '18-'22 CAGR - Gas			5.10%							
Gas Utilities	2022E EPS		18.8x							
Duke Energy Piedmont	$0.37	18.8x		1.0x	19.8x	20.8x		$6.88	$7.25	$7.61
Duke Energy Ohio/Kentucky Gas	$0.19	18.8x		1.0x	19.8x	20.8x		$3.53	$3.71	$3.90
Total Gas Utility Value	$0.55							$10.41	$10.96	$11.51
Commercial Segment	2022E EBITDA									
Midstream Infrastructure:							Weight			
ACP	$407	8.0x	9.0x	0.0x	9.0x	10.0x	50%	1,627	1,831	2,034
Add back ACP debt							50%	942	942	942
All Other	$61	8.0x	9.0x	0.0x	9.0x	10.0x		492	553	614
Transmission Segment	$6	8.0x	9.0x	0.0x	9.0x	10.0x		52	58	64
Segment Net Debt	-$5,055							-5,055	-5,055	-5,055
Add back Renewable Debt	$1,088							1,088	1,088	1,088
Renewables Segment NPV @ 8% Discount	$1,291							1,291	1,291	1,291
New Renewables NPV	$471							471	471	471
Net Infrastructure Equity								909	1,181	1,452
Net Infrastructure Equity Per Share								$1.25	$1.53	$1.99
Parent	2022E EPS									
NMC (Saudi Chemical JV)	$0.05	11.8x		-6.0x	12.8x	13.8x		$0.59	$0.64	$0.69
Parent Interest attributed to utility - 50%	-$0.60	20.2x		0.0x	19.2x	18.2x		-$6.08	-$5.78	-$5.48
Parent Debt- 50%	-$21,165							-$13.71	-$13.71	-$13.71
Total Equity Value								-$19.20	-$18.85	-$18.50
Shares Outstanding									772	
Total Equity Value								$86.00	$93.00	$99.00
Current Share Price								$90.10	$90.10	$90.10
NTM Dividend Yield									4.25%	
Total Return									7.47%	

Source: BofA Global Research estimates, company report, Bloomberg

Please see our latest DUK research here:

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Duke Energy: Mitigation measures to offset pressures and hold the line	Julien Dumoulin-Smith	13 April 2020
Duke Energy: North Carolina: Coal ash, ROE risks; Cleaner upsides, Cost & Reform offsets?	Julien Dumoulin-Smith	26 March 2020
Duke Energy: Upgrading to Neutral: Raising the bar with an improved regulated outlook	Julien Dumoulin-Smith	14 February 2020
Duke Energy: Raising the Ratebase & other nuances	Julien Dumoulin-Smith	13 February 2020

DTE Energy

We forecast 1Q20 adjusted EPS of $1.80 vs. $2.05 in 1Q19 and $1.98 consensus. Our estimate is well below last year's result due to this quarter's unique combination of weather, Covid impacts, and reversals of one time items. We expect consensus estimates to be revised substantially lower going into the Q1 print. We stress non-reg continues to garner disproportionate attention relative to its modest implied value after multiple contraction in midstream sector. We see shares as entirely fairly rated vs. peers (earlier shares offered a double-digit total return on utility-only values).The strategic question embedded is just how to view non-regulated when netting parent level debt against these businesses (with their depressed trading multiples/valuations of late). We appreciate that this is principally a consideration of debt allocation (ascribing some of the holdco debt to the utility or not), but with just ~$2/sh out of $100+/sh stock (<2% of total value), we sense overly focused Street on very limited side of biz.

- **Key Drivers:** Primary drivers include weather which is an 8 cent drag from normalizing 2019 results and a further 17 cent drag given heating degree days (HDD) 16% below normal. Q1 2017 saw a weather impact of similar magnitude with corresponding drag of $13m at the electric utility. We likewise assume weather-related drag of 10 cents at the gas utility given that the HDD deviation from normal was -16% in 2020 vs. +5% in 2019. We additionally assume 1 cent drag at both the electric and gas utilities stemming from demand impact of Covid – this impact is expected to be modest given the timing of shut down orders in late March. We continue to incorporate the impact of new electric rates which went into effect in May 2019 along with correspondingly higher D&A and interest expense. While DTE mgmt. has flagged its previous expectation to utilize financial contingency to mitigate impacts of weather on its utility results, we expect a partial offset to weather impact (and none to Covid impact) in Q1 due to timing.

- **Unknown:** Precise weather-related impacts are difficult to estimate although we see Q1 2017 as a comparable period (albeit with fewer storm expenses). Covid-related demand shifts in late March are expected to show an increase in residential load and a larger (in % terms) decrease across both commercial and industrial (C&I). The Energy Trading business is difficult to forecast owing to the opaque nature of its operations – given significant volatility across most asset classes in the quarter there is potential for an above/below normal quarter, although we do not incorporate this into our estimates.

Table 24: DTE Q1 earnings walk

DTE Energy 1Q20 Earnings Walk	EPS
Adjusted EPS 1Q19	$2.05
Utility	($0.16)
Electric	
Weather - return to normal	($0.03)
Weather - 1Q20	($0.07)
2019 GRC - $273mn effective 5/9/2019	$0.29
D&A, Interest, Other expenses	($0.13)
O&M savings vs. last year	$0.04
Sales impact	($0.01)
OID benefit from investment earnings - 17m gain	($0.09)
Gas	
Weather - return to normal	($0.05)
Weather - 1Q20	($0.10)
D&A, Interest, Other expenses	($0.02)
O&M	$0.02
Sales impact	($0.01)
Tax timing true up from Q1 2019	($0.05)

Table 24: DTE Q1 earnings walk

DTE Energy 1Q20 Earnings Walk	EPS
Non-utility business	($0.03)
GSP	$0.02
P&IP	$0.01
ET	$0.00
Corp & Other	($0.06)
Dilution	($0.06)
1Q20E Adjusted EPS	$1.80
1Q20E Consensus	1.98
2020E BofAe EPS	$6.56
2020E Consensus	6.60
2020 Guidance Midpoint	6.61
Shares Outstanding 1Q19	183
Shares Outstanding 1Q20	188

Source: BofA Global Research Estimates, company report, Bloomberg

Milder weather compounding Covid slowdown in Q1

Q1 2020 was substantially warmer in DTE's service territory than normal, with heating degree days (HDDs) 16% below average levels. The last time the service area experienced conditions with the same order of magnitude deviation from normal was Q1 of 2017 when HDDs 14% above normal created a $13m drag at the electric utility. We also assume that the weather-related drag on the gas business was 10 cents in Q1 2020, as compared to a 5 cent benefit in 2019. The effects of milder weather in 2020 are compounded by the fact that 2019's positive weather result of 5 cents gas and 3 cents electric is being reversed. We expect that DTE mgmt. should be able to utilize its financial contingency to offset a significant portion of weather-related impact in 2020 *throughout the course of the year*, though given timing of warmer months in Q1 we expect a partial offset of weather drag in the quarter, with further mitigation likely in Qs 2-4 through management of timing of O&M expenditures being the primary lever. We note that Q2 is typically a shoulder quarter with relatively low weather impact, while Covid-related slowdown is expected to affect demand in the quarter disproportionately – see more below.

Covid impact on load – Q2 seen most affected

DTE's latest disclosures include earnings sensitivity for all customer classes to a 1% swing in demand. As with most public utilities, residential sales provide the highest margin at $15m annual impact, followed by commercial ($6m), industrial ($1m), and other ($2m). These sensitivities assume a flat 1% impact to demand over the course of a full calendar year. Though DTE has not provided March demand impact by customer class, initial commentary from peer utilities suggests a trend of residential growth in the mid-single digits serving as a partial offset to commercial and industrial sales that decline by 10-15%. Assuming that DTE Electric sees a gain of 5% residential demand and a drop of 15% across the other customer classes through the entirety of Q2, we estimate an earnings impact of -$15m, or 1.2% of DTE's 2020 earnings guidance at the midpoint ($1,270m). Note this is an illustrative case and DTE has not provided demand estimates, and actual demand will vary depending on when Covid stay-at-home restrictions are lifted.

Table 25: DTE electric demand impact

Flat 1% annual impact

Customer type	Sensitivity (%)	Annual earnings impact ($m)
Residential	-1.0%	15
Commercial	-1.0%	6
Industrial	-1.0%	1
Other	-1.0%	2
Total		24
2020 guide midpoint		1,270
Decline impact		-1.9%

Q2 demand shock illustrative

Customer type	Sensitivity (%)	Annual earnings impact ($m)
Residential	5.0%	19
Commercial	-15.0%	(23)
Industrial	-15.0%	(4)
Other	-15.0%	(8)
Total		(15)
2020 guide midpoint		1,270
Decline impact		-1.2%

Source: BofA Global Research Estimates, company report, Bloomberg

We note that DTE's utilities entered 2020 well-positioned with mgmt. touting significant financial contingency that would enable the company to "nail it" in both the electric and gas business – in fact the company reiterated 2020 guidance in March as the Covid pandemic shock was spreading. We expect that mild Q1 weather combined with Covid impact will weigh on earned ROEs in 2020, with the impact partially but not completely offset via O&M management by utilizing the financial contingency built up in 2019. We therefore reduce our forecast for earned ROEs in 2020 at both the electric and gas utilities to 9.9% from 10.0%; note that we had previously reduced our authorized and earned ROE forecast at both the electric and gas utilities for 2021+ to reflect risk around authorized ROEs from the persistent low interest rate environment. With our reduced estimates, we still see the electric and gas businesses achieving results near the low end of mgmt.'s reaffirmed guidance range – with a protracted demand impact related to Covid as the most pressing near-term risk.

Table 26: Utility ROEs incrementally lower in 2020 on weather/Covid

ROEs							
Authorized	2018A	2019A	2020E	2021E	2022E	2023E	2024E
DTE Electric	10.0%	10.0%	10.0%	9.9%	9.9%	9.9%	9.9%
DTE Gas	10.0%	10.0%	10.0%	9.9%	9.9%	9.9%	9.9%
Earned							
DTE Electric	9.8%	10.0%	9.9%	9.9%	9.9%	9.9%	9.9%
DTE Gas	9.5%	10.5%	9.8%	9.9%	9.9%	9.9%	9.9%

Source: BofA Global Research Estimates, company report

Table 27: Utilities still expected to hit guidance range in short + long term: we could readily see upside still

Net Income ($Mn)							
Utility segment	2018A	2019A	2020E	2021E	2022E	2023E	2024E
DTE Electric	669	716	761	830	901	951	1,002
Guidance		*703-717*	*759-773*				
Growth	8%	7%	6%	9%	9%	6%	5%
Guidance CAGR '20-'24		*7-8%*					
BofAe CAGR '20-'24		7.1%					
DTE Gas	159	181	188	206	230	251	265
Guidance		*175-183*	*185-193*				
Growth	7%	14%	4%	9%	12%	9%	6%
Guidance CAGR '20-'24		*9.0%*					
BofAe CAGR '20-'24		8.8%					

Source: BofA Global Research Estimates, company report

Electric rate case decision expected by early May

Under Michigan state law, the commission is required to issue a final decision in the pending rate case within 10 months of the filing, by May 8. The commission has not yet indicated whether it may extend the timeline due to the Covid emergency and staff resources likely focused on ensuring that gas and electric service continues uninterrupted. DTE Electric filed a request for a $343m increase premised on a 10.5% ROE and $18.2B rate base. Staff countered with a recommendation for an increase of $195m, a 9.8% ROE, and $18.1B rate base. Recently, the administrative law judge (ALJ) handling the case issued a recommendation for a rate increase of $99.8m based on an ROE of 9.8% and rate base of $17.1B. At issue in the ALJ recommendation which supports the position of intervener the Association of Businesses Advocating Tariff Equity (ABATE) which claims that DTE's prepaid pension asset of ~$800m be excluded from the working capital portion of rate base as DTE did not establish that the pension asset was fully funded by investor capital or that it provides benefits to ratepayers. This is an area where the ALJ disagrees with commission staff, which approved the inclusion of the asset in rate base in the previous rate case (U-20162) but directed DTE to provide additional evidence that the asset should be included in working capital including the source of the funding of the prepaid pension asset in the current filing. DTE's testimony

asserts that the pension asset is 1) reasonable and prudent as it reduces ongoing pension costs and 2) it contributes to an increased deferred tax component in DTE Electric's weighted average cost of capital, reducing overall cost. The ALJ concludes its argument stating that DTE made "no effort whatsoever" to demonstrate that the entirety of the prepaid pension asset was supplied by investors rather than ratepayers.

Below we include a summary of the rate base impact from the ALJ proposal as compared to both DTE's request and commission staff proposal. Staff's recommendation for approved rate base was generally in line with the company's request, which stands to further highlight the degree to which the ALJ recommendation stands out in proposing to exclude the pension asset.

Table 28: Rate base recommendations

DTE projected rate base ($m)

	DTE	ALJ	Delta	Staff
Net plant	16,775	16,514	(261)	
Working capital	1,392	582	(810)	
Total rate base	18,167	17,096	(1,071)	18,120

Source: MPSC docket #U-20561

Based on intervener, staff, and the ALJ's filings, three outcomes are possible with respect to the pension asset:

- **Accept ALJ recommendation without modification.** In the event that the commission were to accept the ALJ/ABATE position, DTE Electric's revenue requirement would be reduced by $56.8m according to company filings.
- **Accept ALJ recommendation with the modification that pension expense be adjusted which results in higher recovery through rates.** DTE's rebuttal filing claims that to exclude the pension asset without considering the impact on expense is unfairly punitive. The company claims that if the pension asset were excluded from rate base, the pension expense should be increased correspondingly (by $58m per DTE calculation) which would subsequently be recovered in rates, resulting in a largely revenue-neutral outcome.
- **Reject ALJ recommendation – status quo outcome.** This option would not affect the treatment of the pension asset on working capital and DTE would continue to recover. Notably this position is supported by commission staff in docketed reply to exceptions.

Midstream: will gas price recovery de-risk prospects post contracts?

We maintain our forecast in DTE's midstream business, seeing ~9% earnings growth through 2024 from the midpoint of 2020 guidance which already bakes in a ~30% increase over 2019, driven mainly by the full-year contribution of the Momentum midstream assets purchased in Q4 of 2019. Post 2020 growth in the segment is driven primarily by the placing in service of a gathering pipeline at Momentum (late 2020 in-service) as well as continued investment in compression and other organic growth initiatives at NEXUS, Link, and other "legacy" midstream assets.

We likewise maintain a balanced view on DTE's exposure to Indigo Natural Resources, its primary counterparty in the Haynesville basin. Indigo maintains relatively low leverage for its sector (~1.0x EBITDA post-transaction). *Critically, we see the potential for gas price appreciation into the future as offsetting our otherwise concerns embedded on volume related concerns in coming years. For now we see volume-related concerns and broader midstream concerns raised by many investors as simply less relevant given where shares are priced.*

The company is largely hedged forward for its projected 2020 production, with some 2021 volumes hedged as well - while commodity price risk exists given ongoing supply-demand imbalance in US basins, we note Indigo mgmt. appears to be prudently hedging its forward exposure amid an uncertain price environment. We note DTE maintains minimum volume commitments (MVCs) with Indigo covering 90% of its expected volume from the Haynesville basin through 2020, with volume growth covering the remaining 10% of company forecast revenue - note forward sales by Indigo suggest performing under the MVCs should be an achievable goal in the near term.

Bottom line: the market has discounted DTE shares to the point where they trade with little implied value in the midstream business. We stress that investor attention here is disproportionate given healthy utility earnings visibility through the forecast despite near term risks.

EPS Estimates

We previously updated our 2020 estimates to reflect lower earned ROEs of 9.9% at the Electric and Gas utilities (10.0% previously). Our new consolidated 2020 estimate of $6.56 is below the midpoint of the $6.47-6.75 range recently reiterated by mgmt. We continue to see the long-term outlook as largely intact, having previously reduced our earned ROE assumption at the Electric and Gas utilities to 9.9% to reflect rate case risk in a low rate environment. Our updated 2020 estimate is several cents below Street though we stress downside to consensus estimates as the effects of Covid become more fully integrated in forecasts. We also highlight that earnings from the Energy Trading business may exhibit more volatility in the short term, though we continue to forecast a growth trajectory in line with previous mgmt. guidance given the opaque nature of the segment.

Table 29: EPS estimates

Earnings Contribution	2018A	2019A	2020E	2021E	2022E	2023E	2024E
DTE Electric	3.70	3.87	3.96	4.28	4.56	4.57	4.80
DTE Gas	0.88	0.98	0.98	1.06	1.17	1.21	1.27
Total utility	4.57	4.85	4.94	5.34	5.73	5.77	6.07
Non-utility segment							
Gas Storage & Pipeline	1.29	1.15	1.46	1.63	1.81	1.84	1.94
Power & Ind. Products	0.90	0.72	0.72	0.79	0.45	0.53	0.63
Energy Trading	0.22	0.16	0.11	0.13	0.15	0.16	0.16
Corp & Eliminations	(0.67)	(0.58)	(0.65)	(0.71)	(0.72)	(0.67)	(0.64)
% of total	*-11%*	*-9%*	*-10%*	*-10%*	*-10%*	*-9%*	*-8%*
Total non-utility	1.73	1.45	1.64	1.85	1.69	1.87	2.09
DTE Consolidated	6.30	6.31	6.56	7.17	7.40	7.63	8.14
Guidance	*0.00*	*6.02-6.38*	*6.47-6.75*				
Prior Estimates		*6.31*	*6.65*	*7.21*	*7.44*	*7.68*	*8.20*
Consensus		6.24	6.60	7.07	7.48	7.82	
			4.0%				
DTE Guidance 6% CAGR ('20-24)			6.61	7.01	7.43	7.87	8.34
Low End				6.94	7.29	7.65	8.03
High End				7.07	7.57	8.10	8.66
BofAe CAGR '20-'24e		5.3%					
Shares outstanding	*181*	*185*	*192*	*194*	*197*	*208*	*209*

Source: BofA Global Research Estimates, company report, Bloomberg

PO to $112; reiterate Neutral

We view risks around DTE's growth story as balanced, given the premium utility growth seen in the forecast period as balanced by less certain midstream outlook, primarily driven by single counterparty exposure at Blue Union. DTE's updated long-term guidance calls for operating EPS growth at a 5-7% CAGR from the midpoint of 2020's initial guidance of $6.61. Our updated forecast results in a 2020-2024 consolidated EPS CAGR of 5.3%, near the midpoint of mgmt's range. We apply peer group multiples of 17.6x for both the electric and gas utilities (previously, 17.9x/17.9x for electric and gas,

respectively), 8.0x midstream EBITDA multiples to the cogen/legacy coke battery and GSP businesses, a lower 6x EBITDA multiple to the Energy Trading business to reflect its lower-quality earnings profile, and an NPV valuation to the RNG development opportunity which yields an implied EBITDA multiple of 6.8x. We also tweak our valuation discount for the Momentum Midstream biz to -2.0x to reflect ongoing risk around producer activity in US shale basins. With these assumptions our resulting $112 PO reflects high single digit upside potential and we remain Neutral.

Table 30: DTE SOTP

DTE Energy Segments	2022E EPS	Premium /(Discount)	Group Multiple	Applied Multiple	Value
Utility					
Group Peer Multiple - Electric			17.6x		
Group EPS '18-'22 CAGR - Electric			5.00%		
DTE Electric (Distribution)	$4.56	1.0x	18.5x	19.5x	$88.92
Group Peer Multiple - Gas			17.6x		
Group EPS '18-'22 CAGR - Gas			5.10%		
DTE Gas	$1.17	1.0x	18.5x	19.5x	$22.73
Utility Equity Value per Share					$111.65

Non-Utility	2022E EBITDA	Premium /(Discount)	Group Multiple	Applied Multiple	
P&I					
Cogen + Legacy Coke Batteries	79	-2.0x	8.0x	6x	$477
NPV of RNG Development	$558		Implied Multiple ---->	6.8x	$558
REF Tax Credit Value (DCF), 2020-2023 @ 6%	198				$198
Energy Trading	44	0.0x	6.0x	6x	$263
Midstream (GSP)	885	-0.7x	9.0x	8x	$7,313
Allocated EBITDA	560	0.0x	9.0x	9x	$5,038
Momentum Midstream	$325	-2.0x	9.0x	7x	$2,275
Holding Company Borrowings					
Consolidated Projected B/S					20,313
(-) DTE Gas / DTE Electric Debt					(11,758)
Net Non-Utility Net Debt					8,554
Non-Utility Equity Value					$254
Shares Outstanding					197
Non-Utility Equity Value per Share					$1.29

	2022E EPS	Premium /(Discount)	Group Multiple	Applied Multiple	
Corp & Other (ex-Interest Expense)	(0.05)	0.0x	19.5x	19.5x	($0.98)
Utility Equity Value per Share					($0.98)
12 Month Price Objective					$112
Implied Consolidated P/E					17.8x
Dividend Yield NTMe					3.9%
Estimated Total Potential Return					9.7%
Shares outstanding by 2022					197

Source: BofA Global Research estimates, company report, Bloomberg

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Title: Subtitle	Primary Author	Date Published
DTE Energy: Still Focused on Nailing It Despite Covid Concerns: Rate Case Risks, Gas Offsets	Julien Dumoulin-Smith	13 April 2020
DTE Energy: Who's Ready to Reaffirm Guide? DTE Does & names new CFO too	Julien Dumoulin-Smith	25 March 2020
DTE Energy: Angling for a utility-only value for one that can 'nail it'?	Julien Dumoulin-Smith	09 March 2020
DTE Energy: Poised to deliver in '20, but earnings quality concerns persist	Julien Dumoulin-Smith	07 February 2020

Edison International (EIX)

EIX shares have underperformed the broader utility index since early March (-4% vs XLU) despite decoupling and other regulatory mechanisms to offset COVID related pressures given still $800mn in pending equity needs. While we see recent moves by mgmt. to allow for delay of equity issuance into 2H, potentially allowing for the broader market to recover we remain focused on the total quantum of equity needs to right-size the balance sheet. The '20 equity addresses mgmt.'s current expectations for wildfire related liabilities and timely recovery of memo accounts ($1.09bn in aggregate); we believe clarity on these outcome remain protracted and uncertain at best. With shares trading at a 30% discount to the group (20% after adjusting for potential for additional dilution), we sense investor optimism that shares can close the gap and re-rate to some extent. Nonetheless, we remain sober on these prospects pending clearer articulation of equity from mgmt. and maintain our Neutral rating.

1Q20 EPS walk

We forecast 1Q20 EPS of $0.81 compared to 1Q19 results of $0.63 and consensus estimates of $0.77.

- **Key drivers**: Positive YoY drivers include increase FERC and CPUC core contribution (+$0.16), lower O&M expenses (+$0.04), energy efficiency benefits, and higher financing and other benefits, including lower D&A (+$0.08).
- **Unknowns**: We highlight uncertainty with O&M expenses as it continues to be somewhat challenging to handicap given the company will defer costs that are over and above the authorized limit; with $0.14 drag of O&M expected in 2020 compared to $0.25 drag in 2019, we expect a positive variance in 1Q20 and highlight that much of the accelerated covered conductor program occurred in 1H19 last year and not necessarily the same cadence this year. Another unknown item is just how much equity of the $800mn in 2020 guidance has been issued to date; we assume none given the state of equity markets with the issuance likely deferred to 2H20.

Table 31: EIX 1Q20 EPS walk

Edison Electric 1Q20 Earnings Walk	EPS
Edison Electric 1Q19 Adjusted EPS	$0.63
SCE	$0.25
FERC ROE & RB Growth	$0.01
CPUC RB Growth and 52% Equity Cap	$0.15
O&M Effect	$0.04
Depreciation	$0.00
Property Taxes	$0.00
Energy Efficiency	$0.02
Wildfire Mitigation Costs	($0.04)
Interest expense for fund contribution	($0.03)
Financial and Other benefits	$0.08
EIX Parent and Other	($0.07)
HoldCo Drag	$0.00
Dilution	($0.07)
1Q20E Adjusted EPS	$0.81
1Q20 Consensus	$0.77
2020 BofA EPS	$4.45
2020 Consensus	$4.48
2020 Guidance	4.32-4.62

Source: BofA Global Research estimates, company report, Bloomberg

Pending equity needs: waiting on more certainty

The recent $800mn term loan that EIX drew down on likely provides flexibility with the timing of EIX's pending equity issuance ($600mn of "new" equity + $200mn on ATM). While the '20 equity addresses mgmt.'s current expectations for wildfire related liabilities, timely recovery of memo accounts ($1.09bn in aggregate), and a clarity on

these outcome remain protracted and uncertain (mgmt.'s confidence remains a tad cryptic). The recent ALJ approval of the capital structure waiver is just one piece to the puzzle to gain more clarity on forward looking equity assumptions.

Capital structure waiver approved by ALJ

The Administrative Law Judge (ALJ) issued a proposed decision (PD) approving the applications of EIX for the waiver of the capital structure. The ALJ recommended: 1) approve the waiver for *two years* or until the CPUC determines cost recovery for '17/18 wildfire events, whichever comes first (we expect some migration to HoldCo debt through this period likely); 2) limit the scope of exclusions to non-cash charges and debt issuance equal to or less than the aggregate net non-cash charges stemming from the '17/18 fires; and, 3) SCE should be required to submit an advice letter stating it has returned to its authorized cap structure or a timeline/plan over which SCE will return 90 days after the CPUC determines cost recovery of '17/18 fires. The ALJ also recommended EIX should notify the CPUC if its equity ratio declines 1% or more from most recent level reported. *We perceive the terms of approval as adding pressure to provide a clear(er) view of equity needs in parallel to Street - albeit with substantial uncertainties may just provide a transition to HoldCo rather than net increase in equity to pay down OpCo debt that waiver would support for two-years.*

For EIX, the approval would represent one of three steps needed to keep $600mn of 2020 equity needs to address wildfire related costs intact. The other criteria include no movement in the wildfire liability of $4.9bn and cost recovery of $1bn in memo accounts (as well as those associated with 2020). We reiterate our uncertainty on total equity needs but see two-year transition as likely tied to a shift in debt rather than further equity (as best we read prior commentary from mgmt), but this remains unclear (as mgmt has specifically qualified equity contemplated thus far is strictly for 'core' purposes for minimal needs on ongoing basis).

Tracking the memo recovery

Mgmt. recently filed its 2019-2019 Fire Memorandum Account (FMA) update, which initiated track 2 of the 2021 General Rate Case (GRC) proceeding. The company is seeking recovery of $509mn of O&M related expenses and $302mn of capital spending. This is considered track 2 of its memo recovery request with a decision not expected until 1Q21 with the GRC. The more near-term item is from the GSRP with a decision expected in April 2020, although again these costs are not similar to the other memo accounts and is more related to capital spending rather than O&M with the latter having a bigger impact on cash flows. The other items pertain to a decision with Wildfire Memorandum Expense Account (WEMA) for higher insurance cost vs. those approved (requesting $505mn in recovery) with a decision expected in Aug. 2020 and the (Catastrophic Event Memorandum Account) CEMA with a decision in March 2021 (for $88mn request).

We stress that this does not include 2020 costs that mgmt. will file at YE w/ a decision in ’22 (potentially growing by $200-300mn incremental). Currently, mgmt. is deferring these costs, although it’s not getting any cash recovery, hence the impacts to credit metrics. We continue to see uncertainty around these items and look for more clarity in the coming months to understand the totality of equity needs as mgmt. has its own internal planning assumptions around recovery.

Bottom line, recovery clarity could still take some time and we continue to see some risks on recovery (whether with the ~$120 mn of recoveries not necessarily tied to precedence or the ~$500Mn of additional insurance expenditures tied to last year that mgmt. did not receive approval for in its last rate case).

Table 32: EIX Wildfire Memorandum Accounts

Memorandum Account	Capital Expenditure	O&M Spent	Total Request	Timeline
Wildfire Mitigation Plan	302	304		PD 1Q21
Fire Hazard Prevention		198		PD 1Q21
Fire Risk Mitigation		8		PD 1Q21
Total 2018-2019 FMA	302	510	500	
Grid Safety And Resiliency Program	419	42	NA	Apr-20
Wildfire Expense Memo Account	-	341	505	PD Aug 2020
Catastrophic Event Memo Account	57	79	88	PD March 2021
Total Other Wildfire-related Memo Accounts	476	462	593	
Grand Total	778	972	1,093	

Source: BofA Global Research estimates, company report

COVID-19 related Impacts

Mgmt. has noted that most its critical work (safety work, wildfire mitigation spend) continues with only 10-20% of work deferred and is thus far not seeing any impacts to its capex budget or permitting. Given minimal impact to capex, decoupling, and ability to delay 2020 equity issuance, we largely see 2020 EPS guidance as intact.

Decoupling limits impact due to any loss of load

EIX has a decoupling mechanism with cost recovered on an annual basis. The regulatory framework requires the California Utilities to recover authorized revenue based on estimated annual demand forecasts approved in regular proceedings before the CPUC. However, actual demand for natural gas and electricity will generally vary from CPUC-approved forecasted demand due to the impacts from weather volatility, energy efficiency programs, rooftop solar and other factors affecting consumption.

Under the General Rate Case (GRC)/California Public Utility Commission (CPUC) jurisdiction, Investor Owned Utilities (IOUs) get recovery of an uncollectible percentage of revenue based on a historical 10-year average of actual uncollectible expense. To the extent that costs are in excess of the uncollectible factor result, there would be an earnings impact. For Federal Energy Regulatory Commission (FERC) rates, the formula rate mechanism could provide for a true-up. We would expect the Emergency Customer Protections Memorandum Account (ECPMA) to track costs related to COVID-19 given the state of emergency in CA.

Managing the upcoming wildfire season will be critical

Communication with local authorities and the state is crucial given the need to focus on investments to harden the grid ahead of the upcoming wildfire season while at the same time procuring generators for its most critical customers. We see prioritization of wildfire mitigation and communication with the market as critical, especially ahead of the upcoming wildfire season. Public Safety Power Shutoffs (PSPS) efforts are likely to continue into the '20 season; and while weather conditions similar to last year would result in fewer shut-offs, mgmt. is going to continue covered conductors in the riskiest areas (1K circuit miles) and re-inspect structures in more than 50% of high-fire risk areas in order to raise the wind threshold and have an overall smaller impact on customers.

ROE concerns abated for now

Given the volatility of Moody's Baa Index and utilities waived the trigger in the '08 financial crisis (to the upside), we could see something similar happen this time around to avoid volatility in customer rates. We stress that the Moody's BAA Utility Bond index has since rebounded, placing rates within the band and abating any near-term risk to potential CPUC authorized ROEs. Meanwhile, we continue to see potential for a FERC ROE settlement regardless of base ROE policy uncertainties.

EPS Estimates

We provide our latest EPS estimates for EIX, tweaking slightly given the current share price that we assume equity is issued at. EPS estimates largely in-line with street, although above consensus in outer years given we net out equity in our SOTP rather than through dilution in EPS (stress consensus estimates are not transparent on amount of equity assumed).

Table 33: EIX EPS

EIX Mini-Model	2018A	2019A	2020E	2021E	2022E	2023E	2024E
Authorized Capital Structure							
Authorized Equity Capital %	48%	48%	52%	52%	52%	52%	52%
Authorized CPUC ROE	10.30%	10.30%	10.30%	10.30%	10.30%	10.30%	10.30%
FERC ROE Build							
FERC Base Rate	9.92%						
CAISO (RTO Participation Adder)	0.50%						
Avg Project Incentive Adder	0.78%						
Assumed Equity Capital %			47%	47%	47%	47%	47%
Authorized FERC ROE Build	11.2%	11.2%	10.3%	10.3%	10.3%	10.3%	10.3%
Ratebase Growth							
Ratebase - Including Adjustments Below (Avg)	28,601	30,913	33,694	36,114	38,062	39,948	42,069
We include mitigation spending in rate base and then net out EPS impact below							
Guidance Low ($Bn) (Ex. ~$1.6Bn of fire risk mitigation from AB 1054)				-	-	-	
Guidance Mid ($Bn) (Ex. ~$1.6Bn of fire risk mitigation from AB 1054)	28,500	30,800	33,400	35,900	38,200	41,000	
Guidance High ($Bn) (Ex. ~$1.6Bn of fire risk mitigation from AB 1054)				-	-	-	
Breakdown:							
CPUC Ratebase (Avg)	22,107	24,038	26,345	28,863	31,410	33,920	36,432
FERC Ratebase (Avg)	6,144	6,875	7,349	7,252	6,652	6,028	5,637
Ratebase Growth	9.4%	8.1%	9.0%	7.2%	5.4%	5.0%	5.3%
% FERC	23%	22%	22%	19%	16%	14%	13%
Shares (Basic)	326	342	377	379	380	382	384
Shares (Diluted)	326	340	370	380	381	383	385
Ratebase-Only EPS	4.37	4.59	4.77	5.00	5.26	5.50	5.78
Additions/Subtractions to Spend							
Storage Upside (Inlcuded in base CaEx			0.00	0.00	0.00	0.00	0.00
Transmission project - pending potential rejection (~$100 Mn capex)			-0.01	-0.01	-0.01	-0.01	-0.01
Wildfire mitigation spend (~$1.6bn excluded from earning ROE)			-0.10	-0.08			
Charge Ready II ($561Mn of Capital)			0.02	0.04	0.06	0.08	0.08
Changes to Capital Structure and ROE Adjustments							
Cost Savings (ex-Debt Cost Savings)	0.00	0.02	0.00	0.00	0.00	0.00	0.00
Debt Cost Savings	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Interest expense from Wildfire Contribution Debt (~$1.2bn)		0.00	-0.11	-0.11	-0.11	-0.11	-0.11
Energy Efficiency	0.03	0.05	0.04	0.04	0.04	0.04	0.04
AFUDC Benefits		0.24	0.25	0.25	0.25	0.25	0.25
Corp Donations and Executive Comp			-0.14	-0.25	-0.25	-0.25	-0.25
Tax benefits and Other (insurance?)	-0.08						
FERC Recovery	0.02	0.09					
Z Factor Upside (1Q19)		0.04					
Post Tax Adj	0.00						
Parent Drag & Edison Energy				*Breakeven run-rate heading into 2020*			
Edison Energy Group (EEG) --> Can it improve?	-0.04	0.00	0.00	0.00	0.00	0.00	0.00
SoCore Impairment							
Parent and Other	-0.23	-0.33	-0.26	-0.25	-0.25	-0.25	-0.25
Toal Parent & Other Drag (Incl EEG)	-0.27	-0.33	-0.26	-0.25	-0.25	-0.25	-0.25
Total EPS (Basic)	4.14	4.67	4.38	4.63	5.00	5.27	5.54
Total EPS (Diluted)	4.14	4.70	4.46	4.61	4.98	5.25	5.53
Previous estimate		4.70	4.45	4.60	4.97	5.24	5.51
Consensus		4.77	4.44	4.64	4.76	5.11	
Guidance		4.70-4.90	4.32-4.62				

Source: BofA Global Research estimates, company report, Bloomberg

Valuation: $69

We move our PO to $69 (from $61) based on peer multiples of 17.6x (from 16.2x). While we see upside in our SOTP analysis, we still see the total quantum of equity needs as uncertain and dependent on recovery of memo accounts and wildfire liabilities remaining unchanged. We admit disproportionate upside vs. peers even when including additional equity to address balance sheet but unknown around future wildfire exposures keeps us Neutral rated.

Table 34: EIX SOTP Valuation

EIX SOTP							
SCE Components	% SCE	Authorized ROE Reflected	2022E Earnings	2022E EPS	Peer Multiple	Premium/Discount	Value per Share
Group Peer Multiple - Electric					17.6x		
Group EPS '18-'22 CAGR - Electric					5.00%		
CPUC - Core	84%	10.30%	1,682	$4.41	18.5x	-3.0x	$68.28
CPUC/FERC - Further Capital	0%		-9	($0.02)	18.5x	-3.0x	($0.38)
FERC	16%	10.30%	322	$0.84	18.5x	-3.0x	$13.07
Edison Energy			0	0.00	10.0x	0.0x	$0.00
Parent/Other			-96	-0.25	18.5x	-3.0x	($3.88)
Total EPS				$4.98			
Ongoing contribution to Wildfire Fund				$Mn	EPS	Multiple	
NPV of Ongoing Wildfire Contribution ($945mn over 10yrs)				($664)			($1.74)
Total Liabilities				$Mn			
Wildfire Liabilities Assumptions							
Current Charge: 2017 Thomas, Mudslides, Woolsey Fires: Low End of Range				-4,900			
Gross Up Factor			20%	-5,880			
Insurance Receivable				2,000			
Wildfire Liability Incl Insurance Offset				-3,880			
FERC Allocation ~5%			5%	194			
Net Exposure				-3,686			
Post Tax Net Exposure			28%	-2,654			
Equity Issuance in 2020 (reflected in EPS est)				600			
Remaining Exposure				-2,054			
Equity Dilution from wildfire liability funding							
Funding of '17/18 wildfire liabilities							
Liabilities:	Equity Issued	Shares Issued	Shares O/S (pre-dilution)	New Share O/S	Equity Dilution	Equity Value - Prior dilution	Value Per Share
Wildfire Liabilities - Post-tax	*2054*						
Total	2054	34	381	415	9%	$75	
Equity Value							$69
Price Appreciation							11.2%
2020 Yield							4.1%
Total Return							15.29%
Shares- Post Dilution	*415*						

Source: BofA Global Research estimates, company report, Bloomberg

Please see our latest EIX research below:

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Edison International: Can SoCal Recover? The Total Costs Remain the Ambiguity	Julien Dumoulin-Smith	27 March 2020
Edison International: A Veritable Feast of '20 EPS Factors Plus a Splash of FFO/Debt Sobriety	Julien Dumoulin-Smith	28 February 2020
Edison International: Examining the range of equity needs built into expectations	Julien Dumoulin-Smith	31 January 2020
Edison International: Closing the discount as legacy liability uncertainty lingers	Julien Dumoulin-Smith	10 January 2020

Entergy (ETR)

Our 1Q20 EPS estimate of $1.01/sh is slightly below Street estimates at $1.08/sh. Our 2020 estimate of $5.51 was recently updated to below the midpoint of mgmt.'s range of $5.45-5.75. We see the double impact of milder weather in Q1 and potential lost sales from prolonged Covid-related shut in orders as driving downside risk in the near term. We see ETR as well-positioned for managing the difficult operating conditions in 2020 given the opportunity to rely on flexing the O&M lever as highlighted by mgmt. on our recent conference call, as well as significant visibility into industrial project pipeline in its Gulf service territory which remains intact. We continue to see the renewable angle as the principal long-term play as the company looks to replace several GW of aging fossil generation toward the back half of the decade – with the recent 250 MW solar RFP announcement the latest example. Maintain Buy.

ETR 1Q20 Earnings Walk

We forecast 1Q20 adjusted EPS of $1.01 vs. $0.82 in 1Q19 and $1.08 consensus.

- **Key Drivers:** Key positive drivers include the implementation of new rates (+$0.46sh) including ETR AR through the Formula Rate Plan (FRP), ETR LA through the AMI rider and the base rate proceeding, and a full quarter's effect of the SCPS rider and Choctaw in rates at ETR MS. We additionally see weather as being a small uplift though this is driven by normalization of temps vs. 2019 as 2020 HDDs were below normal across the service territory. Negative drivers include higher O&M spend (-$0.05), and higher D&A primarily driven by addition of new generation assets and ongoing investment in transmission and distribution rate base (-$0.14).

- **Unknowns:** Weather is expected to be a small uplift on Q1 results; however magnitude is difficult to estimate. The magnitude by which industrial load growth is affected by Covid related shut downs is a meaningful consideration though we note some latitude to manage this through O&M.

Table 35: ETR 1Q20 earnings walk

Entergy 1Q20 Earnings Walk	EPS
1Q19A	$0.82
Utilities	$0.20
Weather	
Return to normal	$0.12
Quarterly effect	($0.10)
Revenue impact	$0.46
AMI	$0.02
Non-Fuel O&M	($0.05)
Depreciation	($0.14)
Interest Expense and Interest Income	($0.08)
Income tax rate	($0.04)
Parent and Other	$0.03
Pension	($0.01)
Other	$0.04
Dilution	($0.03)
1Q20E Adjusted EPS	$1.01
1Q20 Consensus	1.08
2020 Adjusted EPS	$ 5.51
2020 Consensus	$5.57
2020 Guidance	5.45-5.75

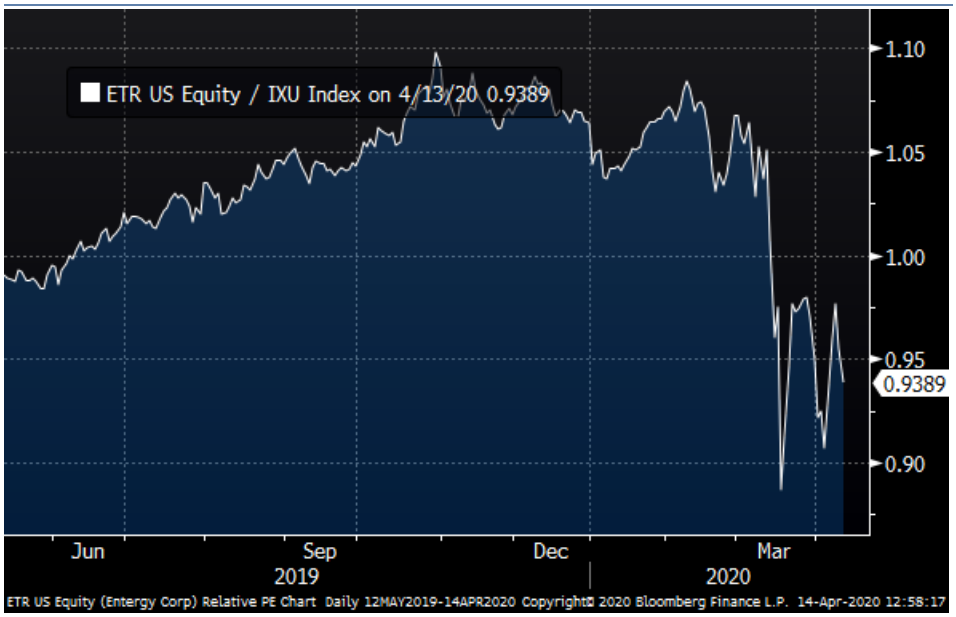
1Q19 shares outstanding	192
1Q20 shares outstanding	200

Source: BofA Global Research Estimates, company report, Bloomberg

What do we think of shares?

Shares of ETR de-rated vs. the peer group at the outset of the Covid crisis and now trade at a relative discount to the group on a forward PE basis – shares remain 1-2x turns below our electric peer group multiple for 2022 EPS since beginning their de-rating in early March. ETR's 2020 forecast included an assumption of 2% growth in weather-adjusted billed sales growth which included +5.5% growth in industrial sales with residential and commercial slightly down – with our previously-lowered estimates, we are assuming a 4-5% decline in industrial sales ($0.08-0.10 EPS impact), similar to that experienced in the 2008-09 recession, with shares continuing to screen cheap with our lower forecast. Mgmt. additionally indicated that no large customers with industrial projects in the pipeline have delayed or otherwise changed plans for new build facilities along the Gulf Coast, a signal that long-term demand growth remains intact despite near term headwinds. We maintain our confidence in ETR's long-term sustained investment profile between its entirely unscrubbed coal portfolio of ~2.2 GW and its largely steam-based gas and oil fleet which totals ~7 GW. We see investment in replacing these aging assets as the driver toward further re-rating with ETR steadily moving down the road of closing legacy nuclear plants and executing on its top quartile ratebase growth among peers and our estimated ~6% EPS CAGR through 2022. The renewable opportunity remains considerable as utility scale solar in its Mississippi and Louisiana territories and potentially wind in Arkansas are poised to replace aging fossil generation in the coming decade, supporting earnings growth over the medium to long term.

Exhibit 2: ETR relative value chart



Source: Bloomberg

Sizing the Covid impact on demand – look to '08

Mgmt.'s most recent comments regarding Covid impact on demand the company does has not seen a meaningful reduction in demand from either Residential, Commercial, or Industrial customers but acknowledges that an impact is expected as the slowdown continues. Given ETR's largely Gulf-region service area, the largest source of its demand is from Industrial customers which account for an estimated 40% of load, followed by Residential (~31%) and Commercial (~29%). Given different characteristics of each load type, mgmt. estimates that margins and corresponding EPS impact from Industrial ($0.02 EPS per 1% change in MWh sold) customers to be lowest among the three groups with Commercial ($0.05) and Residential ($0.09) following.

Table 36: ETR customer classes: we admit more load exposure to industrial, but perceive real residential offset given 9c:2c relative EPS exposure

Customer Class	% of Load	EPS impact
Industrial	40%	0.02
Residential	31%	0.09
Commercial	29%	0.05

Source: BofA Global Research Estimates, company report

During the 2008 crisis, demand from its Industrial customers declined by 4.5% in 2008 and 2009, followed by a rebound where growth averaged ~3% per annum for the decade that followed. While mgmt. expects some as-yet-unquantifiable impact on its Industrial load, thus far the impact has been limited. Mgmt expects the Gulf region to remain resilient during the economic slowdown given access to cheap natural gas feedstock, high-tech nature of industrial operations, and access to inexpensive electricity in its territory.

Managing opex is one of the key levers that mgmt. expects to utilize to offset declining load growth amid a likely slowdown. Flexing spending is a common practice for managing the effects of short term impacts such as above or below-average weather, with the ability to manage spending in the near term to partially mitigate the impact of lower growth. The other key lever being continuous improvement, which results in a more long-term bending of the opex curve – mgmt. points to last year's Q2 result where permanent cost cuts resulted in an increase in headroom for additional capex investment.

Changes in demand are an important driver as ETR has no decoupling in any of the jurisdictions where it operates – LA, AR, TX, MS, and NO. The highest sensitivity to changes in demand is residential sales with $0.09 EPS impact for a 1% change in demand, while the commercial impact of $0.05 and industrial impact of $0.02 are more tempered. While ETR does not have bad debt expense tracking across its jurisdictions, historically it has been able to achieve recovery of outsized bad debt expenses via regulatory assets. Off system sales are generally not a large driver of variability and not expected to be in the current environment. ETR has formula-based ratemaking in all jurisdictions except NO and TX, allowing for more timely recovery than under a traditional rate case structure, another lever that could potentially mitigate lost revenues due to the exogenous Covid shock.

Solar dev: Sunflower approved, 250 MW LA RFP coming

ETR MS' 100 MW Sunflower Solar facility received approval from the state's utility commission in April, clearing the way for the project to go forward. Under ETR's agreement with developer Recurrent Energy, Recurrent will construct the plant with ETR taking over upon completion. Under the proposed recovery mechanism ETR MS will add the $153m project cost to rates contemporaneous with the closing of the transfer from the developer to the utility under ETR MS' existing formula rate plan mechanism. The decision by the utility commission came in under ETR's original estimated time frame of Q2 2020 with expected project completion and transfer date by the end of 2021.

Separately ETR has announced the issuance of a new 250 MW RFP for solar generation in Louisiana. The proposals are to be structured either as build-own-transfer similar to Sunflower or self-build alternatives for up to 250 MW of generation, and/or one or more PPAs for up 100 MW. Projects are required to have a fully executed interconnection agreement with the Midcontinent Independent System Operator (MISO). Optional storage may be included with proposals as well. Draft proposals are due in April and final submissions are due in June with bidder registration to take place in July.

Grand Gulf lease complaint questions recovery

System Energy Resources Inc. (SERI) has been involved in multi-year complaints regarding its ROE and equity component as well as its sale-leaseback renewal. The sale-leaseback renewal docket (EL18-152) received a proposed administrative law judge (ALJ)

decision in April under which the ALJ found that SERI had recovered most of the cost of the original plant under its lease signed in 1988 that ran through 2015 (since renewed), and that there is no need for SERI to continue to recover its annual lease payments of 17m annually since lease renewal in 2015. ETR maintains that the lease transaction was entered prudently and has resulted in significant customer savings over the years, and that recovery should continue under the current lease. We note that the potential impact on near-term earnings would be limited to any reserve taken by SERI in order to account for a potential adverse ruling. While no formal timeframe has been set out for a final ruling by the Federal Energy Regulatory Commission (FERC), past precedent suggests that a final ruling would not be likely until 2021 or later.

EPS estimates

We previously reduced our 2020 estimates reflecting likely near-term impacts from lower industrial demand driven by fallout from the COVID crisis. Similar to the 2008-09 crisis, we adjusted our 2020 estimates to reflect a 4-5% decline in industrial sales (approx. $0.08-0.10 EPS impact per ETR sensitivities), though the key in our view is to what extent mgmt. is able to offset the impacts of lower industrial output with opex reductions. Meanwhile we stress that different from 2008-2009, ongoing industrialization projects do not appear poised to end and its critical to watch how these trend in coming months with regards to '20 industrial sales (there could very well be more of a lag effect stretching into '21 given both 12-month trialing C&I peak demand charges along with the ongoing growth of projects already in construction in petrochem, etc). We remain toward the low end of mgmt's guidance range in 2020 when we expect the most impact from Covid to hit, with a consolidated EPS trajectory within mgmt's long term 5-7% range in the latter years of the forecast period.

Table 37: ETR estimates

EPS by Business							
Subsidiary	2019A	2020E	2021E	2022E	2023E	2024E	2025E
EAI	1.33	1.49	1.61	1.73	1.84	1.93	2.04
ELL	3.51	3.43	3.63	3.96	4.21	4.47	4.75
EMI	0.61	0.71	0.75	0.80	0.85	0.89	0.94
ENOI	0.27	0.23	0.24	0.24	0.24	0.24	0.25
ETI	0.81	0.78	0.91	0.96	1.01	1.08	1.16
SERI	0.50	0.40	0.40	0.41	0.41	0.42	0.43
Other	(0.08)	0.00	(0.00)	0.00	(0.00)	(0.00)	0.00
Utilities	6.95	7.03	7.54	8.08	8.57	9.04	9.57
Parent & Other	(1.55)	(1.53)	(1.58)	(1.69)	(1.69)	(1.70)	(1.72)
Utility Parent & Other (UP&O) - BofAe	5.40	5.51	5.96	6.39	6.88	7.34	7.85
Special Items							
Adjusted UP&O	5.40	5.51	5.96	6.39	6.88	7.34	7.85
Guidance	5.25-5.45	5.45-5.75	5.80-6.10	6.15-6.45			
Midpoint of Guidance	5.35	5.60	5.95	6.30			
CAGR off 2019 Adjusted EPS Guide Mid (5-7% LT Growth)		2.95%	5.52%	6.12%	6.48%	6.53%	6.60%
Competitive Business (EWC)							
Consolidated Estimates	5.40	5.51	5.96	6.39	6.88	7.34	7.85
Prior Consolidated Estimates							
Guidance	5.25-5.45	5.45-5.75	5.80-6.10	6.15-6.45			
Consensus	5.37	5.57	5.87	6.36	6.69		
Dividend	*3.66*	*3.72*	*3.84*	*4.07*	*4.31*	*4.57*	*4.85*
Div Payout 65-75% of UP&O	67.8%	67.5%	64.5%	63.7%	62.7%	62.3%	61.7%
Overall ROE	10.5%	9.6%	9.6%	9.6%	9.5%	9.5%	9.5%

Source: Bank of America estimates, company report, Bloomberg

Valuation: PO $122, maintain Buy

Our PO moves to $122/sh applying our electric utility sum of the parts multiple of 17.6x to each of ETR's utilities and grossing the multiple up for capital appreciation by 5%. We reduce 2.0x valuation premiums at EAI, ELL, EMI and 1.0x premiums at ENOI and ETI to reflect downside risk associated with lost sales. On our estimates, ETR's total return prospects remain compelling at current valuations, particularly as shares have de-rated

vs the peer group of late. Reiterate Buy. *We see ETR as among the most compelling opportunities in our utility coverage given implied concerns on load and Oil & Gas exposure. We emphasize while there could indeed some further load risk, embedded Formula Rate Plans (FRPs) should enable resiliency. These FRP mechanisms are frequently under-appreciated relative to filters screening for decoupling by investors.*

Table 38: ETR SOTP

Entergy: Sum of the Parts Valuation

Group Peer Multiple - Electric			17.6x					
Group EPS '18-'22 CAGR - Electric			5.00%					
Core Regulated Electric Utilities	2022E EPS		Peer Multiple			Equity Value ($/Sh)		
			18.5x					
		Low	Base	High	Premium/Discount	Low	Base	High
Entergy Arkansas (EAI)	$1.73	18.5x	19.5x	20.5x	1.0x	$31.92	$33.65	$35.38
Entergy Louisiana (ELL)	$3.96	18.5x	19.5x	20.5x	1.0x	$73.14	$77.10	$81.05
Entergy Mississippi (EMI)	$0.80	18.5x	19.5x	20.5x	1.0x	$14.72	$15.52	$16.31
Entergy New Orleans (ENOI)	$0.24	17.5x	18.5x	19.5x	0.0x	$4.16	$4.40	$4.64
Entergy Texas (ETI)	$0.96	17.5x	18.5x	19.5x	0.0x	$16.70	$17.66	$18.61
Total Regulated	$7.68	18.3x	19.3x	20.3x		$140.65	$148.32	$156.00
Parent Preferred Income (ELL)	($0.62)		18.5x		0.0x		($11.37)	
Total Utility Value	$7.06	18.3x	19.4x	20.5x		$129.27	$136.95	$144.63

Parent Adjustments	$Mn	Weight	Weighted Value ($Mn)	
HoldCo Senior Notes	1,850	50%	925	($2.24)

	2022E EPS	Implied Interest Rate	Weight	P/E Multiple		
HoldCo Interest Expense - 50% Weighting	($0.72)	9.6%	50%	18.5x	0.0x	($6.69)
Corporate SG&A	($0.35)			18.5x	0.0x	($6.47)
Total Parent & Other						($15.40)

Merchant / Nuclear	Cumulative FCF	NPV @ 10%		
Merchant FCF: NPV Through 2022	$214	$177		$0.86
Total Merchant				$0.86

Total Equity Value Per Share	$115.00	$122.00	$130.00
Price Return	13.6%	20.5%	28.4%
NTM DPS		*$3.72*	
Dividend Yield		*3.7%*	
Total Return	17.2%	24.1%	32.0%
Implied Multiple Today		17.0x	
PO Implied Multiple			

Source: BofA Global Research estimates, company report, Bloomberg

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Title: Subtitle	Primary Author	Date Published
Entergy: Just So Many Ways to Win: Why We We're Still So Constructive: Reiterate Buy	Julien Dumoulin-Smith	25 March 2020
Entergy: The next re-rating angle gets a tad closer: reiterate Buy	Julien Dumoulin-Smith	21 February 2020
Entergy: Specifying the opportunity of the aging fleet: reaffirm our Buy thesis	Julien Dumoulin-Smith	03 December 2019

Essential Utilities (WTRG)

We see WTRG's execution on their capital plans as largely intact outside of a modest $30Mn delay related to temporary work stoppage in PA (which will likely be trued up within the calendar year). We would anticipate some further tailwinds from acceleration in muni deals during a recovery period and await looming equity likely later this year to finance the pending DELCORA acquisition. Meanwhile, we further continue to await developments around the catch up component of repairs tax implementation as additional upside to the recently rolled out guidance with a filing this quarter. We reiterate our Neutral rating on shares of WTRG, seeing risk/reward as fairly balanced at the current valuation.

WTRG 1Q20 Earnings Walk

We forecast 1Q20 adjusted EPS of $0.61 compared to 1Q19 adjusted results of $0.28 and consensus of $0.58. We see consensus as not fully appreciating the adjusted numbers reflecting weather-normalized load on the gas business.

- **Key Drivers:** The primary positive drivers y/y are new rates for the legacy water business and gas contribution following the Peoples Gas acquisition offset by higher O&M and dilution.

Table 39: WTRG 1Q20 Walk

WTRG 1Q20 Earnings Walk		EPS
WTRG 1Q19 EPS	$	0.28
Aqua		0.03
Peoples Gas		0.38
Dilution		-0.08
1Q20 BofAe Adjusted EPS	$	0.61
Consensus		$0.58
WTRG Guidance		$1.53-$1.58
2020 Consensus		$1.56
1Q20 Adjusted Shares Outstanding		254
1Q19 Adjusted Shares Outstanding		178

Source: BofA Global Research, Bloomberg

Contemplating the COVID IMPACT

Latest discussions with management have stressed the capital forecast (and recent EPS guidance) as largely intact outside of a $30Mn delay related to a two week work stoppage in PA when 500 contractors were out of work. We stress this as modest amid the $950Mn to be deployed with an expectation for this to be made up by the end of the calendar year, and see no material issues other than some small timing nuances.

While the company does not have decoupling mechanisms in a sizable way (despite PA companies privy to such mechanisms, the mechanism is only utilized in IL), industrial load is only ~3% of the overall mix for the water biz and less than 1% for gas (gas shoulder season should further limit any NT impact). During the recession in 08-09, the company did not see a large reduction on load, but we stress bill collection as more critical to watch given the moratorium on shutoffs this time. Initial discussions thus far haven't indicated any signs of trouble (typical run rate is about 50bp and 200bps for Aqua and Peoples, respectively. With TX already announcing a provision to track COVID-related expenses, we further await any add'l announcements in their ten state jurisdictions given what we expect to be a clear focus for regulators.

The remaining jurisdictions haven't seen an impact outside PA with regulatory or construction delays and muni conversations ongoing, albeit developments remain fluid: while WTRG doesn't have a particularly busy reg agenda, we could see a slight delay in the DELCORA acquisition (seemingly early next year vs. late this year/early next year) but would nonetheless anticipate equity for the transaction to be raised towards the back half of 2020. Latest conversations suggest ~$300Mn. While any infrastructure/federal

stimulus for water remains a wildcard, we see recovery out of COVID as likely another tailwind for industry consolidation.

Contemplating Repairs & LT Prospects

At their Analyst Day in February, mgmt. noted plans to invest $950Mn in 2020 for the year with visibility to ~$2.8Bn through '22, translating to rate base CAGRs of 6-7% for the water biz and 8-10% for gas (This excludes any acquisitions despite what we increasingly view as a bullish landscape for further muni acquisition acceleration – and reflecting DELCORA alone into rate base would already provide another few hundred bps of growth). Overall, we expect enabling legislation & emerging contaminants – in addition to COVID recovery tailwinds – to drive further consolidation prospects for water longer term.

Meanwhile, we await potential upside from any clarity around commission treatment of the Repairs Tax catch up component. Recall the election of tax repair for People's largest Pennsylvania sub, Peoples Natural Gas, which we perceive to be ~90% of the gas business. The company expects the election to directly contribute ~$0.08-$0.12 in 2020 – and we perceive this as a good run rate going forward. We expect the company to file something this quarter around a catch up component, with potential clarity around any construct later in the year (to determine flow through benefit to shareholders which remains less clear cut and excluded from the latest guidance.

EPS Estimates

The exhibit below reflects our current EPS estimates ahead of the upcoming quarter, with NT numbers coming down slightly. We continue to model to the high end of their LT CAGR guidance.

Table 40: EPS Estimates

EPS Estimates	2020E	2021E	2022E
PA	$0.73	$0.80	$0.86
OH	$0.07	$0.07	$0.08
IL	$0.07	$0.08	$0.08
TX	$0.06	$0.07	$0.07
NC	$0.04	$0.04	$0.05
Other States	$0.07	$0.07	$0.08
Water Utility	1.04	1.13	1.21
Peoples Gas	0.62	0.67	0.72
Parent & Other	*-0.10*	*-0.11*	*-0.14*
EPS	1.56	1.69	1.80
YoY Growth	*6%*	*9%*	*6%*
Guidance	1.53-1.58		
Fully Diluted Shares O/S	*254*	*254*	*254*
Previous EPS	*$1.58*	*$1.69*	*$1.80*
CAGR Guidance: 5-7% through '22 off 2019 Adjusted EPS			
Low End: 5%	1.54	1.62	1.70
Midpoint	1.56	1.65	1.75
High End: 7%	1.57	1.68	1.80
Consensus	1.56	1.65	1.79
DPS	0.99	1.06	1.13
Payout Ratio	*63%*	*62%*	*63%*

Source: BofA Global Research, Bloomberg

Valuation

The exhibit below reflects our latest SOTP after applying the current peer multiples to our valuation: 26.3x for water and 17.6x for gas (vs. 28.2x for water and 18.3x for gas previously). Our PO shifts to $47 and we maintain our Neutral rating seeing risk/reward as balanced at the current valuation.

Table 41: WTRG SOTP

Water Utilities	2022E EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*26.3x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		28.5x							
Water Utilities									
States	2022E EPS	ROE embedded							
PA	$0.86	10.0%	2.0x	29.5x	30.5x	31.5x	$25	$26	$27
OH	$0.08	9.4%	2.0x	29.5x	30.5x	31.5x	$2	$2	$2
IL	$0.08	9.1%	3.0x	30.5x	31.5x	32.5x	$3	$3	$3
TX	$0.07	10.0%	0.0x	27.5x	28.5x	29.5x	$2	$2	$2
NC	$0.05	9.2%	1.0x	28.5x	29.5x	30.5x	$1	$1	$1
Other (including acquisitions)	$0.08	9.2%	0.0x	27.5x	28.5x	29.5x	$2	$2	$2
Water utilities total (ex-Peoples)	$1.21			*29.3x*	*30.3x*	*31.3x*	$36	$37	$38
Gas Utilities									
Peer Gas P/E		*17.6x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		18.6x							
	2022E EPS	ROE embedded							
Peoples Gas	$0.72	12.1%	2.0x	19.6x	20.6x	21.6x	$14	$15	$16
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			-1165	50%			($582)	($582)	($582)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($537)	($497)	($582)
50/50 Weighted Drag from HoldCo Drag							($1,119)	($1,079)	($1,164)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							$45.00	$47.00	$49.00
Current Price								$43.36	
Dividend Yield								2.3%	
Total Return								10.67%	

Source: BofA Global Research, Bloomberg

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BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Essential Utilities: Peoples Set to Close Imminently, but can the People deliver? Dropping Ests	Julien Dumoulin-Smith	09 March 2020
Aqua America: Overflowing Interest: Downgrading to Neutral	Julien Dumoulin-Smith	21 January 2020
Aqua America: Snorkeling in the Deep End: A Closer Look at the Repairs Tax Benefit	Julien Dumoulin-Smith	21 August 2019
Aqua America: Pool Party continues but waiting on the Gas	Julien Dumoulin-Smith	08 August 2019
Aqua America: Diving In: See Opportunity in a Gas & Water Utility Hybrid	Julien Dumoulin-Smith	15 July 2019

Evergy Inc (EVRG)

EVRG 1Q20 Earnings Walk

We forecast 1Q20 adjusted EPS of $0.40 vs. consensus of $0.49 (we note downside risk to Street estimates as Covid effects become more fully reflected over time) and pro-forma 1Q19 results of $0.44. Our full-year forecast for EVRG of $3.06/sh is updated from $3.15 previously as we expect some Covid-related slowdowns to materialize in reduced demand. We remain concerned on load trends for EVRG but given no '20 guidance, this limits near-term revision risk. Given ongoing strategic questions what will mgmt's ability/comfort with articulating cost cuts be to mitigate this outcome. *Management states they will attempt to cut cost however did not provide any further specifics; mgmt. also said it was also difficult to see load impacts given how much later KS was to implement Covid-related stay-at-home orders suggesting negligible impact on 1Q and even early impacts on 2Q.*

- **Key Drivers:** Weather is expected to be a drag of $0.13/sh as we normalize for the positive effects of 1Q19 (5 cents) and account for milder weather in 1Q20 that reduced the number of Heating Degree Days (HDDs) in EVRG's service area. O&M savings including merger synergies are expected to provide an uplift of 6 cents as the company continues to look for ways to cut costs in order to realize full merger synergies, offset Sibley and Jeffery rulings from 2019, and offset potential Covid-related drag on demand. We additionally see 5 cents of accretion from a lower share count in Q1 2020 following EVRG's share buyback program, but note that as this program has been suspended following the Elliott agreement this effect will abate in future quarters.

- **Unknowns:** Weather was noticeably milder in Q1 2020 than normal, with HDDs 15-16% below normal throughout much of EVRG's service territory. We note that weather impact on utility results is driven not just by the aggregate number of HDDs but also in the timing of deviations from norm (Jan HDDs worth more than March), and as such the precise weather impact is difficult to gauge. The Covid effect will likely be modest in Q1 as shut-in rules in EVRG's service territory were implemented in a staggered approach at the end of the quarter – we estimate 1 cent drag. The additional question looking ahead is to what extent, if any, EVRG is able to offset the effects of reduced demand by commercial and industrial (C&I) customers with further cost cuts in the short term.

Table 42: EVRG Q1 walk: a bit weaker too vs Street on mild weather

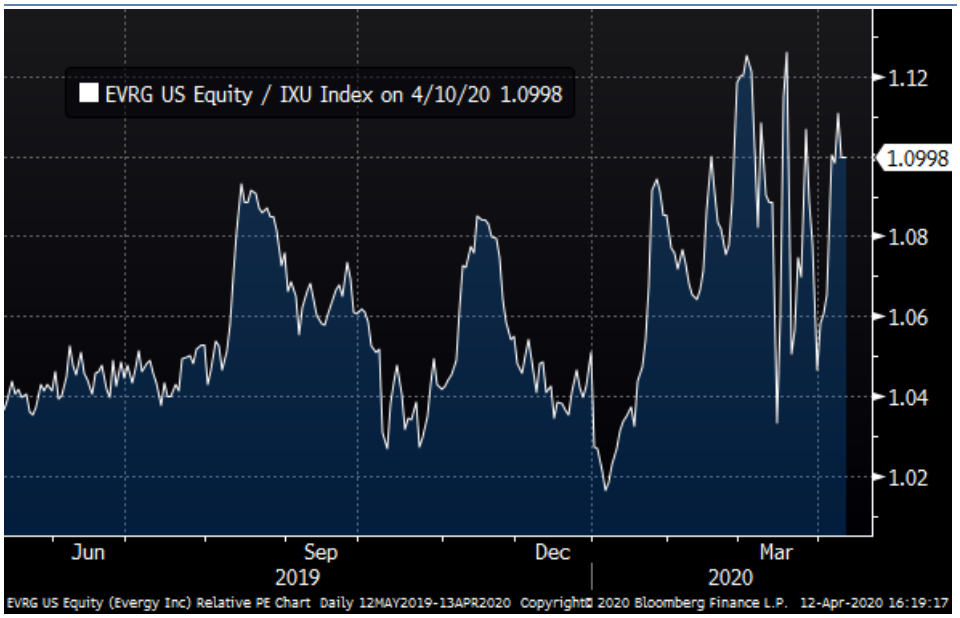
Earnings Walk	Notes	EPS
1Q19 EPS		0.44
Weather normal	Reverse favorable effect in Q1 2019	(0.05)
Weather 1Q20	15-16% HDDs below normal in KS and MO	(0.08)
Other	Effect of COVID on load	(0.01)
1Q20 drivers:		
O&M	Cost savings, includes merger synergies	0.06
D&A expense		(0.01)
Interest expense		(0.01)
COLI	Based on 2020 guidance	0.02
Accretion		0.05
1Q20E BofAe EPS		$0.40
1Q20 Consensus		$0.49
2020E BofAe EPS		$3.06
2020 Consensus		$3.11
1Q19 Share count		253
1Q20 Share count		227

Source: BofA Global Research Estimates, company report, Bloomberg

Shares reflect Covid, but strategic angle is still there

Shares of EVRG have bounced back amid substantial volatility in mid March. We note shares have outperformed the peer group since our upgrade to Buy following EVRG's Q1 results and announcement of agreement with Elliott: Evergy, Inc: Upgrade to Buy on activist engagement, cost controls, capex, & strategic angles too 03 March 2020.

Exhibit 3: EVRG relative chart



Source: Bloomberg

- **We see some short-term impact stemming from Covid.** Both the KS and MO utilities have bad debt recovery imputed in their current rates based on historical test years - recall that EVRG's rate stay outs are until 2022 and 2023 in Missouri and Kansas, respectively. The utilities do not have trackers for recovery of bad debt expense in between rate cases. Likewise the EVRG utilities do not have decoupling in either KS or MO although they have some energy efficiency mechanisms such as Missouri Energy Efficiency Investment Act (MEEIA). Off system sales are generally not a significant driver historically - the last major impact from wholesale pricing was related to the polar vortex in 2014. Estimated EPS impact from a 1% swing in demand is $0.10 ($0.05 from residential, $0.04 from commercial, $0.01 from industrial), *among the highest EPS sensitivity across our coverage universe making shares more at risk of Covid related demand destruction. That said early indications from OG&E of a very modest load impact appear to de-risk EVRG shares, and also notable is the lack of '20 EPS guidance range, forcing more of a long-term focus rather than near-term impacts of Covid in '20 (different vs peers). The real question is to what extent management can source yet further cost cuts during its stay out to offset more ongoing pressures from lower Covid-related load. We also continue to assume recovery of bad debt expenses, a consistent assumption across most jurisdictions, just could be a while before cash recovery is enabled.*
- **Cost-cutting already a big part of the strategy.** The key short-term question for EVRG (and most utilities that are not decoupled) is to what extent mgmt. can flex O&M controls to mitigate the impact of lost sales stemming from shut-in orders. EVRG has been implementing merger synergies from its last transaction and had already included an incremental ~$30m in its 2020 forecast from continuing realization of these savings – for example combining all back office systems across all utilities under one customer management system. In addition, 2019 rulings in the Jeffrey and Sibley matters put additional pressure on mgmt. to realize *further cost cuts* in order to preserve ROEs at the Kansas and Missouri utilities, respectively. To what extent mgmt. can wring out additional cuts to offset mild Q1 weather and lost

sales remains the key question – we lowered out 2020 ests. by 9 cents across the consolidated franchise to account for this additional pressure on ROEs.

Strategic review: timeline and accretion scenario

EVRG's Strategic Review & Operations Committee (SROC) created in EVRG's agreement with Elliott outlines specific dates by which proposals must be submitted, voted on, and presented publicly. Two of the four members of the SROC are the new directors selected by Elliott - industry vets Paul Keglevic and Kirk Andrews - giving the activist manager even representation with incumbent directors. Unsurprisingly, given intense focus by utility mgmt. teams and state utility regulators (not limited to EVRG) on maintaining ongoing service amid the Covid emergency, the SROC issued an updated time frame pushing back its most significant deliverables further into the year. We view the revised timeframe below as merely reflecting the practical realities of evaluating a complex transaction amid work-from-home restrictions and market volatility and remain constructive on the overall direction of the review.

- **SROC recommendation to Board due Jul 30.** The original timeline called for the committee to present to the Board its recommendation of a transaction or standalone strategy by May 30 – note that the specific recommendation will also determine the level of public disclosure, as we detailed previously.
- **Board announcement by August 17.** Previously June 17, giving the Board the same number of days to evaluate as under the previous timeframe.
- **Modified standalone plan by Oct 14 if selected.** Originally the deadline was Sep 4, so the time frame for a presentation of a potential standalone plan has been pushed back by six weeks. We continue to view this as the less likely option given specific wording of the SROC agreement and note that logistics around presenting such a plan may require rethinking in the wake of Covid.

Analyzing accretion from a potential NEE deal: running the math

Below we provide an alternative version of our previous illustrative accretion/dilution analysis on NEE's prospective acquisition of EVRG. For this scenario, we assume no debt addition at parent level, essentially keeping the FFO/Debt unchanged at NEE. The scenario yields $0.15 or 1.5% accretion ex-synergies for 2021E; we view synergies as necessary to sustain accretion through longer-term. We anticipate some degree of financial re-leveraging of NEE nonetheless with upwards of 3%+ accretion to NEE in this instance.

Table 43: Illustrative accretion - NEE acquisition of EVRG

	2020E	2021E	2022E	2023E	2024E
Legacy NEE					
Pre-Transaction NEE Net Income ($Mn)	4,500	4,847	5,402	5,722	5,972
Pre-Transaction NEE Shares Out. (Mn)	491.0	491.0	493.3	500.0	505.0
Pre-Transaction NEE EPS	$9.16	$9.87	$10.95	$11.44	$11.83
Consensus	$9.06	$9.85	$10.62	$11.24	$11.87
EVRG					
Pre-Transaction EVRG Net Income ($Mn)	715	746	774	790	797
Combined Entity					
Combined Net Income ($Mn)	5,214	5,593	6,176	6,512	6,769
Incremental Interest Expense (Tax-Adjusted at 21%)	0	0	0	0	0
Synergies ($Mn)	0	0	0	0	0
Pro Forma Net Income ($Mn)	5,214	5,593	6,176	6,512	6,769
Incremental NEE Shares Issued for Santee (Mn)	67.1	67.1	67.1	67.1	67.1
Pro-Forma NEE Shares Out. (Mn)	558.1	558.1	560.3	567.1	572.1
Pro-Forma EPS	$9.34	$10.02	$11.02	$11.48	$11.83

Table 43: Illustrative accretion - NEE acquisition of EVRG

	2020E	2021E	2022E	2023E	2024E
Accretion (Dilution)	$0.18	$0.15	$0.07	$0.04	$0.01
Accretion (Dilution)	2.0%	1.5%	0.6%	0.3%	0.1%

Source: BofA Global Research Estimates, company report, Bloomberg

Estimates

Our estimates reflect near-term 9 cents consolidated earnings drag related to Covid in 2020, as we see limited oppty for mitigation of lost sales given EVRG's lack of a decoupling mechanism and ongoing efforts to cut costs across the franchise already underway given merger synergies and Sibley/Jeffrey offset requirements. Our estimates are below Street in 2020 though we perceive downside here as consensus forecasts are updated to more fully reflect Covid impacts. We expect Covid to not be a driver of downside risks past 2020 and our estimates in future years remain largely unchanged as we see EVRG as largely able to achieve authorized ROEs in this period.

Table 44: EVRG estimates

Evergy, Inc. Dashboard

EPS Estimates by Subsidiary	2018A	2019A	2020E	2021E	2022E	2023E	2024E
Evergy Metro	$0.76	$1.06	$1.07	$1.13	$1.17	$1.20	$1.22
Evergy Missouri West	$0.35	$0.37	$0.44	$0.47	$0.49	$0.51	$0.52
Kansas Central	$1.58	$1.43	$1.67	$1.78	$1.87	$1.90	$1.91
Parent/Other	($0.19)	($0.08)	($0.11)	($0.11)	($0.13)	($0.14)	($0.14)
GAAP EPS	$2.50	$2.79	$3.06	$3.27	$3.40	$3.47	$3.50
Y/Y EPS Growth %		*11.6%*	*9.7%*	*6.8%*	*3.9%*	*2.0%*	*0.9%*
Prior estimates	$2.50	$2.89	$3.15	$3.29	$3.42	$3.48	$3.52
Consensus (BBG)		$2.92	$3.11	$3.23	$3.39	$3.58	nm
DPS	$1.84	$1.95	$2.07	$2.19	$2.30	$2.42	$2.54
Dividend Payout (60-70%)	73.5%	69.8%	67.5%	67.0%	67.7%	69.7%	72.5%

Source: BofA Global Research Estimates, company report, Bloomberg

Valuation

We updated our PO to $69 reflecting an updated electric utility peer group multiple of 17.6x (17.9x previously). Our valuation is largely unaffected by the near-term drag on our estimates related to milder weather and Covid as both are expected to normalize by 2022. Shares have re-rated vs the peer group since our upgrade to Buy though we still perceive upside to the current share price amid ongoing strategic review.

We perceive many investors as cautious into 1Q updates given exposure to Covid despite backdrop around strategic actions possible.

Table 45: EVRG SOTP

Evergy Sum-of-the-Parts Valuation	2022E EPS	P/E Multiple					Equity Value/Sh		
		Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric			17.6x						
Group EPS '18-'22 CAGR - Electric			5.00%						
			18.5x						
Evergy Metro	$1.17	19.5x		2.00x	20.5x	21.5x	$22.72	$23.88	$25.05
Evergy Missouri West	$0.49	19.5x		2.00x	20.5x	21.5x	$9.58	$10.07	$10.57
Evergy Kansas Central	$1.87	19.5x		2.00x	20.5x	21.5x	$36.42	$38.29	$40.16
Parent & Other	-$0.13	19.5x		2.00x	20.5x	21.5x	-$2.54	-$2.67	-$2.80
EVRG consolidated '22 EPS	$3.40				*20.6x*		$66.00	$70.00	$73.00
	After-tax amount $m		$/sh	Probability					
Deferral of Sibley return + D&A	23		-$0.10	50%			-$2.04	-$1.02	$0.00
Shares outstanding (Average 2022)	227								
Shares outstanding (Y/E 2022)	227								
EVRG Price Objective							$64.00	$69.00	$73.00
EVRG Current Share Price								$60.98	
Implied Return								13.15%	
EVRG Standalone NTM Dividend Yield								3.59%	
Total Return								16.75%	

Source: BofA Global Research Estimates, company report, Bloomberg

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BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Evergy, Inc: The Covid Risks & Prelim Possible NEE Accretion Stats: Reiterate Buy	Julien Dumoulin-Smith	13 April 2020
Evergy, Inc: Timeline & just why is the Elliott deal so constructive?	Julien Dumoulin-Smith	10 March 2020
Evergy, Inc: Upgrade to Buy on activist engagement, cost controls, capex, & strategic angles too	Julien Dumoulin-Smith	03 March 2020
Evergy, Inc: Cost Cutting, PPAs, and Kansas Prospects: Where to focus?	Julien Dumoulin-Smith	14 February 2020

Eversource (ES)

We point to Eversource as one of the more protected names from COVID given its mostly decoupled status and capex upside around grid mod and AMI (incl. EV infra/storage spend) in CT and MA. We expect the call to be relatively muted as many updates are coming later this year. Offshore wind awaits BOEM's (the Bureau of Ocean Energy Mgmt's) cumulative impact study before ES can comment on the timeline of its first project (the small South Fork project to commission in 2022 – before others). Further, approval for AMI / grid mod upside remain protracted with CT's filing potentially being looked at this July, still indicating that the earliest spend could be implemented is '21. Finally, we note that the Columbia Gas of Massachusetts is expected to close in 3Q, with filings expected (including the key one with Mass Department of Public Utilities) in the next month or so. We continue to expect ES maintains its 5-7% LT EPS growth CAGR, estimating that the CAGR remains towards the mid-point even when factoring in upside capex opportunities and the meaningful EPS uplift into '24 associated with offshore wind. We maintain our Underperform rating on shares given pricey nature relative to peers; seeing limited near-term upside capex catalysts ahead. As for the quarter, we expect a $1.02/sh – the same as Consensus.

1Q20 ES EPS Walk

Below we forecast a $1.02/sh quarter for 1Q20, the same as Consensus. This is compared to a $0.97/sh 1Q19 EPS.

- **Drivers**: We find about +12c YoY for the quarter thanks to rate case increases that increased at the beginning of this year (e.g. CLP, NSTAR & WMECO Phase II rates) or were effective over the last year (e.g. interim rate increase for PSNH July 2019).
- **Other**: Adding up the pieces of parent, D&A, interest, property taxes, and other, we find about a -4c hurt this quarter. We highlight that O&M is flat YoY, which indicates the company could 'bend the curve' and save more if needed depending on COVID impacts.
- **Wildcard**: We factor in -2c of weather to reflect PSNH – the only subsidiary not decoupled. Note that weather was very mild in 1Q, but PSNH represents only 6% of ratebase.

Table 46: ES 1Q20 EPS Walk

ES Energy Earnings Walk	EPS
Adjusted EPS 1Q19	$0.97
Utility	
Weather	
Return to normal	$0.00
Current quarter: Really mild, only PSNH not decoupled	($0.02)
Transmission & Distribution	
Ratebase transmission earnings	$0.03
NSTAR Electric & WMECO rates Phase II Jan 1, 2020	$0.02
Aquarion contribution	$0.00
CLP Phase II rates effective May 1, 2019	$0.02
Loss of generation	$0.00
Yankee Gas rates effective Jan 1, 2020	$0.02
Interim rate increase PSNH effective July 1, 2019	$0.03
Other	
Parent, D&A, Interest, Property taxes, Other expenses	($0.04)
O&M	$0.00
Parent	$0.00
One-time: Merger recovery in 4Q18	$0.00
One-time: Loss of NPT AFUDC Earnings	($0.01)
Dilution	($0.00)
1Q20E Adjusted EPS	$1.02
1Q20 BofA Model	$1.02
1Q20E Consensus	$1.02

Table 46: ES 1Q20 EPS Walk

ES Energy Earnings Walk	EPS
2020E BofA EPS	$3.65
2020E Consensus	$3.64
2020 Guidance	3.40-3.50
Shares Outstanding 1Q19	318
Shares Outstanding 1Q20	331

Source: BofA Global Research estimates, company report, Bloomberg

Key points for 1Q

- **COVID**: ES has full revenue decoupling for all of its utilities with the exception of PSNH, which is currently in a pending ratecase. As such, ES revenues are decoupled from load reduction impact at the rest of its utility subsidiaries aside from PSNH. Decoupling base lines rise with base rate increases as well. ES has a bad debt expense rider but only for medical and low-income customers. We see this as common amongst names that do have trackers (typically usually at the gas subs or at specific customer classes).

- **Financing activity strong in 1Q**: We expect ES to discuss its financing over the last few months, including $350mn of parent notes in Jan, $400mn of NSTAR Electric green bonds in March, and closing out the forward by the end of March.

- **Capex upside**: While ES provided a five-year capex roll-forward through 2020 on the last call, the company still has upside spend related to grid mod in CT and NH, AMI in MA and CT ($1bn), and natural gas distribution spend in MA (perhaps related to the NiSource subsidiary acquisition). We still await a more firm timeline associated with these opportunities as they aren't factored into guidance yet. We focus moreso on AMI in CT given activity is starting to pick up on the opportunity that could result in a proceeding starting this July.

- **Offshore wind**: The South Fork project is the first and smallest at (just 90MW + a 40MW upgrade) of ES's offshore wind projects expected to come online with a commissioning date of 2022. We point out that ES is still awaiting a cumulative impact study coming from BOEM, which could impact its online date. We point out that given ES plans to monetize the investment tax credit (ITC), we see less pressure for the project to *have* to commission within a four-year build window to qualify for the credit (it could instead prove continuous efforts towards completion). The more concerning issue would be re-negotiating the power purchase agreement (PPA) with Long Island. We stay tuned here, but we expect ES to wait to provide clarity around South Fork once BOEM's cumulative impact study timeline is certain.

- **NSTAR Gas rate case**: On Nov 8, ES subsidiary, NSTAR Gas filed its expected gas rate request with the MA DPU for a $38mn rate increase at a 10.45% ROE and 54.85% equity ratio. The filing includes a proposed performance based rate (PBR) mechanism including inflation and a 1.3% adder and would support a meaningful 5-year rate stayout. The filing includes a long-term plan to fund safety and reliability improvements following the Merrimack Valley incident with NI subsidiary Columbia Gas, which we expect to support express incremental distribution capex likely to be reflected in the 4Q capex update. Proposed rates would be effective Oct 1st 2020.

- **PSNH**: We also look for updates on the Public Service of New Hampshire (PSNH) rate case (Docket DE 19-057). Recall, the NH PUC Staff recommended a $24.4mn rate increase at a 8.5% ROE, 50% equity ratio, ~$1.15Bn year-end ratebase, denial of proposed multi-year rate plan, and proposal for a Grid Transformation and Enablement Program (GTEP). ES originally requested a $69.3mn increase in permanent rates at a 10.4% ROE, 54.85% equity layer, and ~$1.215Bn ratebase. The NH PUC has already approved a $28mn interim rate increase for PSNH, slightly

lower than the $33mn requested by ES, effective Aug 1st (benefiting 2H19 earnings). A final PUC decision is expected May 20, 2020 barring a settlement.

Estimates

We largely leave estimates untouched owing to Eversource's resilient decoupling mechanisms in all subsidiaries outside PSNH.

Table 47: ES EPS Estimates

EPS by Business	2016A	2017A	2018E	2019E	2020E	2021E	2022E	2023E	2024E
CL&P	1.03	1.17	1.19	1.30	1.32	1.37	1.42	1.44	1.46
PSNH	0.41	0.43	0.36	0.38	0.43	0.45	0.46	0.48	0.51
WMECO + NSTAR	1.10	1.17	1.20	1.39	1.39	1.52	1.65	1.81	1.92
NSTAR Gas	0.10	0.10	0.13	0.12	0.15	0.20	0.23	0.26	0.30
Yankee Gas	0.14	0.12	0.18	0.18	0.19	0.21	0.23	0.24	0.25
Parent (ex-ITCs/Offshore/Aquarion/etc)	0.15	0.11	0.10	0.07	0.06	0.04	0.02	(0.01)	(0.03)
Offshore Wind (PPA NI)								0.02	0.14
Offshore Wind (ITCs)								0.02	0.11
Aquarion			0.10	0.10	0.11	0.11	0.12	0.13	0.15
Consolidated	2.96	3.11	3.25	3.45	3.65	3.90	4.14	4.40	4.81
Guidance			3.20-3.30	3.40-3.50	3.60-3.70				
Consensus		3.12	3.28	3.45	3.64	3.89	4.13	4.38	4.84
Mgmt EPS CAGR: 5-7% off 2018A	2.98	3.11	3.25	3.45	3.65	3.87	4.10	4.35	4.61
Low End				3.41	3.58	3.76	3.95	4.15	4.36
High End				3.48	3.72	3.98	4.26	4.56	4.88
Core Utility EPS (excl. Offshore)	2.96	3.11	3.25	3.45	3.65	3.90	4.14	4.36	4.56
BofAe Utility CAGR '19-'XXE								6.0%	5.7%
BofAe CAGR '19-'24E				6.9%					

Source: BofA Global Research estimates, company report, Bloomberg

Valuation

We MtM the peer multiple to 17.6x and increase premiums to 2x for CL&P, WMECO & NSTAR to reflect decoupling mechanisms (vs 1x for PSNH),1x for gas names, and 3x for Aquarion. Even so, this results in only an $83/sh PO and we reiterate our Underperform rating.

Table 48: ES SOTP Valuation

2022E SotP Analysis - BofAe

All figures in USD millions except per share

Regulated Utilities	2022E NI	EPS	P/E Multiple					Equity Value	
			Peer	Prem/ Discount	Base	Bull	Bear	Base	Bull
Relative Utility Group P/E Multiple									
Group Peer Multiple - Electric			17.6x						
Group EPS '18-'22 CAGR - Electric			5.00%						
Electric Utilities			18.5x						
CL&P	$483	$1.42	18.5x	2.0x	20.5x	21.5x	$27.71	$29.13	$30.55
PSNH	$155	$0.46	18.5x	1.0x	19.5x	20.5x	$8.42	$8.88	$9.33
WMECO & NSTAR Electric	$561	$1.65	18.5x	2.0x	20.5x	21.5x	$32.18	$33.83	$35.48
Group Peer Multiple - Gas			17.6x						
Group EPS '18-'22 CAGR - Gas			5.10%						
Gas Utilities			18.5x						
NSTAR Gas	$79	$0.23	18.5x	1.0x	19.5x	20.5x	$4.32	$4.56	$4.79
Yankee Gas	$78	$0.23	18.5x	1.0x	19.5x	20.5x	$4.24	$4.47	$4.70
Other Segments									
Aquarion - Water Utility	$42	$0.12	18.5x	3.0x	21.5x	22.5x	$2.54	$2.66	$2.79
						NPV			
Add NPV of 1.7GW Offshore Wind						$518	$1.52	$1.52	$1.52
@ 6% Operating Discount Rate @ 50% Ownership w/ 8% Construction Risk Discount Rate									
Parent - Small Investments, etc	$6	$0.02	18.5x	0.0x	18.5x	20.5x	$0.35	$0.35	$0.38
HoldCo Debt Adjustments (50/50 Weighted to P/E and netting out debt)									
Add: Parent Interest Expense @ 50%	$69	$0.20	18.5x	1.0x	19.5x	0.0x	$1.97	$1.97	$1.97
Parent Debt @ 50%	$3,200							-$4.71	
Total	$1,406	$4.14					$78.53	$82.65	$86.80
Shares outstanding (projected avg)								*340*	
Total Equity Value Per Share							$79.00	$83.00	$87.00
Price as of close 04/20/2020								91.56	
FY20 Dividend								2.27	
Dividend Yield								2.5%	
Total Return Projected								-6.9%	

Source: BofA Global Research estimates, company report, Bloomberg

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Eversource Energy: Raising to the midpoint of range; can the offshore clouds part?	Julien Dumoulin-Smith	21 February 2020
Eversource Energy: Fairly muted 4Q update ahead, near-term capex revisions limited; Underperform	Julien Dumoulin-Smith	09 January 2020
Eversource Energy: Focus on CT AMI and grid mod as timeline in focus: Underperform	Julien Dumoulin-Smith	07 November 2019
Eversource Energy: Sunrise-ing on offshore wind: Latest NY contract details released	Julien Dumoulin-Smith	24 October 2019

FirstEnergy (FE)

We reiterate our Buy rating on FE (following our recent upgrade here) with a quiet first quarter call approaching. We expect to see the Street focus on New Jersey given it's the only regulatory rate case the company is in right now (note we see a strength in the stay-out trend in other subs). Here, interim rates already took effect, but a ruling on its 10.8% ROE request is outstanding. We note the company is somewhat shielded from COVID impacts given it recently was awarded decoupling in Ohio making it a third less sensitive to load than before; also important to note is the low portion of revenue industrial sales contribute (7%) and that just 10% of industrial revenue is volumetric-based Further, FE recovers uncollectible expenses in OH / NJ through a rider and in PA / WV / MD through base rates. As for other updates, we continue to look for commentary around extension of the Electric Security Plan (ESP) given the commission removed the requirement for rate case filing in '24; note it still may be too early on this front, though. Finally, we continue to see the company steadily moving forward with its $3bn per year of capex trajectory. We forecast a 1Q20 estimate of $0.62/sh – just 1c lower than Consensus.

1Q20 EPS Walk

Below, we present our EPS forecast for 1Q20. We are roughly in line with Consensus (BofA $0.62/sh vs. Consensus of $0.63/sh). This stems from a $0.67/sh 1Q19.

- **Drivers**: Drivers for the quarter include -4c from mild weather in 1Q20 (not as impactful as peers noting decoupling in Ohio), +4c from Ohio decoupling true up, -6c from Ohio DMR stopping.
- **Other**: We expect flat distribution sales growth, and some impact from Maryland rates and other states' riders.
- **Wildcard**: We highlight COVID impacts are a wildcard, as well as the full extent of weather.

Table 49: FE 1Q20 EPS Walk

FirstEnergy 1Q20 Earnings Walk	EPS
1Q19E Adjusted EPS	0.67
Regulated Distribution	-0.04
Weather Vs normal in 1Q19	0.00
Weather Vs normal in 1Q20	-0.04
OH decoupling	0.04
Distribution sales growth	0.00
MD: $13mn annual impact	0.01
Riders: Including Ohio Grid Mod and PA DSIC	0.02
OH: DCR Rider June 1st 2019 (+$22Mn YoY)	0.01
OH: DMR (stopped recognizing earnings benefit)	-0.06
FE Tomorrow	0.00
O&M: Pension & OPEB	0.01
D&A and taxes	-0.02
Debt maturities	0.00
4Q 2018 we had higher O&M	0.00
Regulated Transmission	0.01
Revenues (net of D&A and taxes): higher ratebase	0.01
Parent and Other	-0.02
Tax rate benefit	-0.02
1Q20E Adjusted EPS	0.62
1Q20E BofAe EPS	0.62
1Q20 Consensus	0.63
1Q Guidance	0.60-0.70
2020 BofAe EPS	2.50
2020 Consensus	2.49
2020 Guidance	2.40-2.60

Source: BofA Global Research estimates, company report, Bloomberg

Items to track

COVID: Decoupling in Ohio makes less sensitive; PA is the real focus

The company's (new) decoupling in Ohio for 2020 makes FE 1/3rd less sensitive to loan than it was beforehand; decoupling or weather normalization is not present in other jurisdictions but FE does have energy efficiency riders (incl. demand response) except in WV. For a -1% decline in load, retail is impacted by -$0.02/sh, commercial by -$0.006/sh, and industrial by -$0.005/sh. Further, FE derives most (i.e. 65%) of its revenue from residential (meaning just 28% from commercial and 7% from industrial). Finally, for industrial customers, only 10% of revenue is volumetric-based while the rest is fixed. As for bad debt, FE recovers uncollectible expenses in OH / NJ through a rider and in PA / WV / MD through base rates. Finally, there's no risk around off-system sales / wholesale revenues given WV is only jurisdiction w/ generation and FE has an ENEC rider there (reconciled annually).

Pennsylvania is what to watch

While Pennsylvania has attracted limited attention this remains *our* focus at present among the numerous Covid exposures given its lack of any contemplated base rate cases and lack of decoupling. That said, margin remains biased towards resi mix, but still an underlying risk on earned ROE trends. We've already moderated our ROEs a bit in this state albeit still assume healthy returns overall in our last EPS est update.

New Jersey: The only rate case activity this year so far

FE filed a JCP&L transmission and distribution rate cases, with formula rates having gone into effect January 1st (subject to refund); a FERC decision on these transmission rates is anticipated in 1H20. The value of the formula rate would be for future years (i.e. there is a minimal anticipated impact on 2020). There is concern given the 10.8% filed but recent models indicating FERC base rates could fall within 8-10% depending on when data is selected.

Also important to note is that FE has a limited regulatory calendar compared to other utilities; this limits risk of downward shifts in authorized ROEs that other names are likely to face this year due to lower Treasuries (leading regulators to suspect lower costs of capital to build infrastructure). Limiting authorized ROE revision risk is increasingly a key theme in the sector after our latest conference and we perceive FirstEnergy as among the quietest large-cap companies from a regulatory perspective through its entire forecast period. While this limits upside capex and further positive revisions, we view its steady EPS growth as enabling its current outlook.

Ohio: Doubt legislation for '20 but perhaps in the future

While we doubt it's possible to pass in 2020 given COVID's situation, we expect the next legislative session to at least consider bills similar to proposed HB 247, 246, and 13. These could provide key investment opportunities (particularly for neighbor AEP) around industrial customers, broadband, and utility-regulator relations, although FE has not shared how exactly this could impact EPS growth for the company. These could also indicate a potential ESP (electric security plan) resolution that extends the current plan from '24 to '30.

Capex likely to be consistent

We continue to anticipate that FE will look to largely stay around the $3bn/ yr capex range in the years to come. We sense regulatory recovery and stable cash flows, balance sheet considerations drive this spend (and as such see less of a risk from Covid) beyond the operational challenges that may exist this year in executing.

Credit discussions with S&P

While FE has more holdco leverage than peers, we anticipate that FE may consider starting to discuss its credit metrics with rating agencies soon, with potential positive news to come from S&P on its FE outlook considering the agency lowered its FFO/debt

threshold to 12%. Note Moody's upgrade threshold is 14% and our reconciliation is mid-12%'s. Recall that issuing $2bn of equity equates to roughly only a 1% increase in FFO/debt, and that the company plans for incremental equity '22 (after which mgmt. has noted could be up to $600mn/yr). With its FES business disposition resolved, we perceive few angles to meaningfully shift its balance sheet outlook.

Estimates

We keep estimates largely the same given decoupling as well as our expectation that there is a more modest pace of consistent growth given ratebase is driven largely outside of any meaningful rate cases.

Table 50: FE EPS Estimates

EPS	2016A	2017A	2018A	2019E	2020E	2021E	2022E	2023E	2024E	2025E
Ohio Utilities	0.50	1.03	1.23	0.92	0.82	0.85	0.86	0.88	0.91	0.95
Ohio Edison (Inc PennPower)	0.35	0.59	0.64	0.50	0.48	0.50	0.52	0.53	0.56	0.58
CEI	0.09	0.27	0.39	0.26	0.20	0.20	0.20	0.21	0.21	0.21
TE	0.06	0.17	0.20	0.15	0.14	0.14	0.14	0.14	0.15	0.15
West Virginia										
MonPower	0.15	0.16	0.25	0.21	0.21	0.22	0.23	0.23	0.23	0.23
Maryland										
Potomac	0.14	0.10	0.10	0.10	0.12	0.14	0.16	0.18	0.19	0.21
New Jersey										
JCP&L	0.19	0.26	0.32	0.32	0.33	0.35	0.35	0.37	0.38	0.41
Pennsylvania	0.73	0.76	0.93	0.92	0.93	0.94	0.94	0.95	0.99	1.02
PennPower (already included in OE)	0.05	0.07	0.07	0.08	0.08	0.08	0.08	0.08	0.08	0.09
Penelec	0.21	0.22	0.32	0.29	0.30	0.31	0.31	0.31	0.32	0.33
WPP	0.27	0.25	0.23	0.24	0.24	0.23	0.23	0.24	0.25	0.26
MetEd	0.21	0.22	0.31	0.31	0.32	0.33	0.32	0.32	0.33	0.34
Regulated Utilities (Inc Transmission)	*1.66*	*2.23*	*2.75*	*2.40*	*2.34*	*2.43*	*2.46*	*2.52*	*2.62*	*2.73*
Regulated Distribution	-0.55	2.32	2.31	2.26	2.16	2.23	2.23	2.26	2.33	2.41
Guidance	2.60-2.70	2.27-2.31	2.34-2.40 w/ adj	2.20-2.26	2.13-2.27					
FET	0.45	0.62	0.58	0.66	0.69	0.74	0.81	0.87	0.94	1.00
Intrastate	0.28	0.13	0.21	0.16	0.18	0.20	0.22	0.26	0.29	0.32
Transmission	0.73	0.83	0.74	0.83	0.87	0.94	1.03	1.13	1.22	1.32
Guidance		.82-.84	.74-.76	.83-.84	.85-.89					
Competitive Energy Svcs.	0.60	0.46	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Guidance		0.42-0.46								
Corporate (reduced by pref)	-0.55	-0.53	-0.56	-0.51	-0.55	-0.55	-0.56	-0.54	-0.53	-0.52
Guidance		-0.51	(.58)-(.56)	(.53)-(.50)	(.58)-(.56)					
Eliminations		0.16	0.13	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Consolidated EPS	2.61	3.07	2.59	2.58	2.50	2.61	2.71	2.86	3.03	3.19
Previous EPS		3.07	2.59	2.58	2.48	2.61	2.69	2.86	3.02	3.17
Guidance		3.00-3.10	2.50-2.60	2.50-2.60	2.40-2.60					
Consensus EPS		3.05	2.54	2.53	2.49	2.64	2.77	3.03		
EPS CAGR off 2.15 (2018)					7.93%	6.72%	5.95%	5.84%	5.87%	5.79%
EPS CAGR off 2.43 ('19 2.55 Midpt less 0.12 DMR)					3.06%	3.70%	3.69%	4.12%	4.49%	4.63%
Y/Y Growth					-2.77%	4.34%	3.67%	5.41%	6.02%	5.31%
EPS CAGR off 2020						4.34%	4.00%	4.47%	4.85%	4.95%
EPS CAGR off 2021							3.67%	4.53%	5.03%	5.10%
Ex CES EPS	2.02	2.61	2.59	2.58	2.50	2.61	2.71	2.86	3.03	3.19
YoY Growth Rate Excl CEC EPS				0%	-3%	4%	4%	5%	6%	5%
Guidance: 5-7% CAGR '18 thru '23										
Bottom - 5%			2.15	2.26	2.37	2.49	2.61	2.74	2.88	3.03
Top - 7%				2.30	2.46	2.63	2.82	3.02	3.23	3.45
Shares	429	444	538	539	541	541	547	559	570	581

Source: BofA Global Research estimates, company report, Bloomberg

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
FirstEnergy: A Reformulated Company: Upgrade to Buy on de-risked strictly regulated profile	Julien Dumoulin-Smith	10 March 2020
FirstEnergy: Holding firm on Neutral after good 4Q	Julien Dumoulin-Smith	10 February 2020
FirstEnergy: Extending the EPS CAGR to '23 at 5-7%: We're right there already too	Julien Dumoulin-Smith	08 November 2019
FirstEnergy: Making sense of 2020 guidance & ratebase comp, shifting down est's slightly	Julien Dumoulin-Smith	05 November 2019

Pinnacle West (PNW)

We expect Q1 Operating EPS of $0.15/sh as compared to $0.16/sh Street estimates. Q1 is as seasonally slow quarter for PNW as its Arizona service territory generates most of its electric demand in the warmer months, particularly Q3. We expect that Covid reduced demand slightly at the end of the quarter as shut down orders spread in the state though the greater impact is likely to come in Q2 or later. They key lever for PNW to offset lost earnings from commercial and industrial customers is control of O&M - in fact mgmt's 2020 guidance already incorporates O&M savings into the forecast and it remains to be seen whether costs can be flexed even more to offset lost revenues. We flag additional possible risk of the rate case slipping further into 2021 as the commission's attention is likely occupied with service reliability issues during the health emergency. We further note that PNW had increased its bad debt expense target for 2020 given last year's disconnect moratorium, suggesting it may be better able to withstand an increase in delinquent accounts than peers – though note the likelihood of regulatory action to address increases in bad debt expense.

1Q20 Walk

We forecast 1Q20 adjusted EPS of $0.15 vs. $0.16 in 1Q19 and $0.16 consensus.

- **Key Drivers:** Weather will be a slight negative driver as 6 cents of benefit from Q1 2019 is normalized and an additional 4 cent uplift from slightly colder than normal conditions in the most recent quarter. We expect $0.03/sh in savings from ongoing O&M initiatives and highlight that the degree to which mgmt. can flex short term costs will drive the ability to offset lost sales (1 cent impact in Q1). We expect higher D&A driven by growing rate base to be an 11 cent drag.

- **Unknowns:** Weather is difficult to estimate given Q1 months have different weightings toward cooling and heating degree days, with January heating playing the biggest role.

Table 51: PNW Q1 walk

PNW 1Q20 Earnings Walk	EPS
1Q19 Adjusted EPS	$0.16
Weather return to normal	($0.06)
Weather effect vs norm	$0.04
Sales volume effect	($0.01)
Gross margin	$0.12
O&M	$0.03
D&A	($0.11)
Property tax deferral	($0.01)
Interest Expense	($0.01)
TEAM	$0.00
Other Opex	$0.00
Dilution	($0.00)
1Q20E Adjusted EPS	$0.15
1Q20 Consensus	$0.16
2020E Adjusted EPS	$4.83
2020 Consensus	$4.82
2020 Guidance	4.75-4.95

1Q19 Shares Outstanding	113
1Q20 Shares Outstanding	113

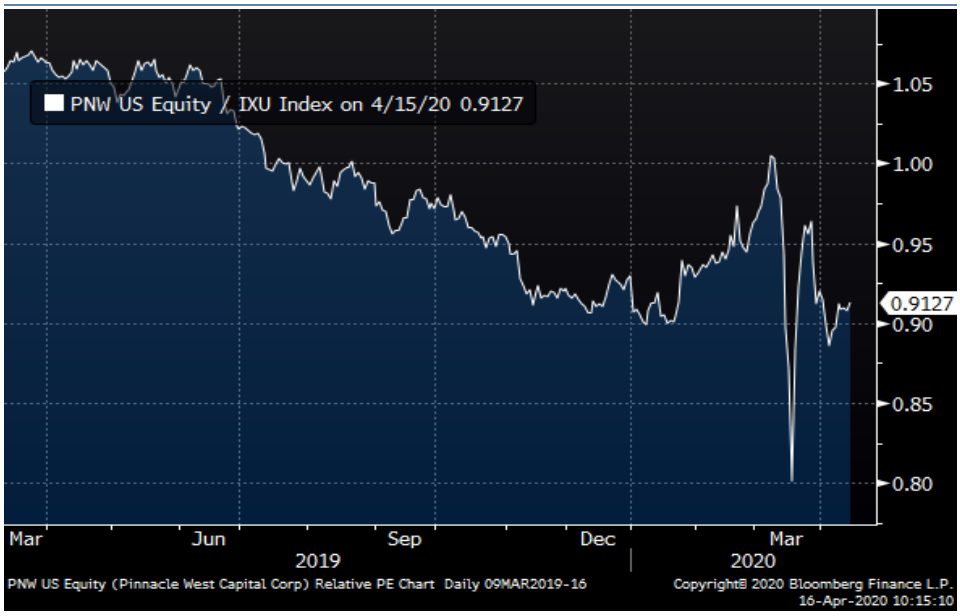
Source: BofA Global Research Estimates, company report, Bloomberg

Stock trading dynamics

Shares of PNW have de-rated slightly following the late March Covid-driven market volatility, and now trade at a relative 2-year PE to the IXU Index near the lows achieved at the end of Q4. PNW's service territory remains largely weighted toward residential

customers at over 50% of total demand, which should insulate its revenues somewhat from an expected decline in sales from commercial and industrial (C&I) customers – note that PNW has single-digit exposure to industrials with the balance being commercial exposure. The primary Covid-related risk on the regulatory front is further delay of the ongoing Arizona Public Service (APS) rate case, with the Arizona Corporation Commission (ACC) already pushing the proposed time frame of the rate case into 2021 (75-day delay) with possibility of additional delays depending on the duration of Covid shut down orders. Electoral concerns make the situation potentially more opaque given potential for turnover at the commission following Nov elections.

Exhibit 4: PNW shares relative value vs. IXU



Source: Bloomberg

Quantifying the impact of Covid shutdowns

APS does not have a separate bad debt expense recovery mechanism in its rates with expense rolled into customer rates based on a historical test year. While APS does not have traditional decoupling, it utilizes the Lost Fixed Cost Recovery (LCFR) mechanism that recovers lost fixed costs related to EE and Distributed Generation. The company estimates a 16-20 cent EPS impact from a 1% reduction in load, with the effect weighted toward residential customers who make up 51% of total load.

PNW proactively released March demand numbers indicating that through the 12th of the month residential sales were flat y/y while commercial and industrial (C&I) grew by 2-3%. For the remainder of the month as the Covid situation unfolded residential sales increased 7% y/y while C&I declined by 12-13%. PNW's annualized EPS sensitivities to a 1% move in demand for resi/comm/industrial are $0.09/$0.07/$0.01. Given PNW's disclosures, we estimate that Q1 EPS impact from Covid-related demand shifts was -$0.01, as an increase in higher-margin residential load mostly offset the larger declines in C&I.

Table 52: March EPS impact – resi mutes the C&I impacts to a large extent– are they the first of many to indicate this substantial offset in sales trends?

	EPS impact per 1% chg in annual sales	% of total load	Mar 1-12 change y/y	Mar 1-12 impact	Mar 13-31 change y/y	Mar 13-31 impact	March cumulative
Residential	0.09	51%	0%	-	7%	0.031	0.031
Commercial	0.07	38%	2-3%	0.006	(12)-(13)%	(0.043)	(0.037)
Industrial	0.01	11%	2-3%	0.001	(12)-(13)%	(0.006)	(0.005)
Total	0.16-0.20	100%	2-3%	0.007	(5)-(6)%	(0.018)	(0.012)

Source: BofA Global Research Estimates, company report

We acknowledge the limits of this disclosure given that it is only for the month of March with only half the month impacted by Covid, while demand in Jan-Feb was likely unaffected by the virus. PNW additionally included a disclosure of a potential $0.06 EPS impact if residential demand were to grow by 6% and commercial and industrial were to each decline by 10% - we note that since these are y/y comparisons they take into account the growth in residential load linked to air conditioning in the warmer Q2 months. PNW additionally disclosed that its pension plan hedges 100% of its interest rate exposure via Treasury futures, suggesting its plan's funding gap has declined YTD by less than the 11% estimated by our mtm analysis (and likely rebounded since our report with the broader market).

Rate case developments and top issues

The ACC issued a procedural order on March 18 that pushed back the timeframe of the pending rate case. By pushing out key milestones including staff and intervener testimony (originally scheduled for May, now due in August) the commission essentially assured that the case will not reach a resolution in 2020. While this assures that at a minimum commission Chair Bob Burns will not rule on the case as he is termed out at the end of the year, there remains uncertainty about the makeup of the commission in 2021 given 3 Republican-held seats are up for election, and the potential impact this would have on the outcome of the case. Below we present the updated rate case timeline while noting that the updated timeline was issued in mid-March as the Covid situation was still unfolding, and there remains the possibility of further delays.

Table 53: APS rate case amended timeline

Event / Item Due	Original	Updated
Application	10/31/2019	
Deadline for Motions to Intervene	2/11/2020	
Staff & Intervenor Testimony w/o Rate Schedules	5/20/2020	8/3/2020
Staff & Intervenor Testimony w/ Rate Schedules	5/27/2020	8/10/2020
APS Rebuttal Testimony	6/18/2020	9/1/2020
Prehearing Conference	7/13/2020	9/26/2020
Hearing Begins	7/17/2020	9/30/2020
Hearing Ends (30 day)	8/31/2020	11/11/2020
Transcripts Filed	9/11/2020	tbd
Briefs Due w/ Final Schedules	9/16/2020	tbd
Response Briefs Due	9/25/2020	tbd
Recommended Opinion and Order	11/25/2020	tbd
Exception Period Ends	12/16/2020	tbd
Open Meeting	12/17/2020	tbd
Deadline for Final Decision (AZ rule)	2/21/2021	tbd

Source: BofA Global Research estimates, ACC

Rate cases unlikely to be settled, potentially decided by different commissions

Both FTS and PNW have electric rate cases pending in front of the ACC. Stakeholders see potential for settlement as unlikely in either rate case given prior ACC utility staff statements, despite the heavy workload placed on staff of late with multiple rate cases pending. Given timing of each case, with FTS having been filed several months prior to PNW, it is increasingly likely that the commission that decides the FTS case will be different by at least one member from the one that decides PNW - recall that 3 of 5 seats are up for election this year including the one held by Chair Burns who is termed out. Bottom line: while Covid-related shutdowns are placing additional strain on an already-overburdened utility staff at the commission, we see a fully litigated path as the most likely resolution for APS's case.

Four Corners scrubbers remain key issue

The scrubbers installed at Four Corners are a meaningful portion of the total revenue ask of $73m - relative to the $184m total revenue increase requested. The recovery of the scrubbers was included in the last PNW rate case and the utility received a favorable administrative law judge (ALJ) recommendation to receive a step-up in rates mid-year in 2018. With the step-up having not been brought forward by the ACC the item now represents a significant discrete ask as part of the current case. Other notable items are

renewable generation / rooftop solar as well as rate making issues including a formula rate proposal and a pilot subscription rate program.

Renewables in focus with new resource filing in June

PNW capex outlook relies heavily on investment in renewable generation, accelerating spend in the near term such that the plan sees rate base growing by ~8% through 2022 vs. a long-term goal of 6-7%. Recall the recent announcement of a 2050 decarbonization goal with intermediate 2030 goal of 65% clean energy by 2030 with 45% renewables. The clean gen plan calls for the addition of 850 MW of battery storage as well as 100 MW of solar generation by 2025 - note storage technology has been developing rapidly with several qualified developers capable of delivering utility-scale solutions today. The storage plan will include a mix of standalone facilities as well as batteries added to existing PNW solar assets. PNW intends to file its new Integrated Resource Plan (IRP) in June, its first since the announcement of the ambitious new green generation goals. Given the focus around its decarbonization agenda we would expect the IRP to include an updated timeline for retiring of coal plants in line with the long-term plans laid out earlier in Q1 along with further renewable generation options.

The APS' recent approval of the 500-kV Ten West Link transmission project from California to APS' Delaney Substation located 60 miles outside of Phoenix should also boost the opportunity for renewable development and procurement. As the proposed line will cross from Arizona into California, it will allow APS to procure excess renewable energy from California during peak generation times. Further, the project has already reported 5,000 MW of interconnection requests from Arizona-based renewable developers which could further boost renewable development. Recall that under a recent ACC ruling, APS and other state utilities are required to sign contracts of 18 years or longer with operators of Qualified Facilities (QFs) under the Public Utility Regulatory Policies Act (PURPA) – APS had initially proposed a 2 year minimum contract tenor but the commission increased it to 18 in its final decision last December.

Lost fixed cost rate finalized

APS received a decision in its most recent Lost Fixed Cost Recovery (LCFR) mechanism filing related to lost energy sales revenues from customers related to energy efficiency initiatives, principally those utilizing distributed generation. The new rate will be $0.372/kW per month for customers on a demand rate and $0.00125/kWh per month for customers on an energy-only rate, with an estimated revenue recovery of $26.6m in 2020, down from $36.2m in 2019. Recall the LCFR is an annual filing under which APS seeks to recover fixed costs related to revenues lost by customers who are electing for distributed generation.

EPS estimates

We tweak our 2020 estimates lower to account for the likelihood of lost revenues due to Covid shutdown orders in place. Our new consolidated estimate of $4.78 is toward the low end of mgmt.'t guidance range and reflects essentially flat EPS growth y/y. We are slightly below Street consensus for 2020 on our updated estimates though we perceive downside to consensus forecasts as Covid-related lost revenues are factored in. As the ACC has not yet flagged a *further* deterioration in the rate case time frame, we do not adjust our estimates for 2021+ which currently assume the existing rate case schedule with a fully litigated resolution in mid-Q1.

Table 54: PNW estimates

PNW EPS Estimates	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E	2025E
EPS From Continuing Operations	$4.55	$4.71	$4.95	$4.96	$5.32	$5.39	$5.79	$6.32	$6.34
Net Income (Loss) Attributable to Noncontrolling Interests	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17
Income From Discontinued Operations	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
Accounting Changes/Non Operating Adjustments	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
Linked to model - EPS	$4.37	$4.54	$4.77	$4.78	$5.15	$5.23	$5.62	$6.15	$6.18
APS - EPS From Continuing Operations	$4.66	$5.24	$5.19	$5.20	$5.58	$5.72	$6.16	$6.69	$6.72
Parent - EPS From Continuing Operations	($0.11)	($0.53)	($0.24)	($0.24)	($0.26)	($0.33)	($0.37)	($0.38)	($0.38)
Net Income (Loss) Attributable to Noncontrolling Interests	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)
EPS From Cont Ops Attributable to Common Shareholders	$4.37	$4.54	$4.77	$4.78	$5.15	$5.23	$5.62	$6.15	$6.18

Table 54: PNW estimates

PNW EPS Estimates	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E	2025E
Previous Estimates	*$4.37*	*$4.54*	*$4.77*	*$4.83*	*$5.14*	*$5.24*	*$5.63*	*$6.16*	*$6.19*
Guidance	4.15-4.30	4.35-4.55	4.75-4.95	4.75-4.95					
Consensus	$4.27	$4.48	$4.70	$4.82	$5.10	$5.34			
Delta vs Consensus			$0.07	($0.04)	$0.05	($0.12)			
EPS CAGR off 2019A				0.3%	3.9%	3.1%	4.2%	5.2%	4.4%
Street CAGR			3.5%	3.1%	4.0%	4.2%			

Source: BofA Global Research Estimates, company report, Bloomberg

Valuation: PO to $84, maintain Neutral

We maintain our Neutral rating on PNW as we see the current share price as adequately reflecting near-term risks around rate case outcomes, including the uncertain rate case recovery of SCR step up associated with Four Corners along with recovery related to Ocotillo. We reduce the valuation discount applied to PNW's peer group electric utility multiple of 17.6x to -2.5x from -1.5x in order to more adequately reflect ongoing rate case risk – with an uncertain timeline potentially pushing the implementation of new rates further out and lingering uncertainty around the outcome of commission elections in the fall. We reiterate our Neutral rating.

Table 55: PNW SOTP

Price Objective $84	
PNW Valuation: P/E Based on 2022E EPS	
	Price Objective
2022E EPS	$5.23
Group Peer Multiple - Electric	17.6x
Group EPS '18-'22 CAGR - Electric	5.00%
P/E Multiple - Utility Average	18.5x
Premium	-2.5x
Price Objective	$84
2020E Dividend	$3.16
Dividend Yield	4.0%
Total Return (%)	9.1%

Source: BofA Global Research Estimates, company report, Bloomberg

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Title: Subtitle	Primary Author	Date Published
Pinnacle West: Positive capex surprise, equity coming post-2020	Julien Dumoulin-Smith	24 February 2020
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Pinnacle West: Framing the wide Street EPS miss & more to come: Downgrade to Neutral, $90 PO	Julien Dumoulin-Smith	08 November 2019
Pinnacle West: Disconnect Meeting: Few Revelations, Maintain Buy	Julien Dumoulin-Smith	05 September 2019

PPL Corporation (PPL)

We remain Neutral rated on shares of PPL into the quarter. While shares have meaningfully underperformed this year, FX remains volatile with current forwards already at the low end of mgmt.'s (recently lowered) assumptions and we see load degradation as particularly concerning for the company. While the UK is decoupled, volumes are only trued up on a two year basis while US utilities are fully exposed outside of some fixed billing components (sensitivities suggest a 1% change in load is a penny impact in each jurisdiction). *We remain focused on the KY footprint as to sales impacts, particularly as a rate case this year seems unlikely given the latest ROE backdrop. Bottom line, we ultimately see risk/reward as balanced at the current valuation.*

PPL 1Q20 Earnings Walk

We forecast 1Q20 adjusted EPS of $0.73 compared to $0.70 1Q19 & $0.72 consensus.

- **Key Drivers:** We expect gross margin growth across the portfolio and currency tailwinds y/y given hedging position in the UK partially offset by dilution and higher expenses.

Table 56: 1Q20 Walk

PPL 1Q20 Earnings Walk	EPS
1Q19 EPS	$0.70
WPD	$0.02
Kentucky	$0.02
PPL PA	$0.01
Corp & Other	($0.02)
1Q20 BofAe Adjusted EPS	$0.73
1Q20 Consensus	$0.72
BofAe 2020E EPS	$2.50
2020 Consensus	$2.47
2020 Guidance	$2.40-2.60
1Q19 Shares outstanding	730
1Q20 Shares outstanding	756

Source: BofA Global Research, Bloomberg

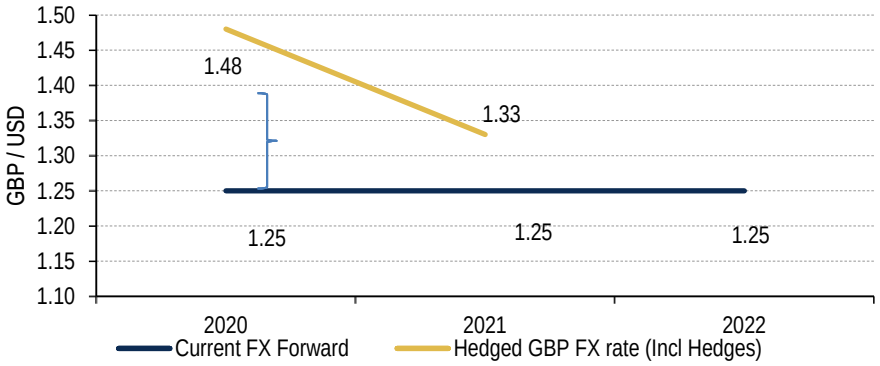
Contemplating COVID Implications

We see PPL as particularly exposed to load degradation amid the ongoing COVID pandemic. While the UK is decoupled, volumes are only trued-up on a two-year basis. While the US has some demand components, we note no decoupling in PA or KY and remain focused on the KY footprint specifically, particularly as any near term rate relief seems less likely on the margin given the latest rate paradigm. For domestic utilities, a 1% change in load is a penny impact in each jurisdiction and the company has some off system sales exposure but no bad debt expense trackers.

FX Outlook: Forwards Imply Low End of Revised Guide

Mgmt lowered expectations with its latest update given current FX rates and forecasts. While the company is 90% hedged for 2020 at an average rate of $1.48, it is only 5% hedged in 2021 at $1.33 and completely exposed in outer years. We note that on an open basis, every 1c in the exchange rate equates to about $0.01/sh of EPS for the company.

Chart 8: Budgeted vs. FX Forwards



Source: BofA Global Research, Bloomberg

WPD RIIO-ED2 Mini Model: OFGEM Prospects

The exhibit below reflects our latest UK mini model for the WPD (Western Power Distribution) business. Recall that Ofgem formally kicked off its RIIO-ED2 process in August 2019 with the publishing of an open letter consultation. A framework was laid out in Mid-December setting the blueprint, confirming the expectation that most design features would follow the earlier RIIO-2 reviews for Transmission and Gas Distribution (being finalised in 2020): a 5 year duration, retaining debt cost indexation, strengthening output incentives, and a move from RPI to CPI inflation indexation (which could ultimately help cash flows). Additional specifics and final decisions for ED (Electric Distribution) will start to shake out over the next couple of years (RIIO-ED1 price control is set to end at the end of March '23).

We therefore expect investors to continue to look for potential read-throughs as Ofgem works through the gas/transmission specific methodology – albeit likely with some delays given the on-going crisis. Developments thus far on the ED2 process have principally reflected those of its earlier counterpart including lower base returns and potentially a similar level to those proposed for transmission and gas. We continue to assume a -3% drop in ROEs under new rates, which we view as a sober set of assumptions *(anywhere in the low 5% to even 7% range on nominal basis appears reasonable in our view given lack of clarity on process).*

We ultimately expect nuances between ED2 and the gas/transmission framework given different risk profiles. However, we see a clear desire from Ofgem to maintain incentives and give the best performing companies an ability to overearn, particularly as distribution networks will be a key enabler of the net-zero carbon target. Any developments out of the COVID crisis will also be critical in terms of nuances around their thought process for UK utilities longer term.

Table 57: RIIO Mini Model

PPL WPD RIIO TABLE	2020E	2021E	2022E	2023E
Nominal RAV (WPD Financials) £Mn	7,996	8,415	8,917	9,449
Equity ratio	35%	35%	35%	35%
Current Allowed ROE	6.40%	6.40%	6.40%	6.40%
ROE Cut	0.00%	0.00%	0.00%	-2.25%
Adjusted ROE	6.40%	6.40%	6.40%	4.15%
UK Net Income (£Mn)	179	189	200	137
US Net Income ($Mn)	261	236	250	172
Hedge Price ($/£)	1.48	1.33	1.33	1.33
% Hedge	90%	5%	0%	0%
Hedge Value	$37.08	$0.75	$0.00	$0.00
Inflation				
Implied RAV Inflation	5.10%	5.24%	5.96%	5.96%
US Net Income Adjusted for Hedges	261	236	250	172

Table 57: RIIO Mini Model

PPL WPD RIIO TABLE	2020E	2021E	2022E	2023E
Depreciation/Pension	729	691	631	611
US GAAP vs UK Reporting	729	691	631	611
Incentives (USD)	2020	2021	2022	2023
Fast Track Award	32	28	28	29
Performance	114	98	106	125
Total Incentives	146	125	134	154
*Implied ROE (Incentives + UK NI / Nominal RAV * 35%)*	*9.26%*	*9.12%*	*9.14%*	*7.13%*
Earned ROE vs. Base ROE (+/-300bps in RIIO)	*2.9%*	*2.7%*	*2.7%*	*3.0%*
Less HoldCo Int	-68	-68	-68	-68
Adjusted US Net Income ($Mn)	1,068	985	946	868
Adjusted EPS	$1.41	$1.30	$1.24	$1.13

Source: BofA Global Research, Bloomberg

EPS Estimates

The table below reflects our latest EPS estimates after reflecting the latest currency forwards and on-going developments, and we continue to stress limited growth ahead given pension headwinds and questions around longer term UK returns, particularly without meaningful FX improvement.

Table 58: PPL Estimates

PPL EPS Estimates	2020E	2021E	2022E	2023E
Regulated Utilities				
International Regulated	$1.41	$1.30	$1.24	$1.13
Pennsylvania Regulated	$0.63	$0.66	$0.69	$0.72
Kentucky Regulated	$0.59	$0.65	$0.69	$0.72
Domestic Utilities	*$1.22*	*$1.31*	*$1.38*	*$1.45*
Parent/Other	($0.13)	($0.13)	($0.12)	($0.12)
Consolidated EPS	$2.50	$2.47	$2.50	$2.46
Prior Estimates	*$2.51*	*$2.48*	*$2.59*	*$2.59*
Consolidated Growth CAGR off 2018 ($2.30 midpoint)	4.31%	2.44%	2.07%	1.39%
Consensus	$2.47	$2.46	$2.56	$2.80
Guidance	$2.40-2.60	$2.40-2.60		
DPS	1.66	1.68	1.69	1.71
DPS Growth (%)	*0.61%*	*1.00%*	*1.00%*	*1.00%*
DPS Payout	66.34%	67.82%	67.84%	69.42%
FFO (CFO pre-W/C) / Total Debt	15.11%	15.18%	15.33%	15.29%

Source: BofA Global Research, Bloomberg

Valuation:

The table below reflects our latest valuation. As shown, we apply the latest peer multiple of 17.6x (vs. 20.6x previously) to our utility estimates for both PPL Electric and PPL Kentucky. We use a 30% premium to RAV for the UK business. Our price objective ultimately shifts to $29. We remain Neutral rated on shares seeing risk/reward as balanced.

Table 59: PPL SOTP

PPL Sum-of-the-Parts							Equity Value		
	EPS	Lower	Peer	Prem/ Disc.	Base	High	Low	Base	High
RAV Approach	C2021 RAV								
WPD RAV	11,058	0.8x	1.0x	0.30x	1.3x	1.8x	$8,846	$14,375	$19,904
Less: WPD leverage (80% Gearing)							($8,846)	($8,846)	($8,846)
							$0	$5,529	$11,058
UK Equity Value							$0	$5,529	$11,058
Implied Valuation / Share							*0.00*	*7.25*	*14.50*
Domestic: Regulated Utilities			2022 P/E Multiples						
Group Peer Multiple - Electric			17.6x						
Group EPS '18-'22 CAGR - Electric			5.00%						
	-	Base Multiple	18.5x						
PPL Electric Utilities	$0.69	17.5x		0.0x	18.5x	19.5x	$9,179	$9,705	$10,230
PPL Kentucky (KU/LG&A)	$0.69	17.5x		0.0x	18.5x	19.5x	$9,218	$9,746	$10,273
Parent/Int Expense	($0.12)	17.5x		0.0x	18.5x	19.5x	($1,661)	($1,757)	($1,852)
			50% Weighting						
PPL Cap Funding Debt	4,530		2,265				-2,265	-2,265	-2,265
Parent Interest Expense (Tax effected @ 21%)	145		73				1,270	1,342	1,415
--> Add back 50% of EPS drag above							-995	-923	-850
PPL Equity Value ($/Sh) Unrounded							$20.64	$29.24	$37.84
Shares Outstanding	2022E EPS						763	763	763
Total PPL Equity Value Per Share	$2.50						$21.00	$29.00	$38.00
Implied P/E							8.4x	11.6x	15.2x
Total Return Calculation									
Current Stock Price								$25.70	
Price Objective								$29.00	
Upside/Downside (%)								12.86%	
Dividend								$1.66	
Dividend Yield								6.46%	
Total Return								19.32%	

Source: BofA Global Research, Bloomberg

See below for our previous research on PPL:

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
PPL Corporation: Have shares round-tripped from their European tryst?	Julien Dumoulin-Smith	18 February 2020
PPL Corporation: Mum on M&A but US prospects need to be back in focus to add to deal confidence	Julien Dumoulin-Smith	06 November 2019
PPL Corporation: Upgrading to Neutral as Ofgem reaffirms the same, known, downside again	Julien Dumoulin-Smith	07 August 2019
PPL Corporation: Solving for 2021: UK overshadows the value proposition	Julien Dumoulin-Smith	19 February 2019

WEC Energy (WEC)

We expect WEC to hit the low end of its guidance range for the quarter despite the weather headwind given ability to flex O&M down as we expect demand impact from Covid to be limited in Q1 and largely weighted toward Q2. WEC is able to utilize its fuel recovery mechanism as a means of partially offsetting lower demand which had been forecast by the company to decline by ~1% in 2020. Accordingly, we maintain our Underperform rating.

WEC 1Q20 Earnings Walk

We forecast 1Q20 adjusted EPS of $1.32 compared to 1Q19 results of $1.33, consensus estimates of $1.33, and guidance of $1.32-1.34.

- **Key Drivers:** Positive YoY drivers include infrastructure investments from the Upstream, Bishop Hill, and Coyote Ridge wind farms (+$0.01), sales growth at the gas utility (+$0.01), reduced O&M expenses (+$0.01). Offsetting results includes the impact of weather which is estimated at 7 cents including a 2 cent drag from normalizing the impact of 1Q19 and incorporating the impact of 2020 milder weather which is estimated at 12% warmer than normal and 16% warmer than 2019.

- **Unknowns**: While Heating Degree Days (HDDs) were 16% above the prior year's level in WI, the exact magnitude of the benefit is difficult to estimate. Recall, WEC is decoupled in IL and at MN gas. Another unknown is the extent to which load growth was affected by Covid-related slowdowns as shut-in orders were generally implemented at the end of the quarter.

Table 60: WEC 1Q20 walk

WEC 1Q20 Earnings Walk	EPS
1Q19 Adjusted EPS	$1.33
Weather - 1Q19 normalized	($0.02)
Weather - 2Q20	($0.05)
Utility sales growth	
Electric	$0.01
Gas	$0.01
Rate Relief	$0.00
Fuel Recovery Mechanisms	$0.02
Interest Expense - re-financing	$0.00
D&A	($0.01)
O&M	$0.01
Storm expense	$0.00
ATC	$0.02
Infrastructure	$0.01
Dilution	($0.00)
1Q20 Adjusted EPS	$1.32
1Q20 Consensus	$1.33
1Q20 Guidance	$1.32-1.34
2019 BofASe	$3.72
2019 Consensus	$3.73
2020 Guidance	$3.71 -$3.75
Share Count	
1Q19	317
1Q20	317

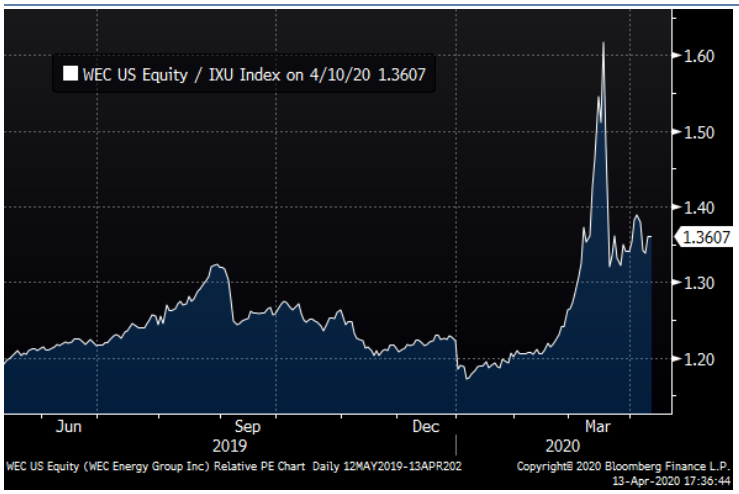
Source: BofA Global Research Estimates, company report, Bloomberg

Stock trading implications

Shares of WEC have performed well vs. the peer group of late reflecting the company's defensive nature amid significant market volatility and investor concerns about the effects on demand from Covid-related shut downs. After re-rating for much of the month of March, WEC trades at roughly 22x forward earnings ('22), a meaningful premium vs. our electric utility peer multiple of ~17x. While shares have consistently traded at a premium to the peer group since 2019, WEC now trades at over 1.3x

premium to the IXU on a 2 year forward PE relative basis, the highest such level in the past 12 months with the exception of the extreme market volatility seen in March. Accordingly we remain Underperform on shares of WEC as the shares remain priced richly relative to the peer group.

Exhibit 5: WEC relative PE chart



Source: Bloomberg

Partial decoupling and a debt tracker to mitigate impact

Most of WEC's jurisdictions do not have a bad debt rider with the exception of IL Gas. Additionally Wisconsin Gas and Wisconsin Electric have bad debt escrow accounting mechanisms. WEC's Illinois Gas and Minnesota Gas businesses have decoupling while the other jurisdictions of Michigan and Wisconsin do not - at both the electric and gas utilities. WEC's electric utilities do not have material exposure to losses from wholesale volumes and accordingly off-system sales are not expected to be a significant source of downside risk. In terms of margin breakdown, 62% of total margin comes from the Electric business with the balance coming from Gas. Residential is relatively heavily weighted among electric demand at 47%, with industrial accounting for 17% and commercial for the balance. 2020 EPS is expected to be impacted by approximately 2-3 cents from a 1% decline in demand and by 0.5 cents from a 1% decline in industrial sales, according to the company. We also highlight that pension funding is less of an issue for WEC than for many utility peers, as the company was fully funded in its *qualified* defined benefit plans at the end of 2019 and over 90% funded on a GAAP basis across all of its pension plans.

Commission latest: new appointee, addressing Covid

Back in March, Wisconsin Governor Tony Evers appointed Tyler Huebner to fill the seat vacated by the retirement of Mike Huebsch on the three-person Public Service Commission of Wisconsin (PSCW). Huebner has been the Executive Director of RENEW Wisconsin since 2013, where he led the organization's efforts to expand and promote the use of renewable energy in the state. He will serve out the remainder of Huebsch's term that expires on Mar 1, 2021. Huebner joins PSCW chair Rebecca Valcq as an appointee of Democrat Gov. Evers, while the third commissioner (Ellen Nowak) was appointed by Republican Scott Walker. We expect that the PSCW will continue to (and perhaps accelerate) its support for renewables investment in the state following this appointment. We expect incumbent utilities WEC and LNT to benefit from increased support for renewables and potentially an increased push for accelerated coal retirements - WEC's Columbia, South Oak Creek, and Weston units being potential candidates. As with other jurisdictions, the issue of undepreciated plant remains a hurdle for possible accelerated retirement, particularly given recent investment in scrubber technology at Columbia.

The PSCW was one of the first utility commissions in the US to act in response to Covid shut downs, suspending late fees and power disconnections for affected customers across the state on Mar 24 and opening a docket to evaluate recovery by utilities of extraordinary expenses incurred in an effort to keep power on for all customers during the declared health emergency. The PSC is working with utilities to identify specific expenses and foregone revenues that have been and are expected to be incurred due to the Covid emergency and is evaluating methods for recovery. Though it remains early days we see this as a constructive and proactive move by the PSC which should at least partially offset WEC's lack of bad debt trackers in Wisconsin.

EPS estimates

We update our 2020 EPS estimate for WEC to reflect headwinds from both lost demand resulting from Covid as well as mild Q1 weather, though the latter point may abate later in the year particularly if warm weather persists into the cooling season and residential load may be boosted by extended stay-in orders. Accordingly we reduce our 2020 estimate to $3.72 from $3.75, toward the low end of mgmt.'s $3.71-3.75 guidance range. Estimates are slightly below Street consensus in 2020-21 and a penny ahead in 2022. The degree to which mgmt. can flex O&M spending in order to offset the effects of Covid related shutdowns remains a key question as stay at home orders persist through Q2 and potentially longer.

Table 61: WEC estimates

WEC EPS Estimates	2018A	2019A	2020E	2021E	2022E	2023E	2024E
WI Electric	$1.13	$1.15	$1.25	$1.27	$1.31	$1.35	$1.38
WPS	$0.55	$0.59	$0.56	$0.59	$0.64	$0.68	$0.71
WI Gas	$0.24	$0.26	$0.39	$0.48	$0.58	$0.67	$0.75
Peoples Gas	$0.42	$0.50	$0.44	$0.49	$0.55	$0.60	$0.65
North Shore Gas	$0.05	$0.05	$0.05	$0.05	$0.06	$0.06	$0.06
ATC	$0.36	$0.39	$0.42	$0.44	$0.47	$0.49	$0.51
We Power (PTF) + Non utility infrastructure	$0.70	$0.76	$0.84	$0.89	$0.92	$0.95	$0.99
MERC/MGU	$0.14	$0.15	$0.13	$0.14	$0.15	$0.15	$0.16
Parent & Int Expense	(0.23)	(0.24)	(0.36)	(0.38)	(0.40)	(0.41)	(0.42)
BofA Estimate	$3.34	$3.60	$3.72	$3.97	$4.27	$4.53	$4.78
Company Guidance			$3.71 -$3.75				
Prior Estimates		*$3.60*	*$3.75*	*$4.00*	*$4.30*	*$4.56*	*$4.81*
BofA CAGR (off 2019 estimate of $3.50)			*6.15%*	*6.50%*	*6.86%*	*6.68%*	*6.43%*
Consensus	$3.33	$3.53	$3.73	$3.99	$4.26	$4.57	
Consensus CAGR			*6.6%*	*6.8%*	*6.8%*	*6.9%*	
Mgmt. Guidance 5-7% off $3.50 in 2019							
Low		$3.48	$3.71	$3.86	$4.05	$4.25	$4.47
Mid		$3.50	$3.73	$3.93	$4.17	$4.42	$4.69
High		$3.52	$3.75	$4.01	$4.29	$4.59	$4.91

Source: BofA Global Research Estimates, company report, Bloomberg

Valuation

We move our PO to $85 after refreshing for updated peer group electric (17.6x) and gas (17.6x) multiples and continue to stress very limited upside with shares trading above our valuation. We update our relative peer group premium for the Wisconsin electric utilities to 3.0x from 2.0x given positive regulatory backdrop in the state including prospects for bad debt recovery and decoupling. We also reduce the premium applied to We Power (PTF) from 2.0x to 1.0x. Bottom line, WEC shares continue to trade at a premium valuation and despite accounting for Wisconsin's positive regulatory backdrop in our SOTP the shares remain expensive, and accordingly we maintain our Underperform rating on WEC.

Table 62: WEC SOTP

Regulated Utilities	2022E EPS	2022E Net Income	P/E Multiple					Equity Value		
			Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric				17.6x						
Group EPS '18-'22 CAGR - Electric				5.00%						
Group Peer Multiple - Gas				17.6x						
Group EPS '18-'22 CAGR - Gas				5.10%						
Applied Multiple				Electric 18.5x Gas 18.5x						
WI Electric	$1.31	416	20.5x		3.0x	21.5x	22.5x	$8,528	$8,944	$9,361
WPS	$0.64	202	20.5x		3.0x	21.5x	22.5x	$4,141	$4,343	$4,545
WI Gas	$0.58	184	18.0x		0.5x	19.0x	20.0x	$3,306	$3,489	$3,673
Peoples Gas	$0.55	173	18.0x		0.5x	19.0x	20.0x	$3,120	$3,293	$3,466
North Shore Gas	$0.06	18	18.0x		0.5x	19.0x	20.0x	$317	$335	$352
ATC	$0.47	148	19.5x		2.0x	20.5x	21.5x	$2,876	$3,023	$3,171
We Power (PTF)	$0.61	193	18.5x		1.0x	19.5x	20.5x	$3,569	$3,762	$3,955
MERC/MGU	$0.15	46	18.0x		0.5x	19.0x	20.0x	$835	$882	$928
Parent & Int Expense	-$0.40	(126)	17.5x		0.0x	18.5x	19.5x	($2,201)	($2,327)	($2,453)
Total Implied Utilities	$3.96	1,254				20.5x		$24,490	$25,744	$26,998
Non Utility Energy Infrastructure	$0.31	98	15.5x		-2.0x	16.5x	17.5x	$1,521	$1,619	$1,717
Implied Valuation Multiple					19.9x					
HoldCo Debt Adjustment										
Add Back: 50% of Interest Expense	$0.11	35	19.5x		0.0x	20.5x	21.5x	$679	$713	$748
Subtract: HoldCo Debt (Net out 50%)	2,200	(1,100)						($1,100)	($1,100)	($1,100)
Total Equity Value								$25,589	$26,976	$28,364
Valuation								$81.00	$85.00	$90.00
Shares Outstanding										317
Rounded 12 Month Target Price										
Stock Price									$97.59	
Upside/Downside									-12.9%	
NTM Div Yield									2.5%	
Total Return									-10.4%	

Source: BofA Global Research Estimates, company report, Bloomberg

See our latest research here:

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
WEC Energy Group Inc: Watch the Cost Trajectory; Accelerating Infra Piece: but this is the debate	Julien Dumoulin-Smith	03 February 2020
WEC Energy Group Inc: Rolling out an ever higher capex plan	Julien Dumoulin-Smith	08 November 2019
WEC Energy Group Inc: Settlement terms more constructive than expected	Julien Dumoulin-Smith	26 August 2019

Xcel Energy (XEL)

After resolving much of the regulatory calendar from filing rate cases in 2019 (even recently announcing a settlement w/o details in TX), XEL is still working to file in 2020 in many states and exploring ability to push off some of the rate cases. We see two states of focus here: MN (using 2015 legislation that allows XEL to recover advanced grid spend through the transmission rider) and CO (depending on in the advanced grid initiative can be recovered via rider). Both depend on regulators, and we saw value in XEL being able to stay out of MN's last year. XEL isn't as exposed to COVID demand impacts as other names given its decoupling mechanisms in CO & MN (accounts for 45% of retail electric sales) and given its impact in prior events (i.e. '08 crisis and low oil prices of '16). Finally, we note our ests reflect XEL now selling Mankato to keep the utility fully regulated (we see viewed positively); while we had factored in 4c/yr for the non-reg asset before the sale, XEL was only expecting 1-2c/yr in early years. With our expectation of LT earnings squarely in the 5-7% trajectory, good FFO/debt metrics, and a consistent earnings growth story, we expect the name to be strong during recovery. Finally, given orig O&M '20 guidance, we expect there's room for savings that counterbalance some impacts from COVID & mild winter overall. As for 1Q, we forecast $0.53/sh vs. $0.62/sh likely un-updated Consensus. Reiterate Neutral.

1Q20 Walk

We expect a $0.53/sh 1Q20 estimate, versus a Consensus of $0.62/sh and a prior year's 1Q19 est of $0.61/sh. We expect Consensus has not been adjusted for weak weather and COVID impacts on demand.

- **Drivers**: With a number of rate cases filed in 2019, XEL has new rates starting in 2020 for MN, CO, NM, and TX (although some taking effect later this year). Impacting 1Q include Minnesota's interim sales true up and nuclear decommissioning (Jan 1, 2020), Colorado's electric rates (Feb 25, 2020), and last year's $4.5mn SPS incremental rate increase (March 11, 2019); these contribute to +5c for the walk. The capital rider revenue and AFUDC contribute another +3c.

- **Other**: We evenly distribute XEL's annual '20 guide between quarters for interest expense, O&M, and property taxes (-5c). We only include -5c of D&A as this will likely be a little more back-end loaded. Finally, we expect -2c of demand impact from COVID since most businesses were shut down for the last 2 weeks in March and some folks were working from home for the last 3 weeks.

- **Wildcard**: We expect XEL to be negatively impacted by the wild winter, likely a few pennies worth (1-3c); note 45% of the electric sales (in CO & MN) are decoupled.

Table 63: XEL 1Q20 Walk

Xcel Energy 1Q20 Earnings Walk	EPS
Ongoing EPS 1Q19	$0.61
Weather	
Return to normal	($0.03)
Current quarter	($0.02)
Rate Changes	
NSPM Minnesota Electric Interim sales true up & Nuke decommissioning ($122mn, Jan 2020)	$0.04
PSCo Colorado Electric rates ($35mn, Feb 25 2020)	$0.01
SPS New Mexico Electric rates ($31mn, 2Q20)	$0.00
SPS Texas Electric rates (requested $136mn, 3Q20)	$0.00
SPS Electric rates ($4.5mn March 2019)	$0.00
Capital rider revenue	$0.02
AFUDC	$0.01
Other	
Interest Expense increase	($0.02)
Increase in D&A expense	($0.05)
O&M (1-2% increase)	($0.01)

Table 63: XEL 1Q20 Walk

Xcel Energy 1Q20 Earnings Walk	EPS
Property taxes	($0.01)
COVID 1Q demand impact (-) and leap year pick-up (+)	($0.01)
Dilution (settled)	($0.00)
1Q20E Adjusted EPS	$0.53
1Q20E BofA Estimate	0.53
1Q20 Consensus	0.62
2020E BofA EPS	$2.72
2020 Consensus	2.76
2020 Guidance	2.73-2.83
Shares Outstanding 1Q19	516
Shares Outstanding 2Q20	525
Tax rate	25%

Source: BofA Global Research estimates, company report, Bloomberg

Key 1Q20 Topics

- **O&M**: XEL's original 2020 guidance includes a 1-2% O&M increase; we could see the company look to bend the curve if it needs from COVID impacts. We see this as a key differentiating strength compared to peers.

- **2019 Rate cases**: XEL is resolving many of its rate cases, having a settlement in principal for its TX case (we expect somewhat slowed down from working remote); we expect cap structure avoids concerns peers recently saw since XEL is integrated in TX and interveners all proposed 51% layers or higher. CO gas just received a schedule from an administrative law judge (would allow rates to be implemented in Nov) and NM is waiting for the commission to decide on the settlement.

- **2020 Rate cases**: As for next cases to be filed, we look for commentary on whether XEL can pursue transmission trackers to recovery other expenses in MN (given 2015 legislation allowed XEL to recover advanced grid spend) and CO (perhaps recovering the advanced grid initiative through a rider). We see rate case stayouts as a key strategy in avoiding ROE risk, and have confidence in XEL's ability. If filed, timelines would be later this summer for CO and in Nov for MN.

- **Mankato sold**: After purchasing Mankato as a non-regulated instead of regulated (which was accretive 3-4c vs 1-2c in the near-term, respectively), mgmt. absorbed feedback on being fully regulated and viewed a purchase as resulting in a better valuation for the company. We removed from our estimates any more PPA buyouts we thus expect to be regulated or not pursued.

- **COVID**: XEL has decoupling mechanisms in both Minnesota (fully) and Colorado (partially) representing 45% of retail electric sales: In MN, sales are trued-up for all electric classes, and in CO, decoupling is for resi and SC&I non-demand classes. XEL doesn't have bad debt recovery but we would expect the company to request deferred accounting if expenses significantly increase. As for looking at historic responses, we note that in 2016 when oil prices were in the $30 range, SPS YTD 2016 sales through 2Q16 declined by 1.1% (resi declined 3.2% and C&I only 0.6%). Meanwhile during the '08/09 crisis, XEL saw weather-adjusted sales down 1.8%. Finally in terms of sensitivity, we highlight the company anticipates a 100bps change in electric equates to a $25mn pre-tax impact (if the full change in sales was for C&I, the impact would be less but it's not separately broken out); we calculate this to be a 3-4c impact using a 21% tax rate.

Estimates

Our estimates remove the non-regulatory Mankato asset (given its sale in '20) and reflect our expectation that lower demand from COVID, mild winter, and oil price are somewhat balanced by more cost cutting. We await O&M announcements on the call.

Table 64: XEL EPS estimates

Subsidiary	2016A	2017A	2018A	2019E	2020E	2021E	2022E	2023E	2024E
Northern States Power Minnesota (NSPM)	0.96	1.01	0.96	1.05	1.11	1.29	1.44	1.53	1.63
Southwestern Public Service (SPS)	0.30	0.30	0.42	0.51	0.59	0.60	0.60	0.61	0.62
Public Service Colorado (PSCo)	0.91	0.94	1.08	1.11	1.06	1.05	1.07	1.14	1.19
Northern States Power Wisconsin (NSPW)	0.14	0.16	0.19	0.15	0.16	0.18	0.20	0.21	0.23
Parent (Excl Mankato)	(0.10)	(0.12)	(0.18)	(0.17)	(0.15)	(0.17)	(0.19)	(0.21)	(0.22)
Consolidated	2.21	2.29	2.47	2.64	2.76	2.94	3.12	3.28	3.44
EPS Growth (%)			*8%*	*7%*	*4%*	*7%*	*6%*	*5%*	*5%*
Prior Estimates			*2.47*	*2.64*	*2.83*	*2.99*	*3.14*	*3.31*	*3.46*
Guidance (Excl Mankato)	2.17-2.22	2.25-2.35	2.45-2.49	2.60-2.65	2.73-2.83				
Consensus			2.46	2.62	2.76	2.96	3.14	3.31	#N/A N/A
Mgmt EPS CAGR: 5-7% off 2018 base ($2.43)	2.21	2.29	2.47	2.60	2.78	2.95	3.12	3.31	3.51
		low	*2.43*	*2.55*	*2.73*	*2.87*	*3.01*	*3.16*	*3.32*
		high	*2.43*	*2.65*	*2.83*	*3.03*	*3.24*	*3.47*	*3.71*
BofAe CAGR '18-'23e (off $2.43)	6.2%								
BofAe CAGR '18-'24e (off $2.43)	5.9%								
Target FFO/Debt			17%	18%	17%	17%	17%		
BofAe FFO/Debt		22%	19%	19%	17%	18%	17%	17%	

Consolidating				2.64	2.76	2.94	3.12	3.28	3.44
Guidance				2.60	2.78				
Difference				*0.04*	*(0.02)*				

Source: BofA Global Research estimates, company report, Bloomberg

Valuation

We MtM the peer multiple (now 17.6x) and derive a $66/sh PO with the same 3x premium awarded for the quality mgmt., decoupling, and opportunity for more O&M. Reiterate Neutral.

Table 65: XEL SOTP Valuation

Regulated Utilities	2022E Net Income	EPS	P/E Multiple					Equity Value		
			Bear	Peer	Prem/ Discount	Base	Bull	Bear	Base	Bull
Group Peer Multiple - Electric				17.6x						-
Group EPS '18-'22 CAGR - Electric				5.00%						-
										-
Relative Utility Group P/E Multiple				18.5x						
Northern States Power Minnesota (NSPM)	$773	$1.44	20.5x	18.5x	3.0x	21.5x	22.5x	$29.49	$30.93	$32.37
Southwestern Public Service (SPS)	$325	$0.60	20.5x	18.5x	3.0x	21.5x	22.5x	$12.38	$12.98	$13.58
Northern States Power Wisconsin (NSPW)	$106	$0.20	20.5x	18.5x	3.0x	21.5x	22.5x	$4.04	$4.24	$4.43
Public Service Colorado (PSCo)	$575	$1.07	20.5x	18.5x	3.0x	21.5x	24.5x	$21.93	$23.00	$26.21
Total/Average Utility Earnings (excl Mankato)	$1,779	$3.31			3.0x					
Parent/Unallocated (excl Mankato)	-$103	-$0.19	20.5x	18.5x	3.0x	21.5x	22.5x	-$3.93	-$4.13	-$4.32
		NPV								
Add NPV of Mankato Non-Ratebase Acquisition		$308						$0.57	$0.57	$0.57
Add back 50% of HoldCo interest	$74	$0.14	20.5x	18.5x	3.0x	21.5x	22.5x	$2.80	$2.94	$3.08
Less: 50% of HoldCo Debt	-$2,524							-$4.70	-$4.70	-$4.70
Total	$1,675	$3.12						$62.57	$65.83	$71.23
Shares Outstanding (2022e)									*537*	
Total Equity Value Per Share								$63.00	$66.00	$71.00
Price as of close 04/20/20									$67.15	
Dividend FY20									1.72	
Dividend Yield									2.6%	
Total Potential Return Projected								-4%	1%	8%

Source: BofA Global Research estimates, company report, Bloomberg

Table 66: BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Xcel Energy Inc: Upgrade to Neutral: Rate Case Risks Poised to be Resolved	Julien Dumoulin-Smith	31 January 2020
Xcel Energy Inc: Rate case clarity in time for more in 2020	Julien Dumoulin-Smith	09 January 2020
Xcel Energy Inc: Rolling in Mankato as a Contracted Plant; Waiting on Deals in Key States	Julien Dumoulin-Smith	25 October 2019

Source: BofA Global Research

Table 67: Stocks Mentioned

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
LNT	LNT US	Alliant Energy Corp	US$ 49.99	A-1-7
AEE	AEE US	Ameren Corp	US$ 73.24	A-1-7
AEP	AEP US	American Elec Power	US$ 82.91	A-1-7
AWK	AWK US	American Water	US$ 126.46	A-3-7
ED	ED US	Consolidated Edison	US$ 85.47	A-2-7
DTE	DTE US	DTE Energy	US$ 100.76	A-2-7
DUK	DUK US	Duke Energy	US$ 86.65	A-2-7
EIX	EIX US	Edison Intl	US$ 60.01	B-2-8
ETR	ETR US	Entergy Corp.	US$ 96.45	A-1-7
WTRG	WTRG US	Essential Utilities	US$ 42.24	A-2-7
EVRG	EVRG US	Evergy	US$ 59.12	A-1-7
ES	ES US	Eversource Energy	US$ 87.77	A-3-7
FE	FE US	FirstEnergy	US$ 44.49	A-1-7
PNW	PNW US	Pinnacle West Capit	US$ 76.60	A-2-7
PPL	PPL US	PPL Corp.	US$ 25.25	B-2-8
WEC	WEC US	WEC Energy Group Inc	US$ 95.88	A-3-7
XEL	XEL US	Xcel Energy	US$ 64.35	A-2-7

Source: BofA Global Research, Bloomberg

Price objective basis & risk

Alliant Energy Corporation (LNT)

Our $56 PO is based on a sum of the parts analysis employing relative premium and discounts to the large cap regulated peer multiple of 17.6x 2022E P/E. While our PO is on a 1 year basis we note the 2022 P/E multiple reflects a discount back to 2019. We note that electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector.

We apply a 2.0x P/E premium on IPL as we see the ratecase overhang being resolved. We apply a 3.0x P/E premium on Eastern Wisconsin Electric Company reflecting 1) low risk investment nature of the state, 2) above average ROEs, 3) higher than average growth runway for investments, and 4) bad debt deferral. At ATC, we reflect a 2.0 x P/E premium on LNT's 16% share in the transmission company. Growth expectations for this segment are high, paired with above average ROEs that we believe face less downward pressure vs. regulated state distribution ROEs. We apply an in line multiple at the parent to account for the blend of numerous businesses some which benefit from long term stable PPAs via intercompany generation.

Risks to our price objective are: 1) adverse rate case outcomes, 2) further equity dilution beyond our estimates, 3) interest rate risk, 4) natural disasters, and 5) lower allowed ROE's

Ameren Corporation (AEE)

Our $85 price objective is predicated on a P/E based sum of the parts, valuing each business subsidiary relative to the 2022E ratebase weighted peer multiple of 17.6x for electric. We apply a 3.0x premium to peers at AEE Missouri to account for the improving

prospects of capital spend, supplemented by a regulatory jurisdiction becoming more favorable. We apply a 3.0x premium to peers at AEE Illinois to account for decoupling on the distribution business which aids in earnings predictability. The overall business is expected to grow at a more meaningful clip than that of peers - we see a 10% EPS CAGR at IL 2020-2024. At ATXI, we apply a 0x premium to peers to reflect the latest potential step down in FERC ROEs. At the Parent, we assume an in line multiple given the healthy debt metrics with FFO/Debt at 17%+. Electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector.

The upside (downside) risks to our price objective are the utilities earning their allowed returns or better (worse), a significant increase (decrease) in 30-year U.S. Treasury bond yields, and positive (adverse) regulatory outcomes that could impact mgmt's ability to earn its allowed return

American Electric Power (AEP)
Our price objective of $93 is based on SOTP analysis. We ascribe a peer forward P/E multiple (17.6x) with a 0x premium for its transmission-only Utilities segments as well as Kentucky Power, a 1x premium for its T&D utilities, and a 0x premium for regulated utilities. We ascribe limited value to the nascent renewables business & SRE Renewables deal ($0.03/sh), based on a in-line peer P/E multiple given uncertainty. We note that electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. We assume 100% likelihood of the North Central wind project and assign it a 0x premium under the reg utes as well.

Downside risks to our price objective are 1) regulatory outcomes are less favorable than expected, which could result in reduced ROE, 2) large capital intensive are subject to delays or cost overruns, which can change the return profile, 3) natural disasters or catastrophic events can affect system reliability and are subject to regulatory cost recovery risk, 4) utilities are subject to interest rate risk to fund their business, which affects cost of capital, 5) commodity risk affects the generation business margins and indirectly affects the regulated business as a pass through cost, 6) consumer advocates are focused on bill inflation, which can affect regulatory outcomes, 7) non-regulated businesses are inherently more risky and subject to execution risk and commodity variation.

American Water Works (AWK)
Our PO for American Water Works is $133. We apply the sector average 26.3x P/E multiple to American Waters 2022E earnings based on the water peer multiple and a 8.3% group EPS CAGR for '18-'22E. We think this multiple is justified as in our view AWK largely drives the peer multiple as the largest publicly traded water utility. We ascribe a 3x premium for NJ, PA, and IL, and a -3x discount to the military biz. Meanwhile, we ascribe a 12x multiple to the non-regulated Retail biz. Also a -1x P/E for Cali utility. no prem/discount for 'Other' segment with smaller state exposures.

Risks to the downside are increase in market interest rates, potential impact of tax reform on utilities, operational errors, changes in valuation levels for water utilities. Risks to the upside are accelerating muni acquisitions, multiple expansion, and constructive legislation in regulatory jurisdictions.

Consolidated Edison (ED)
Our $93 PO is based on a sum-of-the-parts analysis applying premiums and discounts to the regulated group multiples (17.6x/17.6x for electric/gas respectively) with a 1.0x premium to reflect defensive nature of the stock. We note that both electric and gas peer P/E multiples are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We applied inline peer regulated multiple at CECONY despite its rate certainty for conservatism as our higher capex expectations are reflected in our EPS outlook. We apply a discounted PE for infrastructure projects given the lack

of clarity around the capital structure. We further apply an EV/EBITDA approach on 2022E EBITDA to the CEB business using a 10.0x multiple for both the legacy portfolio and the renewables portfolio seeing it as having higher quality returns.

Downside risks: ED, like all utility stocks, is also sensitive to changes in the market level of interest rates. Utilities historically underperform if bond yields rise, and outperform when they fall. Further downside risks are the inability to recontract storage, adverse regulatory outcomes, a deteriorating regulatory environment, or unforeseen disasters such as the Harlem gas explosion, the SRE transaction not being completed. Customer inflation is also a downside risk. PCG related counterparty exposure is among the nearest exposures to watch.

DTE Energy (DTE)

We value DTE Energy at $112 using a SOTP approach.
We value the utility segment on a 2022E forward P/E multiple basis and the non-utility seg. on a 2022E forward EV/EBITDA mult. basis. For the utility segment we apply a 1x premium to our both reg. electric and gas utility peer mult. of 17.6x. Both electric and gas peer P/E mult. are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We subtract out Corp & Other expense excl. interest rate. For GSP we use a midstream peer group multiple of 9x, with a -0.5x discount for Momentum. P&I, we apply a 8x EV/EBITDA mult, despite the lower equality of these earnings and opaque disclosures, as mgmt has been able to execute on new project origination. We value the reduced emissions fuel (REF) tax credits separately using a DCF methodology at 6%
discount rate.
Upside risks to our PO are capex expansions, higher authorized ROEs, and strong performance in the ET segment. Downside risks are interest rate hikes, execution risk on organic growth initiatives at the nonregulated business, and less favorable regulatory environment.

Duke Energy (DUK)

Our $93 PO is derived from a sum-of-the-parts valuation. We value the Electric and Gas utilities using peer 2022E P/E multiples. We apply a 1.0x multiple premium to Duke's operations in Florida to reflect more favorable regulatory environments. We apply an in-line multiple to the Carolinas given risk ahead. We value the other regulated electric utilities and the gas utilities at peer group multiples of 17.9x 2022E P/E, respectively. Both electric and gas peer P/E multiples are grossed up by 5% for the groups CAGR to reflect capital appreciation across the sector. The commercial midstream, and transmission are valued on a 2022E EV/EBITDA basis. We use a 11.0x multiple for midstream and transmission segment, although we assume a 50% weighting for ACP given risks to completion. We add the net present value of renewable segment using an 8% discount rate. We subtract out the impact of commercial debt, and add back for the renewable debt.

Upside risks: constructive rate case results, higher capital expenditure additions vs our assumptions, ACP ahead of schedule, lower interest rates. Downside risks: poor rate case results, operating errors, and negative changes in the regulatory environment, ACP delays. Macro risks: Increases in interest rates and decreases in equity market valuations.

Edison International (EIX)

Our $69 PO is based on SOTP, applying a 3x disc to the FERC and CPUC jurisdictional subsidiaries, and the parent/other segment 17.6x on 2022E (grossed up by 5% to reflect capital appreciation across the sector). The disc reflects CA ongoing wildfire risk despite the improved construct through AB1054. We apply 10x 2022E P/E to the Edison Energy segment to reflect uncertainty in the nascent biz. We net out ongoing contribution to the fund on an NPV basis. Lastly, we assume equity financing to fund '17/18 wildfire claims.

Downside risks: 1) Regulatory outcomes less favorable than expected. 2) Natural disasters or catastrophic events can affect system reliability and are subject to regulatory cost recovery risk. 3) Interest rate risk. 4) Non-reg businesses are inherently more risky and subject to both execution risk and commodity variation. 5) CA has specific risks given the differentiated regulatory regime. 6) CA wildfires.
Upside risks: rate case outcome above what's embedded in companies' guidance and BofA estimates, lower interest rates, more constructive regulatory / legislative outcomes to address wildfire risk

Entergy (ETR)
Our $122 PO is SOTP based. We assign P/E multiples (peer multiple of 17.6x) for 2022E on most segments, in line with peer multiples (and grossed up by 5% to reflect capital appreciation across the group) due to similar growth, and strip out 50% of the holdco senior notes. The Merchant business is also added as a DCF (10% discount rate, no terminal value). Both electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector.

Downside risks: 1) Regulatory outcomes or earned ROE's could worsen, 2) Rate making mechanisms could change in the future, 3) Failure to get trackers or ROE adjustment mechanisms could hurt realized ROE, 4) weather can affect operations and earnings, 5) Interest rate risk affects cost of capital, 6) Consumer advocates or utility staff may focus more on issues that challenge the company ROE, 7) ETR has had safety issues in the past, which have affected regulatory relationships and company liabilities, 8) Exit from the competitive business could present unforeseen challenges.

Essential Utilities (WTRG)
Our price objective is $47 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 2.0x premium to Peoples Gas given the organic growth opportunities.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Risks to the upside include upward revisions to street estimates and further accretion from implementation of the Repairs Tax Benefit.

Evergy, Inc (EVRG)
Our $69 price objective for EVRG shares is based on sum of the parts valuation, applying an in-line utility peer 2022E P/E of 17.6x. Electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We further apply a +2.0x turn discount across all jurisdictions based on our perception of improving regulatory relationships and possibility of further stakeholder engagement.

Downside risks to our price objective are adverse regulatory outcomes in rate cases, higher interest rate environments, adverse and unexpected risks associated with operating a nuclear facility, the possibility that the strategic review committee does not result in a transaction recommendation and that a modified standalone plan disappoints in rate base and earnings growth when presented later in 2020.

Upside risks to our price objective are favorable regulatory outcomes in rate cases, lower interest rate environments, higher than anticipated O&M benefits and merger synergies, ability to recover capital tied to retired coal plant.

Eversource Energy (ES)
Our sum of the parts based price objective of $83 uses P/E multiples on 2022E earnings. For electric utilities, we attribute a 2x premium NSTAR and 1x for CL&P, reflecting future potential positive revisions to capex and earnings, while maintaining an in line multiple of 17.6x P/E for PSNH. For gas, we apply an in-line to the peer 17.6x multiple, given recently compressed spread relative to electric peers. Both electric and gas peer

P/E multiples are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We value Aquarion at a 22.6x multiple to reflect the premium water utilities are currently trading at. We reflect ES' 50% ownership in Revolution and South Fork offshore wind sites on NPV basis. We take out 50% of parent debt, and 50% of interest to accurately reflect parent leverage.

Upside risks to our price objective are additional capex announcements on the T&D side, as well as success in offshore wind RFPs or other larger projects such as Northern Pass.

Downside risks are reduction in authorized ROEs, inability to meet earned ROE expectations, as well as failure to receive permitting on incremental capex opportunities

FirstEnergy (FE)
Our PO of $47 is based on a SOTP: Multiples are driven by relative P/E premiums/discounts to the 2022 regulated peer multiple of 18.5x. Electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. For NJ, we apply an in line multiple to account for slightly higher ROEs vs. the national average and a generally constructive commission. In PA, we apply a -1x disc to reflect O&G royalties (albeit limited). In OH, we apply a -4x P/E discount multiple and a -2x discount to others. We argue this accounts for overearning risk. Finally, we apply a 0x P/E premium to peers 2022E multiple to the Transmission business given some limited ability to invest and FERC ROE difficulties. We removed impact of DMR payments. We subtract out the holding co debt given the high parent lev. We net out potential liabilities from a potential FES bankruptcy by assuming all known 'extra' potential liabilities.

Downside risks: 1) Reg outcomes may improve/deteriorate, 2) legislative solutions may materialize for challenged parts of biz or FE could lose/fail to gain legislative support in key states, 3) int rates positively/negatively affect cost of cap, 4) reg staff or cons advocates may focus on issues beneficial/detrimental to ROEs, 5) exit from comp power biz may or may not have substantive liabilities accrued to equity holders.

Pinnacle West (PNW)
Our price objective of $84 is based on a peer utility 2022E P/E multiple of 17.6x with a -2.5x discount to account for PNW's risk around its pending rate case as well as headline risk related to disconnect policy review. Electric and gas peer P/E mult is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We ascribe an in-line premium despite clear renewable capex backdrop given ongoing regulatory risk associated with the company's upcoming rate filing and 2020 election risk.

Upside risks: 1) Regulatory relationships/outcomes could improve, including changes at the elected commission 2) load growth in territory above expectations 3) Riders and capital trackers could help achieve ROE 4) positive weather helps earnings 5) interest rate risk changes cost of capital - lower rates could improve 6) Consumer advocates or utility staff could become focused on issues that improve ROE

Downside risks: 1) Regulatory relationships/outcomes could decline, including changes at the elected commission 2) load growth in territory below expectations 3) Riders and capital trackers could hurt ROE 4) negative weather hurts earnings 5) interest rate risk changes cost of capital - higher rates could worsen 6) Consumer advocates or utility staff could become focused on issues that hurt ROE 7) Solar advocates in the state have engaged in public confrontations with the utility, which could change public relations in the future.

PPL Corporation (PPL)
Our $29 price objective is based on a sum of the parts methodology applying respective premium/discounts to the 2022E peer group multiple of 17.6x. Electric peer P/E multiple is grossed up by 5% to reflect capital appreciation across the sector. We apply a 1.3x

RAV multiple in our base case for our Western Power Distribution (WPD) RAV approach, seeing the higher ROEs relative to other distribution networks commanding a premium valuation.

Downside risk to our price objective is exposure to FX rates. Since the UK segment represents a significant portion of PPL's earnings, a Federal Reserve decision to raise interest rates could produce a fall in the GBP/USD currency rate that would adversely affect our estimates and valuation for PPL. Also, like all utility stocks, PPL has historically underperformed if bond yields rise. Upside risks are a rising $/pound (GBP) price, positive regulatory outcomes, and decreasing treasury yields.

WEC Energy Group Inc (WEC)
Our $85 PO is based on a 2022E SoTP analysis, based on the large cap electric group multiple of 17.6x and the gas regulated multiple of 17.6x. Both electric and gas peer P/E multiples are grossed up for a year to reflect capital appreciation across the sector.

We apply a 3.0x premium to WEC's electric subs to compensate for surety in earnings growth for the next two years following the Commissions affirmation of the recent settlement on above average ROE's of 10%+. We apply a 0.5x premium to the gas utilities, including Peoples Gas and North Shore Gas with the Gas System Modernization Program (GSMP) and capex forecasts de-risked following the ICC order. We ascribe a 2x premium vs. the group at ATC to account for the steady nature of earnings growth as well as above average ROE's that are set at a federal level by FERC. We give Power the Future (PTF) a 2.0x premium multiple given the ROE is set indefinitely on historical and new investments. We ascribe an in line multiple for the parent accounting for the interest expense which finances overall utility operations. For the HoldCo adjustment to debt, we net out 50% of HoldCo debt from equity valuation and adjust to add back the parent drag on interest expense.

Upside Risks to achieving our price objective include 1) stronger than expected execution 2) accelerating capital opportunities and 3) favorable ratecase outcomes

Xcel Energy Inc (XEL)
Our PO is $66. We value Xcel Energy using a sum of the parts (SOTP) approach. Given the difference in geography, earnings strength, growth opportunity and risk profile, we divide the segments by subsidiary.

We use 2022E forward P/E multiples to derive a value for the different business segments, including the parent segment. We use on a peer multiple of 17.6x . Electric peer P/E multiple is then grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We apply a 2x premium to subsidiaries. We see this multiple as appropriate as the company has growth opportunities, resolving regulatory drag and resolving uncertainty around rate cases. We include Mankato as a non-reg asset in our SOTP. We also net back 50% of the parent interest expense and instead subtract out 50% of parent debt to more accurately reflect HoldCo leverage.

Downside risks are interest rate increases, regulatory risk such as lower authorized ROEs or less favorable riders/trackers for renewables and transmission, interest rate risk, execution delays, and weather anomalies.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AES	AES	AES US	Julien Dumoulin-Smith
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Utilities Group (as of 31 Mar 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	72	50.35%	Buy	51	70.83%
Hold	38	26.57%	Hold	28	73.68%
Sell	33	23.08%	Sell	24	72.73%

Equity Investment Rating Distribution: Global Group (as of 31 Mar 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1602	52.15%	Buy	1005	62.73%
Hold	713	23.21%	Hold	463	64.94%
Sell	757	24.64%	Sell	382	50.46%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

***INCOME RATINGS*, indicators of potential cash dividends, are: 7 - same/higher (dividend considered to be secure), 8 - same/lower (dividend not considered to be secure) and 9 - pays no cash dividend.** *Coverage Cluster* is comprised of stocks covered by a single analyst or two or more analysts sharing a common industry, sector, region or other classification(s). A stock's coverage cluster is included in the most recent BofA Global Research report referencing the stock.

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BofAS or an affiliate was a manager of a public offering of securities of this issuer within the last 12 months: Amer Elec Power, Ameren Corporation, DTE Energy, Duke Energy, Essential Utilities, Evergy, Eversource Energy, FirstEnergy Corp, Xcel Energy Inc.
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North American Utilities & IPPs

AGA Digital Takeaways: What We Learned on Day 1

Industry Overview

Holding the line on ’21 remains the focal point

We hosted meetings on Day 1 of the online version of the AGA conference with AEE, AGR, CNP, ED, DUK, WTRG, MDU, NWE, SRE, SO, and WEC. Much of the discussion remains focused on holding the line on both costs and rate case strategy heading into ’21 for most companies. We stress an implicit pivot on how costs are managed into ’21 to ensure their sustainability, with several companies increasingly contemplating labor-related savings annualizing into ’21 based on headcount freezes enacted (as well as forthcoming voluntary headcount reductions/early retirement options increasingly considered should Covid impacts last beyond ’20 too). That said, the most critical considerations remain how to *establish a test year* based on current year (inclusive of updated load growth & updated/suppressed cost inputs) while similarly facing pressures on authorized ROEs. We suspect companies will *continue* to attempt to delay any future rate increases on customers beyond 2021, suggesting another year of cost cutting necessary to keep EPS intact. By contrast, 2022 could prove substantially more active on rate activity as ’21 should provide a ‘normalized’ set of assumptions and the palatability of rate cases proves more intact among regulators. We could see this accentuate all the more the differences between companies benefitting from automated structures such as decoupling and formula rates, in contrast to those companies without any such mechanisms. We also see a need to remain vigilant on costs. We anticipate another wave of modestly cautious updates by 2Q and definitely by the 3Q as discussions around next year begin to frame up (cost cutting once more should feature prominently in these updates we think). While 1Q ended up proving more intact than anticipated, largely due to affirmations on outlook on ’20 to cost reductions the question remains just if companies can sustain reductions & still execute on contemplated growth: increasingly tricky backdrop albeit risks to sector EPS remain quite limited to downside (1-2% order of magnitude).

What companies stood out from our meetings?

We see AEE’s strong affirmation on its outlook as quite notable, seeing sizable latitude between its recently concluded MO rate case and ongoing costs to ensure continued earning close to its authorized level. Following earlier fears permeating in the marketplace we perceive shares as substantially intact with mgmt. notably confident on its outlook despite its volumetric exposure in Missouri. In fact, we continue to see latitude to execute against its plan if not *more* on the back of its forthcoming IRP this fall. We could see a net increase in capex, bolstering doubts that seem to be emerging around shares. Related we also saw SO’s confidence in ongoing pivot at Vogtle as worthwhile given pivot on employee execution. SRE appeared quite confident on its CA outlook again, but note emerging risk of capex deferrals in Mexico is likely under-appreciated among investors and could partially offset in its outlook. We maintain our Underperform on CNP as we maintain our concerns on prospects for execution at levels contemplated. We see DUK’s Sept update on its IRP as likely understated & explaining its recent pos re-rating relative alongside greater confidence in cost cuts. Rate case risks loom here otherwise.

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Thematic Prospects

1. Execution intact; bill arrears remain quite early

We note few incremental comments in recent days on load trends, with most of the focus increasingly focused on the ramp in bill arrears from customers. With April bills just becoming due now, preliminary data does not necessarily show the full ramp. While residential customers are typically eligible for non-disconnect and avoidance of late feeds, we also note discussion among many companies of the benefits provided from the CARES act in allowing funds disbursed to small businesses to qualify towards paying utility bills (in addition to employee labor expenses, etc) such that this class of customers is likely to remain more intact than otherwise expected.

2. Renewable delays, but not really an issue

We stress that few investors really appreciate the potential *benefits* of forthcoming PTC guidance latitude from IRS. We could actually see this add to the net NPV of projects (seeing currently '21 contemplated projects) partially qualify for the full 100% PTC. This would appear the most constructive to NEE of companies covered.

3. Capex upsides still quite real

We perceive investors need to appreciate that companies could very well see capex increases altogether as they move forward with a wider array of coal plant retirements on an accelerated basis including AEE, ETR, and DUK among others. We see this all likely forthcoming in 2H despite a related backdrop & fear of capex *slippage from 2020 into future years* to limit pressure on balance sheet metrics. This remains a key potential variable as companies seek to hold the line on the outlook in '20 as virus could very well imperil guidance more than otherwise perceived/reflected in sales guidance presently with greater corresponding impacts to balance sheets than appreciated as well.

Ameren (AEE)

Standing by the main points from the 1Q call: *quite confident*

Mgmt. reiterated much of what was discussed on its earnings call last week (as discussed in our last note), including its affirmation of 2020 guidance $3.40-3.60/sh under adjusted assumptions including the constructive Missouri (MO) rate case outcome, O&M savings, and a YoY sales decrease expectation of -2.5% (a -$0.10 item). There's still lack of clarity around how much of an O&M swing AEE is factoring in (recall mgmt. stated on the 1Q call original guidance had a YoY increase in expenses, changed to a YoY decrease). We hope for further clarity as peers have provided a sense of how much is factored in – important in tracking impacts if stay-at home orders last a little longer than anticipated. Either way, as we previously calculate a 1% change in O&M is equivalent to roughly $0.10/sh, we still expect AEE has room left for other O&M savings if need be to keep '20 in its guide. We maintain Buy given this, that also see growth opps, and the company's strong FFO/debt metrics that are better than those of peers.

Capex and growth rate

AEE affirmed its 6-8% EPS CAGR from '20-'24, emphasizing its $36bn 10-year capex plan (as well as its $16bn 5-year plan). Mgmt. pointed out that the plan's capex is largely focused on grid modernization as well as projects that enhance reliability, resiliency, and security. AEE doesn't have big generation growth other than the $1.2bn invested in wind, which is still expected to commission mostly this year (perhaps just $100mn rolls into 2021 due to COVID-related supply chain delays). We see further opps for gen-related growth, but it's too soon for the company to firmly fold upside into guidance; this includes the IL downstate legislation & associated renewable and electrification of transportation proposals, as well as potential generation trajectories proposed this fall through Missouri's integrated resource plan (IRP).

Missouri rate case settlement: When's the next one?

Mgmt. reiterated its constructive rate review outcome including having the commission affirm its 95% / 5% sharing as well as a decrease in revenues by -$32mn, fuel cost expenses by -$115mn, and other costs by -$50mn. This results in a net +$133mn pre-taximpact, with rates taking effect April 1st. We calculate the annual impact of this

result is $0.40/sh annually, i.e. $0.30/sh for 2020 given it impacts nine of twelve months. Note the electric result was an ROE of 9.4-9.8% as well.

Recall prior to COVID & this rate case result, AEE had indicated it was planning to file *another* MO rate case once its wind program came online YE 2020 to reduce lag beyond what PISA (plant in-service accounting) provides in deferring 85% of depreciation. While the company had never provided an exact sense of timing, one could have assumed that AEE might have wanted to file July 2020 for a true up by year end that would have included the wind projects. However, we note that mgmt. again expressed it was happy with the construction result of this last recent settlement. Moreover, now with COVID, *AEE is still debating the timing of when to come in next to limit regulatory lag but be conscious on the backdrop.* In other words, we see AEE looking to balance the recent rate case result (which we believe would support a stay-out) with wanting to bring 2020 wind investments into rate base (which we believe would support an earlier case, but with some flexibility given PISA eliminates as much loss on depreciation of rate base) and then COVID impacts (which in itself has a push-pull: We'd see reason to push out given economic impact on customers but reason to pull forward to balance impacts of lower demand and bad debt expense). Nothing is on the table yet in terms of the next filing, but AEE mentioned the Commission Staff did open a workshop to look at tools around costs from COVID.

We discussed potential alternatives to a full rate case, noting that AEE chose PISA rather than decoupling. We still wonder whether the MO commission could be amenable to a stabilization filing, like LNT is pursuing in Wisconsin (i.e. keeping rates stable by using cost costs and other accounting mechanisms to balance the increase to rate base the wind would provide). We also could see AEE look to pursue accounting authority orders (AAOs) related to COVID-specific costs in MO.

Coal update: Still waiting on this fall

AEE did not provide a glimpse into any future potential accelerated coal retirements. It noted its unique situation since it has not made as many investments in scrubbing equipment as peers have, resulting with coal representing just 12% of rate base now, expected to drop to 8% in 2024 without facing stranded costs. Plants outside of Meramec (which is set to retire in '22) are still operating at 70% capacity factors, and the state has historically appreciated the ownership aspect of generation.

While not discussed, we still see accelerated unscrubbed coal retirements as untapped potential not only as a catalyst in which to pursue more rate based renewables (which could be discussed this fall as the IRP is due), but also as a way to pursue better ESG metrics as well (see our recent ESG flows note here, which suggested flows have continued strong this year, but utilities as a whole are underutilized even with some of the largest clean energy rate of changes proposed – we could see an opp'y here). We think that if not this fall, AEE could also be waiting for the result of the 8th Circuit environmental issue around Rush Island (with oral arguments likely later this year) and/or securitization legislation in MO to be pushed forward.

Illinois: Downstate bill isn't off the table yet

While impacted by 30-year Treasury rates, AEE's Illinois formula rates in the electric segment result in no regulatory lag. The company continued to discuss the Downstate legislation including extension of formula rates with the 100bps adder – in addition to plans for more renewables and electrifying the transportation sector – by specifically noting that the legislation is based on a strong foundation that has driven investment, jobs, and reliability in the past. We interpreted the company still sees palpable backing by environmental & labor group, in addition to geographically and politically diverse legislators. While investors appear quite worried about sustaining status quo; we note the program officially expires in coming years (and would otherwise seemingly result in a more traditional litigated rate case). While timing could yet get shifted out we perceive a clear bias towards an extension, likely in oru vie won more favorable ROE terms given the wide discrepancy from other 'normal' returns for companies. This backdrop makes us more constructive on shares despite the more acute recent arguments suggesting risks to their LT EPS CAGR carrying forward current EPS CAGR outlook.

Avangrid (AGR)

New England Clean Energy Connect (NECEC) saga continues

As we noted here, AGA recently filed a lawsuit in Maine at the Superior Court level regarding the state's referendum to derail the NECEC transmission project through this November's election. The suit is based on AGR's view that (1) the referendum exceeds the power of the law as it's not a rule for all (focused on just one project) and it's retroactive, and that (2) there is a separation of powers issue that is allowing the legislative branch to exert power over the judicial and executive branches. The outcome is needed before the item would go on the ballot this November. AGR did not address impacts to capex deployment yet, noting it continues to first focus on receiving the remaining permits as well as ensuring the referendum is challenges and voters have all the information to make an educated decision. We point out that construction is now not expected to start until the end of August; the ME DEP permitted the project recently so the only two outstanding permits are the Army Corps expected in August (which is necessary to start US construction) and then the Presidential permits 60 days later (which is necessary to cross the Border into Canada). The silver lining in the delays faced by AGR is that a concurrent non-appealable order in Massachusetts (which was appealed by NextEra) won't be ruled on until this June. As such, AGR has gained flexibility on when exactly the project contractually needs to be in service; the company is still anticipating a '22 in-service date as of now, but can bleed into '23 if difficulties cause further delay (i.e. giving AGR a risk mitigating factor of more time and latitude if it is delayed more). Bottom line: AGR pulled its long-term guidance on the 1Q call and by the time we expect an update (at the Analyst Day likely in line with Iberdrola's), AGR will have referendum clarity on whether this project will go forward.

Note also in ME, AGR recently teamed up with two wind generators (EDPR and Clearway) to propose wind farms (~325MW) for the state's request for proposal (RFP) due last week. AGR would be responsible for transmission gen-ties – and the projects represent significant distances. Stay tuned here, with the RFP announcement likely this December. *These transmission interconnects would be modest upside to the plan.*

ROEs: Company expecting largely around authorized once all said and done

AGR anticipates it will finalize its New York rate case settlement with interveners this month such that it is able to file a joint proposal with the Commission soon. As noted in our recent upgrade to Neutral from Underperform (here), AGR anticipates the final order to be approved this fall, with rates taking effect in September but being made-whole as of April 17th. We point out two key discussions in our eyes: First whether the commission will allow recovery of some bad debt expenses, and second the ability to earn at the authorized ROE. AGR noted in 2009 the commission put in place a methodology for recovery after a generic hearing. It expects something similar – we'd expect more likely a generic proceeding but if need be through the settlement. Note CT and ME already opened dockets recovered to bad debt, and AGR seemed confident some sort of recovery would be possible in NY due to past precedent.

As for earning as close to the allowed as possible, the outcome on minor storm recovery particularly with staging costs is key. NY had limitations on how many staging costs it could recovery, and would allow just 3 events at NYSEG and 2 at RGE. AGR is seeking more events and more dollars to recover. It also is looking to deploy incremental dollars for maintenance, equipment failures, and enhancing the system (due to age or quality). In other words, AGR is looking for capital, O&M, head count, and storm recovery – mostly at NYSEG. Once rates are in place, mgmt. expects to earn around the allowed ROE. This would indicate the first year of limited lag for NY Is 2021.

As for ME, the company expects to earn around the allowed ROE as well – although likely closer to having 2020 as the first full normal year. Note the company is facing 1x items in 2020 that will prohibit earning at the authorized return, and until September 2021 at

the earliest the company faces a -100bps penalty on its authorized ROE. This penalty will be lifted if AGR proves its customer standards metrics.

Question of capex and resolution on bad debt unlikely in JP

We perceive a generally cautious attitude on storm related capex & opex coming out of the NY rate case resolution. While already an ambitious plan articulated in its capex projection, we perceive a potential for modestly reducing expectations. Meanwhile resolution in the joint proposal of bad debt recovery appears increasingly unlikely in our view and would likely be joined together with other utilities including ConEd. We stress recovery appears to be dimming in a separate Covid docket in sharp contrast to many other regions nationally.

Offshore wind update: Waiting on BOEM with study all focused on distance

AGR indicated that the Bureau of Ocean Energy Management (BOEM) communicated last that it is still on target to issue its cumulative impact study this June 12th. The company expects it will be an all-encompassing finding on project density – i.e. how far apart turbines must be in the New England area. Note that the industry up to this point has largely agreed upon a one-nautical mile spacing in all directions (N/S/E/W) and that the Coast Guard has indicated it is in line with this spacing; most fishermen negotiations were reflecting of this as well. We point out that AGR is still waiting to comment officially on how Vineyard Wind will be included its updated EPS CAGR (i.e. to commission in 2023 or 2024?). Due to the delay from the original online-date of '21-'22, AGR has a silver lining of being able to explore larger turbines with more capacity, improving its density of its total offshore wind lease area (having originally looked to 9.5MW turbines, but now looking at turbines 12MW+).

On track '20 and succession

Finally, the company indicated its '20 projects are on track and that it is not seeing a COVID-related slow-down. We expect AGR is one of the more shielded companies from lower demand and other impacts due to its decoupling at Networks. We stay tuned for succession plans, likely to be announced by Jim Torgerson's departure at the end of June.

Centerpoint Energy (CNP)

While CNP remains a highly debated name, we remain cautious on the overall outlook and see downside to shares given both ambitious 5-7% growth targets that are difficult to achieve as best we can tell (w/ inclusion of mandatory converted shares offset by interest expense savings) with upside case principally centered around the strategic review process, which has yet to be clearly articulated. With Change of Control at a sector-record at ~$10Mn for the chair, we believe the question remains whether this could potentially evolve further with additional incentives, a dynamic we've seen elsewhere among companies evaluating strategic actions, although still no timeline on this process. Meanwhile, there are some signs of progress on the new CEO search although still no definitive timeline. At the end of the day, we continue to see a challenged outlook and maintain our Underperform rating.

Succession planning: Still no definitive timeline although making progress

During our call, mgmt. highlighted that several candidates have been identified for a new CEO appointment, and is in the process of narrowing down the list and working to prepare arrangements. That said, mgmt. was unable to put a more specific timeline on the process. Given wider governance concerns around the structure & compensation of the board, we see this as critical to re-establishing confidence in the strategic direction of the company. While an astute CEO appointment would be the most obvious upside angle, especially if it were to come from in-state peer, we could see the process be more drawn out.

What about the strategic preview process? CoC critical to watch

While mgmt. talked down the M&A angle on its earnings call, commentary from our AGA meeting suggested that the advisory board committee would look to optimize the business by assessing all assets and the business as a whole with still plans to announce something by the Analyst Day in early 2021. Given we perceive limited independence of recently appointed board member Lesar and current Chair Milton given historic relationship, we continue to see changes around Change of Control (CoC) incentives as critical to watch. Yet there was no more specificity as to when these payments will be subject to annual review or around additional details for the process itself beyond the fact that the interim CEO/CFO will be involved in the process. With CoC at a sector-record at ~$10Mn for the chair, we believe the question remains whether this could potentially evolve further with additional incentives, a dynamic we've seen elsewhere among companies evaluating strategic actions. We note the chair has three years left prior to mandatory retirement age; we also still note the decision by CNP in past efforts around strategic actions *not* to pursue a sale. Bottom line, we remain less convinced about the motivations on this front, although recognize this is a key upside angle.

What about the dynamics in IN?

With ~$300mn/yr of IN electric capex that will need to be backfilled and largely dependent upon the Integrated Resource Plan (IRP) filing, mgmt. highlighted that it remains on track for its June filing with expectations to bring a more balanced portfolio mix of new generation to the table. While details of the plan have not been disclosed, mgmt. highlighted a much more engaged stakeholder process taking in factors from both the coal industry and the renewable energy in order to balance low cost needs with stakeholder objectives. Meanwhile, despite 80% of capex trued up on an annual basis, we remain concerned around COVID pressures and ability to earn authorized returns; see recent read-throughs from in-state peers AES and NI on load trends as also cautious given Commercial & Industrial (C&I) load declines in the mid-teens, and it remains unclear if resi trends of +10-11% can be sustainable.

Consolidated Edison (ED)

We maintain our Buy rating on ED as we continue to see the shares as largely de-risked following implementation of new rates at its CECONY (Con Ed co. of New York) subsidiary and given its decoupled electric and gas business. Nonetheless mgmt. continued to strike a sober tone on assumptions for recovery of Covid-related items including higher bad debt expense and direct expenses. Mgmt. acknowledged that the timing of a potential commission docket for Covid recovery would likely come after the state has better visibility into the length and depth of the economic downturn, particularly as it relates to unemployment. On the financing front the company reports ample liquidity following the establishment of a new $750m credit facility. No change in plans to issue $600m of equity in 2021 as the company continues to see annual equity needs, thus any delay would cause requirements to increase in future years.

'20 guidance cut driven by Covid which is seen as a current-year drag

Mgmt. sees the impact of Covid on financial results as seen in lower revenue from disconnect fees, late payment fees, no access charges, and related O&M items to largely be limited to 2020. Incentive programs built into rates are reset on an annual basis, with the expectation that the Covid impact from these will also be limited to 2020. Looking beyond 2020 the company sees its multi-year earnings CAGR guidance as intact given expected recovery in subsequent years as fee collections normalize. The reduced 2020 guidance range of $4.15-4.35 was driven in part by the negative contribution from weather in the CECONY Steam business (ED's largest non-decoupled segment). Mgmt. estimates that thee Q1 drag on Steam was approximately 80-20 due to weather and reduced consumption stemming from Covid stay at home orders in the end of March. Mgmt. did not give a forecast for the segment for the remainder for the year though noted that Steam is economically sensitive – it is unclear to what extent demand will continue to be reduced by remote working employees given that large office buildings in the city may continue to take steam even at reduced occupancy rates.

Bad debt expense largely depends on depth and duration of downturn

ED sees its bad debt expense as largely dependent on the path of economic recovery in the NY City area, in particular the length of time that unemployment rates stay elevated and to what level unemployment rises. Mgmt. provided color into the determination of bad debt expense in a rate proceeding – the beginning point is the actual bad debt expense in a historical test year with a normalization process that takes place to account for one-time or unusual events during the test year, making the final outcome difficult to forecast. At present mgmt. is using 2008-09 as a template in the absence of more detailed data – in both instances collections for delinquent accounts were suspended, though the reduction in demand has been faster in 2020 as compared to the prior recession. Mgmt. sees a potential for a generic cost recovery docket to be opened by the NY commission, though does not expect clarity in the near term as the commission remains focused on delivery of service to customers.

Equity needs remain $600m in '20, liquidity seen as adequate

ED established a line of credit in April that will allow it to draw down up to $750m to fund operations and capex in the near term. The company sees its current year equity needs as unchanged at $600m though acknowledged the possibility of drawing down the credit line *prior* to an equity issuance (by mid year) if market conditions precluded an issuance by that time frame. Looking further out mgmt. sees annual equity needs "as far as the eye can see" making pushing out the current equity needs difficult as they would accumulate in the following year. Mgmt. stressed market conditions and ensuring the best possible price as the key factor in its timing decision. *Bottom line, could see this come by mid-year depending on market conditions. With this company among the single remaining marketed issues for the year to be issued we perceive disproportionate 'overhang' and hence concerns on shares reflected today.*

Duke Energy (DUK)

Despite Duke's recently announced sizeable cost cutting plan to offset expected load declines this year, we maintain our Neutral rating on shares given lingering risks in the Carolinas with 3 untested NCUC commissioners and potential for delay at ACP with NWP12 timing. With the near-term uncertainty in the Carolina rate cases given litigated ROEs, coal ash pressures and implementation timing, Duke's execution of its cost cut initiatives will be critical for the company to maintain its +4-6% EPS growth target (reaffirmed on 1Q call). On the other hand, we see potential progress with the Clean Energy report from the NC where we see pathway for alternative rate making mechanism (MYRPs, ROE banding, securitization, riders, etc.), although specifics around a particular outcome remains premature: we see our AGA meeting as a net positive driven by growing confidence around future Carolinas spend (watch large re-write on capex outlook with the IRP) as well as focus into '21 on cost cutting. Specifically its forthcoming IRP should both add to cash flow potentially with accelerated depreciation of plants – improving balance sheet while laos providing a further uptick in capex this ~September.

Regarding ACP, we continue to perceive challenges in having all permits approved by the tree-felling window in November; in addition to potential risk that the 9th does not approve the motion to stay for the recently narrowed NWP12 order (likely hear on the stay next week). Long term, we see the upcoming NC IRP in September including a meaningful amount of incremental opportunity by way of clean energy for Duke, but risk remains around the natural gas build out due to uncertainty at ACP.

ACP needs 4 items resolved this yr to remain on schedule; NWP12 in focus

With 47% interest in the $8bn Atlantic Coast Pipeline (ACP), the project continues to be an overhang on DUK shares as there are several items that need to be resolved this year to keep the expected in service timeline of early 2022 intact. Moreover, the recent Nationwide Permit 12 (NWP12) vacature order out of the US District Court of Montana, which was narrowed last week to only new oil and gas pipelines, has become an incremental obstacle for ACP and all other new pipelines across the nation. On Friday (5/15), after declining to grant an immediate stay of the MT Court's narrowed order, the 9th Circuit US Court of Appeals established an expedited briefing schedule concluding on May 22 (this Friday) to address the defendants' motions for a stay implying the 9th's critical decision on the motions to stay for NWP12 will likely come next week (May 25-29). Duke hopes this motion to stay is granted next week allowing the project schedule to remain in line with expectations. This assumes the other three items are resolved this year, which include: 1) biological opinion from the US Fish and Wildlife Service (expected by end of 2Q20) – a pre-requisite for water crossings authorized by the NWP12, 2) a favorable SCOTUS ruling on Appalachian trail crossing (expected in next few weeks), and 3) an air permit for the Buckingham, VA Compressor station (expected by YE20). FERC likely needs all these major permits in place to approve recommencing construction and tree felling. Bottom line, we continue to see risk of a delay at ACP with a potential motion to stay for the narrowed vacature of NWP12 presenting incremental delay risk.

Upcoming IRP to be broader than DUK's typical IRPs historically

Duke's upcoming North Carolina Integrated Resource Plan (IRP) that will be filed in September is expected to be broader than the company's usual IRP as it will contain more carbon reduction initiatives, renewables, third party providers, and distributed generation. The carbon reduction initiatives will include more thoughts on the early retirement of coal plants. We expect the commission will look to find a balance between the lowest cost plan and aligning de-carbonization efforts, which Duke likely incorporates into its IRP. The company is trying to reflect a composition of assets that is less base load, but rather more on the grid and smaller generation assets. Further we perceive the NC IRP filing could create additional opportunities for DUK in terms of clean energy and coal reduction opportunities, although see risks to natural gas build considerations given still uncertainty around ACP.

Securitization as a potential tool for coal retirement in the Carolinas

For the early retirement of coal plants, we believe Duke could potentially securitize these early retirement costs such that they are not penalizing the rate payer, creating headroom. Duke has used securitization for storms in the past, and we perceive this as an attractive tool for Duke to potentially apply to coal retirements if the corresponding amendment is made to the legislation (assuming put forth in the Clean Energy study by year-end). We will continue to watch for this as another potential lever for Duke.

Multi-year rate plan legislation

Duke continues to push the Public Utilities Commission (PUC) for alternative rate mechanisms to move forward, specifically, a multi-year rate plan (MYRP). With the upcoming report due from the Governor's committee on Clean Energy, there remains potential for Duke to have a recommendation back to the legislation that would include a MYRP, ROE banding, securitization, and/or rider capability. There are a wide range of tools available, but it will take time to educate the necessary parties. All of these tools would be positive for Duke, but there are a number of steps it will take to get there as past efforts stalled/failed. With that said, we see both increased confidence from the company and corresponding stakeholder commentary as supportive for DUK's legislative prospects in the 2021 long session.

Offsetting COVID-driven load declines with cost cuts; some sustainable cuts

On the 1Q update, Duke announced targeted cost cut reductions of $350-450mn to offset annualized load decline expectations of 3-5% this year. A portion of these cost savings are savings that Duke will benefit from beyond 2020 (i.e. structural) and some are not. Recall, Duke noted hiring freezes into '21 and corporate IT reductions as a tailwind for O&M agility. The new processes Duke is putting in place will drive efficiencies and yield cost savings through the incorporation of more digital, analytics and robotics throughout the organization. These new processes likely require less people going forward, which will sustainably lower the company's overall cost structure. Duke has dedicated resources working on these efficiency gains, and we expect to get more transparency on the major cost savings buckets later this year.

Essential Utilities (WTRG)

NT COVID Implications De-Risked, with LT Recovery Prospects Emerging

With their 1Q report earlier this month, WTRG reaffirmed 2020 guidance of $1.53-$1.58 and a 5-7% EPS CAGR through '22. We stress the largely residential profile of the water biz as providing some protection against load degradation while the gas biz enters shoulder season against the pandemic backdrop for now, as we monitor duration on a go-forward basis and any second waves or further escalation. While early action was taken to maintain a more conservative amount of liquidity, bad debt has been our primary concern. That said, discussions with mgmt. stressed last week's order in PA as helping to de-risk this given their particularly large presence in the state: recall, last Wednesday, the PA PUC issued a letter directing utilities to track COVID expenses and authorized regulatory assets for incremental uncollectible expenses incurred above those embedded in rates since the PUC's March 13, 2020 Emergency Order -any regulatory asset created under the authorization contained in the Secretary's Letter will be subject to review by the PUC in future proceedings. While this won't provide immediate help to cash flow, it should help limit degradation to P&L in the nearer term.

Meanwhile, we perceive the latest economic pressures broadly as likely to further accelerate consolidation in the industry as muni budgets are further flex'd from the crisis - and stress any further resulting acquisitions would be upside to mgmt's latest reaffirmed targets. States we are watching in the near term include TX & OH following the passage of FMV legislation in the states early last year and VA passing the legislation more recently. While we perceive TX bids as likely more competitive, WTRG is currently the only large water utility in the state of OH - and we see particular opportunities as likely to emerge following the Campbell acquisition. Meanwhile, we see NC as another state to watch given the new commission dynamic, albeit muni acquisitions there seem less clear cut relative to the more challenged munis in PA and IN.

Overall, mgmt. stressed confidence in our latest discussions around both volume and magnitude of muni acquisitions, and we perceive particularly bullish prospects for further consolidation for the water industry going forward.

Latest discussions also pointed to their intact balance sheet (following the Peoples acquisition despite some add'l debt to improve liquidity) with equity only needed to finance acquisitions. While continuing to allude to $300Mn in equity for DELCORA (& some latitude for further add'l acquisitions), we see timing as either 4Q or 1Q given a likely somewhat protracted process from the COVID backdrop and the current market environment.

Watch Repairs Tax Developments for the Catch Up Component

After closing on the Peoples Gas acquisition in Mid-March, the company elected the current component of repairs tax, reducing income tax by $5.9Bn for the quarter with expectations to drive $0.08-$0.12 worth of contribution for the year. Latest discussions suggested a filing for the catch up component in June or July with the process taking six to nine months. *We see this as the critical debate driving shares.*

Under implementation for the water biz, seven years of a ten year amortization went to the shareholder while three went to the ratepayer under what we stress as a particularly constructive outcome. While it remains to be seen how the commission will rule this time around, a constructive outcome remains clear cut upside to their numbers.

We remain Neutral rated on shares of WTRG, seeing risk/reward as balanced.

MDU Resources (Not Rated)

Catching Up Post Cut on COVID & More

MDU Resources (MDU) is a $4.4Bn market cap company based out of Bismark, ND that operates in 44 states. The company is a mix of regulated electric, natural gas, pipelines, and an unregulated construction materials and services business. MDU recently narrowed its 2020 EPS guidance from $1.65 - $1.85 to $1.50 - $1.70 with a 5-8% long-term CAGR while also lowering its revenue guidance for the construction business by $100M (while pulling margin guidance) following weak 1Q weather and as they continue to navigate the COVID crisis. Despite the lower guide, the company has a record backlog of $1.3Bn for construction services and a backlog of over $900Mn in construction materials.

Despite the more uncertain backdrop, management remains committed to M&A primarily through bolt on acquisitions, noting potential for more distressed opportunities in particular going forward and financing will likely be determined on a case by case basis. Shy of acquisitions, the company doesn't anticipate any near term equity needs and FFO/Debt metrics remain north of S&P's upwardly revised target of 22% (from 15% previously). Bottom line, while organic growth remains the primary driver of mgmt's capital allocation on a go forward basis, mgmt. has clearly identified a desire and opportunities for further acquisitions.

Northwestern Energy (NWE)

Contemplating Prospects & Evolving COVID Crisis

With their latest AGA update, NWE reaffirmed their recently revised 2020 guidance of $3.30-$3.45, but didn't provide any additional color around the latest weeks of load data. As previously noted, guidance assumes flat gross margin growth through the remainder of the year at the midpoint and we continue to watch any decoupling developments after the MT commission recently denied the intervener motion for reconsideration (around the potential ROE reduction for NWE if decoupling is implemented). While decoupling for NWE was initially contemplated for July, the MT commission plans on opening another docket to explore impacts of implementation during the pandemic and latest discussions suggested postponement would be beneficial given 90% relates to resi load (which has seen an uptick as expected given latest lockdowns across the nation). As such, we perceive NWE as likely to advocate for postponing any action around the mechanism into 2021 *(a presumably more normalized baseline)* despite a clear cut desire to implement in LT (not just in a five year pilot). Nuances & timeline to implementation remain critical both in the near term and longer term in MT.

We stress another nuance to watch is bad debt in particular given management's assumption of recovery in the latest guidance - albeit we continue to perceive a constructive backdrop in both SD and MT. The company has filed a joint expense recovery filing in SD with plans to file soon in MT.

Rate Cases & LT Gen: Awaiting MT RFP Bids

While the company doesn't plan to file any rate cases this year, discussions suggested they will continue to evaluate every April - and we don't perceive any firm decisions as having been made regarding a potential filing for next year. That said, given the capital spent and investment underway in SD with the latest generation win (and known and measurable gen spend into '21), we see a SD filing as more likely than not - and ultimately view a constructive backdrop for the state. We would expect MT filings to be more challenging on the margin given the aggressive cost cuts underway in '20 - as well as the likely ROE environment (with outstanding FERC uncertainty even as potentially weighing on state returns). All that said, we perceive bias towards a MT generation filing as opposed to a full rate case if the company is able to be successful with any generation bids in the state. Following an extension of the timeline, initial RFP bids are now due in July and we perceive confidence around maintaining the schedule and turning things around in a reasonable amount of time. Preapproval of a project could help mitigate impact in pushing out a rate case to '22.

Meanwhile, the company continues to work through potential approval to acquire additional Colstrip that would reduce their generation needs in MT and are hopeful to have clarity by the end of the year if ultimately approved. The company earlier notified the MT PSC that Talen Energy has purported to exercise its right under the Colstrip Ownership and Operation agreement to acquire a portion of the transaction that was negotiated between Puget Sound Energy and NWE for the proposed sale of the 185MW of Colstrip Unit 4. If Talen purchases a portion of the Puget Unit 4 interest, NWE would acquire at least half of Puget Sound Energy's interest equating to 92.5MW with a purchase price of $0.50, with the PPA with Puget Sound shifting to 45MW (from 90 initially contemplated) for five years. With any approval and potential close expected to play out by the end of the year, we continue to see rejection of the add'l Colstrip as best case scenario as meaningful generation spend and rate base is critical to driving longer term EPS growth.

We maintain our Underperform rating, seeing NT risk to the revised '20 guide under a protracted crisis and a lack of LT growth without meaningful generation.

Sempra Energy (SRE)

We maintain our Neutral rating as we continue to see shares as fairly valued given average implied upside as well as the uncertainty in LNG development given the market backdrop and limited recent developments after 1Q call as we await ECA FID (and financing disclosures). However, we stress SRE is one of few peers to have reaffirmed '20 guide at the top-end and provided visibility into '21 in the wake of COVID with potential upside at the CA utilities with clear bias to earn at more robust historical earned ROE levels. Confidence in TX also remains notable as incremental capex depends on interconnect approvals rather than the base plan despite the oil patch woes.

While IEnova concentration continues, mgmt. stresses that majority of $1bn growth capital can be deferred while confidence in counterparty contracts given continued payment and fixed/pass-through rates. Deferal of segment capex remains a unique risk. Further, we continue to see an equity issuance as unlikely as management prioritizes shareholders over a potential credit downgrade at Moody's (currently on downgrade review). Note SRE targets 16% FFO/debt in 2020 vs the 17% Moody's downgrade threshold; see Fitch/S&Ps outlook as critical given likely foregone conclusion at Moody's. Bottom line, while we see potential upside to the utility outlook, LNG uncertainty continues to linger with both the credit outlook (sending mixed messages to LNG counterparties?) and lack of tangible data points beyond ECA phase 1.

On balance we see upside to our ests consistent with management commentary on its 1Q call. That said, we suspect investors in SRE largely under-appreciate the consternation at IENova emerging in recent months.

California returning to a premium regulatory environment?

With recent constructive rate cases, we perceive confidence in mgmt.'s ability to earn closer to its historical earned ROEs. SRE has a history of earning strong ROEs relative to its authorized rates – see our report: Sempra Energy: Focus on the Utility: Raising expectations on (adamant) continued mgmt. confidence 06 February 2020. We continue to believe our estimates could very well see an improving trend through the forecast period. Sempra continues to allocate a significant amount of capital towards safety and reliability (80%+ of 5-yr capex relates to safety and reliability), and the company got nearly everything it asked for in the last general rate case under RAMP (risk mitigation phase). Bottom line, we perceive SRE's CA jurisdiction to be the most well positioned given the healthy ROE outlook and upside to spending initiatives to further align with state policy (wildfire mitigation/de-carbonization).

Balance Sheet: equity continues to seem unlikely with Moody's action likely

We continue to see FFO/Debt achieving the 16% threshold by YE2020, which compares to Moody's 17% threshold to maintain its BBB+ rating. With the addition of ECA LNG and management's commitment to its shareholders (i.e. no equity), we believe it will be difficult for SRE to maintain its BBB+ rating at Moody's. However, we expect the other agencies to grant more latitude to SRE with the Port Arthur FID pushed to 2021 as of the 1Q call, which gives the company more time to improve its metrics. We continue to see FFO/debt at 17% in 2022. Given ECA phase 1 could still move forward with the current threshold and Port Arthur would be project financed for 2-3yrs (with equity likely needed in year 3) we see no equity needs through the forecast period. Hence, we see a downgrade at Moody's as likely inevitable given commitment to no equity and company target of 16% FFO/Debt in 2020, but not at the other agencies that will likely allow SRE more leeway.

Texas: mgmt. still feels good about current capex plan

Management was clear it remains confident regarding the current capex plan at Oncor in the face of COVID and blatant exposure to the apex of the oil downturn in West Texas. The company does not expect an update to the Oncor capex program until its annual meeting in October, where the company will refresh the 5-year capital program as it

typically does each year. While management is cognizant of the steep decline in activity in the oil patch, it noted three areas offset to this, which include 1) Dallas Ft. Worth being one of the fast growing metropolitan areas in the country with 18k hookups in 1Q alone, 2) >100 GW of renewable generation in the queue in Texas, and 3) marginal producers in the Permian demand for converting diesel generation (30c/KW) to lower cost natural gas. On top of those three areas, management sees up to $750mn of ongoing capex deployment and has 13 renewable interconnects in the queue that are not in the base plan (i.e. incremental). *Despite clear risk of renewable project delays, management appears to feel confident a future roll forward could be at least as constructive as its latest update from late 2019. This was surprising in our view.*

IEnova: deferring of growth capital but not a material concern

At IEnova, mgmt. highlighted that its counterparty contracts continue to pay with over 50% backed by government entities (PEMEX, etc) with fixed rates/past through transmission costs. Despite confidence in navigating the regulatory climate, consternation persists following recent dynamics with the President and avoidance of subsidizing private industry. That said, mgmt. acknowledged that growth capital of $1bn+ associated with fuel terminals are likely to be deferred as the company looks to align with counterparty timing (BP, Valero, etc.). While majority of contracted EBITDA comes from ECA imports and pipelines with total income from the Mexican unit roughly 10-15% of SRE consolidated, we continue to monitor developments with the government bodies as it pertains to both ECA phase 1 approval and ability to execute on growth capex. See our colleagues note on IEnova for more.

Reiterate LNG update from 1Q call

Management had no change in messaging on the LNG front during its AGA update noting confidence in the future of the LNG business. The company emphasized its discipline where it looks for LNG returns well in excess of those at the utilities to justify the investments. SRE expects a Final Investment Decision (FID) on ECA LNG phase 1 this quarter (2Q20) subject to receiving an export permit. Once the project is sanctioned, the company plans to announce the financing terms. SRE noted it is reasonable to expect some of IEnova construction capital will be deferred from 2020 to 2021due to COVID-related pressures. We perceive the delay on logistics/terminals given lower liquids makes room in capex budget for ECA related spend. We expect SRE likely sells down some of its ownership stake to counter parties, adding some latitude to the balance sheet. Recall, as of the 1Q call, SRE secured the sale of two 20-year Supply Purchase Agreements (SPA) with Total and Mitsui for a total of 2.5Mtpa from ECA LNG phase 1. Further, the Port Arthur FID is still expected in 2021 (previously expected in 3Q20 ahead of COVID). On Cameron LNG Phase 2, MOU negotiations will likely take some time to turn into Sale and Purchase Agreements (SPAs) given the uncertain market environment. Net net, we continue to be cautious on LNG growth given the current market backdrop, but see this reiterated update as a moderate positive under the current circumstances of the market.

Incremental capex upside via RNG, hydrogen, DG, and mobile home parks

Despite an already robust 5-yr capex plan ($32bn 2020-2024), Sempra identified that the company has incremental upside to capex via 1) Renewable Natural Gas (RNG), 2) hydrogen, 3) distributed generation (DG), and 4) mobile home park upgrade programs. Recall, SoCalGas committed to replacing 20% of its traditional natural gas supply with RNG by 2030. We would note Sempra continues to be very focused on distributed generation, particularly in fuel cells, which could help supplement public safety power shutoffs (PSPS) especially for more isolated communities. These initiatives all provide upside to capex at the utilities over the next five years that is not baked into guidance. While we do not currently model these several items into our capex, it could drive eventual bias to positive estimate revisions.

Southern Company (SO)

We sensed an overall confident tone from mgmt. during our meetings on ability to sustain both cost cuts into the future (potentially 2/3 of upper end of $400mn range) and execution on Voglte w/ improvements in absenteeism and focus on upcoming Cold Hydro testing in the June/July timeframe. Meanwhile, mgmt. remains confident in the ability to overcome increased arrears/bad debt expense both from an EPS and cash flow impact. Aside from ability to defer costs in GA/MS (and annual filings in AL and gas LDCs insulated), the utilization of CARES Act loans for commercial and low income customers (loans forgiven as long as utility bills are paid) should help to alleviate cash flow impact. While we still see workforce reduction transition as important to monitor as well as remaining cost contingency relative to percentage to complete (w/ utilization of contingency a good barometer to monitor in terms of execution on costs), focus on upcoming testing data points remain critical to the SO story as start of Unit 3's Cold Hydro testing and execution will indicate if SO can turn the switch on. Net-net maintain Neutral rating given critical execution ahead.

Vogtle execution: watching productivity as Cold Hydro the next key inflection

Following reaffirmation of the aggressive schedule for Unit 3 (May '21) and regulatory in-service date and costs for both units (albeit pushed the aggressive schedule for Unit 4 back to its original May '22 date), commentary during our AGA call suggested no material updates although it has seen a noticeable improvement in absenteeism after reduction in workforce (to 7k from 9k). While we still see workforce reduction transition as important and remaining cost contingency relative to percentage to complete (w/ utilization of contingency a good barometer in terms of execution on costs) as critical to monitor, execution on upcoming testing items remain the most critical inflection point to the story. To that end, we look to Unit 3 start of conducting Cold Hydro testing in the June to July 2020 timeframe, although mgmt. continues to highlight that it has headroom in its plan so that Cold Hydro doesn't need to be done until Sept. to meet the Nov. 21 deadline. *Bottom line, execution at Vogtle for the remainder of 2020 will be critical to the SO story, and we will be keen to hear an update on the next data point in June/July with regard to the start of Unit 3's Cold Hydro testing.*

Examining cost savings and sustainability through outlook

With expectations for load to be down 2-5% for FY20 ($250-400mn impact in base revenues), mgmt. has been broadly confident that focus on O&M reductions would offset the substantial majority of load declines. During our discussions, mgmt. further opined on the ability to sustain these cost reductions more indefinitely, suggesting that nearly 2/3rs of its targeted range could be sustained (hiring freeze and new work from home capabilities) while 1/3rd are likely to be a headwind in future periods as there can only be a delay in items such as vegetation mgmt. for a period of time. While we perceive ability to maintain '20 guide (at least conceptually) as a positive given pervasive concerns of EPS guidance reductions across the space through focus on cost reductions, the broader commitment to '20 rather than explicit reaffirm is similar to that of CMS and is a tad cautious. That said, mgmt. highlighted a review of headcount reductions at the end of the year if the duration of COVID latest longer than expected as the most obvious upside angle to increased cost savings; albeit we perceive this as potentially the least palatable with regulators given the importance of maintaining jobs.

Watching bad debt expense w/ COVID; CARES Act all the more relevant

SO's gas utilities already have riders and trackers in place that help recover most of their bad debt expenses, but its electric utilities do not. This leaves the electric utilities more exposed to bad debt expense due to COVID. However, similar to a number of other states, both the Georgia and Mississippi commissions have announced orders to implement regulatory assets that will allow recovery for COVID-related cost. In Alabama, there is already a bad debt recovery mechanism within the Rate Stabilization and Equalization (RSE) mechanism. Mgmt. has highlighted that it has yet to see a material increase in arrears payments, although has ample liquidity ($7bn) to withstand a 40% of

customers in arrears ($1bn impact per quarter vs 15% modeled expectations). Aside from ability to defer costs in GA/MS, the utilization of CARES Act loans for commercial and low income customers (loans forgiven as long as utility bills are paid) should help to alleviate cash flow impacts. While we believe SO will ultimately be able to recover most of its bad debt expenses associated with COVID, the timing of this recovery presents uncertainty and further negative revision risk to near-term estimates.

Southern Power: No major impacts from COVID given profile

The vast majority of growth is expected to come from the current wind assets in its portfolio and Hypothetical Liquidation at Book Value (HBVL) accounting as the company did tax equity financing on those assets to further enable growth at the 5% clip. Mgmt. highlighted that even if it stopped investing today it could maintain the 5% growth through the plan period, although remains optimistic around potential upside with $500mn/yr in investments in the outer years of the plan; mgmt. highlighted it has seen some battery opportunities in CA this year. Further, with contracts for gas plants (CTs and CCTGs) based on capacity payments and renewables on take or pay contracts; it does not expect to see any degradation in the revenue stream due to COVID.

Elsewhere, mgmt. remains committed to its Gas LDC business, although continues to see challenges with midstream given the difficulty in rectifying permits (pervasive throughout the space).

WEC Energy Group (WEC)

Our discussions with mgmt. largely focused on the outlook for 2020 in the wake of Covid, with management continuing to emphasize early stages in terms of visibility on demand for the remainder of the year while stressing confidence in its ability to manage O&M expense; long-term mgmt. stresses that the pipeline of large industrials coming to Wisconsin remains intact with a recent addition of a large ship builder to the other high-profile projects previously announced.. Renewable updates were limited other than the previously communicated update on Badger Hollow 1 which has been pushed back by several months in an effort to manage the onsite workforce. Company mgmt. acknowledged being linked to Bloomberg News reports on a possible M&A transaction but declined to comment on the story. Mgmt had earlier talked down M&A on its call seeing few opportunities to find accretive prospects that would meet its 5-7% EPS growth. We continue to maintain our Underperform rating.

Early days in state reopening, but cost cutting remains key lever

WEC mgmt. reiterated its confidence in being able to manage O&M such that higher expenses and lost sales linked with the shut down orders during the Covid pandemic are expected to be offset. Among tailwinds cited was a lower level of maintenance required by leaks in the gas distribution system given the warmer than average winter. We continue to see cost cuts over and above mgmt.'s initial guidance range of 2-3% of day to day O&M as key to achieving the 2002 EPS guidance range of $3.771-3.75. Mgmt. noted that the reopening of business in the state of Wisconsin has been moved ahead of schedule previously laid out by the governor which initially lifted the stay at home order in late May with a phased reopening of some businesses including bars and restaurants in the middle part of the month. Recall that the company provided an updated forecast for electric sales with its Q1 reporting – now assuming small C&I sales declining by 4.6% and large C&I sales declining by 10.5% - mgmt. did not indicate that the forecast has shifted following the early suspension of stay at home orders following a state court ruling in early May.

Generation updates: modest delays in renewables, additional detail on Riverside

Badger Hollow 1 remains the one renewable project with notable delays – following a recent decision to push back construction the project is now expected to be in service in Apr/May 2021 after initially targeting an in service date of year-end 2020. Mgmt. cited the need to maintain social distancing guidelines, making it difficult to mobilize a workforce of ~100+ workers in an area of the state resources for bringing in a large work crew are limited. On the non-renewables front the company is pushing forward with its LNG project which was submitted to the commission earlier in the year and is expected to come for approval later in 2020. Mgmt. provided some additional color on the option to purchase a stake from the newly operational Riverside plant – the option gives WEC the opportunity to purchase a stake in the unit over a four year period; additionally WEC and LNT have the option to co-invest in new utility-scale projects being developed by either party – mgmt. flags the second option as advantageous given the availability of locations available for siting new renewables. Overall, the company expects to maintain adequate reserve margins for the foreseeable future given its ongoing renewables buildout and the retirement of 1800 MW of coal generation assets over the past several years.

Large industrials keep plans intact, ship builder plans to build

Importantly, the *long-term industrial sales forecast is intac*t with mgmt. still expecting large-scale industrial projects from Foxconn, Amazon, Milwaukee Tools, and others to come online as currently forecast with no expectation of altered plans in the state. As a positive data point mgmt. flagged Marinette Marine as a new large-scale project coming online in the Green Bay area as an addition to the industrial pipeline. Bottom line: mgmt. indicated that given the current line of sight the capital plan remains intact as growth in the state continues to be supported by large-scale industrial projects, with an expected updated capex plan coming in the fall in line with the company's normal update schedule.

Stocks mentioned

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
AEE	AEE US	Ameren Corp	US$ 72.23	A-1-7
AGR	AGR US	Avangrid	US$ 41	A-2-7
CNP	CNP US	CenterPoint Energy	US$ 17.49	B-3-7
ED	ED US	Consolidated Edison	US$ 73.11	A-1-7
DUK	DUK US	Duke Energy	US$ 84.92	A-2-7
WTRG	WTRG US	Essential Utilities	US$ 41.23	B-2-7
SRE	SRE US	Sempra Energy	US$ 124	A-2-7
SO	SO US	Southern Company	US$ 54.42	A-2-7
WEC	WEC US	WEC Energy Group Inc	US$ 87.62	A-3-7

Source: BofA Global Research

Price objective basis & risk

Ameren Corporation (AEE)

Our $75 price objective is predicated on a P/E based sum of the parts, valuing each business subsidiary relative to the 2022E ratebase weighted peer multiple of 15.8x for electric. We apply a 2.0x premium to peers at AEE Missouri to account for the improving prospects of capital spend, supplemented by a regulatory jurisdiction becoming more favorable - but lack of decoupling. We apply a 3.0x premium to peers at AEE Illinois to account for decoupling on the distribution business which aids in earnings predictability. The overall business is expected to grow at a more meaningful clip than that of peers - we see a 10% EPS CAGR at IL 2020-2024. At ATXI, we apply a 0x premium to peers to reflect the latest potential step down in FERC ROEs. At the Parent, we assume an in line multiple given the healthy debt metrics with FFO/Debt at 17%+. Electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector.

The upside (downside) risks to our price objective are the utilities earning their allowed returns or better (worse), a significant increase (decrease) in 30-year U.S. Treasury bond yields, and positive (adverse) regulatory outcomes that could impact mgmt's ability to earn its allowed return

Avangrid (AGR)

Our PO of $47 is based on an SOTP. The utilities are valued on a 2022E with a 1x disc to the electric peer P/E of 17.2x and 17.8x on the gas, given perceived risk to earned ROEs. Both electric and gas peer P/Es are grossed up to 2020 by 5-5.1% to reflect capital appreciation across the sector. We apply a 10X 2022E EBITDA multiple on the renewables sales earnings but strip out the tax credits/hedge value and apply a DCF (8%, no terminal) and an 8x EBITDA multiple for the small thermal assets (both based on comps). We back out 50% of the non-reg debt at the parent also. We include the value of the two offshore wind awards assuming $3500/kW cost, 6% disc, and 6% construction risk disc. We use an in-line discount for CMP's NECEC transmission project, but probability weight it 40% (broken out as well).

Upside risks: 1) ROE improvement in AGR's network business 2) Improvement in wind resources net capacity factor 3) higher than expected growth from offshore wind opp's.

Downside risks: 1) Iberdrola controls over 80% of AGR, limiting liquidity and exerting control over AGR's activities 2) Reg. relationships/outcomes could deteriorate 3) Existing and likely increasing exposure to the renewables biz results in a number of PPA related risks including commodity, recontracting & tax benefit recovery risk 4) Lack of adequate capital recovery mechanisms could threaten ROE's 5) The renewables biz may not expand as fast as expected or have worse returns 6) Offshore delays.

CenterPoint Energy (CNP)
We value CenterPoint Energy at $18 using a SOTP approach: electric business on an in-line utility multiple of 16.5x on 2022E P/E. We take out any earnings attributable to the transition bonds amortization, as those are temporary and instead add back the DCF value of future payments. For CNP's gas utilities we use an in-line utility gas peer multiple of 16.5x. Both electric and gas peer P/E multiples are grossed up by 5% to reflect capital appreciation across the sector. We integrate Vectren into our model and apply a 60/40% weighting to the gas/electric multiple. For VESCO we apply a 12x P/E multiple. We subtract parent interest expenses at a weighted average multiple. Further we net out the perpetual preferred, and apply a 50/50 weighting to parent debt and add back interest expense for recapitalization. We add CNP's interest in ENBL at the market value. We net out holdco interest at the weighted average P/E.

Downside risks: execution risk, decreases in capex which could support or weaken earnings ability, lower authorized returns, interest rate increases, and lower earnings from ENBL.
Upside risks: increase in capex, higher authorized returns, interest rate increase, better performance from the midstream biz.

Consolidated Edison (ED)
Our $85 PO is based on a sum-of-the-parts analysis applying premiums and discounts to the regulated group multiples (16.0x/16.5x for electric/gas respectively) with a 1.0x premium on gas and electric to reflect decoupling, and a -1.0x discount on steam to reflect volume exposure. We note that both electric and gas peer P/E multiples are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We applied inline peer regulated multiple at CECONY despite its rate certainty for conservatism as our higher capex expectations are reflected in our EPS outlook. We apply a discounted PE for infrastructure projects given the lack of clarity around the capital structure. We further apply an EV/EBITDA approach on 2022E EBITDA to the CEB business using a 10.0x multiple for both the legacy portfolio and the renewables portfolio seeing it as having higher quality returns.

Downside risks: ED, like all utility stocks, is also sensitive to changes in the market level of interest rates. Utilities historically underperform if bond yields rise, and outperform when they fall. Further downside risks are the inability to recontract storage, adverse regulatory outcomes, a deteriorating regulatory environment, or unforeseen disasters such as the Harlem gas explosion. Customer inflation is also a downside risk. PCG related counterparty exposure has abated as a source of risk but remains worth monitoring.

Duke Energy (DUK)
Our $83 PO is derived from a sum-of-the-parts valuation. We value the Electric and Gas utilities using peer 2022E P/E multiples. We apply a 1.0x multiple premium to Duke's operations in FL/IN to reflect more favorable regulatory environments. We apply an in-line multiple to the Carolinas given risk ahead. We value the other regulated electric utilities at 15.8x and the gas utilities at peer group multiples of 16.3x 2022E P/E, respectively. Both electric and gas peer P/E multiples are grossed up by 5% for the groups CAGR to reflect capital appreciation across the sector. The commercial midstream, and transmission are valued on a 2022E EV/EBITDA basis. We use a 9.0x multiple for midstream and transmission segment, although we assume a 50% weighting for ACP given risks to completion. We add the net present value of renewable segment using an 8% discount rate. We subtract out the impact of commercial debt, and add back for the renewable debt.

Upside risks: constructive rate case results, higher capital expenditure additions vs our assumptions, ACP ahead of schedule, lower interest rates. Downside risks: poor rate case results, operating errors, and negative changes in the regulatory environment, ACP delays. Macro risks: Increases in interest rates and decreases in equity market valuations.

Essential Utilities (WTRG)
Our price objective is $47 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 2.0x premium to Peoples Gas given the organic growth opportunities.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Risks to the upside include upward revisions to street estimates and further accretion from implementation of the Repairs Tax Benefit.

Sempra Energy (SRE)
Our $127 PO is based on a SOTP valuation based on 2022E net income. We apply a 1x discounted multiple to SDG&E and no premium multiple to SoCal Gas earnings (vs peer multiples of 16.3x and 17.1x, respectively). We use an in-line multiple for TX utility business given uncertain regulatory outlook despite T&D upside. For the LatAm business we value post-tax est for both sale of Peru & Chilean utilities. We value Cameron using a DCF at a 10.0% dis using a CAPM approach off its adjusted beta. We run a DCF on other LNG development and probability weight for project execution. We value the balance of the midstream segment using an EV/EBITDA approach using a 10.0x multiple as the Cameron import pipeline EBITDA doesn't step up until 2020. We further adj. for HoldCo debt & parent drag.

Downside risks: 1) negative reg risk from CA regulatory changes & int'l govts where SRE operates 2) incremental costs associated with Aliso canyon, 3) unanticipated cost overruns or delays for the Cameron LNG & other large organic growth projects 4) Capital markets or execution risk around the proposed Oncor transaction 5) rising rates, volatile natural gas prices & FX risks for SRE's int'l businesses Upside risks: 1) positive regulatory outcomes, 2) higher capex, 3) execution on Cameron ahead of our expectations, 4) lower interest rates.

Southern Company (SO)
Our $58 PO is derived from a SOTP. We use a P/E val approach on 2023 and use peer multiples of 15.7x for electric and 16.2x for gas, respectively (with dis/prem applied per asset depending on growth/risk): we then gross this multiple by +5% to account for sectorwide EPS growth to derive a 12-month forward PO. We subtract the 50% of the 2022 parent interest expense multiple by an electric P/E peer multiple to reflect parent lev supporting the utilities. We net out total parent drag and add back the remaining parent interest expense with a 50% weighting. Both electric and gas peer P/E multiples are grossed up by 5% to reflect capital appreciation across the sector.

Upside risks are: 1) Regulatory outcomes or RO's could be better vs expectations, as exposed to multiple state jurisdictions 2) Additional riders and capital trackers can help the company achieve better than expected ROE, but failure to get riders would hurt SO 3) The nat. gas related biz are relatively new and could prove more or less able to earn an ROE in line with or different from their allowed ROE, 4) high capital forecasts and subsequent earnings streams vs our assumptions
Downside risks are: 1) Regulatory outcomes or ROE's could be worse than expectations, particularly since exposed to mult. state jurisdictions, 2) SO has exposure to Vogtle which could shift earnings, 3) Weather patterns could influence usage or natural disasters could affect system reliability 4) Utilities are subject to interest rate risk.

WEC Energy Group Inc (WEC)
Our $81 PO is based on a 2022E SoTP analysis, based on the large cap electric group multiple of 16.3x and the gas regulated multiple of 16.7x. Both electric and gas peer P/E multiples are grossed up for a year to reflect capital appreciation across the sector.

We apply a 3.0x premium to WEC's WI electric & gas subs to compensate for surety in earnings growth for the next two years following the Commissions affirmation of the recent settlement on above average ROE's of 10%+. We apply a 1x premium to the gas utilities, incl IL's Peoples Gas and North Shore Gas with the Gas System Modernization Program (GSMP) and capex forecasts de-risked following the ICC order. We ascribe a 2x premium vs. the group at ATC to account for the steady nature of earnings growth as well as above average ROE's that are set at a federal level by FERC. We give Power the Future (PTF) a 2.0x premium multiple given the ROE is set indefinitely on historical and new investments. We ascribe an in line multiple for the parent accounting for the interest expense which finances overall utility operations. For the HoldCo adjustment to debt, we net out 50% of HoldCo debt from equity valuation and adjust to add back the parent drag on interest exp.

Upside risks are stronger than expected execution and accelerating capital oppt'y.

Downside risks are inability to achieve historical track record on cost cutting and ability to cont. to scale regulated investments given growing portion from contracted renewables.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

Special Disclosures

BofA Securities is currently acting as financial advisor to Iberdrola SA in connection with the proposed sale of 50% ownership of the Dry Lake II Wind Farm and 50% of the Copper Crossing Solar Project to Axium Infrastructure Inc, owned by its subsidiary Avangrid, which was announced on 17 September 2019.

BofA Securities is currently acting as Financial advisor to Sempra Energy in connection with its proposed sale of 100% stake in Chilquinta Energia S.A., and Tecnored S.A as well as its 50% interest in Electrans S.A. to State Grid International Development Limited, which was announced on October 14, 2019.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AES	AES	AES US	Julien Dumoulin-Smith
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Utilities Group (as of 31 Mar 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	72	50.35%	Buy	51	70.83%
Hold	38	26.57%	Hold	28	73.68%
Sell	33	23.08%	Sell	24	72.73%

Equity Investment Rating Distribution: Global Group (as of 31 Mar 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1602	52.15%	Buy	1005	62.73%
Hold	713	23.21%	Hold	463	64.94%
Sell	757	24.64%	Sell	382	50.46%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

***INCOME RATINGS*, indicators of potential cash dividends, are: 7 - same/higher (dividend considered to be secure), 8 - same/lower (dividend not considered to be secure) and 9 - pays no cash dividend.** *Coverage Cluster* is comprised of stocks covered by a single analyst or two or more analysts sharing a common industry, sector, region or other classification(s). A stock's coverage cluster is included in the most recent BofA Global Research report referencing the stock.

Price charts for the securities referenced in this research report are available at https://pricecharts.baml.com, or call 1-800-MERRILL to have them mailed.
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The issuer is or was, within the last 12 months, an investment banking client of BofAS and/or one or more of its affiliates: Ameren Corporation, Avangrid, CenterPoint, Consolidated Edison, Duke Energy, Essential Utilities, Sempra Energy, Southern Company, WEC Energy Group Inc.
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Aqua America

Diving In: See Opportunity in a Gas & Water Utility Hybrid

Initiating Coverage: BUY | PO: 45.00 USD | Price: 41.00 USD

Bank of America Merrill Lynch

Equity | 15 July 2019

Making a Splash: The gas uplift is real for EPS growth

We are initiating coverage on WTR, the second largest publicly traded water utility, with a Buy rating and $45 price objective. While we view the water sector overall as particularly pricey, we see a unique EPS revision potential for WTR as enabling a unique opportunity: we are above Street pro-forma for the Peoples Gas transaction (even with the full share o/s uplift), with our '20 EPS indicating upwards of $1.74 vs. Street of $1.55 (albeit unclear on what basis); we remain above Street on '21 EPS too with largely flat EPS still ($1.75 vs. Street of $1.66). While proforma EPS remains opaque prior to close, opportunities around Peoples Gas around repairs tax enable a potentially strong start to the EPS profile. While less confident on a precise figure, we perceive an upward bias relative to Street EPS expectations. While shares have already meaningfully rallied off lows, we sense a further re-rating opportunity as comfort emerges around the combined outlook. The deal comes on the heels of WTR's own step-down in EPS with normalization of earned ROEs at its principal subsidiary in PA, which has enabled outsized returns vs. authorized levels for years.

Water remains a pricey, but high quality & growth niche

We see the water sub-sector as lower risk vs. utility peers, with low overall consumer bills, opportunities for municipal consolidation across both water & waste-water systems affording a long tail of opportunities at above-sector growth. Smaller capital investments & recovery mechanisms limit material exposure to discrete project approval & afford for a more consistent return profile. Gas utilities fit many of these criteria with few large discrete projects

Valuing the Combined Company: The Right Move.

We use a SOTP analysis to value the company, applying a blended multiple (26.2x for water and 21.2x for gas). The Peoples Gas acquisition comes as water utilities are trading at what we see as an unsustainable premium to adjacent sectors. The ability to add among the highest growth utility assets at a discount to its own water multiple as particularly de-risking shares & strategically opportunistic.

Estimates (Dec)

(US$)	2017A	2018A	2019E	2020E	2021E
EPS	1.36	1.41	1.22	1.74	1.75
GAAP EPS	1.36	1.41	1.22	1.74	1.75
EPS Change (YoY)	3.0%	3.7%	-13.5%	42.6%	0.6%
Consensus EPS (Bloomberg)			1.36	1.55	1.66
DPS	0.81	0.86	0.92	0.99	1.06

Valuation (Dec)

	2017A	2018A	2019E	2020E	2021E
P/E	30.1x	29.1x	33.6x	23.6x	23.4x
GAAP P/E	30.1x	29.1x	33.6x	23.6x	23.4x
Dividend Yield	2.0%	2.1%	2.2%	2.4%	2.6%
EV / EBITDA*	1.1x	8.0x	26.2x	16.4x	15.6x
Free Cash Flow Yield*	-1.1%	-1.4%	-1.9%	-1.4%	-1.0%

* For full definitions of *iQmethod*℠ measures, see page 29.

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Stock Data

Price	41.00 USD
Price Objective	45.00 USD
Date Established	15-Jul-2019
Investment Opinion	A-1-7
52-Week Range	32.09 USD - 42.14 USD
Mrkt Val (mn) / Shares Out (mn)	8,845 USD / 215.7
Average Daily Value (mn)	37.97 USD
BofAML Ticker / Exchange	WTR / NAS
Bloomberg / Reuters	WTR US / WTR.N
ROE (2019E)	8.1%
Net Dbt to Eqty (Dec-2018A)	127.1%

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*iQ*method℠ – Bus Performance*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Return on Capital Employed	5.1%	3.9%	4.4%	5.2%	5.1%
Return on Equity	12.6%	9.7%	8.1%	8.6%	8.3%
Operating Margin	41.5%	38.7%	48.1%	70.3%	71.2%
Free Cash Flow	(97)	(127)	(170)	(120)	(87)

*iQ*method℠ – Quality of Earnings*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash Realization Ratio	1.6x	1.9x	1.7x	1.8x	1.9x
Asset Replacement Ratio	3.5x	3.4x	3.3x	2.6x	2.5x
Tax Rate	6.6%	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	108.3%	127.1%	98.1%	101.2%	103.9%
Interest Cover	3.9x	2.8x	3.4x	3.5x	3.3x

Income Statement Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Sales	805	835	902	949	966
% Change	0.6%	3.7%	8.0%	5.3%	1.7%
Gross Profit	810	838	1,044	1,596	1,657
% Change	-1.3%	3.5%	24.6%	52.9%	3.8%
EBITDA	14,226	1,941	597	954	999
% Change	-33.6%	-86.4%	-69.2%	59.7%	4.8%
Net Interest & Other Income	(88)	(99)	(132)	(196)	(211)
Net Income (Adjusted)	**240**	**192**	**272**	**413**	**416**
% Change	**2.4%**	**-19.9%**	**41.6%**	**52.1%**	**0.6%**

Free Cash Flow Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Net Income from Cont Operations (GAAP)	240	192	287	442	445
Depreciation & Amortization	137	147	191	330	356
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	14	(15)	0	0	0
Other Adjustments, Net	(9)	45	(10)	(26)	(3)
Capital Expenditure	(478)	(496)	(639)	(865)	(885)
Free Cash Flow	**-97**	**-127**	**-170**	**-120**	**-87**
% Change	**NM**	**-31.5%**	**-33.9%**	**29.7%**	**27.7%**

Balance Sheet Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash & Equivalents	4	4	3	5	5
Trade Receivables	99	101	126	193	200
Other Current Assets	28	42	46	57	58
Property, Plant & Equipment	5,400	5,930	9,103	9,638	10,168
Other Non-Current Assets	801	887	2,462	2,462	2,462
Total Assets	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**
Short-Term Debt	117	160	289	312	333
Other Current Liabilities	167	239	258	309	315
Long-Term Debt	2,008	2,398	4,330	4,664	4,980
Other Non-Current Liabilities	2,083	2,158	2,158	2,158	2,158
Total Liabilities	**4,375**	**4,955**	**7,035**	**7,442**	**7,785**
Total Equity	**1,958**	**2,009**	**4,706**	**4,913**	**5,108**
Total Equity & Liabilities	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**

* For full definitions of *iQ*method℠ measures, see page 29.

Company Sector

Water Utilities

Company Description

Aqua America is a regulated water utility providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI. In Oct 2018, The company announced acquisition of Peoples Gas, a gas utility providing distribution services to 740,000 customers in PA, WV, and KY. The acquisition is expected to be closed by mid- 2019.

Investment Rationale

We see our Buy rating as supported by meaningfully above Street EPS projections on the back of its pending Peoples Gas business and above average ratebase growth.

Stock Data

Average Daily Volume	926,118

Quarterly Earnings Estimates

	2018	2019
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NA

Bank of America Merrill Lynch

Investment Thesis

We are initiating coverage on WTR with a Buy rating and $45 price target. Our estimates are meaningfully above the street, and we see higher revisions to numbers likely providing support for shares to move yet higher even after their de-risking post equity offering, particularly as we see risk to the multiples of pure water peers with less diverse growth prospects. We see growth as largely driven from Peoples Gas moving forward, where we expect the company to capture strong earnings power from repairs tax benefits in PA. We see an 11% total return to our price objective of $45, with further potential EPS upside if particularly successful in extracting ROE benefits in its core Peoples Gas utility from repairs tax benefits.

Strong Returns with Constructive Reg Backdrop

Following the acquisition expected to close this Fall, the company will be largely located in PA (the company received regulatory approval for Peoples in KY and WV and hearings PA hearings were recently completed) - a constructive utility jurisdiction, and will have a variety of mechanisms in place across states in which it operates to help drive recovery through rates. 46% of the company's legacy business is DSIC eligible, which they can leverage to stay out of formal ratecases, with a step up to 57% of spending DSIC eligible under the combined company. We have seen WTR utilize a repairs tax benefit in their legacy business that has helped to drive earnings without rate cases, and we could see a similar development on the gas side of the business post acquisition. If implemented, this should help to drive returns meaningfully higher over the next several years before any benefit is pushed back through to customers in a ratecase. We expect this to be a big driver of near term earnings, and a large reason why our estimates are well above the street.

What Are the Right ROEs for the Water Biz?

While ROEs are somewhat nuanced across WTR's footprint given varying mechanisms and the black box nature of some ratecase ROEs such as WTR's recent PA case, we expect the company to generally earn their authorized returns across most jurisdictions. 46% of WTR's business is currently DSIC eligible, which they can leverage to stay out of ratecases longer when returns start to fall. While their latest authorized ROE in Pennsylvania - the company's largest jurisdiction - isn't known, we suspect it to be close to around 10%. However, the company should benefit more in 2019 given the forward looking nature of the test year, with returns hovering at authorized levels across their water business looking forward. We see the regulatory construct in NC as the most challenging, with the commission historically focusing on water consumption, which typically declines 1% annually. That said, we note the company's small presence in the jurisdiction (~100K customers). While not likely to be material, an acceleration in muni acquisitions can also challenge modeling ROEs and create some regulatory lag.

Why Diversify into Gas? Ensuring Organic Prospects

Why invest in a gas utility when premiums are so material for stand-alone water companies? We see this as a bit of an experiment as to how investors will value a hybrid utility company considering the strong investor appetite for water today.

We see the gas transaction as principally motivated by its desire to firm up its own EPS growth outlook with the Peoples Gas business projected to grow its ratebase by 8-10% per mgmt. guidance, notably *higher* than WTR's stand-alone prospects of 7% (this is itself slower than the 8.7% EPS CAGR we have for its closest competitor AWK). We appreciate that gas utilities have more meaningful near-term prospects, but the underlying tension that is less clear is the question of how sustainable the ratebase growth profile is for each company? We believe current Street perception is that the ratebase growth outlook for water is more sustainable than that of gas. Should the reality be that gas growth is indeed more sustainable – whether on a discrete basis for Peoples Gas or for the wider gas utility industry –the valuation premium currently ascribed to the water industry could be in question, particularly as it continues to expand.

What about having other businesses? AWK experience has been positive

Contrasting with the Peoples Gas business, American Water, its closest competitor also maintains ongoing non-regulated operations as part of its overall business mix. The company has highlighted how this will not expand beyond 15% of the overall company and is designed to provide complementary opportunities to raise cash in a manner to minimize external equity. We see this firm cap as effective in reducing Street focus on this business at large. While actually achieving EPS growth for AWK has been another story given the specific non-reg efforts pursued, investor willingness to discount the company for these less valuable businesses has been less clear.

Without a set of comparisons, it's hard to say what the 'right' water multiple (and premium vs. electric utilities should be).

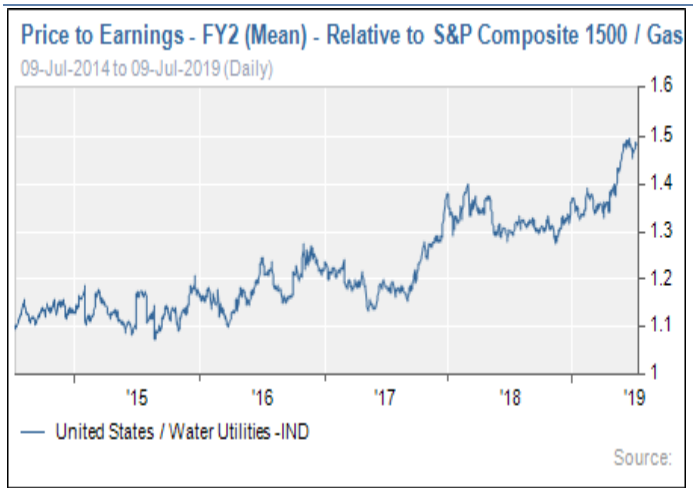
AWK's decision to pursue non-reg efforts as well as WTR's decision to pursue non-water efforts should in theory partially dilute down their exposure to pure-play water utility earnings growth. However, there is little evidence thus far this indeed the case.

We value Aqua America using a SOTP approach, ascribing an average of peer water utilities for its core water operations and ascribing a gas multiple for its gas businesses. We see upside to street estimates for WTR as supportive, particularly given the uncertainly around the water multiple more broadly. Our forward looking estimates reflect earnings on a combined basis with Peoples Gas.

Water: A Premium Product?

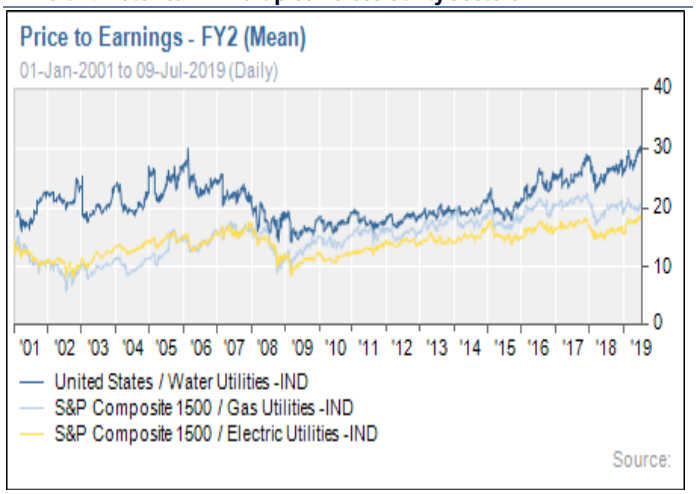
The exhibits below show the historical two year forward P/E ratio for water, gas, and electric utilities, as well as a history of water's premium over gas. While water has consistently traded at a premium to gas and electric, we note a strong acceleration in the spread more recently. We believe the historical premium is largely driven by water utilities' lower project risk associated with smaller and frequent projects, lower compliance and regulatory risk, and lower overall levels of scrutiny.

Exhibit 1: Historical Water Premium Relative to Gas



Source: BofA Merrill Lynch Global Research, FactSet

Exhibit 2: Historical PE multiples Across Utility Sectors



Source: BofA Merrill Lynch Global Research, FactSet

Water Growth Leading the Charge

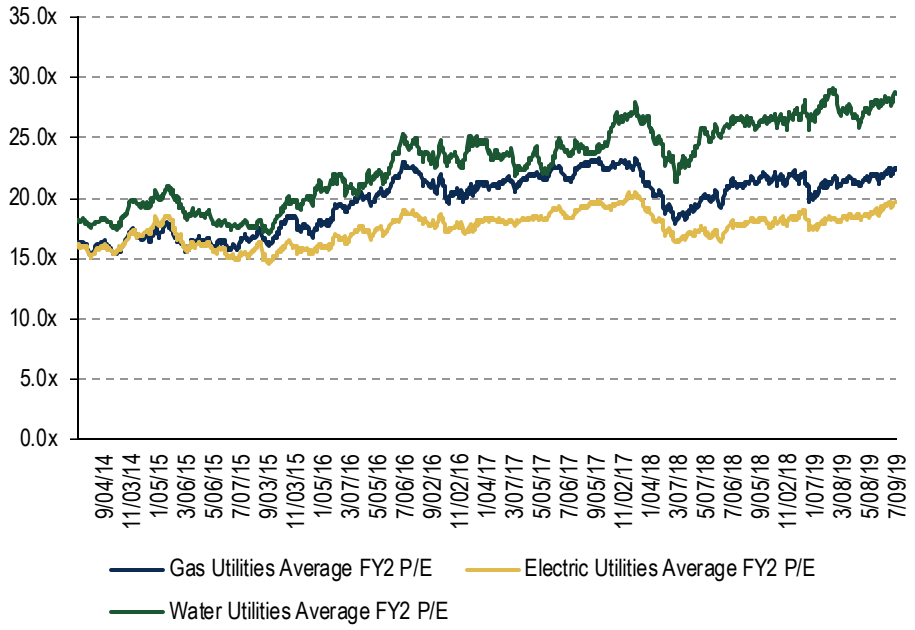
In the exhibit below, we reflect Consensus estimates for growth across the water, electric, and gas utility sectors. From 2018 through 2021, water is expected to grow at the fastest pace, at an 8% CAGR relative to 5% CAGRs for gas and electric, respectively. We also highlight the smaller variation y/y across the water space.

Table 1: Just how fast do utilities grow?

	2018	2019	2020	2021	2018-2021 CAGR
Water Utilities	4%	6%	9%	9%	8%
Gas Utilities	13%	-2%	10%	7%	5%
Electric Utilities	8%	2%	7%	6%	5%

Source: BofA Merrill Lynch Global Research, Bloomberg

Chart 1: Historical PEs Across Sectors



Source: BofA Merrill Lynch Global Research, FactSet

How did the Peoples Gas Transaction Come About?

The company is acquiring Peoples Natural Gas from SteelRiver Infrastructure Partners. SteelRiver is the successor of Babcock & Brown Infrastructure Fund North America, The current company was created through the acquisition of Peoples in February 2010, TW Phillips in May 2011, Equitable in December 2013, and Delta Gas in September 2017. Our sense is that the Steel River fund was looking to sell as it approaches maturity, presenting an opportunity for Aqua America to diversify their business.

Why does water trade at such a premium & does adding gas create a risk?

This is the second critical question for Aqua America in its bold move to acquire Peoples Gas. We believe much of the outsized premium for water utilities broadly is a direct result of a capital flows from ESG-specific funds allocating capital into the most palatable utilities. We ascribe a scarcity premium to water utilities relative to available capital. That said, we question the sustainability of the water premium broadly following the latest re-ratings, and expect gas driven earnings growth to provide relative support.

Business Overview

Aqua America is the second largest publicly traded water utility with corporate headquarters in Byrn Mawr, Pennsylvania. The company currently operates in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana and Virginia. Following the close of the acquisition of Peoples Natural Gas now expected in Fall 2019 (from mid-2019 previously), the company will also operate in West Virginia and Kentucky, with a pro forma rate base of over $7Bn (70% of combined company net income and rate base in water and wastewater).

Aqua Pennsylvania

Aqua Pennsylvania is the company's largest operating subsidiary, and accounted for ~53% of operating revenues and 71% of the regulated segment income in 2018.

Recent & Pending Acquisitions: Momentum in Muni Tuck-Ins

The acceleration of Fair Market Value Legislation in a number of jurisdictions has made muni acquisitions more palatable, and we continue to expect WTR to drive incremental rate base growth through additional tuck-ins. The company completed six muni acquisitions in 2018 for an incremental 100mn in rate base, with another 6 signed agreements pending closing. While we don't anticipate any large water acquisitions, we expect to see additional announcements over the course of the year. Mgmt has noted active pursuit in four of their existing states totaling over 400K customers, but has not disclosed the particular states they are pursuing the larger acquisitions.

Table 2: Acquisitions in 2018

Acquisitions - Closed in 2018	State	Rate Base	Customers	Ratebase Composition	Customer Concentration
Sun Valley	PA	0	81	0%	1%
Firestone Trace	OH	0	367	0%	3%
Manteno	IL	25	3,890	24%	27%
Limerick	PA	64	5,497	60%	39%
Peotone	IL	13	3,083	12%	22%
East Bradford	PA	5	1,240	5%	9%
Total		**107**	**14,158**	**100%**	**100%**

Inorganic Growth	*14,158*
Organic Growth	*8,500*

Source: Company report

The company is currently awaiting approvals for another six acquisitions YTD, largely concentrated in the state of PA (~95% on purchase price basis) with an overall purchase price consideration of $110M that would likely add another 19.4K customers (with 18k based out of PA).

Table 3: Pending Acquisitions - YTD

Pending Acquisitions	State	Purchase Price	Customers	Ratebase Composition	Customer Concentration
New garden	PA	30	2,106	27%	11%
Schuy kill	PA	4	600	3%	3%
Grant Park	IL	2	540	2%	3%
Cheltenham	PA	50	10,450	46%	54%
Sky line	IL	4	752	3%	4%
East Norriton	PA	21	4,952	19%	26%
Total		**110**	**19,400**	**100%**	**100%**

Source: Company report

Peoples Natural Gas

In 2018, WTR announced the acquisition of Peoples Natural Gas in an all-cash transaction that reflects an enterprise value of $4.3Bn (including $1.3Bn of debt). The company is headquartered in Pittsburgh, PA and provides natural gas distribution services to over 740K customers in three states (PA, KY, and WV; with KY and WV

expanding WTR's legacy geographic footprint). The company has ~15,500 miles of distribution pipeline, 1,500 miles of gathering pipeline and 250 miles of intrastate transmission pipeline. WTR has noted a 3,100 mile bare steel and cast pipe replacement opportunity at about 150 miles per year (implies 20+ years increased capex). In the near term, the company projects annual rate base growth of ~8-10% following a Pennsylvania rate case filed in January and new rates expected in the fall. Through the acquisition, WTR seeks to create a multi-platform regulated utility company, and expects the acquisition to be accretive to earnings in the first full year.

Pipeline Opportunity: Peoples has identified 3,000+ miles of bare steel and cast iron pipe to be replaced under their Long-term Infrastructure Improvement Plan (LTIIP) by 2034 in its PA service territory. The company currently has a Distribution System Improvement Charge (DSIC) in place that allows for the accelerated recovery of capital between rate cases. We see this as a key component of the company's ability to make timely recovery with minimal regulatory lag.

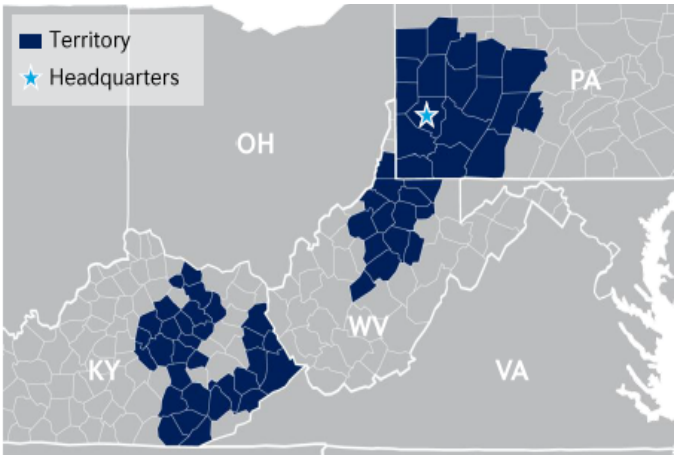
Operating Territories

Below we include the map of operating service territories of WTR and Peoples Gas on a standalone and pro forma basis. While WTR is currently present in the states of PA, OH, TX, IL, NC, NJ, and IN, Peoples Gas currently provides services in the states of KY, WV, and PA. Pennsylvania remains the only state where the footprints overlap.

Exhibit 3: Aqua America service areas– stand alone

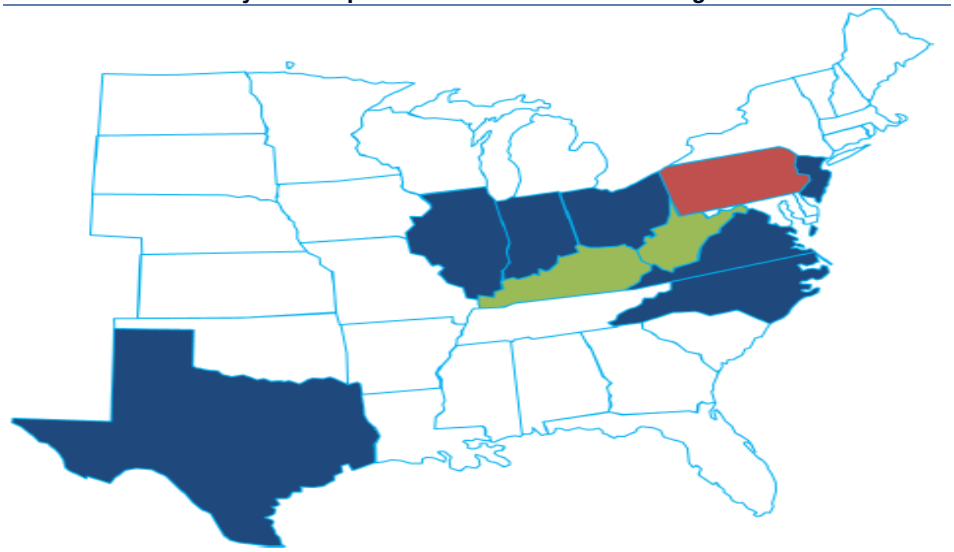
Source: Company Report

Exhibit 4: Peoples Gas service areas – stand alone



Source: Company Report

Exhibit 5: Combined Entity – Post acquisition service territories – PA being the common state



Source: Company Report

Bank of America Merrill Lynch

Rate Base: History and Beyond

Ratebase – WTR prior to Peoples Gas Transaction

We highlight that standalone ratebase for WTR as of yearend '18 stood at $4.5B for WTR with 878k water and 128K waste water connections, respectively. PA remains the single largest contributor to the company, contributing ~69% of the total ratebase; given the size of its existing operations and future growth prospects, PA is likely to remain the most critical state in WTR's service territories.

Table 4: Aqua – Standalone – Ratebase/Customer Details

States	Rate Base ($M)	Water Connections	Wastewater Connections	Total Customers	Ratebase Composition	Total Customer Concentration
PA	3,095	440,487	28,115	468,602	69%	47%
OH	317	145,938	6,878	152,816	7%	15%
IL	320	65,214	15,222	80,436	7%	8%
TX	235	64,360	17,480	81,840	5%	8%
NJ	171	53,639	6,213	59,852	4%	6%
NC	204	81,074	19,114	100,188	5%	10%
IN	83	1,226	26,979	28,205	2%	3%
VA	75	25,843	7,787	33,630	2%	3%
Total	**4,499**	**877,781**	**127,788**	**1,005,569**	**100%**	**100%**

Source: Company report

In 2018, WTR closed six acquisitions across the states of PA, OH, and IL that contribute $107M to the YE2018 ratebase, adding ~14K customers in the process (in addition to +8.5K of customer growth organically). The company has guided to 2%-3% customer growth from the legacy water business, with management noting about 70bp from new homes and the remainder from muni acquisitions.

Revenue Surcharge

Revenue surcharge is a mechanism through which regulators allow utilities to recover depreciation and capital costs associated with capital expenditures related to replacing and maintaining infrastructure systems. By permitting utilities to add a surcharge on to customer bills without a full rate case, utilities can reduce regulatory lag between completion of a capital project and the recovery of its costs through a formal rate review process. While WTR is permitted to apply a surcharge in seven states for its water utility operations, six states allow a surcharge for its wastewater operations.

Below we include the tables on rate cases/surcharges that are already approved by the respective regulatory commissions, as well as the cases pending before the commission. While completed and approved rate cases and surcharges in the states of IL, OH, and PA will add ~$5M of annual revenues, pending proceedings if approved could increase revenue requirement by another $78M. That said, settlement agreements pending approval in PA contemplate a $47Mn in revenue vs. an original request of $71Mn.

Table 5: Completed Surcharges in 2019

2019 Completed Surcharges	Revenue Increase ($M)	Type
IL	2	Surcharges
OH	1	Rate Case
OH	2	Surcharge
PA	0	Surcharges
Total	**5**	

Source: Company report

Table 6: Pending Surcharges

Pending Surcharges	Revenue Increase	Type	Docket ID
NJ	7	Rate Case (W)	WRT18121351
NC	1	Surcharge (w)	W-218, Sub 497A
NC	0	Surcharge (ww)	W-218, Sub 497A
OH	(4)	Tax Compliance Surcharge	18-1843-WW-UNC & 18-1841-ST-UNC
OH	2	Surcharge (w)	19-567-WW-SIC
PA	58	Rate Case (w)	R-2018-3003558
PA	13	Rate Case (ww)	R-2018-3003561
Total	**78**		

Source: Company report

Capex

WTR expects standalone rate base to be ~$5B at the end of 2019, and the company is projecting a CAGR of 7% through 2021. This is driven by $1.4B in investments over the next three years, with $550M earmarked for 2019. 46% of WTR's current capex is DSIC eligible.

WTR has guided to capital spending for Peoples Gas of $297Mn and $360Mn the next couple of years, largely driven by its Long-term Infrastructure Improvement Plan (LTIIP) for 3,100 miles of gas pipelines (~150 miles/year for next 20 years). 70% of Peoples capex is DSIC eligible to help reduce the regulatory lag. Under a combined entity, management expects capital spending to be 57% DSIC eligible.

Table 7: Peoples gas – Capex Plan

	2016	2017	2018E	2019E	2020E	2021E
Capex $M	140	205	280	297	360	360

Source: Company report

Could Clean Water Legislation Provide another Lever?

The Federal Safe Drinking Water Act, the Clean Water Act, and related state laws and regulations could provide further potential capital opportunities. While the US Environmental Protection Agency (EPA) has established health advisory levels at 70 parts per trillion for Perfluorooctanoic acid and Perfluorooctanesulfonic acid, states are increasingly looking to further limit such levels. Our sense from management is that installation of additional filters relating to stricter regulations could be an incremental $100Mn opportunity.

Texas the Latest to Adopt Fair Market Value Legislation

In 2016, fair market value legislation was enacted in Pennsylvania, WTR's largest jurisdiction, allowing the public utility commission to utilize fair market value to set ratemaking rate base (as opposed to the depreciated original cost of water or wastewater assets) for qualifying muni acquisitions. Under the process, independent valuation experts perform appraisals and the ratemaking base is the lower of the purchase price or average of the appraisals. The legislation ultimately provides a more accretive opportunity through these acquisitions, and we expect to see further tuck-ins across the water utility sector as the legislation gains momentum in additional jurisdictions. We highlight that six other states that WTR operates in currently have fair value legislation: Illinois, Indiana, New Jersey, North Carolina, Ohio and most recently Texas. Virginia is now the only state where Aqua operates without the legislation at the moment.

Ratebase – Peoples Gas

The table below reflects the rate base by state for Peoples Gas as of the end of 2018. Of the $2.1 total ratebase, PA represented $1.9Bn with small allocations for KY and WV. Looking forward, the company expects to grow ratebase at a 8%-10% CAGR through 2021.

Table 8: Peoples gas – Ratebase - standalone

State	Rate Base ($M)	Connections
PA	1,939	693,244
KY	108	38,701
WV	26	12,868
Total	**2,073**	**744,813**

Source: Company report

Peoples Gas filed its PA rate case earlier this year (Docket No. R-2018-3006818) for the first time since 2012. The request is for a revenue increase of $94.9m with a projected rate base of ~$2.1B for the test year ending October 2020. While rates are expected to go into effect in fall 2019, the rate case proceeding is ongoing. After rates go into effect, we expect the company to look at utilizing the repairs tax benefits to drive

material earnings growth for the gas business over the next several years. Under the treatment, the company could maintain any new revenue requirement while driving down the tax rate through expensing as opposed to capitalizing certain improvements.

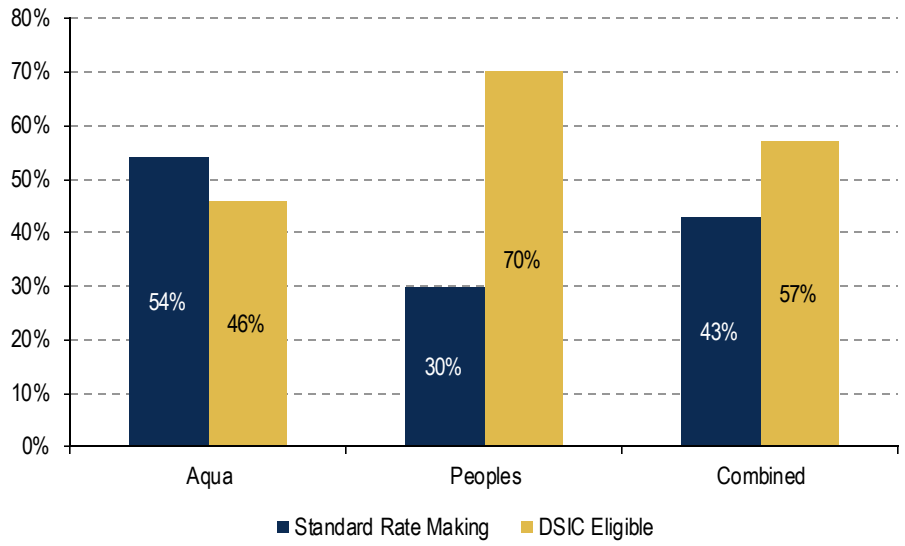
Table 9: Applicable surcharge and Mechanisms

Stae	Allowed Surcharge	Mechanism
Aqua		
IL	2.5% avg annual increase	QIPS
IN	10%	DSIC
NC	5%	WSSIC
NJ	Water - 5%	DSIC
OH	12.75% - water; 9% - wastewater	SIC
PA	7.5% - water; 5% - wastewater	DSIC
Peoples		
PA	5%	DSIC
KY	No Cap	PRP
DSIC	*Distribution System Improvement Charge*	
WSSIC	*Water and Sewer System Improvement Charge*	
QIPS	*Qualifying Infrastructure Plant Surcharge*	
PRP	*Pipeline Replacement Program*	

Source: Company report

Below, we highlight the % of planned capex from 2019 through 2021 that is eligible for DSIC and that of which is dependent on Standard Rate Making procedures. On a combined basis, management has highlighted over half of pro forma capital spending will be DSIC eligible, an incremental 11% relative to WTR's standalone mechanisms.

Chart 2: % of capex 2019-2021 recovered through DSIC



Source: Company report

Projected Combined Rate base

In the exhibit below, we reflect average rate base by company and on a pro forma basis. Management has guided to 7% for the standalone water utility with stronger growth of 8%-10% for Peoples Natural Gas. Our water utility rate base assumes just under 100Mn in annual tuck in acquisitions.

Table 10: Projected Ratebase

Average Ratebase	2019E	2020E	2021E	2022E	2023E
Water Utility	4,748	5,171	5,513	5,842	6,158
Ratebase growth		8.9%	6.6%	6.0%	5.4%
Guidance (RB CAGR 7% 19-21E, excluding acquisitions)			**7.8%**		
Peoples Gas	2,100	2,293	2,482	2,679	2,881
Ratebase growth		9.2%	8.3%	7.9%	7.6%
Guidance (RB CAGR 8-10% 19-21E)			**8.7%**		
Pro Forma	**6,848**	**7,464**	**7,996**	**8,521**	**9,039**
Ratebase growth		9.0%	7.1%	6.6%	6.1%
CAGR			**8.1%**		

Source: BofA Merrill Lynch Global Research estimates, company report

Combined Company Will Be Heavily Exposed to PA Jurisdiction

The Pennsylvania Public Utility Commission (PUC) consists of five commissioners – Gladys Brown Dutrieuille (D – Chairman), David Sweet (D – Vice Chairman), John Coleman (R), Andrew Place (D), Norman Kennard (R) – and 503 commission staff members. The commissioners are appointed to serve five years with the governor appointing a chairman. No more than three commissioners may be from the same political party.

NJ Jurisdiction

The New Jersey Board of Public Utilities (NJ BPU) consists of five commissioners – Joseph Fiordaliso (D - President), Mary-Anna Holden (R), Dianne Solomon (R), Upendra Chivukula (D), Robert Gordon (D) – and 247 staff members. The commissioners are appointed to serve six years with the governor appointing president. The NJ BPU has adopted fair market value legislation as well as a 5% DSIC mechanism for the water utility.

KY Jurisdiction

The Kentucky Public Service Commission (PSC) consists of three commissioners – Michael J. Schmitt (R – Chairman), Robert Cicero (R – Vice Chairman), Talina R. Mathews (R) – and approximately 70 staff members. The commissioners are appointed to serve 4 years with the governor appointing a chairperson.

IL Jurisdiction

The Illinois Commerce Commission (ICC) consists of five commissioners – Carrie K. Zalewski (D – Chairman), Brien Sheahan (R), Sadzi Martha Oliva (R), D. Ethan Kimbrel (D), Maria S Bocanegra (I – Acting Commissioner) – and 232 staff members. The commissioners are appointed to serve five year terms with the governor appointing the chairman.

IN Jurisdiction

The Indiana Utility Regulatory Commission (IURC) consists of five commissioners – Jim Huston (R – Chairman), Sarah Freeman (D), Stefanie Krevda (R), David Ober (R), David E. Ziegner (D) – and approximately 75 staff members. The commissioners are appointed to serve four year terms with the governor appointing a chairman to serve for four years.

NC Jurisdiction

The North Carolina Utilities Commission (NCUC) currently consists of six commissioners – Charlotte Mitchell (D – Chair), TroNola D. Brown-Bland (D), Jerry Dockham (R), James Patterson (R), Lyons Gray (R), Daniel Clodfelter (D) – and about 60 staff members. The commissioners are appointed by the governor to serve a term of six years, with the chairperson appointed to serve four year terms. With the recent resignation of Ed Finley and terms up for James Patterson and Jerry Dockham, Gov Cooper nominated three new commissioners Floyd Mckissick (D) Kimberly Duffley and Jeff Hughes, all of which are pending approval.

OH Jurisdiction

The Public Utilities Commission of Ohio (PUCO) consists of five commissioners – Sam Randazzo (I – Chair), Beth Trombold (I), Lawrence Friedeman (D), Dennis Deters (R), Daniel Conway (R) – and about 330 staff members. The commissioners are appointed by the governor to serve five year terms, with the governor electing a chairperson to serve through the duration of their tenure. The next appointment will be at the conclusion of Friedeman's term in April of 2020.

TX Jurisdiction

The Public Utilities Commission of Texas consists of three commissioners – DeAnn Walker (R – Chair), Arthur D'Andrea (R), Shelly Botkin (R) – and about 215 staff members. The commissioners are appointed by the governor to serve five year terms, with the governor electing a chairperson to serve through the duration of their tenure. The next appointment will be at the conclusion of Botkin's term later this year. The company transitioned to being regulated by the Texas PUC in 2014, and has been enjoying a 12% current authorized ROE, which we expect to fall under a PUC ratecase proceeding.

WV Jurisdiction

The Public Service Commission of West Virginia consists of three commissioners – Charlotte Lane (R – Chair), Brooks McCabe (D), Renee Larrick (R) – and about 230 staff members. The commissioners are appointed by the governor to serve six year terms, with the governor electing a chairperson to serve through the duration of their tenure.

Table 11: Commissioners by Jurisdiction

State	Commissioners	Position	Political Inclination	Took Office	Term Expires
NJ	Joseph L. Fiordaliso	President	D	2019	2025
	Mary-Anna Holden	Commissioner	R	2018	2024
	Dianne Solomon	Commissioner	R	2013	2019
	Upendra Chivukula	Commissioner	D	2014	2020
	Bob Gordon	Commissioner	D	2018	2023
PA	Gladys Brown Dutrieuille	Chairman	D	2019	2023
	David W. Sweet	Vice Chairman	D	2018	2021
	Norman J. Kennard	Commissioner	R	2017	2019
	Andrew G. Place	Commissioner	D	2015	2020
	John F. Coleman, Jr.	Commissioner	R	2017	2022
KY	Michael J. Schmitt	Chairman	R	2016	2019
	Robert Cicero	Vice Chairman	R	2016	2020
	Talina R. Mathews	Commissioner	R	2017	2021
IL	Carrie K. Zalewski	Chairman	D	2019	2024
	Brien J. Sheahan	Commissioner	R	2015	2020
	Sadzi Martha Oliva	Commissioner	R	2017	2022
	D. Ethan Kimbrel	Commissioner	D	2018	2023
	Maria S. Bocanegra	Acting Commissioner	I	2019	2023
IN	Jim Huston	Chairman	R	2014	2021
	Sarah Freeman	Commissioner	D	2016	2022
	Stefanie Krevda	Commissioner	R	2018	2022
	David Ober	Commissioner	R	2018	2020
	David E. Ziegner	Commissioner	D	1990	2023
NC	Charlotte Mitchell	Chair	D	2017	2023
	ToNola D. Brown-Bland	Commissioner	D	2017	2023
	Jerry C. Dockham	Commissioner	R	2013	2019
	James G. Patterson	Commissioner	R	2013	2019
	Lyons Gray	Commissioner	R	2016	2021
	Daniel G. Clodfelter	Commissioner	D	2017	2023
OH	Sam Randazzo	Chairman	I	2019	2024
	M. Beth Trombold	Commissioner	I	2018	2023
	Lawrence K. Friedeman	Commissioner	D	2017	2020
	Dennis P. Deters	Commissioner	R	2019	2021
	Daniel R. Conway	Commissioner	R	2017	2022
TX	DeAnn T. Walker	Chairman	R	2017	2021
	Arthur C. D'Andrea	Commissioner	R	2017	2023
	Shelly Botkin	Commissioner	R	2018	2019
WV	Charlotte Lane	Chairman	R	2019	2025
	Renee A. Larrick	Commissioner	D	2017	2023
	Brooks F. McCabe	Commissioner	R	2014	2021

Source: BofA Merrill Lynch Global Research, SNL

Merger Timeline

The exhibit below reflects the merger timeline for the Peoples Gas acquisition. Following the hearings related to the acquisition on June 11th, the company provided updated timing expectations of Fall 2019 from mid-year 2019 previously.

Table 12: Merger Timeline

Date	Proceedings
10/23/2018	*WTR announced Peoples acquisition*
11/13/2018	*WTR filed merger applications with PA/WV PUCs*
11/20/2018	*WTR filed merger applications with KY PUCs*
3/13/2019	*KY PSC approved merger*
3/27/2019	*Merger settlement filed with WV PSC*
3/29/2019	*$750M Investment from CPPIB*
4/18/2019	*Announced pricing of common stocks and tangible equity unit offerings*
4/24/2019	*Announced pricing of $900M senior notes offering*
2Q19	*WV PSC approved merger*
2Q19	*Targeted final order on PA merger proceedings*
6/11/2019	*Updated targeted closing date of merger to fall 2019*
Fall 2019	*Targeted closing date of merger*

Source: Company report

Bank of America Merrill Lynch

With the Company's updated timeframe for their expectations around the close of the Peoples Gas acquisition, we are projecting the transaction to close near the beginning of 4Q. The company has noted that they expect the transaction to be accretive to earnings in 2020 and longer term.

Comparing Aqua America with its peers

In the exhibits below, we reflect the latest WTR metrics relative to other water utilities. As the second largest publicly water utility (after AWK), the company is trading at 23.5x versus the broader water sector at 26.2x 2021 estimates on average. We see the street as largely underestimating the earnings ability for Peoples Gas in the near term, and see upside to estimates as largely supportive of valuation. The company's 2% dividend is in line with peers.

Table 13: DPS Comparison Across Water Comps

					DPS ($)			
Companies	**Ticker**	**Market Cap ($M)**	**Price ($)**	**Div Yield**	**2019**	**2020**	**2021**	**2022**
American Water	AWK	21,027	116.63	2%	1.97	2.15	2.36	2.58
SJW Group	SJW	1,791	62.87	2%	1.18	1.29	1.39	1.52
Artesian Water	ARTNA	339	36.41	3%	na	na	na	na
Connecticut Water Service	CTWS	845	69.90	2%	1.31	1.38	1.47	1.59
Middlesex Water Company	MSEX	983	59.49	2%	na	na	na	na
California Water Services	CWT	2,450	50.94	2%	0.79	0.83	0.87	na
Average				**2%**	**1.31**	**1.41**	**1.52**	**1.90**
Aqua America	**WTR**	**8,837**	**41.00**	**2%**	**0.9**	**1.0**	**1.1**	**na**

Source: BofA Merrill Lynch Global Research estimates, FactSet. Priced as of 12 July 2019.

Exhibit 6: Water Comps

						P/E Multiples					Earnings per Share					
	Ticker	**Market Cap**	**EV**	**Short Int**	**Days**	**2018A**	**2019E**	**2020E**	**2021E**	**2022E**	**2018A**	**2019E**	**2020E**	**2021E**	**2022E**	**CAGR**
Water Utilities																
American Water	AWK	21,206	27,673	2.9%	5.4	35.6x	33.0x	30.3x	27.7x	25.5x	3.30	3.56	3.88	4.24	4.61	8.7%
SJW Group	SJW	1,791	1,879	0.8%	1.2	30.0x	30.3x	27.4x	23.9x	20.5x	2.10	2.08	2.30	2.64	3.07	10.0%
Artesian Water	ARTNA	336	482	0.7%	3.0											
Connecticut Water Service	CTWS	845	1,152	1.4%	2.2	31.5x	29.6x	27.9x	25.7x		2.23	2.36	2.51	2.73		7.1%
Middlesex Water Company	MSEX	991	1,138	1.5%	2.5	30.7x	27.7x	26.9x	25.5x		1.96	2.17	2.24	2.36		6.4%
California Water Services	CWT	2,452	3,507	4.0%	5.1	40.9x	36.5x	31.6x	29.3x		1.25	1.40	1.61	1.74		11.7%
Average		**36,507**		**2.4%**	**4.4**	**33.0x**	**31.2x**	**28.4x**	**26.2x**	**23.0x**		5.6%	9.0%	9.1%	11.6%	**8.3%**
Aqua America	WTR	8,886	9,166	5.3%	11.3	29.3x	33.8x	23.7x	23.5x	22.4x	1.41	1.22	1.74	1.75	1.84	7.0%

Source: BofA Merrill Lynch Global Research, Bloomberg

What about Gas comps?

The 8-10% ratebase CAGR contemplated for Peoples Gas appears meaningfully ahead of peer gas utilities. We do not ascribe a premium to the gas utility in our valuation, however, as we believe the balance of the stand-alone gas utility sector is awarded a premium in part because of M&A expectations. We do not see WTR as a seller; rather the question is if it will continue to acquire gas utility platforms to complement its organic EPS growth outlook.

Exhibit 7: Gas Comps

	Ticker	Market Cap	EV	Short Int	Days	P/E Multiple					Earnings Per Share					
						2018A	2019E	2020E	2021E	2022E	2018A	2019E	2020E	2021E	2022E	CAGR
Gas Utilities																
Atmos Energy Corp	ATO	12,518	15,586	3.0%	4.5	27.1x	24.7x	23.4x	21.7x		3.95	4.33	4.58	4.93		7.7%
Spire Inc	SR	4,337	6,933	2.0%	4.3	23.1x	22.8x	21.9x	21.0x	19.4x	3.70	3.74	3.91	4.07	4.41	4.5%
New Jersey Resources Corp	NJR	4,462	5,646	3.5%	7.2	18.9x	25.0x	22.8x	20.9x		2.65	2.00	2.19	2.39		NM
Northwest Natural Gas Co	NWN	2,137	2,807	4.4%	6.1	31.6x	29.3x	27.8x	26.7x		2.22	2.40	2.52	2.64		5.8%
ONE Gas Inc	OGS	4,813	6,291	2.1%	4.8	28.0x	26.4x	25.3x	23.9x		3.26	3.46	3.61	3.83		5.5%
Southwest Gas Holdings Inc	SWX	4,825	na	1.3%	2.3	23.8x	23.0x	21.4x	19.8x	18.4x	3.82	3.94	4.25	4.59	4.95	6.7%
UGI Corp	UGI	9,260	14,241	4.3%	6.4	19.3x	22.1x	17.2x	16.2x		2.75	2.41	3.09	3.28		6.0%
NiSource Inc	NI	11,014	20,705	4.3%	5.1	22.7x	22.7x	21.9x	20.2x	18.8x	1.30	1.30	1.35	1.46	1.57	4.8%
South Jersey Industries Inc	SJI	3,107	5,755	7.0%	12.8	22.5x	30.4x	21.0x	19.3x		1.49	1.11	1.60	1.75		5.3%
Average		**56,472**		**3.6%**	**6.0**	**24.1x**	**25.2x**	**22.5x**	**21.2x**	**18.9x**		-1.8%	9.8%	6.7%	8.0%	**5.8%**

Source: BofA Merrill Lynch Global Research, Bloomberg

Bank of America Merrill Lynch

EPS Estimates

The exhibit below reflects our EPS estimates based on the expectation for the acquisition to close later this year. Given the tangible equity unit offering in connection with the acquisition, the company will provide EPS based on a share conversion and excluding the ongoing interest expense from the units. The equity units will convert between 1.1790 and 1.4442 shares per purchase contract depending on share price, and we assume ~16mn incremental shares based on price. That said, we expect parent drag to be mostly limited to holdco debt.

Our '21 estimates of $1.75 are well above the street at $1.66, driven primarily from an expectation of stronger earnings at Peoples Gas. Earned ROE degradation at PA, also itself a gradual process drives the relatively flat outlook for its core water utilities through the near-term as well.

Table 14: EPS Estimates

EPS Estimates	2019E	2020E	2021E	2022E	2023E
PA	$0.79	$0.80	$0.77	$0.82	$0.86
OH	$0.07	$0.07	$0.07	$0.08	$0.08
IL	$0.07	$0.07	$0.08	$0.08	$0.09
TX	$0.06	$0.06	$0.06	$0.06	$0.06
NC	$0.04	$0.04	$0.04	$0.04	$0.05
Other States	$0.08	$0.08	$0.09	$0.09	$0.10
Water Utility	**1.11**	**1.12**	**1.11**	**1.18**	**1.24**
Peoples Gas	**0.16**	**0.70**	**0.75**	**0.79**	**0.82**
Parent & Other	*-0.05*	*-0.08*	*-0.10*	*-0.12*	*-0.14*
EPS	**1.22**	**1.74**	**1.75**	**1.84**	**1.92**
YoY Growth		*43%*	*1%*	*5%*	*4%*
Shares O/S	*223*	*238*	*238*	*250*	*254*
Fully Diluted Shares O/S	*235*	*254*	*254*	*254*	*254*
Consensus	**1.36**	**1.55**	**1.66**		
Consensus '19-'21 CAGR					
BofAML CAGR 2019-2021					
DPS	**0.92**	**0.99**	**1.06**	**1.13**	**1.21**
Payout Ratio	*76%*	*57%*	*60%*	*61%*	*63%*

Source: BofA Merrill Lynch Global Research estimates, company report

Valuation

With our estimates, we set a price objective of $45 based on a SOTP analysis. We apply the water utility multiple of 26.2x to the water segment (with no discounts to reflect no over-earnings by '21 at any of the subsidiaries) and 21.2x for the gas segment (with a -1x discount to reflect risks related to both no takeout premium reflected in the balance of the sector in our judgement as well as its over-earning ROE profile particularly upfront), grossing each up for the respected growth CAGR. The question is just over what period of time can Peoples Gas navigate substantive rate increases without sacrificing a refund of merger synergy benefits fully; WTR's PA segment was able to maintain its over-earning position for upwards of 7-years. We net out 50% of holdco debt and 50% of interest expense. While we see risk to the water utility multiple premium broadly, we expect WTR to be supported from strong earnings growth and estimates moving higher.

Table 15: WTR SOTP

Water Utilities	2021 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*26.2x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		**28.4x**							
Water Utilities									
States	**2021E EPS**	**ROE**	**embedded**						
PA	$0.77	10.0%	**0.0x**	27.4x	28.4x	29.4x	$21	$22	$23
OH	$0.07	9.9%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$2
IL	$0.08	9.6%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$2
TX	$0.06	10.0%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$2
NC	$0.04	9.9%	**0.0x**	27.4x	28.4x	29.4x	$1	$1	$1
Other (including acquisitions)	$0.09	9.9%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$3
Water utilities total (ex-Peoples)	**$1.11**			*27.4x*	*28.4x*	*29.4x*	**$30**	**$32**	**$33**
Gas Utilities									
Peer Gas P/E		*21.2x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		**22.4x**							
	2021E EPS	**ROE**	**embedded**						
Peoples Gas	**$0.75**	14.1%	**-1.0x**	**20.4x**	**21.4x**	**22.4x**	**$15**	**$16**	**$17**
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			**-752**	50%			($376)	($376)	($376)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($364)	($379)	($393)
50/50 Weighted Drag from HoldCo Drag							($740)	($755)	($769)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							**$43.00**	**$45.00**	**$46.00**
Current Price								$41.00	
Dividend Yield								2%	
Total Return								**11.89%**	

Source: BofA Merrill Lynch Global Research estimates

Bank of America Merrill Lynch

Debt and Capital Structure

The exhibit below reflects our estimated debt construction across the pro-forma portfolio. We expect debt to move towards 15% at the holdco level, creating an additional parent lag. Our sense from management is that they will look to hold enough debt to finance a run rate of $100Mn in annual muni acquisitions.

Table 16: Debt Projections

Debt by Construct	2019	2020	2021	2022
Regulated - Legacy Business	2,419	2,588	2,750	2,906
Peoples Gas	1,300	1,387	1,478	1,572
Holding Company	611	689	752	822
Total Debt	**$4,330**	**$4,664**	**$4,980**	**$5,300**

Debt by Construct (%)	2019	2020	2021	2022
Regulated - Legacy Business	56%	55%	55%	55%
Peoples Gas	30%	30%	30%	30%
Holding Company	14%	15%	15%	16%

Source: BofA Merrill Lynch Global Research estimates

S&P: (Aqua Pennsylvania)

Following the announcement of the People Gas acquisition, S&P placed subsidiary utility Aqua Pennsylvania on credit watch with negative implications for the A+ issuer rating and their AA- first mortgage bond rating. S&P noted this reflects the likelihood that the transaction would result in materially weaker consolidated financial measures for the overall group. For the rating agency to keep their current investment rating, they look for consolidated FFO/Debt to be 13%-23%, with their current forecast projecting 11.5%-13% following the close of the transaction.

Moodys: Baa2 – Stable Outlook

In late April, Moody's launched on WTR with a Baa2 rating and a stable outlook issued a on the senior unsecured debt. The rating agency noted the low-risk of water and waste water operations and strong regulatory support in the primary jurisdiction of Pennsylvania and diversity across the rest of the portfolio. That said, they expect a declining financial profile due to the pending acquisition (PNG is currently rated Baa2 positive) and debt funded capex. Post close, Moodys expects holding company debt to be roughly 15% of consolidated debt on their calculation.

While Moody's Stable outlook takes into account the weaker financial profile, key ratios of FFO/net debt and retained cash flow (RCF) are expected to be maintained above 12% and 7%, respectively. We see these as the two key indicators to monitor for potential equity needs.

Table 17: Moodys Metrics

	2016	2017	2018	2019E	2020E	2021E	2022E
CFO	**412**	**396**	**384**	**614**	**745**	**798**	**846**
+/-: Working Capital Adjustments	(1)	7	17	10	26	3	4
CFO Pre-WC	**411**	**403**	**401**	**624**	**771**	**801**	**850**
+/-: Other Adjustments	(4)	3	1	1	1	1	1
FFO	**407**	**406**	**402**	**625**	**772**	**802**	**851**
Less: Dividend	131	141	151	205	234	251	282
CFO Pre-W/C - Dividends	**280**	**262**	**250**	**418**	**537**	**550**	**568**
Less: Capex (Includes Acquisitions)	395	486	644	4,939	865	885	905
FCF	**(114)**	**(231)**	**(411)**	**(4,531)**	**(354)**	**(337)**	**(341)**
Retained Cash	**277**	**267**	**251**	**419**	**538**	**551**	**569**
FFO / Debt	20.3%	18.3%	15.3%	13.3%	15.3%	14.9%	14.8%
RCF / Debt	13.8%	12.0%	9.5%	8.9%	10.6%	10.2%	9.9%

Source: BofA Merrill Lynch Global Research estimates, Moodys

Management Bios

Board of Directors

We see WTR's board as particularly qualified relative to the balance of the utility sector with numerous former corporate & business-unit level CEOs, but what is particularly remarkable are the multiple executives who have been previously involved in senior management positions within the utility industry. For instance, the experience offered from SO and DUK, two large cap utility peers, is particularly relevant in addressing strategy. The board recently voted to increase the size of their board to 8 members with the election of Francis Idehen, in line with peer AWK. Francis is a particularly relevant director given his prior role in IR at Exelon.

Christopher H. Franklin is Chairman, Chief Executive Officer and President

Christopher H. Franklin is Chairman, Chief Executive Officer and President of WTR. He was previously president and chief operating officer, regulated operations. He has held several key executive roles in public affairs, customer operations and as regional president of the company's southern and mid-western operations, and was responsible for company's corporate and public affairs federal, state and municipal legislative affairs, investor relations, and communications. He joined WTR in 1992 as director, corporate and public affairs. Prior to that, he worked at PECO Energy Company (an Exelon Company) as regional, civic and economic development officer and was responsible for the review, recommendation and promotion of economic development initiatives in the Philadelphia region. He serves as a director on the National Association of Water Companies' board of directors. Previously, he served on the board of directors of ITC Inc.

He earned his B.S. from West Chester University and his M.B.A. from Villanova University.

Elizabeth B. Amato - Director Since 2018

Ms. Amato, a director since 2018, appointed to the Executive Compensation Committee and the Corporate Governance Committee of the Board, is a human resources executive with over twenty years of leadership experience. She has been Executive Vice President and Chief Human Resources Officer of United Technologies Corp. since November 2015. Previously, she was Senior Vice President, Human Resources and Organization of UTC from August 2012 to November 2015. She joined UTC in 1985 and held a variety of the most senior human resources leadership positions across the corporation in both aerospace and commercial building systems, including UTC Climate, Controls & Security (2011-2012), Carrier (2010-2011), Pratt & Whitney (2006-2009) and Sikorsky (1997-2006).

She holds a bachelor's degree in political science from Davidson College and a law degree from the University of Connecticut. She is a recipient of the YWCA Women Achievers Award, is currently a member of the National Academy of Human Resources CHRO Board Academy, and is a member of the Board of Directors for Children's Healthcare Charity, Inc.

Nicholas DeBenedictis - Chairman Emeritus

Nicholas DeBenedictis currently serves as chairman emeritus. He recently stepped down as the non-executive chairman of the board of Aqua America. Previously, He served as Chairman and CEO of Aqua America (formerly Philadelphia Suburban Corporation) from June 1993 to July 2015. Prior to that, he served as senior vice president of corporate and public affairs for PECO Energy from 1989 to 1992 and was responsible for government relations, economic development and environmental policies, plus implementation of the utility's public policy positions. He also serves on the Board of Exelon. Before that, he worked as president of the Greater Philadelphia Chamber of Commerce from 1986 to 1989. He worked as a Secretary of the Department of Environmental Resources (1983-1986) and Director of the Office of Economic Development (1981-1983) in Pennsylvania

government's cabinet positions. Before joining the cabinet, he was associated with the U.S. Environmental Protection Agency fort eight years (1973-1981). He served in the Army Corps of Engineers between 1970 and 1973 reaching the rank of Captain. He is the current president of the Pennsylvania Society, and currently serves on the policy committee of the Pennsylvania Business Council and is a former Chairman of the Council (formerly the Pennsylvania Business Roundtable). He also serves on the Board of Directors for many regional businesses, economic and environmental organizations that include Drexel University, Exelon Corporation, PNC Bank - Southeast Pennsylvania Advisory, P.H. Glatfelter Company, and Independence Blue Cross. He is a past president of the National Association of Water Companies.

He earned his Bachelor's degree in business administration from Drexel University in 1968, and a Master's degree in environmental engineering and science from Drexel in 1969. He received an Honorary Doctorate of Science degree from Widener University, an Honorary Doctorate of Letters degree from Drexel University, and an Honorary Doctor of Humane Letters from Misericordia University.

Daniel J. Hilferty - Lead Independent Director, Director since 2017

Daniel J. Hilferty is Lead Independent Director of the company since 2017. He worked as president and chief executive officer of Independence Blue Cross. Previously, he worked as a Senior Vice President of Corporate and Government Affairs at Mercy Health Corporation in Bala Cynwyd, PA and then as President and CEO of AmeriHealth Caritas Family of Companies (formerly Amerihealth Mercy) in Philadelphia PA from 1996 to 2009.

He earned his undergraduate degree from St. Joseph's University in Philadelphia, Pennsylvania, and a master's degree in public administration from American University. He also serves on the boards of the Greater Philadelphia Chamber of Commerce, the Catholic Foundation of Greater Philadelphia, and FS Investment Corporation III and as chairman of the board of directors for the Blue Cross Blue Shield Association.

Ellen T. Ruff - Director since 2006

Ms. Ruff is director since 2006. She has over 30 years of experience with a major utility company in various management, operations, legal planning and public affairs positions. She is also a partner in the law firm of McGuire-Woods, LLP. Previously, she served as President, Office of Nuclear Development, for Duke Energy Corporation, from December 2008 until her retirement in January 2011. Prior to that, she worked as President of Duke Energy Carolinas from 2006 through 2008. She served Duke Energy organization in various capacities, including: Vice President and General Counsel of Corporate, Gas and Electric Operations; Senior Vice President and General Counsel for Duke Energy; Senior Vice President of Asset Management for Duke Power; Senior Vice President of Power Policy and Planning; and Group Vice President of Planning and External Affairs.. She is also a director of Mistras Group, Inc

Lee C. Stewart - Director Since 2018

Mr. Stewart, a director since 2018 is a private financial consultant with over 40 years of experience as an investment banker, corporate executive and professional director. He has been appointed to the Audit Committee and the Risk and Investment Policy Committee of the Board. Previously, he was Vice President at Union Carbide Corporation from 1996 to 2001, and as Chief Financial Officer of Foamex International, Inc from 2001 to 2002. After that, he served as a director of AEP Industries, Inc., a chemical company listed on the Toronto Stock Exchange from 2000 till 2011, as a director of ITC Holdings Corp. from 2005 to 2016, as well as associated with Momentive Performance Materials Inc., a specialty chemical company in silicone and advanced materials from May 2013 through its successful emergence from bankruptcy in October 2014. He has been director of P.H. Glatfelter, a global supplier of specialty papers and engineered materials, since 2002 and is also director of Mood Media, Inc.

Mr. Stewart has a bachelor's degree from the Wharton School of the University of Pennsylvania

Christopher Womack - Director Since 2019

Mr. Womack is a director of the company since 2019. He has served as President, External Affairs, Southern Company from December 2008 until the present. He has worked in various executive leadership positions at Southern Company since 1988 that includes Executive Vice President, Georgia Power Company from March 2006 to December 2008, Senior Vice President, Fossil & Hydro Power, Georgia Power Company from December 2001 to March 2006, and Senior Vice President, Human Resources from March 1998 to December 2001. He also served as a legislative aide in the U.S. House of Representatives from 1979 to 1987.

Francis Idehen – Director Since 2019

Mr. Idehen is the newest director of the company and was elected to the board at the beginning of June when the board voted to increase their size to 8. He currently serves as managing director and COO at Grosvenor Capital Management, a position he has held since 2017. In his current capacity, he is responsible for overseeing core operations functions, including fund finance, corporate finance, technology, compliance and legal. He is also a member of the firm's operations committee and labor impact fund investment committee. Previously, he has held senior roles at Exelon from 2011-2017, serving as treasurer, head of investor relations and managing director of Exelon's investment office. Prior to that, Idehen served as a Senior Portfolio Manager at Intel. Mr. Idehen has a bachelor's degree in economics from Yale University and an MBA from Harvard Business School.

Leadership Team

Rick Fox - Executive Vice President and Chief Operating Officer, Regulated Operations

Rick Fox serves as Chief Operating Officer (COO) of Aqua America since July 2015 and is responsible for the company's regulated operations, including engineering and environmental compliance.

Prior to that, he served as regional president for Aqua America since January 2012, responsible for managing utility operations in Texas, Illinois, North Carolina, Indiana and Virginia. Before that he was vice president, customer operations and responsible for all customer service operations for Aqua America's regulated operating subsidiaries, including the company's national customer call centers, national meter operations, and company-wide billing and collections. He joined Aqua America in 2002 as manager of customer service following 17 years in the chemical manufacturing industry in both operations and technical management.

He earned his B.S. in chemical engineering from Virginia Polytechnic Institute and State University, and his M.B.A from Villanova University, where he achieved Beta Gamma Sigma honors. He is a member of the American Institute of Chemical Engineers.

Christopher P. Luning - Senior Vice President, General Counsel and Secretary

Christopher P. Luning was appointed Senior Vice President, General Counsel and Secretary for Aqua America, Inc. in May 2012. He is the company's chief legal counsel and responsible for the company's legal, human resources, internal audit, and safety departments. Previously, he worked as a vice president, corporate development and was responsible for corporate development activities. He joined Aqua America in 2003 as assistant general counsel. Prior to WTR, he worked at Hovnanian Enterprises, Inc. as legal counsel.

He earned his B.S. business/political science from Albright College and his J.D. in 1993 from Villanova University. He is licensed to practice law in Pennsylvania and New Jersey.

Matt Rhodes - Executive Vice President, Strategy and Corporate Development

Matt Rhodes works as Executive Vice President, Strategy and Corporate Development for Aqua America since June 2018 and responsible for assisting the chief executive officer with developing, communicating, executing, and sustaining strategic initiatives, with an emphasis on growth. He is also responsible for overall corporate development, as well as acquisitions of regulated and market-based businesses.

Previously, he worked as Managing Director at Goldman Sachs in the Natural Resources Investment Banking Group with a focus on power and utility clients. Prior to that, he served at Bank of America and Duke Capital partners in energy finance roles.

He earned his BBA from the University of Texas at Austin and an MBA, with honors, from the Stern School of Business at New York University.

Robert A. Rubin - Senior Vice President, Chief Accounting Officer and Controller

Robert A. Rubin serves as senior vice president, controller and chief accounting officer (CAO) of Aqua America, since January 2012, and responsible for external and internal financial reporting, taxes, coordinating external audits, corporate accounting and maintaining compliance with accounting standards and principles throughout the company. Previously, he worked as chief accounting officer of the company from 2004 to 2012. Prior to that, he worked as controller for the company from 1999-2004. He joined Aqua America in 1989 as an accounting manager. Prior to that he was associated with KPMG LLP

He is a Certified Public Accountant with a B.S. in accounting from Penn State University and associated with the Pennsylvania and American Institutes of Certified Public Accountants and the National Association of Water Companies – Taxation Committee.

Dan Schuller - Executive Vice President, Chief Financial Officer

Dan Schuller is Executive Vice President and Chief Financial Officer for Aqua America, Inc. and responsible for accounting, tax, treasury, regulatory relations, planning, Sarbanes-Oxley compliance and capital spending in regards to return on investment. Previously, he served as Executive Vice President, Strategy and Corporate Development for Aqua America and was responsible for Aqua's strategic growth initiatives. Prior to Aqua America, he was associated with J.P. Morgan Asset Management – Infrastructure Investments Group as an investment principal. Prior to joining J.P. Morgan, he was a manager at Mars & Co., an international strategy/general management consulting firm and was responsible for consulting engagements related to growth and profitability for Fortune 500 companies and conducted due diligence for private equity firms.

He earned his B.S., M.S. and Ph.D. in civil engineering from Purdue University and also a member of the American Society of Civil Engineers.

Financial Statements

Income Statement

Table 18: Income Statement

	2016	2017	2018	2019E	2020E	2021E	2022E	2023E
Regulated	*800*	*805*	*835*	902	949	966	1,004	1,042
Other & Eliminations	*20*	*5*	*3*	3	3	3	3	3
Peoples Gas	*0*	*0*	*0*	139	643	687	733	770
Operating revenues	**820**	**810**	**838**	**1,044**	**1,596**	**1,657**	**1,740**	**1,815**
Operating expenses:								
Operations and maintenance	297	282	308	351	500	513	525	534
Regulated	278	282	292	336	485	498	510	519
Other & Eliminations	20	0	16	15	15	15	15	15
Depreciation	131	136	146	191	330	356	382	409
Amortization	2	0	1	-	-	-	-	-
Taxes other than income taxes	56	57	60	68	98	101	103	105
Regulated	54	55	57	66	96	98	101	103
Other & Eliminations	2	2	3	3	3	3	3	3
Total operating expenses	**487**	**476**	**515**	**610**	**928**	**969**	**1,011**	**1,049**
Operating income	**333**	**334**	**323**	**434**	**668**	**687**	**730**	**766**
Allowance for funds used during construction	-9	-15	-13	(13)	(13)	(13)	(13)	(13)
Change in fair value of interest rate swap agreements	0	0	60	-	-	-	-	-
Gain on sale of other assets	0	0	-1	-	-	-	-	-
Equity earnings in joint venture	-1	0	-2	(2)	(2)	(2)	(2)	(2)
Other	8	5	2	-	-	-	-	-
Other expense (income)	**(2)**	**(11)**	**46**	**(15)**	**(15)**	**(15)**	**(15)**	**(15)**
EBIT	**336**	**345**	**277**	**449**	**683**	**702**	**745**	**781**
Interest expense, net	81	88	99	132	196	211	226	241
Income before income taxes	**255**	**257**	**178**	**317**	**487**	**491**	**519**	**540**
Provision for income taxes (benefit)	21	17	-14	32	49	49	52	54
Net income	**234**	**240**	**192**	**285**	**439**	**442**	**467**	**486**
Adjustments	0	3	59	2	3	3	1	
Adjusted NI	**234**	**243**	**251**	**287**	**442**	**445**	**468**	**486**
EPS								
Diluted	**1.32**	**1.36**	**1.41**	**1.22**	**1.74**	**1.75**	**1.84**	**1.92**
Fully Diluted Share Count	178	178	178	235	254	254	254	254

Source: BofA Merrill Lynch Global Research estimates, company report

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Balance Sheet

Table 19: Balance Sheet

Balance Sheet	2016	2017	2018	2019E	2020E	2021E	2022E	2023E
Assets								
Property, plant and equipment, at cost	6509	7004	7648	12,396	12,932	13,461	13,983	14,499
Less: accumulated depreciation	1508	1604	1718	1,910	2,239	2,595	2,977	3,387
Net property, plant and equipment	**5,002**	**5,400**	**5,930**	**9,103**	**9,638**	**10,168**	**10,690**	**11,206**
Current assets:								
Cash and cash equivalents	4	4	4	3	5	5	5	6
Accounts receivable and unbilled revenues, net	97	99	101	126	193	200	210	219
Inventory, materials and supplies	13	14	16	20	30	31	33	34
Prepayments and other current assets	13	13	23	23	23	23	23	23
Assets held for sale	2	2	3	3	3	3	3	3
Total current assets	**129**	**131**	**147**	**176**	**254**	**263**	**275**	**286**
Regulatory assets	949	714	788	788	788	788	788	788
Deferred charges and other assets, net	31	38	39	39	39	39	39	39
Investment in joint venture	7	7	7	7	7	7	7	7
Goodwill	42	42	53	1,628	1,628	1,628	1,628	1,628
Total assets	**6,159**	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**	**13,427**	**13,953**
Liabilities and Equity								
Aqua America stockholders' equity:								
Common stock at $.50 par value, authorized 300,000,000 shares, issued 181,151,827 and 180,700,251 in 2018 and 2017	90	90	91					
Capital in excess of par value	798	807	820					
Retained earnings	1033	1133	1174					
Treasury stock, at cost, 3,060,206 and 2,986,308 shares in 2018 and 2017	-71	-73	-76					
Accumulated other comprehensive income	1	1	0					
Total stockholders' equity	**1,850**	**1,958**	**2,009**	**4,706**	**4,913**	**5,108**	**5,293**	**5,473**
Long-term debt, excluding current portion	1760	2029	2419					
Less: debt issuance costs	22	22	21					
Long-term debt, excluding current portion, net of debt issuance costs	**1,738**	**2,008**	**2,398**	**4,330**	**4,664**	**4,980**	**5,300**	**5,619**
Current liabilities:								
Current portion of long-term debt	151	114	145	274	296	317	339	360
Loans payable	7	4	15	15	15	15	15	15
Accounts payable	47	59	77	96	147	153	161	168
Book overdraft	13	22	9	9	9	9	9	9
Accrued interest	18	21	23	23	23	23	23	23
Accrued taxes	26	24	22	22	22	22	22	22
Interest rate swap agreements	0	0	60	60	60	60	60	60
Other accrued liabilities	40	41	47	47	47	47	47	47
Total current liabilities	**302**	**284**	**399**	**547**	**620**	**647**	**676**	**705**
Deferred credits and other liabilities:								
Deferred income taxes and investment tax credits	1269	769	845	845	845	845	845	845
Customers' advances for construction	92	93	93	93	93	93	93	93
Regulatory liabilities	251	542	531	531	531	531	531	531
Other	116	107	97	97	97	97	97	97
Total deferred credits and other liabilities	**1,727**	**1,512**	**1,567**	**1,567**	**1,567**	**1,567**	**1,567**	**1,567**
Contributions in aid of construction	542	571	591	591	591	591	591	591
Total liabilities and equity	**6,159**	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**	**13,427**	**13,953**

Source: BofA Merrill Lynch Global Research estimates, company report

Cash Flow Statement

Table 20: Cash Flow Statement

Cash Flow Statement	2016	2017	2018	2019E	2020E	2021E	2022E	2023E
Cash flows from operating activities:								
Net income	234	240	192	287	442	445	468	486
Adjustments to reconcile net income to net cash flows from operating activities:								
Depreciation and amortization	133	137	147	191	330	356	382	409
Deferred income taxes	17	14	-15					
Provision for doubtful accounts	6	5	5					
Stock-based compensation	5	6	8					
Loss (gain) on sale of utility system and market-based business unit	-1	1	0					
Gain on sale of other assets	0	0	-1					
Interest rate swap agreements	0	0	60					
Net change in receivables, inventory and prepayments	-4	-6	-18	(10)	(26)	(3)	(4)	(4)
Net change in payables, accrued interest, accrued taxes and other accrued liabilities	5	-1	1					
Pension and other postretirement benefits contributions	-10	-16	-14					
Other	11	3	5					
Net cash flows from operating activities	**396**	**381**	**369**	**469**	**745**	**798**	**846**	**892**
Cash flows from investing activities:								
Property, plant and equipment additions	-383	-478	-496	(639)	(865)	(885)	(905)	(925)
Acquisitions of utility systems and other, net	-9	-6	-146					
Acquisitions				(4,300)				
Net proceeds from the sale of utility systems/other	8	1	1					
Other	1	2	1					
Net cash flows used in investing activities	**-383**	**-480**	**-640**	**-4,939**	**-865**	**-885**	**-905**	**-925**
Cash flows from financing activities:								
Customers' advances and contributions in aid of construction	7	7	7					
Repayments of customers' advances	-4	-7	-6					
Net proceeds (repayments) of short-term debt	-10	-3	12	129	22	21	21	21
Proceeds from long-term debt	504	591	1332	1,813	333	317	320	318
Proceeds from Amortizing Notes				119				
Repayments of long-term debt	-373	-359	-914					
Change in cash overdraft position	-8	9	-13					
Proceeds from issuing common stock	1	1	5	1,294				
Prepaid Stock Purchase Contracts	0	0	0	571				
Proceeds from stock Purchase agreement	0	0	0	750				
Proceeds from exercised stock options	4	3	1					
Share-based compensation windfall tax benefits	1	0	0					
Repurchase of common stock	-3	-2	-3					
Dividends paid on common stock	-131	-141	-151	(205)	(234)	(251)	(282)	(307)
Other	-1	-1	-1					
Net cash flows from (used in) financing activities	**-12**	**100**	**271**	**4,470**	**121**	**87**	**59**	**33**
Net (decrease) increase in cash and cash equivalents	1	0	-1	0	2	0	0	0
Cash and cash equivalents at beginning of year	3	4	4	4	3	5	5	5
Cash and cash equivalents at end of year	**4**	**4**	**4**	**3**	**5**	**5**	**5**	**6**

Source: BofA Merrill Lynch Global Research estimates, company report

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Price objective basis & risk

Aqua America (WTR)
Our price objective is $45 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 1.0x discount to Peoples Gas as we expect earned ROEs to be driven down over time.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Electric Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Aqua America	WTR	WTR US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	AES	AES	AES US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Pattern Energy Group	PEGI	PEGI US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Terraform Power	TERP	TERP US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

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Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	61	44.20%	Buy	47	77.05%
Hold	42	30.43%	Hold	30	71.43%
Sell	35	25.36%	Sell	27	77.14%

Equity Investment Rating Distribution: Global Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1516	51.23%	Buy	942	62.14%
Hold	687	23.22%	Hold	431	62.74%
Sell	756	25.55%	Sell	380	50.26%

* Issuers that were investment banking clients of BofA Merrill Lynch or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Merrill Lynch Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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US Electric Utilities & IPPs

Power Points: ENBL lowers '19, WTR 2Q, AEE equity raise a bit more

Industry Overview

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Equity | 07 August 2019

ENBL posts solid 2Q19 but points to low-end on '19

ENBL reported 2Q19 earnings of $124mn with adjusted EBITDA of $281mn, slightly ahead of expectations. The earnings contribution translates to ~$0.12/sh for CNP's 53.8% ownership and ~$0.12/sh for OGE's 25.5% ownership. Operationally, volumes continued to improve, principally at the natural gas business (90% of mix) with gathering (+4.3% YoY), processing (+9% YoY), and transportation (+14.4% YoY) all up and offsetting the decline in the oil biz. That said, ENBL mgmt. is now pointing to the low-end of guidance for 2019 net income of $435-$505mn as it doesn't expect hedging benefits that occurred in 4Q18 to follow through into 2H. We see this as cautionary for CNP in particular as concerns increase over midstream weakness given the recent decline in energy prices potentially impacting the company's 2019 and LT guidance. We reiterate our Buy rating on CNP, given confidence in mgmt's outlook and as we see a possible inflection on resolution of TX rate case settlement possible by mid-Sept. However, we look for affirmation of '19 guidance on the 2Q call. For OGE, we maintain our Neutral rating as we await potential indication of upside to capex with pending rate case nearly complete.

WTR: Expect Call to Focus on Pending Acquisition

WTR posted 2Q19 adjusted EPS of $0.37 compared to consensus at $0.36, with mgmt. reaffirming its 2019 guidance range of $1.45-$1.50 (excluding impacts related to the Peoples transaction). Management reiterated expectations for an organic rate base growth CAGR of 7% through '21(we still guide to 7.8% inclusive of acquisitions) and the closing of the Peoples transaction in the fall of 2019. The company also highlighted the recently received a letter of intent from the Delaware County Regional Water Control Authority (DELCORA) to exclusive discussions that could result in a combination with Aqua Pennsylvania Wastewater; if this occurs, we would view it as a nice potential tuck-in acquisition in a constructive jurisdiction where mgmt. could expand in the relatively niche wastewater sub-segment. Mgt is hosting a call at 11am ET, and we expect focus to largely center around the pending acquisition of Peoples and the potential to take advantage of the Repairs Tax benefit for the business; will mgmt. opt to spread this benefit thru its forecast period & how much of an initial jump will be realized? With shares valued off '21 & eventually '22 by 4Q, we stress spreading may become less relevant to valuation as longer-term ability to retain some amount of repairs benefits. We perceive upward bias to Street EPS expectations from Repairs Tax Benefit and further re-rating of shares as comfort emerges on the combined outlook; maintain Buy rating.

AEE: Prospectus for share issuance indicates slightly more

Ameren sold 7.549mn shares for $74.30/sh, indicating a total raise of $560.89mn; not all of the amount will be included in the resulting equity dilution for the company. Even so, this suggests more 2020 equity need than we include in our model to help finance the $1.2bn wind program; we model $350mn in '20. We still expect dilution in '20 even though the forward sale could be settled as late as March '21. We see clarity around the equity need as a positive for the company given some may have been anticipating the raise already. However, we reiterate it is offset by the slightly higher raise than some in the Street anticipated (we perceive up to ~$500 Mn had been in expectations). The equity raise also affirms to us mgmt. is unlikely to be more aggressive on its balance sheet; note the MO rate case is pending.

United States
Electric Utilities

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Refer to important disclosures on page 5 to 8. Analyst Certification on page 3. Price Objective Basis/Risk on page 2.

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Timestamp: 07 August 2019 06:58AM EDT

Stocks mentioned

BofAML Ticker	Ticker	Company name	Price	Rating
AEE	AEE US	Ameren Corp	US$ 75	A-2-7
WTR	WTR US	Aqua America	US$ 41.15	A-1-7
CNP	CNP US	CenterPoint Energy	US$ 28.86	B-1-7
OGE	OGE US	OGE Energy Corp	US$ 42.49	A-2-7

Source: BofA Merrill Lynch Global Research

Price objective basis & risk

Ameren Corporation (AEE)

Our $81 price objective is predicated on a P/E based sum of the parts, valuing each business subsidiary relative to the 2021E peer multiple of 19.1x. We apply a 1.0x premium to peers at AEE Missouri to account for the improving prospects of capital spend, supplemented by a regulatory jurisdiction becoming more favorable. We apply a 1.0x premium to peers at AEE Illinois to account for formulaic rates and decoupling on the distribution business which aids in earnings predictability. The overall business is expected to grow at a more meaningful clip than that of peers - we see a 9% rate base CAGR at IL nat gas through 2023 - and at ATXI, we apply a 1.5x premium to peers even when contemplating the latest potential step down in ROEs. At the Parent, we assume an in line multiple given the healthy debt metrics with FFO/Debt at 19%+. Electric peer P/E multiple is grossed up for a year to 2019 by 5% to reflect capital appreciation across the sector.

The upside (downside) risks to our price objective are the utilities earning their allowed returns or better (worse), a significant increase (decrease) in 30-year U.S. Treasury bond yields, and adverse regulatory outcomes that could affect mgmt's ability to earn its allowed return

Aqua America (WTR)

Our price objective is $45 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 1.0x discount to Peoples Gas as we expect earned ROEs to be driven down over time.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

CenterPoint Energy (CNP)

We value CenterPoint Energy at $31 using a SOTP approach: electric business on 1x premium to the utility multiple on 2021E P/E. We take out any earnings attributable to the transition bonds amortization, as those are temporary and instead add back the DCF value of future payments. For CNP's gas utilities we apply an in-line multiple to the utility gas peer multiple of 21.1x (from 21.2x). Both electric and gas peer P/E multiples are grossed up for a year to 2019 by 5% to reflect capital appreciation across the sector.We integrate Vectren intor our model and apply a 60/40% weighting to the gas/electric multiple. For VISCO/VESCO we apply a 12x P/E multiple, and an 11x P/E multiple for the announced synergies. We subtract parent interest expenses at a weighted average multiple.We value the Energy Services segment we rely on a 12x P/E. We add CNP's interest in ENBL at the market value. We take a 50/50 interest/debt approach, where we net out 50% of interest and 50% of HoldCo debt.

Downside risks: execution risk, decreases in capex which could support or weaken

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earnings ability, lower authorized returns, interest rate increases, and lower earnings from ENBL.

OGE Energy Corp (OGE)

We value OGE at $45 based on a sum of the parts, separating the utility business from the Enable stake.

For the utility business we apply the peer multiple of 19.2x on 2021E EPS and a 0.5x premium given the improving regulatory environment in OK. Electric peer P/E multiple is grossed up for a year to 2019 by 5% to reflect capital appreciation across the sector.

For the Enable Midstream Partners, LP stake we rely on the current market price of ENBL multiplied by the number of the shares owned by OGE to determine the equity value. We attribute no value to the GP shares, as we don't anticipate IDRs materializing over the next three years.

Downside risks are further declines in the regulatory environment possibly resulting in lower ROEs or other hurdles hindering OGE's ability to earn its authorized return. While not as exposed due to low parent interest, we see interest rate hikes as another potential downside risk. Finally, execution risk on existing capex schedule could put further pressure on earnings growth. Declines in value of ENBL share could also provide downside to our valuation.

Upside risks are shifts towards a more favorable Oklahoma regulatory environment, which could ease OGEs ability to earn its authorized return in the jurisdiction and possibly increase capex plan as management views prospects in the state more positively. Improvements in value of ENBL share could also provide upside to our valuation.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Electric Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Aqua America	WTR	WTR US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	AES	AES	AES US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Pattern Energy Group	PEGI	PEGI US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Terraform Power	TERP	TERP US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

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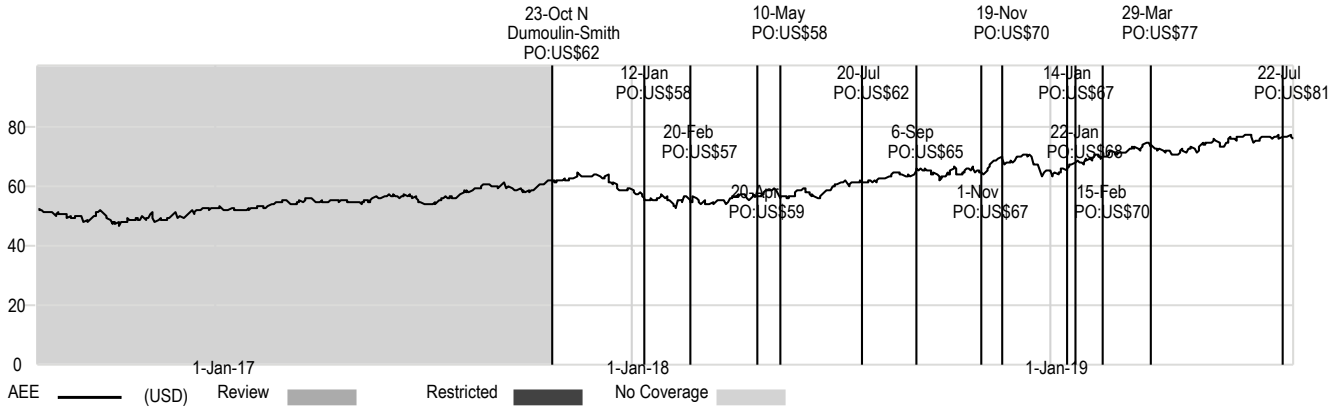
Important Disclosures

AEE Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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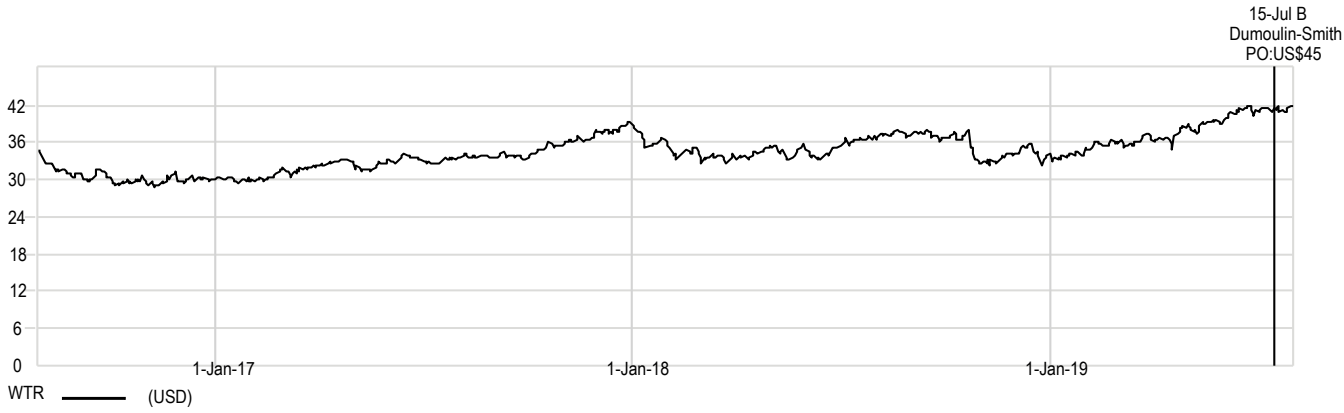
WTR Price Chart



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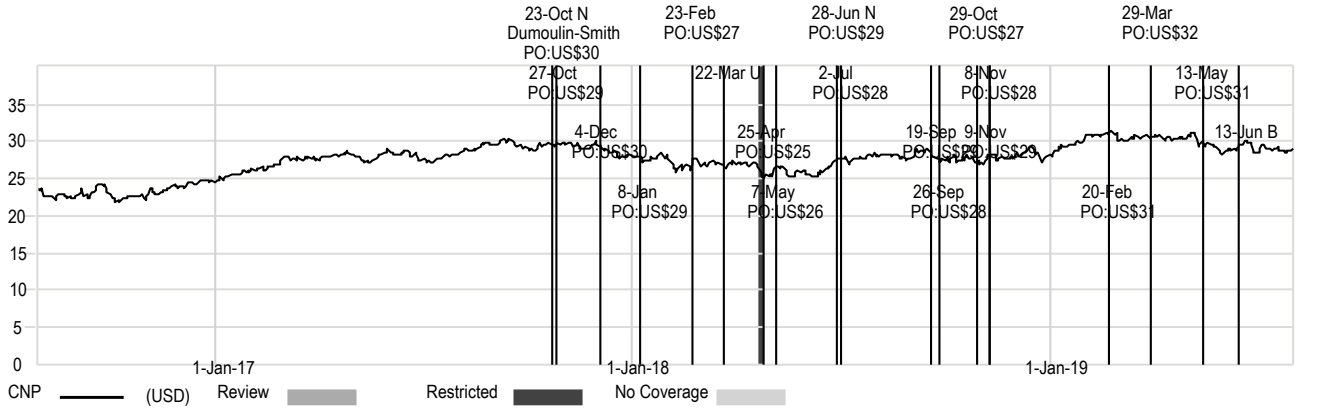
CNP Price Chart



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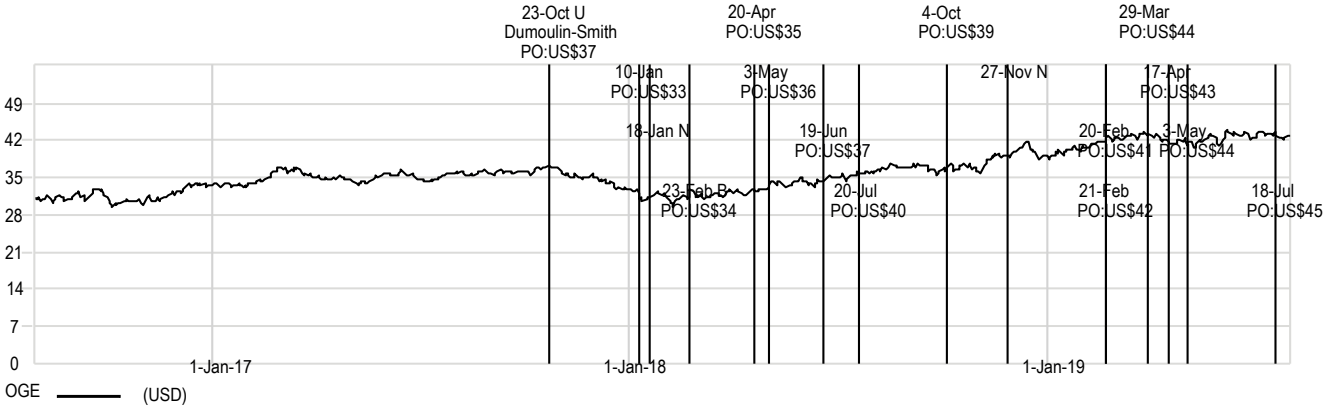
OGE Price Chart



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Equity Investment Rating Distribution: Utilities Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	61	44.20%	Buy	47	77.05%
Hold	42	30.43%	Hold	30	71.43%
Sell	35	25.36%	Sell	27	77.14%

Equity Investment Rating Distribution: Global Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1516	51.23%	Buy	942	62.14%
Hold	687	23.22%	Hold	431	62.74%
Sell	756	25.55%	Sell	380	50.26%

* Issuers that were investment banking clients of BofA Merrill Lynch or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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Aqua America

Pool Party continues but waiting on the Gas

Maintain Rating: BUY | PO: 45.00 USD | Price: 42.06 USD

Bank of America Merrill Lynch

Equity | 08 August 2019

Executing on Legacy Water Biz and Tuck-Ins

WTR's latest update shows further execution on the core water business and continued focus on tuck in acquisitions. Following Ohio's adoption of FMV legislation in January, the company announced a purchase agreement earlier this month to acquire a small utility in Campbell (3.2K customers) to drive the latest addition to the $100Mn in expected rate base from signed muni acquisitions. Outside of the Peoples acquisition, we expect water tucks ins to continue driving incremental growth. The Fair Market Value legislation has been passed in 7 of the 8 states the company operates in (following TX in June). Thus, we could see mgmt start to pursue a wider geographic footprint as additional states become more appealing; mgmt highlighted a path to 30K customers as critical. More materially, we highlight DELCORA's recent announcement of intent to commit to exclusive discussions with WTR for a potential acquisition. While purchase price (& thus rate base opportunity) are yet to be negotiated, FMV legislation potentially could facilitate a step up from the ~$240Mn depreciated asset base. If such a scenario materializes, it could be a meaningful driver, albeit it may come with some kind of equity issuance.

Peoples Acquisition Remains on Track: October Order?

Following earlier approvals from the KY and WV PSCs for the Peoples acquisition, the company continues to await final approval from PA after filing a non-unanimous settlement. Latest commentary from management highlighted expectations for an October order from the commission with the transaction to close shortly after. Following the close of the transaction, we would expect more guidance around any upside at the Analyst Day tentatively set for December 5th.

Valuation: Repairs Tax Upside Remains Key

With the latest developments, our estimates are unchanged. We remain above the street as we still credit the company with execution of the repairs tax benefit. Our PO ultimately remains unchanged at $45. Maintain Buy given what we perceive as meaningful upside to estimates from Repairs Tax Benefit and further potential re-rating of shares as comfort emerges on the combined outlook.

Estimates (Dec)

(US$)	2017A	2018A	2019E	2020E	2021E
EPS	1.36	1.41	1.30	1.74	1.75
GAAP EPS	1.36	1.41	1.30	1.74	1.75
EPS Change (YoY)	3.0%	3.7%	-7.8%	33.8%	0.6%
Consensus EPS (Bloomberg)			1.36	1.57	1.66
DPS	0.81	0.86	0.92	0.99	1.06

Valuation (Dec)

	2017A	2018A	2019E	2020E	2021E
P/E	30.9x	29.8x	32.4x	24.2x	24.0x
GAAP P/E	30.9x	29.8x	32.4x	24.2x	24.0x
Dividend Yield	1.9%	2.0%	2.2%	2.3%	2.5%
EV / EBITDA*	1.1x	8.1x	26.5x	16.6x	15.8x
Free Cash Flow Yield*	-1.1%	-1.4%	-1.9%	-1.3%	-1.0%

* For full definitions of *iQmethod*℠ measures, see page 8.

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Stock Data

Price	42.06 USD
Price Objective	45.00 USD
Date Established	15-Jul-2019
Investment Opinion	A-1-7
52-Week Range	32.09 USD - 42.32 USD
Mrkt Val (mn) / Shares Out (mn)	9,074 USD / 215.7
Average Daily Value (mn)	43.86 USD
BofAML Ticker / Exchange	WTR / NAS
Bloomberg / Reuters	WTR US / WTR.N
ROE (2019E)	7.5%
Net Dbt to Eqty (Dec-2018A)	127.1%

DELCORA: Delaware County Regional Water Control Authority

PSC: Public Service Commission

FMV: Fair Market Value

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Timestamp: 08 August 2019 09:32AM EDT

iQprofile℠ Aqua America

iQmethod℠ – Bus Performance*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Return on Capital Employed	5.1%	3.9%	4.4%	5.2%	5.1%
Return on Equity	12.6%	9.7%	7.5%	8.6%	8.3%
Operating Margin	41.5%	38.7%	48.1%	70.2%	71.1%
Free Cash Flow	(97)	(127)	(170)	(120)	(87)

iQmethod℠ – Quality of Earnings*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash Realization Ratio	1.6x	1.9x	1.9x	1.8x	1.9x
Asset Replacement Ratio	3.5x	3.4x	3.3x	2.6x	2.5x
Tax Rate	6.6%	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	108.3%	127.1%	97.0%	100.1%	102.8%
Interest Cover	3.9x	2.8x	3.4x	3.5x	3.3x

Income Statement Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Sales	805	835	902	949	966
% Change	0.6%	3.7%	8.0%	5.3%	1.7%
Gross Profit	810	838	1,044	1,596	1,657
% Change	-1.3%	3.5%	24.6%	52.9%	3.8%
EBITDA	14,226	1,941	597	953	998
% Change	-33.6%	-86.4%	-69.2%	59.6%	4.8%
Net Interest & Other Income	(88)	(99)	(132)	(194)	(210)
Net Income (Adjusted)	**240**	**192**	**251**	**414**	**416**
% Change	**2.4%**	**-19.9%**	**31.0%**	**64.5%**	**0.6%**

Free Cash Flow Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Net Income from Cont Operations (GAAP)	240	192	287	442	446
Depreciation & Amortization	137	147	191	330	356
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	14	(15)	0	0	0
Other Adjustments, Net	(9)	45	(10)	(26)	(3)
Capital Expenditure	(478)	(496)	(639)	(865)	(885)
Free Cash Flow	**-97**	**-127**	**-170**	**-120**	**-87**
% Change	**NM**	**-31.5%**	**-33.9%**	**29.8%**	**27.7%**

Balance Sheet Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash & Equivalents	4	4	3	5	5
Trade Receivables	99	101	126	193	200
Other Current Assets	28	42	46	57	58
Property, Plant & Equipment	5,400	5,930	9,103	9,638	10,168
Other Non-Current Assets	801	887	2,462	2,462	2,462
Total Assets	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**
Short-Term Debt	117	160	288	310	331
Other Current Liabilities	167	239	258	309	315
Long-Term Debt	2,008	2,398	4,305	4,638	4,955
Other Non-Current Liabilities	2,083	2,158	2,158	2,158	2,158
Total Liabilities	**4,375**	**4,955**	**7,008**	**7,415**	**7,758**
Total Equity	**1,958**	**2,009**	**4,733**	**4,940**	**5,135**
Total Equity & Liabilities	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**

* For full definitions of *iQmethod℠* measures, see page 8.

Company Sector

Water Utilities

Company Description

Aqua America is a regulated water utility providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI. In Oct 2018, The company announced acquisition of Peoples Gas, a gas utility providing distribution services to 740,000 customers in PA, WV, and KY. The acquisition is expected to be closed by mid- 2019.

Investment Rationale

We see our Buy rating as supported by meaningfully above Street EPS projections on the back of its pending Peoples Gas business and above average ratebase growth.

Stock Data

Average Daily Volume	1,042,678

Quarterly Earnings Estimates

	2018	2019
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NA

Bank of America Merrill Lynch

Capitalizing on Fair Market Value Legislation

During 2Q, Texas became WTR's seventh state to adopt Fair Market Value Legislation when they adopted the legislation in June after Ohio adopted the legislation earlier in the year. Just this month, the company entered a purchase agreement to acquire the water system in Campbell, OH (3,200 customer connections), bringing the total signed purchase agreements for municipalities to 22.6K customers in 2019 and 2020. With WTR the only regulated water utility on size after acquiring operations from AWK, we could see more development in this state in particular following the latest move. Overall, management has noted ~$100Mn in rate base acquisition activity signed set to generate ~$5Mn of incremental earnings. While some of the transactions will close in 2020, the company remains on track to grow customers between 2-3% in 2019.

More materially than the typical tuck-ins, the board of directors of Delaware County Regional Water Control Authority (DELCORA) announced a letter of intent in July committing to exclusive discussions with Aqua Pennsylvania Wastewater that could result in a combination with DELCORA, who currently serves 500K people in 42 municipalities across Delaware and PA. While a sizable opportunity, management noted it would look to put an ATM program in place to raise some add'l equity, partially offsetting potential upside. Aside from a major acquisition, the company doesn't expect any other additional near term equity needs.

On the call, management noted a willingness to expand its footprint to additional states as Fair Market Value legislation gains momentum. We believe All expansion to additional states is increasingly likely following the successful push for passage of the legislation in 7 of the 8 states they operate in.

Peoples Acquisition: Still Guiding to Fall Close

The company received regulatory approval for the Peoples transaction from the Kentucky Public Service Commission in March and the West Virginia Public Service Commission in April after reaching unanimous settlements in the states. Following the approvals in those jurisdictions, the company filed a PA settlement agreement in June that is currently pending before the PA PUC (all but 2 intervenors to the case have entered into or chosen not to oppose the settlement agreement). With the settlement currently under review by the commission given the non-unanimous nature, the company continues to guide to a Fall decision. Specifically, management noted on the call that they expect an order from the commission on October 24th, with the transaction closing shortly after. That said, there is no statutory timeline for the commission to rule on the decision in the state.

EPS Estimates

The exhibit below reflects our EPS estimates which are largely unchanged as we await further developments on the pending acquisition. We remain above the street on '21, driven primarily from an expectation of stronger earnings at Peoples Gas. Earned ROE degradation at PA (assumed to be a gradual process) drives the relatively flat outlook for the core water utilities through the near term. *We appreciate there is substantial latitude in framing the '20 EPS & beyond based on the outlook of this acquisition around repairs tax. We emphasize the shape & form of deal approval remain critical to earnings trajectory, particularly given some mgmt commentary on smoothing its outlook. We stress some scenarios could result in EPS higher than Street consensus still though.*

Table 1: WTR SOTP

EPS Estimates	2019E	2020E	2021E	2022E	2023E
PA	$0.84	$0.80	$0.77	$0.82	$0.86
OH	$0.07	$0.07	$0.07	$0.08	$0.08
IL	$0.08	$0.07	$0.08	$0.08	$0.09
TX	$0.07	$0.06	$0.06	$0.06	$0.06
NC	$0.04	$0.04	$0.04	$0.04	$0.05
Other States	$0.08	$0.08	$0.09	$0.09	$0.10
Water Utility	**1.18**	**1.12**	**1.11**	**1.17**	**1.24**
Peoples Gas	**0.17**	**0.70**	**0.75**	**0.79**	**0.82**
Parent & Other	*-0.05*	*-0.08*	*-0.10*	*-0.12*	*-0.14*
EPS	**1.30**	**1.74**	**1.75**	**1.84**	**1.92**
YoY Growth		*34%*	*1%*	*5%*	*4%*
Shares O/S	*193*	*238*	*238*	*250*	*254*
Fully Diluted Shares O/S	*221*	*254*	*254*	*254*	*254*
Previous EPS	***$1.22***	***$1.74***	***$1.75***	***$1.84***	
Consensus	**1.36**	**1.57**	**1.66**		

Source: BofA Merrill Lynch Global Research, Bloomberg

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Valuation

On our unchanged estimates, our PO remains $45. We continue to apply a 1x discount to Peoples Gas to reflect related removal of any sector takeout premium as well as discounting the strong returns we ascribe to it in the near term.

Table 2: WTR SOTP

Water Utilities	2021 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*26.2x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		**28.4x**							
Water Utilities									
States	**2021E EPS**	**ROE**	**embedded**						
PA	$0.77	10.0%	**0.0x**	27.4x	28.4x	29.4x	$21	$22	$23
OH	$0.07	9.9%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$2
IL	$0.08	9.6%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$2
TX	$0.06	10.0%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$2
NC	$0.04	9.9%	**0.0x**	27.4x	28.4x	29.4x	$1	$1	$1
Other (including acquisitions)	$0.09	9.9%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$3
Water utilities total (ex-Peoples)	**$1.11**			*27.4x*	*28.4x*	*29.4x*	**$30**	**$31**	**$33**
Gas Utilities									
Peer Gas P/E		*21.2x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		**22.4x**							
	2021E EPS	**ROE**	**embedded**						
Peoples Gas	**$0.75**	14.1%	**-1.0x**	**20.4x**	**21.4x**	**22.4x**	**$15**	**$16**	**$17**
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			**-727**	50%			($363)	($363)	($363)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($351)	($325)	($379)
50/50 Weighted Drag from HoldCo Drag							($715)	($688)	($743)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							**$43.00**	**$45.00**	**$46.00**
Current Price								$42.06	
Dividend Yield								2%	
Total Return								**9.18%**	

Source: BofA Merrill Lynch Global Research, Bloomberg

Price objective basis & risk

Aqua America (WTR)
Our price objective is $45 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 1.0x discount to Peoples Gas as we expect earned ROEs to be driven down over time.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Specifically, we derive a value of $31 or the Water Business and $16 per share for the Gas utilities. We then deduct $688M which accounts for $2 per share, and gives us our PO of $45.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Electric Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Aqua America	WTR	WTR US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	AES	AES	AES US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Pattern Energy Group	PEGI	PEGI US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Terraform Power	TERP	TERP US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

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Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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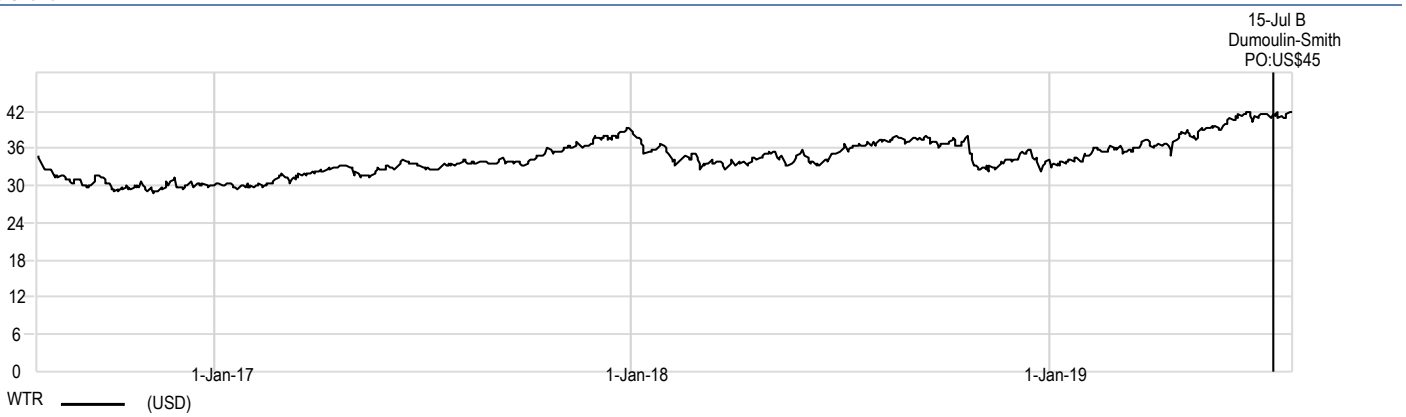

B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Utilities Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	61	44.20%	Buy	47	77.05%
Hold	42	30.43%	Hold	30	71.43%
Sell	35	25.36%	Sell	27	77.14%

Equity Investment Rating Distribution: Global Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1516	51.23%	Buy	942	62.14%
Hold	687	23.22%	Hold	431	62.74%
Sell	756	25.55%	Sell	380	50.26%

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Underperform	N/A	≥ 20%

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Aqua America

Snorkeling in the Deep End: A Closer Look at the Repairs Tax Benefit

Reiterate Rating: BUY | PO: 45.00 USD | Price: 44.18 USD

Bank of America Merrill Lynch

Equity | 21 August 2019

Repairs Tax Remains Focal Point...but What Will Qualify?

As WTR continues to progress through the approval process for the pending Peoples acquisition, we provide our latest model with slight tweaks to our estimates ahead of a potential order (Management has guided towards an Oct 24th ruling but note there is no statutory timeline for an order in the state). While latest discussions with the company suggest that they continue to work through a potential settlement, we see likelihood of one materializing as limited. That said, pending what we still perceive as a likely close during 4Q, the company plans to host an Analyst Day the first week of December that should provide a broad update for the combined company. We would expect a consolidated EPS range for 2020 and some longer term growth guidance to be provided, as well as potential clarity around sizing the repairs tax benefit opportunity for the gas business. The previously employed strategy consists of two components – a current portion based on qualified capex which can be elected (with the benefit flowing through in the income statement immediately) and a catch up adjustment component to reflect prior investments that are currently capitalized and depreciated for tax purposes. While the company has clearly articulated plans to elect the *current* component, the *catch up* component remains somewhat more of a wildcard given the requirement of a commission order and potential nuances around how it could be treated. In the past, the company was able to amortize the catch-up deduction for the PA water business over a 10-year period of time to provide additional tax relief. That said, we perceive the commission is more likely to give at least some benefit back to customers if enacted now. Nonetheless, we don't see the catch up component as necessary for our base case scenario, particularly given the likelihood of a ramp in capital investments going forward. While quantifying qualified capex remains somewhat more challenging, we continue to suspect robust ability to earn in PA, which makes up around 90% of the gas business.

Valuation: Shifting +$1/sh to $46/sh on higher multiple

We shift our '20-22 estimates 1% lower as we assume more conservative ROEs for Peoples Gas. That said, we remain 3% above the Street on '21 given what we still perceive as a robust earnings profile likely to materialize as the company moves to elect the current component post transaction close. On our new estimates and after reflecting the latest mark to market of peer multiples, our price objective shifts up $1 to $46.

Estimates (Dec)

(US$)	2017A	2018A	2019E	2020E	2021E
EPS	1.36	1.41	1.30	1.74	1.75
GAAP EPS	1.36	1.41	1.30	1.74	1.75
EPS Change (YoY)	3.0%	3.7%	-7.8%	33.8%	0.6%
Consensus EPS (Bloomberg)			1.39	1.58	1.67
DPS	0.81	0.86	0.92	0.99	1.06

Valuation (Dec)

	2017A	2018A	2019E	2020E	2021E
P/E	32.5x	31.3x	34.0x	25.4x	25.2x
GAAP P/E	32.5x	31.3x	34.0x	25.4x	25.2x
Dividend Yield	1.8%	2.0%	2.1%	2.2%	2.4%
EV / EBITDA*	1.1x	8.4x	27.3x	17.1x	16.3x
Free Cash Flow Yield*	-1.0%	-1.3%	-1.8%	-1.3%	-0.9%

* For full definitions of *iQmethod℠* measures, see page 7.

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Stock Data

Price	44.18 USD
Price Objective	45.00 USD
Date Established	15-Jul-2019
Investment Opinion	A-1-7
52-Week Range	32.09 USD - 44.60 USD
Mrkt Val (mn) / Shares Out (mn)	9,531 USD / 215.7
Average Daily Value (mn)	51.25 USD
BofAML Ticker / Exchange	WTR / NAS
Bloomberg / Reuters	WTR US / WTR.N
ROE (2019E)	7.5%
Net Dbt to Eqty (Dec-2018A)	127.1%

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Timestamp: 21 August 2019 08:49AM EDT

iQprofile℠ Aqua America

iQmethod℠ – Bus Performance*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Return on Capital Employed	5.1%	3.9%	4.4%	5.2%	5.1%
Return on Equity	12.6%	9.7%	7.5%	8.6%	8.3%
Operating Margin	41.5%	38.7%	48.1%	70.2%	71.1%
Free Cash Flow	(97)	(127)	(170)	(120)	(87)

iQmethod℠ – Quality of Earnings*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash Realization Ratio	1.6x	1.9x	1.9x	1.8x	1.9x
Asset Replacement Ratio	3.5x	3.4x	3.3x	2.6x	2.5x
Tax Rate	6.6%	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	108.3%	127.1%	97.0%	100.1%	102.8%
Interest Cover	3.9x	2.8x	3.4x	3.5x	3.3x

Income Statement Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Sales	805	835	902	949	966
% Change	0.6%	3.7%	8.0%	5.3%	1.7%
Gross Profit	810	838	1,044	1,596	1,657
% Change	-1.3%	3.5%	24.6%	52.9%	3.8%
EBITDA	14,226	1,941	597	953	998
% Change	-33.6%	-86.4%	-69.2%	59.6%	4.8%
Net Interest & Other Income	(88)	(99)	(132)	(194)	(210)
Net Income (Adjusted)	**240**	**192**	**251**	**414**	**416**
% Change	**2.4%**	**-19.9%**	**31.0%**	**64.5%**	**0.6%**

Free Cash Flow Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Net Income from Cont Operations (GAAP)	240	192	287	442	446
Depreciation & Amortization	137	147	191	330	356
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	14	(15)	0	0	0
Other Adjustments, Net	(9)	45	(10)	(26)	(3)
Capital Expenditure	(478)	(496)	(639)	(865)	(885)
Free Cash Flow	**-97**	**-127**	**-170**	**-120**	**-87**
% Change	**NM**	**-31.5%**	**-33.9%**	**29.8%**	**27.7%**

Balance Sheet Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash & Equivalents	4	4	3	5	5
Trade Receivables	99	101	126	193	200
Other Current Assets	28	42	46	57	58
Property, Plant & Equipment	5,400	5,930	9,103	9,638	10,168
Other Non-Current Assets	801	887	2,462	2,462	2,462
Total Assets	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**
Short-Term Debt	117	160	288	310	331
Other Current Liabilities	167	239	258	309	315
Long-Term Debt	2,008	2,398	4,305	4,638	4,955
Other Non-Current Liabilities	2,083	2,158	2,158	2,158	2,158
Total Liabilities	**4,375**	**4,955**	**7,008**	**7,415**	**7,758**
Total Equity	**1,958**	**2,009**	**4,733**	**4,940**	**5,135**
Total Equity & Liabilities	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**

* For full definitions of *iQmethod℠* measures, see page 7.

Company Sector

Water Utilities

Company Description

Aqua America is a regulated water utility providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI. In Oct 2018, The company announced acquisition of Peoples Gas, a gas utility providing distribution services to 740,000 customers in PA, WV, and KY. The acquisition is expected to be closed by mid- 2019.

Investment Rationale

We see our Buy rating as supported by meaningfully above Street EPS projections on the back of its pending Peoples Gas business and above average ratebase growth.

Stock Data

Average Daily Volume	1,159,263

Quarterly Earnings Estimates

	2018	2019
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NA

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Smoothing Out the Impact: What Would it Look Like

With the election of the repairs tax benefit the company plans to pursue for 2020, earnings will see a large step up as the company expenses capital costs as opposed to depreciating them over a useful life for tax purposes. The magnitude of the initial increase will ultimately be determined by how much of the capital investment program qualifies for the treatment and whether the commission allows the company to use a catch up component for costs that are currently being depreciated. Our sense is that capital investments back to 2012 could potentially be privy to such treatment – albeit investment was likely more muted relative to the current capital plans – and we don't see management relying on such election. We perceive the commission is more inclined to give at least partial benefit of any catch up component back to customers. If management is able to reach an acquisition settlement – which we don't see as likely given the current timeline – that could include a balancing account to help drive more stable earnings growth in a similar mechanism that has been employed by NEE for storms. Alternatively, the company could look to manage capex in a way that accelerates qualified expenses y/y. We see the level of overall eligibility as the more critical question into the transaction's close and the potential Analyst Day later this year.

EPS Estimates

The exhibit below reflects our latest EPS estimates. Our '20-22 estimates shift -1% lower as we assume more conservative ROEs for the Peoples Gas business (albeit still close to 14%). We remain 3% above the street for '21 given what we still perceive as a strong earnings potential from the election of the Repairs Tax Benefit, regardless of the company's ability to capture any benefit from the catch up adjustment. Despite any additional efforts by the company to smooth the impact from the benefit, we perceive a continued upward bias to street estimates.

Table 1: EPS Estimates

EPS Estimates	2019E	2020E	2021E	2022E	2023E
PA	$0.84	$0.80	$0.77	$0.82	$0.86
OH	$0.07	$0.07	$0.07	$0.08	$0.08
IL	$0.08	$0.07	$0.08	$0.08	$0.09
TX	$0.07	$0.06	$0.06	$0.06	$0.06
NC	$0.04	$0.04	$0.04	$0.04	$0.05
Other States	$0.08	$0.08	$0.09	$0.09	$0.10
Water Utility	**1.18**	**1.12**	**1.11**	**1.17**	**1.24**
Peoples Gas	**0.17**	**0.68**	**0.72**	**0.77**	**0.81**
Parent & Other	*-0.05*	*-0.08*	*-0.10*	*-0.12*	*-0.14*
EPS	**1.30**	**1.72**	**1.73**	**1.82**	**1.90**
YoY Growth		*32%*	*1%*	*5%*	*5%*
Shares O/S	*193*	*238*	*238*	*250*	*254*
Fully Diluted Shares O/S	*221*	*254*	*254*	*254*	*254*
Previous EPS	*$1.30*	*$1.74*	*$1.75*	*$1.84*	
Consensus	**1.39**	**1.58**	**1.67**		
Consensus '19-'21 CAGR					
BofAML CAGR 2019-2021					
DPS	**0.92**	**0.99**	**1.06**	**1.13**	**1.21**
Payout Ratio	*71%*	*57%*	*61%*	*62%*	*64%*
Share Count	**193**	**238**	**238**	**250**	**254**

Source: BofA Merrill Lynch Global Research, Bloomberg

Valuation: PO Shifts to $46

The exhibit below reflects our latest SOTP on our new estimates and after marking to market for the latest peer multiples (27.9x vs. 26.2x and 20.7x vs. 21.2x for water and gas, respectively). We continue to apply a 1x discount to Peoples Gas to reflect removal of any sector takeout premium as well as discounting the strong returns we ascribe to it in the near term. Our lower gas contribution and multiple was more than offset by the sharp increase in peer water multiples. Overall, our water valuation shifts up $3, while lower gas contribution and higher corporate drag are a $2 headwind relative to our prior valuation. Net net, our PO ultimately shifts up $1 to $46.

Table 2: WTR SOTP

Water Utilities	2021 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*27.9x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		**30.2x**							
Water Utilities									
States	**2021E EPS**	**ROE**	**embedded**						
PA	$0.77	10.0%	**0.0x**	29.2x	30.2x	31.2x	$23	$23	$24
OH	$0.07	9.9%	**0.0x**	29.2x	30.2x	31.2x	$2	$2	$2
IL	$0.08	9.6%	**0.0x**	29.2x	30.2x	31.2x	$2	$2	$2
TX	$0.06	10.0%	**0.0x**	29.2x	30.2x	31.2x	$2	$2	$2
NC	$0.04	9.9%	**0.0x**	29.2x	30.2x	31.2x	$1	$1	$1
Other (including acquisitions)	$0.09	9.9%	**0.0x**	29.2x	30.2x	31.2x	$3	$3	$3
Water utilities total (ex-Peoples)	**$1.11**			*29.2x*	*30.2x*	*31.2x*	**$32**	**$34**	**$35**
Gas Utilities									
Peer Gas P/E		*20.7x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		**21.9x**							
	2021E EPS	**ROE**	**embedded**						
Peoples Gas	**$0.72**	13.7%	**-1.0x**	**19.9x**	**20.9x**	**21.9x**	**$14**	**$15**	**$16**
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			**-738**	50%			($369)	($369)	($369)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($370)	($342)	($399)
50/50 Weighted Drag from HoldCo Drag							($739)	($710)	($767)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							**$44.00**	**$46.00**	**$47.00**
Current Price								$44.42	
Dividend Yield								2%	

Source: BofA Merrill Lynch Global Research, Bloomberg

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Price objective basis & risk

Aqua America (WTR)
Our price objective is $46 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 1.0x discount to Peoples Gas as we expect earned ROEs to be driven down over time.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Specifically, we derive a value of $34 or the Water Business and $15 per share for the Gas utilities. We then deduct around $3 per share related to corp drag, which gives us our PO of $46.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Electric Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Aqua America	WTR	WTR US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
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	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
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	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	AES	AES	AES US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Pattern Energy Group	PEGI	PEGI US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Terraform Power	TERP	TERP US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

US - Electric Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst

iQmethod℠ **Measures Definitions**

Business Performance	**Numerator**	**Denominator**
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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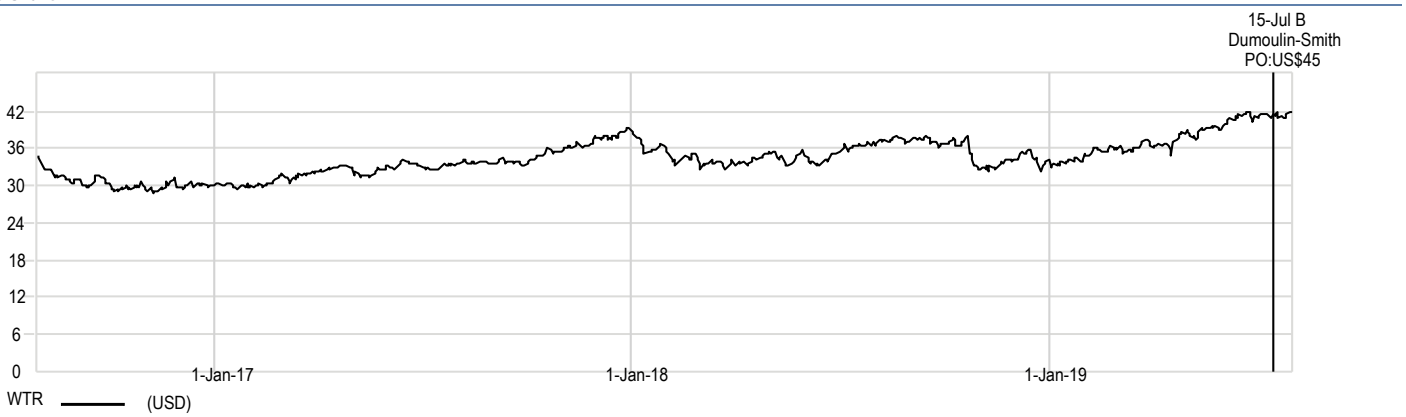
WTR Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Utilities Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	61	44.20%	Buy	47	77.05%
Hold	42	30.43%	Hold	30	71.43%
Sell	35	25.36%	Sell	27	77.14%

Equity Investment Rating Distribution: Global Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1516	51.23%	Buy	942	62.14%
Hold	687	23.22%	Hold	431	62.74%
Sell	756	25.55%	Sell	380	50.26%

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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North American Utilities & IPPs

Water on Wall Street: Takeaways from Our Inaugural Conference

Industry Overview

Splashing into the Water Industry

On Thursday, we hosted our Inaugural Water on Wall Street Conference in New York City with AQUA, AWK, AWR, CWT, HASI, MSEX, SJW, WTR, and YORW as well as a number of state regulators and industry experts. There were a variety of panels throughout the day with updates from company mgmt. and latest thoughts on trends and the state of the water industry. Key themes included what to make of emerging contaminates and expectations for further consolidation across the water industry against a backdrop of accelerating legislation momentum and stressed municipalities. Open the note for full takeaways.

Legislation, Infra Pressures to Drive Consolidation

Across the panels, speakers continuously emphasized the incredibly fragmented nature of the water industry. There are over 50K community water systems in the US, ~85% of which are publicly owned. This translates to a modest share for IOUs, particularly when contrasted with electric and gas (~3,000 electric utilities, the majority of which are structured as IOUs) and we increasingly view a clear cut opportunity for continued consolidation across the space. Given limited governmental funds and rising pension liabilities, we perceive a growing struggle around muni's abilities to inject the investments needed to maintain the water systems (with at least 1,200 systems deemed to be non-compliant with regards to the safe water act). Enabling legislation continues to pick up across states with FMV (FL likely to introduce next) & Single Tariff legislation gaining momentum and the Water Accountability Act starting to emerge (with IN following NJ's lead). We see this as creating a perfect backdrop to enable acquisitions - albeit not all of these states are created equal - with capital likely to flow to the most constructive jurisdictions. Meanwhile, discussions highlighted more limited participation from private equity players with underexposure to the space and a slower momentum around P3s in the US relative to other countries. Bottom line, we continue to expect an acceleration of tuck in acquisitions for the IOUs. One critical question is whether a constructive outcome with JEA in FL will drive more large acquisitions going forward.

Contemplating Emerging Contaminants

Another key focal point all day at the conference was around emerging contaminants and how they are changing the industry. Relative to the more publicized fire risks facing electric utilities, contamination is a critical – and likely still underappreciated - risk for the water industry. The EPA has currently established health advisory levels for PFAs at 70 parts per trillion, and concerns were voiced around how commissions will treat investment without a more clear cut standard. A handful of states have already started setting their own levels of stricter standards, and we perceive it as a likely driver of capital investment as awareness continues to be raised. While costs to treat will vary widely depending on technology and what contaminants are in the water, we perceive it as around $0.02-$0.10 per thousand gallons (note that AWK processes 1 billion gallons of drinking water daily). Bottom line, we would expect this to increasingly be a capital investment consideration and a potential driver for consolidation longer term as a more standard set of guidelines are adopted and municipalities are forced to comply.

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NYAW: New York American Water

JEA: Jacksonville Electric Authority

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How do we think about the sector?

Growth remains consistently robust and the merits of a premium to the electric and gas peers remains clear. We perceive the latest re-rating higher as preventing consolidation more broadly, but could very see a return to consolidation should sector valuations normalize closer to historic norms (on corporate side). That said, municipal deals will continue, albeit always on a protracted basis given the local approvals typically required. We perceive the sector as among the single highest quality within our coverage universe albeit with valuations (earnings yields) approaching that of the cost of debt, it's hard to see how re-rating improves barring significant shifts in interest rates lower. We maintain our Buy rating on WTR and Underperform on AWK.

So what do we recommend?

Despite the latest underperformance this week, we continue to stress the premium valuations ascribed to the water sector broadly, with the group still trading at 25.6x 2022 estimates (vs. electric and gas peers both trading at 18.5x). While we appreciate the scarcity element and visibility into longer term growth, we see risk as underappreciated at these levels – despite growing attention to contamination. We remain Underperform rated on shares of AWK, with estimates coming down out of their latest Analyst Day, and our concerns for convergence of sector multiples. Meanwhile we highlight our Buy rating on shares of WTR given their discrete opportunities into the expected closing of the Peoples Gas transaction; we perceive an upward bias to estimates upon implementation of the Repairs tax.

Water Universe

Table 1: Water Universe

						P/E Multiples					Earnings per Share					
	Ticker	Market Cap	EV	Short Int	Days	2018A	2019E	2020E	2021E	2022E	2018A	2019E	2020E	2021E	2022E	CAGR
Water Utilities																
American Water	AWK	21,409	31,584	2.2%	4.4	35.9x	33.3x	30.4x	27.9x	25.7x	3.30	3.56	3.89	4.25	4.61	8.7%
Aqua America	WTR	9,739	10,749	6.0%	5.2	32.0x	34.7x	26.2x	26.1x	24.8x	1.41	1.30	1.72	1.73	1.82	6.6%
SJW Group	SJW	2,005	2,092	0.8%	2.2	33.6x	39.6x	30.6x	27.0x		2.10	1.78	2.31	2.61		7.6%
Artesian Water	ARTNA	342	492	0.5%	3.4											
Connecticut Water Service																
Middlesex Water Company	MSEX	1,100	1,328	2.6%	4.5	32.2x	32.3x	31.4x	29.7x	26.4x	1.96	1.96	2.01	2.13	2.39	5.1%
California Water Services	CWT	2,423	3,479	3.9%	9.5	40.4x	35.1x	31.7x	29.2x		1.25	1.43	1.59	1.72		11.4%
The York Water Co	YORW	583	668	1.6%	6.9	44.4x	39.0x	37.7x	35.0x		1.01	1.15	1.19	1.28		8.2%
American States Water	AWR	3,178	3,789	4.6%	7.8	49.6x	42.1x	40.2x	37.8x	33.8x	1.74	2.05	2.15	2.28	2.55	10.0%
Average (ex AWR/YORW)		**37,018**		**2.6%**	**4.9**	**34.8x**	**35.0x**	**30.1x**	**28.0x**	**25.6x**		0.1%	14.8%	8.1%	8.8%	**7.9%**

Source: BofA Global Research, Bloomberg

Regulatory updates

Speakers highlighted views that surcharges including Distribution System Investment Charge (DSIC) programs are critical for return on capital that can be reinvested in future infrastructure projects. Commissions seem to be considering more innovative tools to help as well, whether DSICs, decoupling, or future test years. Commissioners also look to NJ and other states that are considering implementing water quality accountability standards – particularly to level the playing field and ensure smaller and medium-sized utilities keep in line with the same standards as IOUs. We see reducing lag for AWK in its core geographies remains a strategic priority with 59% tracked – and a return to lag in '20 thru rate cases emphasizing this need in particular. Regulatory support across key states remains clear and all the more pressing given litany of water quality issues lingering including lead, arsenic, and now proliferation of PFAS materials (principally fire retardants used that stay in environment; a particular issue on military installations).

We perceive legislation such as Fair Market Value legislation, Single Tariffs, and the Water Quality Accountability Act will all continue to gain momentum, setting up opportunities for further consolidation. We look to Texas as another evolving geography to watch for potential consolidation, especially for Aqua America.

Company Highlights

We include our latest company takeaways below:

Aqua America (WTR – Buy, A-1-7, $45.12)

WTR continues to await final approval for the pending Peoples gas acquisition, which we would expect to come over the next several weeks. Upon close, mgmt noted a path to growing the gas rate base at 8-10% for 15-20 years, a faster pace than the organic 7% that the company expects from the water biz. Nonetheless, mgmt highlighted their continued appetite for water and remains bullish on acquisition opportunities (Recall the company announced the acquisition of DELCORA following the initial Peoples transaction, which will already dilute down the 70-30 mix of water-gas that is expected upon close). We perceive less likelihood of mgmt further diversifying away from the pro-forma water & gas portfolio, with the company particularly talking down interest in anything non-regulated. Further – despite the recent move by peer AWK to optimize their portfolio and divest of NYAW and Keystone – we see more of a willingness from WTR to continue to pursue the thriving municipal market. When it comes to entering new territories, mgmt continues to suggest visibility to 30K customers in the state before jumping in. On the other hand, after previously exiting Florida operations, the company noted a lack of interest in pursuing JEA, and we don't expect the state as a likely candidate to grow the footprint (despite the pending FMV legislation). Following the close of the Peoples transaction, we expect the conversation to shift more towards Repairs Tax (and quantifying the impact given limited new details at this point), which we see as a critical driver of earnings and the reason we remain above the street. Reiterate Buy given upside to estimates.

American Water Works (AWK – Underperform, A-3-7, $118.43)

Following their Analyst Day earlier in the week, AWK highlighted their latest five-year plan of $8.8-$9.4Bn, which is $800Mn higher than the previous five-year plan. The company has also laid forward longer term visibility with a ten-year plan of $20-$22Bn for 2020-2029. With the latest guidance, mgmt. reiterated their expectations for 2019 EPS of $2.56-$3.64 while launching 2020 EPS guidance of $3.79-$3.89. Despite the recently announced pending sales of Keystone and NYAW assets, mgmt. has clearly articulated that they don't plan to sell off any additional assets, and the company should be poised to capitalize on the growing trend of M&A amid the latest momentum of legislation & compliance requirements. We further stress the recent decision to de-lever the balance sheet as providing additional flexibility to pursue acquisitions. That said, we reiterate our Underperform rating given the lofty valuation.

American States Water (AWR – Not Rated)

American States Water Company (AWR) is a consolidated low volatility water company that operates through 2 subsidiaries; 1) Golden State Water Company (GSWC) and; 2) American States Utility Services (ASUS). GSWC is a regulated water and electric utility the serves 261,000 and 24,000 customers across California, respectively. Meanwhile, ASUS is a contracted service for water/wastewater systems that serves military bases under 50-year contracts. The EPS breakdown is 76% GSWC (8% belonging to the electric utility with the other 24% coming from ASUS). The company expects to have continued military success as it won two RFP's for military bases over the past two years. Although the company operates an electric utility in California, mgmt is not overwhelmingly concerned about wildfire risk given the system does not contain any transmission lines and is also at 7,000ft of elevation (less winds). AWR emphasized that it has been able to continue to seek the benefits of forward test years.

California Water Service Group (CWT – Not Rated)

CWT mgmt. discussed the company's growth priorities, rate setting backdrop, and unique regulatory environment in the state. CWT recently filed a settlement with the CPUC in the company's general rate case which includes $609Mn of new capital spend

and $200Mn of authorized improvements spent in prior years – mgmt. notes this represents 85% of the company's ask, an improvement over the 80% established in the previous case. The company had been expecting a settlement before the end of the year but mgmt. now expects the timeline to be pushed to Q1 2020 given the ongoing PCG situation remains the top priority for the CPUC. Mgmt. flagged that the company actively works with regulators to remain in sync with state priorities, highlighting its decoupling mechanism as generally supportive of state water conservation efforts - in particular in light of the drought conditions seen during the previous decade. In terms of M&A (mgmt. has made tuck-in acquisitions in the past year in Washington state and Hawaii), the company sees systems with 1,000 – 5,000 customers as its target range. CWT plans to file its Cost of Capital with the CPUC next May, as public water utilities in the state synchronize their filings – mgmt. expects an improved cost of debt (4.5% currently vs 5.5% in the previous filing) to provide some headroom in the upcoming filing. Inverse Condemnation remains a risk for water utilities though not to the extent that it affects electric utilities. While water availability remains an issue in Western states including California, supply for residential and commercial customers is a lesser concern in mgmt's view with 80% of California demand driven by agricultural customers.

Middlesex Water (MSEX - Not Rated)

MSEX mgmt. expects to deploy $325m in capital in 2019-21 in its New Jersey and Delaware service territories. The spending will be driven by three projects including a Western Transmission Main ($50m), new treatment plant ($70m), and unlined and aging pipe replacement ($35m). The total plan is forecast by mgmt. to grow to $1.1B by YE 2021 with an approximate $800/300 split between NJ and DE. MSEX remains open to consolidating smaller municipal systems, having recently acquired a 1000-customer system in Delaware. While the company has not articulated a formal goal for EPS growth in the forecast period, mgmt. does expect its DPS payout ratio to increase from 49% in 2019 to a range of 65-70% in the coming years. MSEX is subject to a Distribution System Improvement Charge (DSIC) in both its NJ and DE jurisdictions which allows accelerated recovery of certain pre-approved investments subject to a cap. Mgmt does not anticipate approaching its 7% cap in Delaware in the near term owing to the system's relatively young age.

SJW Group (SJW – Not Rated)

SJW Group has completed transformative M&A activity – amounting up to 40 acquisitions in the last 10 years alone. The company sees these purchases as great for diversification when it comes to location (the company sits across four states), regulatory environment, weather, and availability of water; SJW Group sees diversification as a level of comfort and safety. Each geograpy provides different benefits: Silicon Valley, CA represents 60% of earnings, the Austin-to-San Antonio, TX region grew 16% last year (8% organically and the rest through M&A), and the CT and ME communities provide what SJW sees as the best in class regulatory relationships. The company has increased its payout ratio in recent years to increase its competitiveness with other companies. Finally, we note the company now has the third largest pure-play water utility ratebase in the country.

The York Water Co (YORW – Not Rated)

The York Water Company (YORW) is a water utility that serves customers ~200K across the state of Pennsylvania and is currently the oldest stock that trades on the NYSE (founded in 1819); The company currently has a 42/57% debt/equity ratio coupled with an A- credit rating from S&P. The company also has an average demand of 20Mn gallons of water per day (vs. 40Mn capacity) and is replacing 1% of its infrastructure per year (based off a 100yr rate). Of all of the publicly traded water companies YORW is the most expensive; it trades at 35x '21 earnings vs. the comp set avg of ~29x (inclusive of YORW). In addition to its water utility services, the company also owns and operates wastewater collection systems, which mgmt thinks will grow near-term given constructive legislation in the states (Act 11). The act ultimately combines water and wastewater revenue into one – meaning that the company can now buy a wastewater

system and allocate the cost over all its customers, thus preventing rate shock. Further positive legislation in the state includes Act 120 which allows the company to replace led lines at no cost to the customer. Mgmt emphasized that their presence in one state – and a constructive one at that – as a key advantage relative to larger peers.

PE investment in water infrastructure

Broadly, private equity investment in infrastructure has increased at a 16% CAGR over the last 10 years, to nearly $500bn by 2018 (incl. $312bn unrealized value, $179bn dry powder). This has resulted in upward pressure to valuations on private infra asset valuations, while fundamental valuations have not changed materially, given the tremendous amount of capital looking to be deployed. Water assets, however, have seen limited activity, averaging only 2.8% of annual infrastructure deal flow (3% water in 2018). Select opportunities do exist in certain areas including industrial water, water-as-a-service, technology deployment, and on-site residential wastewater.

We see this as driven by a number of challenges to water investment. These include:

1. **Investment size:** Few opportunities in the $200-$500mn EV range, with the market generally divided between larger publicly traded companies and municipal assets as well as many much smaller systems. Roughly 56% of systems serve less than 500 customers, representing only 1.6% of people served.
2. **Rising valuations:** Many assets reaching above 2x rate base valuations
3. **Change of control regulations:** Commissions skeptical of the PE model
4. **Limited flow of Public-Private Partnerships:** Municipalities have shown limited willingness to privatize facilities
5. **Diverse asset class:** Wide range of opportunities including IOUs (investor-owned utilities), water technologies, wastewater, water-as-a-service, etc.
6. **Political-related issues**

Storm Water Remediation

We highlight sustainable infrastructure opportunities as including stormwater remediation, environmental restoration, and water & wastewater infrastructure. Within wastewater infrastructure, the American Society of Civil Engineers estimates $271bn of needed facility upgrades in order to meet demand of an incremental 56mn users by 2032, while $1tn may be needed to update and upgrade water infrastructure.

HASI sees opportunities within storm water remediation, including $7mn investment in four projects to slow pollution runoff into downstream waterways in the Chesapeake Bay area. Waterway restoration and wetland mitigation credits are another opportunity: credits are generated through state or private restoration projects, and then banked and sold to offset environmental impact. In addition to the Chesapeake Bay and Great Lakes areas, these have some prevalence in the Gulf Coast with refineries needing to mitigate the impact on land in order to obtain permits for construction.

Public sector funding poses various limits. Federal funding includes the WIFIA (Water Infrastructure Finance and Innovation Act of 2014) program, which only funds 49% of the project cost, with a 35-year maximum duration. While state revolving funds have a low cost of capital with a 30-year maximum loan term, projects are ranked with preventative maintenance and plant expansion not considered to be a priority. Tax-exempt funding sources need voter approval and also take time to implement.

Private capital is also available for infrastructure funding purposes, with water public-private partnerships (P3) an option, although we note these can be challenging to find given a limited number of opportunities as well as municipal hesitancy. Specifically, P3s are contracts that allow a private partner to construct, upgrade, operate, and/or manage

a public service facility or system while investing capital, while the public entity remains ownership; income generated is shared between the two parties.

While HASI did not specify return criteria for their water investments, we note that their sustainable infrastructure portfolio yields 5.6% while their BTM portfolio has an 8.0% yield; their overall portfolio yield is 7.7% as of 3Q19. HASI expects water returns to increase over time given an underserved market with pressure for infrastructure investment to build in this market.

Price objective basis & risk

American Water Works (AWK)
Our PO for American Water Works is $130. We apply a 26.0x P/E multiple to American Waters 2022E earnings based on the water peer multiple and a 8.3% group EPS CAGR for '18-'22, as we see AWK largely driving the peer multiple as the largest publicly traded water utility.

Risks to the downside are increase in market interest rates, potential impact of tax reform on utilities, operational errors, changes in valuation levels for water utilities. Risks to the upside are accelerating muni acquisitions, multiple expansion, and constructive legislation in regulatory jurisdictions.

Aqua America (WTR)
Our price objective is $47 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 0.5x discount to Peoples Gas as we expect earned ROEs to be driven down over time.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Aqua America	WTR	WTR US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	AES	AES	AES US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Terraform Power	TERP	TERP US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

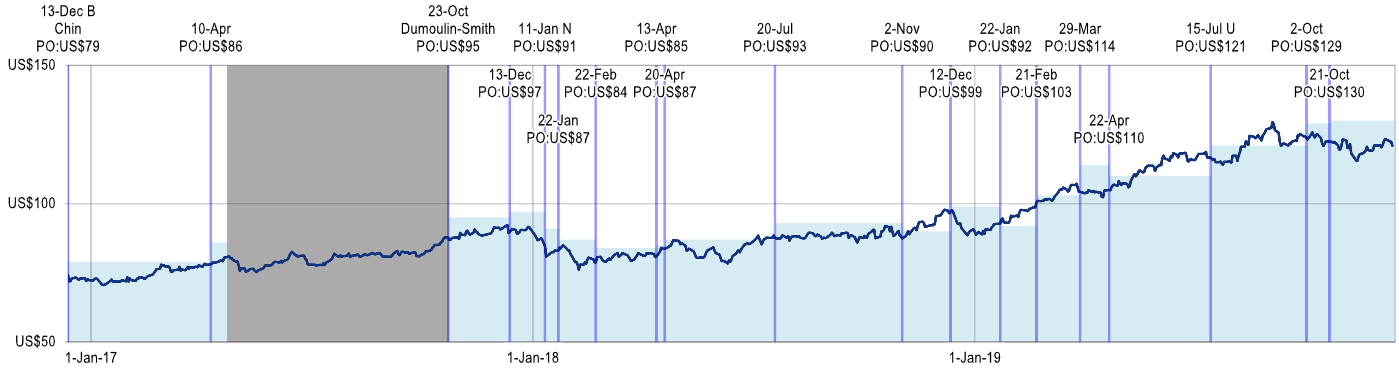
North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Pattern Energy Group	PEGI	PEGI US	Julien Dumoulin-Smith

Disclosures

Important Disclosures

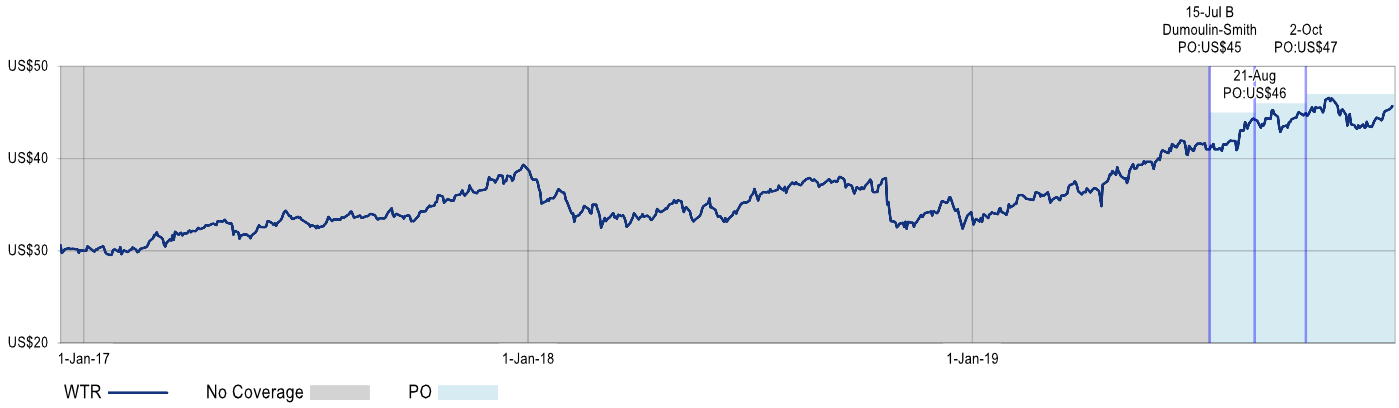
American Water (AWK) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Aqua America (WTR) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Utilities Group (as of 30 Sep 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	67	47.86%	Buy	51	76.12%
Hold	36	25.71%	Hold	24	66.67%
Sell	37	26.43%	Sell	26	70.27%

Equity Investment Rating Distribution: Global Group (as of 30 Sep 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1517	50.30%	Buy	964	63.55%
Hold	680	22.55%	Hold	434	63.82%
Sell	819	27.16%	Sell	408	49.82%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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US Electric Utilities & IPPs

The Virtual Boston Conference Day 2: Who Said What?

Industry Overview

Summarizing the key events & updates

Our latest sector-wide Power, Utilities & Renewable Leaders conference concluded yesterday. While we hosted 50+ companies overall, stand out meetings yesterday included PEG, FE, ETR, and PCG. Day 2 Company write-ups included below include: AEE, ATO, BKH, CWEN, CMS, D, DTE, DUK, EIX, ETR, WTRG, ES, FE, HASI, NI, OGS, PCG, PNW, PEG, SR, RUN, VST, XEL.

On PEG, we see mgmt. as confident in addressing ongoing dockets and more critically poised to further its divestments in Power, offset dis-synergies, and ultimately seek further refinements of ZECs eventually too. Offshore appears clear too as a further avenue of interest for investors. Meanwhile, FE (Neutral) stated they believe a rate case could come sooner than '24, albeit with just -10c at risk based on regulatory capital structure derived off ratebase; this outcome could be substantially more accretive than our earlier concerns. That said, the pathway to such a rate case filing amidst numerous other pending dockets – and resolution in this favorable regard remains pending a lot of execution. As for ETR, we see mgmt. as quite firm in its expectations for an AR FRP extension to materialize by March 15th (rather than conceding the point of any eventual rate case). Further, LA settlement by late March also key. While we see capex cut risks under less bill headroom, we see affirmation of regulatory structures altogether as enabling some improvement off among widest discounts in group. Finally, PCG's ability to sidestep equity needs and pivot dialogue more constructively with CPUC continues to impress despite the continued pressure on the shares.

Financing with Preferreds continues to expand

Amidst an effort to limit dilution given wide discounts (EIX, ETR) and overall limit/delay dilution (NI), we look for equity-linked alternatives to prove a growing trend in utilities. With ~50% equity content treatment from the rating agencies and modest coupons, we perceive a sharp shift in financing alternatives. FE also affirmed its intent to evaluate such avenues (seemingly over asset sales) to fund any eventual B/S fix required. We see this as an expanding subject of focus from many companies – watch SEC filings for clues on extent of any such offerings.

Texas: Deep Freeze implications

So much of the conference was dedicated to understanding the vast array of implications. While a handful stand out as beneficiaries (SR principally; SO in part), we are looking at an array of cautious datapoints around cost recovery and rate impacts. With few datapoints from regulators yet on the 'crowding out' effect yet of higher fuel cost recovery charges we believe the discount will remain for some time (despite affirmation from many that recovery should prove forthcoming – whether through normal recovery mechanisms or discrete securitizations). We stress Gas LDC inflation in particular remains a cautious point. *We don't expect sharp recoveries post Texas.*

The Bigger Picture from the Administration

Few companies had good anecdoctes, but those that did are focused on transmission.

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Just Where is Biden Going?

While front and center issues such as Texas rate impacts dominated dialogues this week, the bigger picture question of just where and how this new administration intends to achieve its clean energy goals remains opaque. We note the EEI CEOs appear to have had an initial meeting with DOE Sec Granholm this week alongside our conference. Early datapoints would appear to indicate a clear focus on transmission, consistent with our earlier discussions with the FERC. While XEL is among the first companies to come back with an expanded transmission plan in response to the election (and its own state targets for 80% by 2030), we expect others to come back later this year with revised outlooks. This view on transmission was shared by many, but remains in part dictated by the planning processes of key RTOs such as SPP and MISO. This should come in three forms: 1) larger project planning awards; and 2) addressing interconnection queues and processes – helping to accelerate deployment; and 3) on the margin, we could see some greater authority on eminent domain granted.

Where is this transmission upside coming? We heard it across the board. AEE, FTS, WEC would be direct beneficiaries of processes in MISO (updates later this year even with latest plan release possible), while others like SO and DUK could see those opportunities arise out of yet to be finalized generation resource planning. Even if unsuccessful in garnering greater renewables for itself, DUK should benefit from added transmission spend from legislation.

What appears clear to us though is that this spending may not materialize meaningfully for some time – adding to longer-dated prospects in the 2024+ timeframe. While we've perceived an acceleration for some time, we see growing acceptance of both a renewed uptick in transmission spend in 2024-2026 as well as generation replacement in this period as well. We see further roll-forwards of updates late this year (EEI principally) inclusive of 2026 in 5-year views as particularly relevant in initially reflecting this accelerating fact pattern.

Biden & subsidies – where to go from here?

We remain sober on more subsidies directly for clean energy – seeing this as potentially protracted. Rather, we remain focused on storage benefits. This remains the arena in which a new subsidy could bolster the market immediately and seemingly offers greater margin to utilities and developers alike given the integration 'complexity' relative to thin margins on offer for solar today.

The blowback from Texas on resource planning

While we identified this in our Day 1 takes, we stress a focus on *retaining assets while still adding renewable resources*. The focus on costs remains on proving out the economics of adding additional solar & wind relative to the *variable* cost of dispatching coal assets (rather than all-in fixed cost structure - which are not trivial). Shifting towards seasonal dispatch for coal assets – principally winter – appears an over-arching trend that started in the Northeast but appears to be spreading elsewhere. On-site fuels during harsh winter weathers that challenge gas deliveries - this includes both coal but especially oil resources to backstop the grid.

Expect more discussion grid support with more renewables too. XEL's next update would appear to be a $0.5-1.0 Bn voltage support effort to pair with its transmission proposal. This remains another avenue to watch peer companies propose, particularly across vast distances in the West with ever greater renewable penetration.

Competition is pervasive

Owning the renewables directly remains a challenge for utilities – and we view a backdrop of competition as adding a greater degree of opacity around capex planning. Assumptions on the split of PPA vs owned opportunities in ratebase is key, in our view (SO, DUK, but also for other smids too: EVRG, POR, PNW).

Ameren (AEE)

Our update with Ameren mgmt. covered several key pending pieces of legislation and their relative levels of support. We note that downstate legislation picked up a key sponsor in the chair of the Utilities Committee which is an incremental positive. While AEE mgmt. expressed clear support for the downstate legislation and its modification of the ROE mechanism to use an average of national rates, it remains unclear to what extent competing legislation including the Clean Energy Jobs Act (CEJA) can garner further support or potentially be reconciled with downstate legislation. Maintain Neutral on AEE.

Renewed support for higher transmission spending

Ameren mgmt. reiterated the growing need for higher levels of investment in regional transmission. Recall that on the Q4 call the company flagged investment in "multi-value" transmission projects (MVP) across its Midcontinent Independent System Operator (MISO) footprint in order to increase the reliability of the grid and ease regional congestion, particularly in light of its own ambitious renewable buildout plan. While such investments would likely have modest upside in the current investment plan through 2025, mgmt. reiterated that it sees upside and potential for sustained rate base expansion as part of its longer-term spending plan, in particular during the 2025-29 period. Ameren's current 5-year plan includes a robust +11% transmission rate base CAGR through 2025, which mgmt. notes does not currently include multi-value projects which have largely been completed, suggesting upside beyond the current plan if a new group of projects were proposed and approved by MISO and relevant regulators.

Downstate bill garners key support

We note that the downstate energy legislation currently making its way through the state house in IL recently picked up the sponsorship of the chair of the influential Utility Committee. Among the key components included in this bill is a modification of the current formula-based ratemaking mechanism and its 580 bps adder in favor of one based on an average of authorized ROEs from the previous 12 months adjudicated nationwide. While we note the proposed methodology is necessarily backward-looking, it would certainly serve to align IL allowed ROEs more closely with national levels as average ROEs tend to drift higher or lower over time. While the current 30Y UST + 580 bps methodology was originally intended to achieve the same goals, today's low levels of interest rates have resulted in far below-average ROEs. The downstate legislation also includes a 40 bps performance-based band based on measurable metrics.

Rate case filing in MO concurrent with wind approvals

Ameren expects a busy regulatory schedule in MO with an impending base rate case filing coming later this month, as well as filing for certificates of convenience and need (CCNs) for the latest renewable generation proposed in its latest resource filing. In MO the rate case process typically lasts 11 months and the most recent wind projects received CCNs after 5-6 months, suggesting that by Q3 the contours of both processes should come into focus. Recall that MO has been a relatively constructive jurisdiction of late, in particular with Ameren's most recent case outcome achieved in Q1 of 2020 given substantial cost offsets more than made up for a top line reduction in revenues and ended up with a ~$100m post-tax annual increase. While Ameren needs to make this filing in order to add its soon-to-be-completed wind generation into rates we note that the current bias across the sector remains toward staying out of rate case filings given regulatory sensitivity around bill increases during the Covid pandemic.

Atmos Energy (ATO)

How to think about financing needs with upcoming $2.5bn bill due

With ATO one of the few gas utilities not to have short-term financing in place (despite $2.8bn in liquidity), mgmt. highlighted that it would expect to have its financing in place by the end of March when bills are due. That said, the company continues to leave open the door for some equity content (as well as ST debt, LT debt and cash on hand) to meet its obligations. We also wonder if there could be some sort of posturing as a negotiating tactic with 3rd parties given the different approach that ATO has taken. At the end of the day, mgmt. did reiterate its 2021 EPS guidance and LT EPS CAGR of 6-8%, so it should provide some confidence that there is clearly a preference for debt (as it awaits approval from regulatory bodies).

Not much new on strategy for recovery or lessons learned in policy hearings

Mgmt. highlighted that hearings last week with executives didn't provide much info given the focus on energy needs, and it still remains too early to predict its regulatory strategy for recovery. Securitization also remains an option in Texas with the session ending in May (special session in June/July if needed), although here too it remains very early in the process and could be somewhat protracted given subsequent approval required from regulators (assuming a bill is introduced and passed) and the time to get financing in place. From a regulatory standpoint, mgmt. highlighted that there is a peaking component to consider for recovery, although the base charge component is 59% of the customer bill; we perceive the peaking component could be somewhat tricky given the likely pushback from those without flowing natural gas. Given the substantial impact to customer bills and discussions from policy makers around these concerns, we see this likely an overhang on shares until more clarity evolves.

$2.5bn seems like a best estimate at this point

In terms of reducing the $2.5bn number, mgmt. highlighted it has good confidence in its estimate and it's still going through force majeure considerations (freeze offs in the West). At this point we don't necessarily see ability to further mitigate these gas purchase costs.

Black Hills Corp (BKH)

Texas Setbacks, but Confidence in Plan

Ahead of our meetings with management, BKH reaffirmed their recently issued guidance despite the latest cold weather challenges - with the company previously disclosing a ~$600Mn elevated purchased gas cost and $800Mn ST debt facility in tandem to improve liquidity. As we await firmer details around regulatory recovery across jurisdictions, we note that several of their states have issued orders requesting applications to seek deferred accounting treatment and we believe recovery is likely over the next 2-3 years (albeit with Arkansas and Kansas potentially more protracted).

Despite the latest setbacks, discussions more broadly continued to highlight confidence in the company's recently laid out five year outlook and inaugural long term trajectory of 5-7%. We further don't view the latest events as impacting equity financing timing with conversations suggesting constructive conversations with rating agencies (recall FFO thresholds are 13% and 12% for Moody's and S&P, respectively) and levers to avoid breaching these thresholds ahead of incoming cash.

Elevated Level of Spend and CO Developments on the Horizon

We perceive particular confidence to achieve at least a $600Mn run rate in annual spend to drive 5-6% growth, with potential for yet elevated levels of investment and asset-light opportunities to further boost margins. This should help offset any challenges around ROE pressures for any upcoming rate cases to help drive elevated growth. After the Colorado commission extended the comment period for the RRR, comments are now due early next week after the earlier rate case dismissal. If a constructive resolution is reached, look for the prior rate case to be reinstated on a 60 day delay from the original procedural schedule that sought new rates for this Fall. If the company has to re-file the rate case, we would look for a new filing in CO this summer. Either way, watch parallel developments around efforts to incorporate another rider for additional relief with more minimal lag.

We reiterate our Buy rating on the shares, stressing elevated rate base growth at an attractive valuation – and see the latest guide of 5-7% LT EPS growth affirming our confidence in what we view as a Best-in-Class SMID.

Clearway Energy (CWEN)

Still confident on 5-8% div growth with upper end of range for '21

Mgmt reaffirmed confidence on LT div growth of 5-8%, with the upper end anticipated for '21 even after adjusting for the the one-time $20-30mn TX storm impact. The high end is still expected (with $325mn CAFD outlook also intact for '21) given a number of significant dropdowns of late, with pro forma CAFD recently raised to $385mn, up $40mn from $345mn after including Agua Caliente (closed Feb 3rd) and the 1.6 GW CEG co-investment. Other opportunities in the pipeline include the 1.1-1.7 GW co-investment with CEG (target closings 2021-2023) which is in the works, in addition to the recently signed agreement for the 264 MW Mount Storm Wind. Notably, this project has a 10-yr contracted energy hedge; we note ~$10mn CAFD on $96mn corp capital, or a 10.3% CAFD yield, with this deal expected to close 1H21. With ~1.7 GW of wind and ~600 MW of solar in the portfolio, mgmt appears to be comfortable with this level of exposure to more volatile wind production, given the higher ~9-10% IRRs to be found vs. solar.

More color on the financing strategy for growth

Mgmt has noted that all commitments made through Nov 3rd have effectively been funded, with deals thereafter to be funded via a combination ATM issuance as well as potential block equity deals in cases where it makes sense, in addition to project debt, green bonds, and retained CAFD. We note CWEN recently issued a $925mn green bond (3.75% senior unsecured notes due 2031) to finance new projects and refi the $600mn 5.75% senior notes. Mgmt highlighted increasingly greater demand for higher-yield debt.

Addressing TX: No change to guidance, need for upgrades will be assessed

Clearway had previously estimated a direct cash impact of $20-$30mn from the recent ERCOT weather event, prior to any potential mitigation factors (although we note cost savings will likely be limited). The impact appeared to have been driven by weather-driven wind outages and contractual hedge obligations from certain facilities. The company is currently assessing potential initiatives that could improve fleet resiliency in response to the TX event. That said, given the low-probability nature of this event, we expect a cost-focused approach to this endeavor. We note that a minority (likely well below 10%) of CWEN's renewable PPAs are firm commitment contracts.

CA gas assets: Re-contracting opps vs. up for sale?

Our discussions also focused on the improving backdrop for Clearway's contracted gas assets in California (two CCGTs, one peaker), with existing PPAs set to expire in 2023. Mgmt continues to assess all options including a combination of bilateral re-contracting on its gas assets given the robust environment (with mgmt aiming for ~7-10-yr contracts for greater earnings stability) and/or divestment of some or part of its ownership. We expect that addressing this uncertainty will be a priority in 2021. We note recent multiples as high as 14x EV/EBITDA from recent comparable West coast deals. For re-contracting efforts, we estimate that RA market prices may be in the $5-6/kw-mo range, with upward movement likely since this summer's rolling blackouts (we continue to assume $6/kw-mo for El Segundo, Marsh Landing, and Walnut Creek).

CMS Energy (CMS)

IRP Focus – Accelerating coal retirements, incremental renewable oppty

Among key discussion focuses with CMS mgmt included its upcoming IRP filing in June. Mgmt continues to indicate likely focus on accelerating coal retirements with Campbell 1 and 2 scheduled for 2031 and Campbell 3 scheduled for 2039 given latest state emission targets set, which could drive incremental renewables spend. We note that Campbell units 1 and 2 account for a relatively smaller portion of overall rate base (4%) than unit 3 (5.5%) and thus we see these as the most likely candidates for a potentially *accelerated* retirement when CMS releases its next IRP proposal. Indeed our channel checks with interveners including the Sierra Club identified these units as a focus of negotiations with environmental groups, further bolstering our view. Recall, while CMS is only required to file an IRP every 5 years, mgmt expressed a preference in filing more frequently with a voluntarily submission every 3 years, given the clarity provided from tri-annual IRP filing cycles around capital spend around resource planning.

Indeed discussions with mgmt affirm focus on retiring remaining coal units with 5 remaining (2 to be retired in 2023 already under first IRP filing in 2018). In terms of replacing capacity with accelerated retirements, mgmt expressed IRP filing to focus upon incremental renewables beyond 6GW of solar through 2030 already approved in the last IRP as well as on battery energy storage deployment, and demand-side management.

ERCOT comparison – better managed wind assets/grid, more extreme conditions

With the latest cold snap and outages across TX, discussions were focused on resiliency with mgmt keen to address key differences between its own operations and ERCOT. In terms of underperformance of wind assets in ERCOT during the cold snap as blades froze, CMS mgmt emphasized that MI was substantially colder than TX (~20 degrees) during this same period without the same issues for its wind assets. To this point, CMS mgmt expressed its wind turbine generally all have lubricant and conditions for components such as the gearbox, paired with its ability to forecast icing conditions to take pre-emptive actions to prevent asset failure, all without having to reach the point of heated turbine blades mentioned in 'winterization' discussions on ERCOT. CMS emphasized its engineering team does a lot of work on loss of load expectations during extreme weather conditions and actively works with MISO around backup and reserve margins – further noting the capacity market in MISO supporting resiliency and appropriate grid planning relative to failures in ERCOT.

That said, given that CMS is already embedding loss of load situations and managing extremes effectively, with its upcoming IRP – despite likely greater scrutiny on reliability and resiliency side of the equation – mgmt does not expect a significant amount of incremental capex from this angle.

With some peer utilities expressing early discussions on shift from coal retirements to usage as a seasonal asset, CMS mgmt was firm in its view that this is neither economic nor feasible (with CEO expertise incl. having operated coal plants). Coal units require consistent management as coal can spontaneously combust when wet and coal piles freeze, making usage as a peaking unit impractical relative to investing in natural gas - in additional to lower heat rate/efficiency even when retrofitting an existing coal unit to gas. Carbon capture is also better for gas relative to coal.

How to effectively decarbonize heating – gas infra remains critical here on H2

Discussions also focused upon CMS mgmt's long-term plan to future-proof its gas pipeline infrastructure in tandem with its plans. Mgmt notes that heat pumps are generally not effective below a certain temperature range (below 30 degrees) with heat pump homes requiring natural gas as a backup still in MI. Notably, mgmt highlights that fully shifting all space heating in MI to electric (currently 75% nat gas and 25% propane – latter being more rural areas) would increase customer utility bills 3x (also needing

modification of homes to HVAC systems) and would also substantially burden the electric grid flipping CMS from a summer peaking utility (as its resources are planned for) to a winter peaking utility with 3x higher peak.

As such, CMS mgmt emphasizes its nat gas pipeline infra remains essential in the most economical way to decarbonize space heating. Near-term CMS expects to reach net-zero methane by 2030. For long-term decarbonization, green H_2 remains particularly notable for use in decarbonizing space heating, but importantly metal pipeline is faced with stress corrosion cracking at even 20% H_2 blending with nat gas. As such, CMS emphasizes a continued trend of replacing cast iron pipe with plastic with 14K miles of plastic pipe and 12K miles of metal pipe in its system currently. Its $10Bn in spend through '30 is primarily to replace 2K miles of metal pipes with plastic and to reduce methane to reach net zero methane target by 2030. Beyond pipe replacement, mgmt notes H_2 space heating would require upgrades of appliances in homes as well as likely upgrades to valves and packing at points where pipe is sealed. CMS emphasizes working closely with organizations such as EPRI on H_2. Bottom-line, decarbonizing space heating presents a substantial investment runway with long build-out process for CMS.

Additional areas to support decarbonization include energy efficiency (1% annually supports ~$10mn in earnings), bio-sequestration (tree planting), RNG, and carbon capture.

Nat gas storage potential to be used as green H2 storage for seasonal ESS

With its substantial net gas storage fields, CMS emphasizes potential to be used as storage for green H_2 produced long-term as well, where H_2 can then be used for either space heating or even for electric generation with retrofits to gas plants (CMS mainly uses GE and expects retrofitted turbines capable of handling green H_2) as seasonal long-duration storage assets.

Dominion Energy (D)

Remain comfortable w/ the VA construct: Filing suggesting no refund a positive

For the upcoming triennial review (2017-2020), mgmt. highlighted it intends to file with the State Corporation Commission (SCC) at March end, suggesting no refund required. We stress GAAP earnings, including the ~$630.7mn expense in 1Q20 that will reduce reported 2020 earnings (14+% ROE otherwise) and $247mn in 2019 for coal plant retirements. We note a key consideration for the upcoming triennial review will be treatment of the coal plant retirement amortization in which D elected to period expense these plants (upfront expense) given the discretion of the SCC. We also view ability to utilize $300-325mn in CCRO investments as a positive, and remain comfortable with potential outcome here. While the time period is expected to be relatively long, with a hearings in Aug/Sept. and a final decision in March, we view both the commission makeup (with Navarro a clean energy proponent) and the construct as assuaging concerns on this front. *We still look for updates from the SCC to see how the new composition votes as there are few datapoints subsequent to her nomination to the role.*

SC rate case pause continues: settlement discussions moving forward

The SC rate case remains on 6-month pause as the DESC agreed in the January 2021 rate proceeding. The parties are required to report monthly on settlement progress with parties currently in settlement discussions. We continue to view the core debate to be around the rate increase during a pandemic. We continue to estimate that the financial impact to be relatively minimal (~2.5c) with a delay, although see the concession from Dominion as likely garnering additional political capital in the state. We still see probable bias for a settlement, with the SC Public Service Commission (PSC) indicating a preference for a settlement vs a fully litigated case, where we estimate a 9.5% authorized ROE (vs staff rec. of 8.9% and company request of 10.25%) as a reasonable outcome. Mgmt. voiced confidence in the case that it filed noting it has not had an SC base rate case in 8 years. We note that while securitization has come up in the past and is likely to continue, mgmt. seems less concerned on the margin given similar proposals have been defeated. While storm securitization is a useful tool, we believe securitization of NND would not be beneficial to D's EPS outlook, although see this as a low probability event.

Combing through the details on capex: watch storage and solar spend

Mgmt.'s 5-yr capex ('21-'25) of $32bn reflects a 43% increase from prior 5-yr plan with 87% of the $23.8bn in spend VA rider eligible (potential for triennial rate review offsets) and base rates diluted down ~26% by 2025. This capex program yields an impressive rate base growth in VA at +13% and 9% overall. We note discussions with mgmt. indicated that there could be some variability (to the upside) with solar spend through federal procurement/policies, although the current law allows for up to 1GW per year (2/3 rate base and 1/3 PPA), coinciding with mgmt.'s current plan. On storage, mgmt. highlighted that this $2bn in spend is likely somewhat less defined given 3 pilot projects ongoing, although did highlight its pumped storage project as progressing well. Undergrounding of distribution appears to be solidified. Net-net, we continue to view the capex profile as favorably, although look for variability in storage and/or solar.

Winter weather event impacts muted

Mgmt. highlighted minimal impacts in terms of fuel purchased costs for its gas LDCs with Utah having some mitigates due to storage and the wexpro model with 50% of supply under a rate base model. No other impacts on assets in Texas were noted (small asset on Ft. Hood, but no impact).

DTE Energy (DTE)

Our update with DTE focused on company mgmt's ongoing efforts to maintain bill stability including its current electric case stayout which is aided by strong residential sales which enabled the company to push back its deferred tax item recovery until December. On the non-regulated side we see some competitive pressures on the Renewable Natural Gas (RNG) portion of the Power & Industrial (P&I) part of the business given additional entrants to the market of late and expect the Energy Trading segment to post a positive contribution in Q1 from long positions that benefitted from price spikes following last month's severe weather. Encouragingly mgmt. affirmed confidence in attaining 5-7% EPS growth on a consolidated basis (post-spin remainco) in '22 despite tax credit earning cliff pressures and share count dilution from settlement of its equity units. Maintain Buy on DTE.

Steady electric rates through '22 expected

Mgmt. provided an update on the expectations for the next electric rate case filing, given strong retail sales to start the year. Recall that the current electric stay out was partially achieved by the utilization of an accumulated deferred income tax (ADIT) asset that was scheduled to flow back beginning in April, though DTE has recently filed to push back the recovery timeframe to December, allowing for rate stability through most of 2022. Given the rate case process in the state of MI that requires cases to be concluded within a 10 month window, the company expects to file in late 2021 for rates effective the following year. The current pending gas rate filing requesting a $195m increase based on a 10.25% ROE is expected to reach a resolution by the end of the current year (current ROE is 9.9%).

Cold snap was a net positive

DTE mgmt. reported strong performance of its electric generation fleet during the extreme cold weather seen in Feb with no material outages or customer impacts – given the strong uptime of its generation fleet DTE electric was able to export 2,000 MW to the MISO grid, while this does not impact earnings it did generate a $20m credit via the company's power supply recovery mechanism which will flow back to ratepayers – an incremental positive in the company's efforts to maintain stable bills in the absence of a rate case filing. The Energy Trading business generated gains as a result of being long spot pricing at the time of market volatility in mid-Feb, though mgmt. reported that the segment remains mostly a support function and does not hold large unhedged positions, in particular on the short side where losses could potentially be unlimited. While some midstream customers, particularly in the Haynesville basin, experienced well shut-ins, the majority of contracts are demand-based and mgmt. reports no meaningful impact on Q1 results from lower levels of activity during the severe weather.

RNG contracting more competitive

The P&I segment principally operates in the RNG market and on-site cogeneration for industrial customers. Mgmt has experienced a slightly more competitive environment in bidding for RNG inputs (manure from ag operations) where contracts have multi-year tenors, though the company continues to actively source new supply and to bring on new projects despite the more competitive environment. Demand, in particular from California given the Low Carbon Fuel Standard (LCFS) remains robust and mgmt. reports being well contracted in the near term. Despite previously pushing out its renewable energy fuel (REF) tax credit earnings cliff to the end of 2021, mgmt. sees a further extension as unlikely though expects to be able to backfill lost earnings over time.

Duke Energy (DUK)

Still waiting on key updates in NC: Rep Ark commentary positive on margin

With upside to the LT plan largely predicated on the IRP/legislative process in NC where, we wonder just how much renewable ownership is possible (relative to HB589 at 30%) and whether mgmt. can hit the top-end of its capex plan in '25-29 ($65-79bn, RAB of $140-150bn in '29) without progress on the legislative front. Mgmt. highlighted that it assume 25-50% ownership, which it feels is conservative. Still with public data points likely few and far between, aside from Rep. Dean Ark (co-chair of the Committee on Energy and Public Utilities) commentary that suggested intent to pass legislation this year and cross-over date for bills in May, we continue to wait for progress on this front. Meanwhile, mgmt. confirmed that regulatory reform such as multi-year rate plans (MYRP) and ROE banding are not needed to hit the mid-point of guidance, although would indeed enhance the LT plan given it reduces regulatory lag. We note that while the Rocky Mountain Institute endorsed these items, getting it through in legislation will be critical to monitor. *We remain quite focused on the legislation- both around the pace of acceleration on carbon reduction as well as proscribed ownership %'s. We stress that much of the 'upside' coming from legislation is likely relatively protracted (2024+) – but utility rider reform could be the most near-term tangible benefit. We also stress regardless of procurement cycle, the transmission investment is a clear opportunity in this '24 time period, and particularly accelerating should the state pursue offshore wind (East-West capacity would need to be substantially expanded).*

Texas impact: 600MW impacted, Gas LDCs not significant

Mgmt. highlighted that it had 600MW of renewables that were affected from the freeze given the inability to produce output; we estimate this likely measured in $MN's. While it did have a 100MW asset that has Brazos as a counterparty, its only 1 of 3 off-takers on the asset. Separately, mgmt. highlighted minimal impact to its gas LDCs across OH, KY, TN, and NC and would expect to recover fuel costs through the typical gas clause mechanism. Bottom line, we see an overall limited impact to DUK on an absolute and percentage terms basis.

IN: could be upside to spending but expect slower transition

While DUK recently sold a ~20% interest in IN to GIC for $2bn to eliminate equity needs with a nice recycling of capital, we don't believe additional transactions are likely in the NT given key data points that await from the Integrated Resource Plan (IRP) filing that mgmt. intends to file. This transition of the fleet is indeed likely to be slower than NC, although mgmt. highlighted that it looks to utilize the least cost financing tool. To the extent the opportunity set for the coal transition accelerates, we could see further sell down to fund growth over-time. Still with IN coal lobbyist particularly strong, we stress not to get too far ahead of expectations here.

Edison International (EIX)

Preference for additional preferred equity seems likely

Following the $1.25bn preferred issuance that has a 5.375% coupon (w/ reset date based on the 5yr treasury rate – potentially something to monitor given increasing interest rates) and is expected to have 50% equity content ($625mn) treatment from the rating agencies, we believe remaining $375mn of equity content could come in the form of preferred as well. While mgmt. left the door open for ATM utilization, the company also suggested that it has the balance sheet capacity to do *more* preferred and also acknowledged PCG's issuance considerations where it could be a different market depending on the product. To that end, we see this as indicating that there is more a preference to do preferred equity than ATM for remaining $375mn.

Customer bill impact: not too many solutions aside from securitization

While the customer bill impact will be a key consideration going forward given the substantial wildfire related spend (and O&M that will be difficult to ratchet back), mgmt. did not highlight any ability to sell assets to mitigate those considerations. While it has seen generally lower rate increases vs. peers, this still remains a consideration. One potential solution could be securitization of bad debt expenses from COVID (although not likely under collections as EIX does not likely meet the requirements). We view this as a potential useful tool given the rate impact that would occur earlier in the year otherwise.

FERC ROE focus in part

Mgmt remains confident that with its fully resolved FERC ROE at 10.3% on a settled basis from its last case this could help avoid the pitfalls of the +50bp RTO adder that otherwise appears at risk in the state. We see some risk of degradation still upon future reviews.

Entergy (ETR)

We caught up with the mgmt. team at Entergy principally focusing on the prospects for outcomes in the ongoing Arkansas Formula Rate Plan (FRP) docket which may see a resolution by the middle of the month. We also discussed the latest System Energy Resources (SERI) complaint filed last week which adds a further Federal Energy Regulatory Commission (FERC) proceeding in addition to the ongoing sale-leaseback case which has been in focus since the Administrative Law Judge (ALJ) ruling came down nearly one year ago. On balance we see a uniquely large number of uncertain regulatory outcomes upcoming, though mgmt. continues to highlight its ongoing contingency planning (as well as recent reiteration of guidance) to deal with the potential for adverse outcomes. Maintain Buy on ETR which we see as deserving of a higher valuation than lower-growth peers.

Arkansas resolution could come by mid-March

Entergy mgmt. laid out several potential paths to resolutions of its FRP proceedings – both for the 2021 rate increase where the Arkansas Public Service Commission (APSC) has initially ordered a $1m annual increase and in the broader 5-year renewal docket. Recall that based on the most recent commission filings, Mar. 15 is the target date by which the commission expects to rule on both issues. In addition to ongoing discussions at the regulatory level, state lawmakers recently put forward an amendment to the APSC appropriation bill seeking to clarify the netting portion of the FRP statute which with a retroactive application would result in approval of ETR's $67m requested increase for 2021 – note that the posted agenda for AR's Joint Budget Committee meeting on Mar 4 does not include the proposed amendment, suggesting sides have not yet reached a consensus. In our meeting mgmt. did not offer new specifics on progress of stakeholder talks citing confidentiality of the process, *though we note the recent reiteration of the long-term guidance assumes the FRP is renewed for an additional five years, a confident signal despite persistent uncertainty.*

SERI gets a new challenge from AR, LA

The APSC along with its LA counterpart have submitted a rate complaint to FERC alleging that ETR has overcharged its AR, LA, New Orleans, and MS opcos via its Unit Power Sales Agreement (UPSA) with SERI. The complaint alleges $360m of costs that were not prudently incurred were passed on to ETR's customers via the UPSA, resulting in elevated bills in service areas where incomes are below national averages. The complaint further alleges that an $800m uprate project undertaken in 2012 failed to increase the plant's output, further harming customers. Given the recency of the latest filing ETR mgmt. only affirmed that it intends to respond to the complaint through the FERC forum. We note however that the SERI has already been the subject of an adverse ALJ ruling one year ago in its leaseback and FIN-48 proceeding, and this latest complaint threatens to push back de-risking of this situation for months or even years given the busy FERC calendar.

Pref proposal coming in proxy; O&M levers

Mgmt. reiterated its expectation of seeking shareholder approval for a preferred issuance in its upcoming proxy, potentially with a convertible component, though the size of the preferred issuance will not be disclosed until the proxy filing. Further mgmt. affirmed its existing levers for managing different regulatory outcomes, including pension, tax, and interest in the context of its flat O&M outlook (inclusive of normalization of 2020 one-time items). On balance we see some degree of levers around Prefs vs common equity, as well as further O&M levers; we perceive some caution to affirming level of cost opportunities that exist ahead of details on the fate of AR.

Essential Utilities (WTRG)

Robust Muni Opportunities despite DELCORA Hiccups

We hosted our latest meetings with WTRG following their earlier guidance roll forward and recent full year results – and ahead of a potential decision from the PA commission in coming weeks around their pending DELCORA transaction.

After the Delaware County Court of Common Pleas issued an order supporting the pending acquisition of DELCORA by rejecting the county's attempt to block the sale, the county appealed the decision and the ALJ recommended the PUC deny the transaction. Given that there are only four commissioners right now in the state, we could very well see a stalemate or see the commission send it back to the ALJ to reconsider add'l evidence as the company works through their concerns. The company expects the commission to address the transaction on either March 11th or March 25th – with the latter seemingly more likely. We stress that the equity doesn't need to be pulled until August if there is a slight delay in the transaction.

Discussions further highlighted potential for muni opportunities to arise out of the pandemic as budgets are further pressured. The company has already outlined $420Mn in rate base opportunities from signed APAs that should generate ~$21Mn in earnings, with announcements of further deals seemingly on the horizon. Following the adoption of Fair Market Value legislation in TX and VA, the company now has the constructive legislation in all eight states of their water footprint. While their water biz has a footprint in TX, the company has noted no material financial impact to the water biz and no financial impact to the recent cold weather events for the gas biz given the location of their operations.

We reiterate our Buy rating on shares, seeing value relative to AWK and longer term re-rating potential as management continues to perform and drive incremental growth through municipal acquisitions.

Eversource Energy (ES)

Offshore Prospects, CT Troubles, and Confidence in Plan

Latest discussions with ES echoed earlier commentary from Orsted around the improving BOEM landscape under the Biden administration – with the company optimistic around a pending schedule from the agency. Despite latest competitive pressures materializing – and particularly evident in the recent NY award with ES not winning any of the ~2500MW – ES continues to have plenty of spare capacity for additional projects and we look towards upcoming RFPs across their footprint. We could yet see further potential tailwinds arise from add'l legislative efforts, with the Clean Future Act the latest push at the Federal level: Similar to earlier developments around tax credits, any further benefits would flow through to ES/Orsted since they don't have flow backs with their customers for the currently contemplated project (contrasted to Ocean Wind with PEG). At the state level, we continue to watch climate policy in Massachusetts legislature and potential for incremental offshore wind targets: we see potential for another 1600MW RFP for offshore wind and more utility owned solar to pass in the next several weeks.

Recall with full year results, the company firmed up their capital plan and noted expectations to be in the upper half of their previously announced 5-7% core regulated CAGR longer term. Annual spend of $275Mn related to Columbia Gas exceeded our expectations and helped drive an 8% consolidated rate base CAGR through 2025 - and latest discussions continue to suggest integration of the acquisition as going well. We view additional ramp in spend at Columbia Gas as just one of the potential upside levers to the formal plan in addition to AMI and EV projects that could materialize. While we continue to await further developments of offshore awards and more granular timing, we expect the projects already awarded to take management comfortably above the current growth rate as they start to come online. While we still see challenges in CT the biggest risk, we perceive a relatively improved environment since late last year and continue to monitor ongoing dockets.

Bottom line, we see risk/reward as balanced. Maintain Neutral.

FirstEnergy (FE)

Deal on rate case appears a unique angle to watch

Mgmt appears keen to resolve its regulatory issues swiftly. What is remarkable to us is the potential to file a rate case either by '24 or even prior – but with mgmt. quite confident that the downside can be limited to just 10c (vs the much more meaningful step change we had been contemplating). It would appear the difference relate to the actual book equity of the Ohio utilities relative to use a hypothetical capital structure. Should mgmt. prove able to reset its rates (risking just -10c-ish) we see this as a uniquely constructive outcome to de-risk the backdrop for the utilities. We see potential further de-risking of shares to enable further re-rating despite the positive improvements already. The question remains just how and whether an (accelerated) rate case would be agreed to given the litany of parallel dockets underway. We view the company as still sincerely interested in pursuing further opportunities to de-risk the backdrop rapidly and come to conclusion around a range of dockets opened up in the wake of bribery investigations.

Asset sales: not so much?

On balance we do not see asset sales as much of a priority considering the tax leakage and relative size of cash needs. We suspect converts and other such structures appear preferable despite being open to sales processes. We see limiting dilution to shares at current levels as a key priority for mgmt.

Greater transparency with AG deal and further steps taken

Our discussions focused around FE's continued steps toward improving transparency and company culture. After FirstEnergy reached a deal with Ohio AG Dave Yost to forgo decoupling revenues, they took this a step further on their earnings call by also choosing to forgo LDR (Lost Distribution Revenues) benefit. Combined, this led to a -15c impact to '20 earnings. With the likely replacement of HB6 perhaps with legislation similar to HB10, we note no provision for LDR in the current pending bill. Mgmt highlighted that per its SEET filing, Ohio ROEs average at 7.6% for 2020 (10% for OH Edison, ~4-5% for CEI and Toledo), relative to 11.9% in 2019. The two main drivers for the decline include the collection of DMR revenues (excluded from '20) as well as the LDR-related charge taken in 2020. With no LDRs in '21+, mgmt would expect ROEs to be as similar ~7.6% levels going forward. Deconsolidation for the SEET threshold is still in pending legislation (passed by Senate thus far), although even Ohio Edison is still well below the SEET threshold (~17-18%) at ~10%.

Internal investigation remains ongoing, but minimal news of late appears pos

With recent 10-K disclosures of 'immaterial' transactions around improperly charging customers, mgmt noted that they have been in discussions with multiple states around addressing these issues and see minimal risk. Otherwise, we have seen minimal announcements and we view this as a positive, although the internal investigation is still underway with an ongoing DOJ investigation. FE is working to address liquidity issues with its FE Forward program potentially bringing cost reductions through O&M and capex efficiencies in addition to broader company transformation over a multi-year period. Further, equity issuance in 2022/2023 could potentially be used as a source of funds to finance a potential penalty (admittedly this longer perceived timeline brings some concerns around length of the federal investigation).

Hannon Armstrong (HASI)

A new era of growth, with further programmatic deals anticipated

With a recently announced 7-10% 3-yr EPS CAGR (up from the prior 2-6% through YE-20), discussions focused on the opportunities ahead given an expanding renewables outlook. Mgmt reiterated strong relationships with its partners Clearway and Engie, emphasizing the close collaboration as well as opportunities for further transactions, particularly given HASI's historical preference for programmatic deals. We expect that these meaningfully sized partnerships could provide Hannon with even further visibility to continue to expand its already robust pipeline That said, while 2020 was a successful year with $1.9bn originations, we expect that $1.0-$1.5bn will be a more normalized run-rate, although we could see upside to investments from an expanding $3.0+bn pipeline. We emphasize that mgmt did not reduce guidance in response to the ERCOT weather event. After assessing the situation, HASI determined that impact was likely minimal and any potential losses would principally be tied to force majeure disputes in the event that facilities were unable to operate. That said, given their preferred equity seniority, mgmt perceives a minor impact to returns over a 20-30 year life. HASI continues to be comfortable with achieving a portfolio yield in the ~7% range.

Mgmt expects leverage to stay in the 1.5-2x range for a period. Although the company's advocacy for an IG rating remains ongoing, it is not a key focus vs. other priorities (given relatively open access to capital markets). We note that mgmt recently amended its ATM equity issuance program, raising it to $500mn from the $350mn from May 2020.

Energy efficiency poses a strong opportunity

Under a Biden administration, we continue to see energy efficiency as an opportunistic growth sector for HASI (which had historically been a key component of earnings growth in the past). Notably, the ESPC program under Obama was expanded twice through executive order, and we see likelihood that Biden could take a similar approach to supporting this program, sometime this year, thus presenting a significant potential opportunity for Hannon. Additionally, we see federal procurement of renewables as another key area of growth, with currently only ~10% of the federal government's procured electricity sourced from renewables. We see the possibility of a new target set for ~35% procurement by 2030+. Finally, a carbon tax also remains on the table, although seemingly less likely than other options.

What to expect on REIT status?

An ongoing point of discussion appears to be the ability of HASI to maintain its REIT status given its increasing focus toward resi solar and other renewable equity stakes. While HASI remains confident in their REIT status over the next three years, they have stated that they see multiple paths ahead and would consider scenarios in which they are not a REIT if it were to mean additional investment opportunities. This remains a low probability event. That said, if Hannon were to go this route, we would expect them to disclose this shift well in advance, with a substantial amount of planning and discussion with agencies.

Tightening resi solar returns – in-line with SPWR commentary

In terms of the resi solar project equity financing business, mgmt expresses that its initial entry into this space was well-timed with much higher returns and particularly attractive rates given its ability to finance mezzanine debt (SunStrong JV with SPWR). That said, HASI mgmt acknowledges that its resi solar portfolio as well as resi solar industry broadly has matured, particularly with the latest economic downcycle and proven asset performance, though resi solar assets remain very much in the money with a lot of value in yield for prior deals still.

As such, HASI expresses that ability for future resi solar biz is more challenging as returns are less attractive from a yield perspective, particularly as resi solar service providers such as RUN can issue corporate capital at extremely attractive spreads rather

than needing project equity from a provider such as HASI. Nonetheless, HASI expressed that its SunStrong JV with SPWR will remain a good source of ongoing business given that it is more of a relationship than one-off project equity transactions. All-in, HASI expressed resi solar is not yet a point where this biz is not attractive at all, though acknowledging returns have definitively tightened – ultimately expect slower LT growth in resi solar (mostly ongoing basis with SPWR) for HASI but emphasis on ability to focus on other asset classes given diversified approach.

NiSource (NI)

2021 guidance has upside and affirmed with PA order

NI mgmt. reaffirmed '21 guidance today with the PUC order on Columbia Gas of PA's (NI Subsidiary) pending rate case, where the PA PUC granted a $65.2m rate increase with 9.86% ROE vs NI's original request of $100mn/10.95% ROE – in-line with previous guide and plan. We continue to think that NI appears among the few remaining utilities with material COVID latitude built into '21 guidance. That said, the company expects things to return to normal in 3Q21 with a vaccine in place. 5c is upside to this year should impacts be less than perceived and remains upside to the LT guidance range.

Financing coming soon; talking down portfolio optimization

On financing, the company plans to issue total amount of $600m to $1bn hybrid in 1H21with equity content at 50% or greater, we look to see updates in coming couple months. This will help dictate remaining equity needs in plan depending on size. On portfolio optimization, mgmt. seemed to talk down this angle given considerations on NIPSCO electric with its gas LDC. While not explicitly expressing a preference, we see somewhat less an emphasis on this for now.

ONE Gas (OGS)

OK regulatory asset order approved, but still waiting on recovery framework

Mgmt. highlighted it received the order to defer costs into a regulatory asset in OK (as well as in TX and OK). Mgmt. highlighted that hearings last week with executives didn't provide much info given the focus on outages, and did not seem to indicate any lessons learned. The company's gas cost estimate of $2.2bn remains a confident estimate. While volumes were higher than curtailments with 3-4BCF from OK and 10-12BCF from TX, we wonder around the recovery construct (mgmt. indicated a return on carrying cost with a shorter collection period vs. typical rate base asset), especially for those customers that did not receive gas (as those that did take on more volume will not necessarily have more of the burden). Given the substantial impact to customer bills and discussions from policy makers around these concerns, we see this likely an overhang on shares until more clarity evolves.

Securitization could be a path: but uncertain

Securitization also remains an option with the session ending in May in TX and OK (KS as well), although here too it remains very early in the process and could be somewhat protracted given subsequent approval required from regulators (assuming a bill is introduced and passed) and the time to get financing in place.

Not yet committing to LT growth rate

While mgmt. did not withdraw its LT guidance range, it did not necessarily commit to the 5-7% given some of the uncertainty. Securitization seems to be the key driver of this, and then otherwise the LT financing plan to help affirm its growth.

PG&E Corp (PCG)

We remain constructive on shares of late as we believe pressures on shares fail to reconcile with the improving regulatory & financing backdrop. On balance, we see an ever growing sense that the securitization outcome could well no longer involve equity at all – reducing key sensitivities around dilution. Moreover, don't expect equity should shares remain at their

current levels finding other alternatives. We don't look for any further capex updates in the near-term after a meaningful series of unveils with 4Q; also don't look for mgmt to pursue Preferreds akin to EIX given their commitments to existing capital structure between debt & equity.

Enhanced oversight enables Safety cert and improved trust

Mgmt continues to emphasize the point of further trust and coordination between the CPUC and PG&E as the enhanced oversight requires regular 90-day update on progress towards milestones. Overall we sense continued improvement among parties.

Defining equity needs and the customer rate impact

Mgmt. initiated EPS growth of 10% from 2021-2025, which embeds the equity needed to fund growth/additional spend in plan; we estimate this to be ~$200mn/yr likely though an ATM. Mgmt. confirmed 52% of the $2bn in additional spend to be a reasonable proxy. Additionally, mgmt. narrowed its 2021 equity needs to 0-$400mn (from prior $450-750mn) following recent asset sales agreement of $954mn, and highlighted potential to reduce those needs further (potentially to zero) with a successful resolution of its alternative proposal in the securitization filing. Further, the company highlighted additional asset sales that could be utilized to reduce the customer rate impact given items such as O&M on wildfire spend likely out of its control. This includes non-core asset sales such as undeveloped land (1/3 customer, 2/3 shareholder mix), developed properties (customer benefit), Hydro generation assets (although likely smaller in size given age, at least NT), and real estate (large building in Oakland, for instance). We continue to see ability to strip costs out of the business and other forms of solutions to reduce customer costs as key to gaining comfort in the capex profile and customer rate impact going forward.

PinnacleWest (PNW)

Our meeting with mgmt. of PNW focused on prospects for some form of concurrent recovery of clean generation investment, despite the company's recent capex cut. With the rate case currently in the hearing process we perceive that parties remain broadly opposed to the Advanced Energy Mechanism (AEM) rider as proposed by PNW. Given the need for a recovery mechanism we additionally touched on potential for a subsequent rate case filing including timing and equity needs. Overall we believe that PNW shares will remain under pressure until a proposed order is issued by the ALJ (the next concrete data point) and potentially beyond, given the broad perception of a cautious outlook in the current case. Maintain Underperform on PNW.

Renewable rider not likely despite lower capex

PNW's recent Q4 update included a resetting of its 3-year capex forecast including a reduced Clean Generation bucket owing to mgmt's assessment of the likelihood of inclusion of its AEM proposal. We note that during the hearing phase the bias across a majority of stakeholders appears to still oppose the proposed AEM, though staff has suggested potentially utilizing an existing renewable tracker instead. We expect this is likely an interim proposal as PNW's AEM was originally intended to provide not just for recovery of renewable investment, but also funding of the Coal Community Transition (CCT) program and consolidating several existing trackers into one mechanism (as requested by the commission). While the ultimate outcome remains unclear we believe that for the purposes of this rate case the bias remains against approval of the AEM, while longer term prospects are more constructive given state decarbonization priorities. Recall that PNW also increased its targeted level of transmission and distribution capex in the near term in order to accommodate its projected customer growth – we expect that the near-term capex shifts have shifted a greater portion of clean generation spend into future periods (including the second half of the decade).

Reliability will drive generation additions, coal shut downs

Despite its service territory being near both CA and TX, jurisdictions which have dealt with significant electric reliability issues in recent months, PNW mgmt. reiterated the company's commitment to retire the last of its coal burning fleet by 2031. Recall that on Day 1 of our conference we heard from several management teams who alluded to the possibility for keeping some coal assets operating in a peaking or seasonal capacity in order to ensure reliability – this does not to be a strategy contemplated by PNW beyond its current 2031 targeted date for exiting coal.

Commission legislation not likely to have near term impact

Pending state legislation intended to give lawmakers the authority to regulate generation resources has proceeded through party line votes – PNW mgmt. indicates it sees a likelihood of the legislation being signed in to law by the governor. Mgmt reaffirmed its commitment to the company's long-run decarbonization plan and maintains that other than clarifications on the bill's language regarding the procurement of lowest-cost resources, the bill as written should not have a near term impact or alter plans to reduce CO_2 emissions over the long run. Importantly under the legislation the authority to set electric utility rates is not addressed and remains under the sole discretion of the ACC.

Public Service Enterprise Group (PEG)

Scarcity value from T&D-only biz remains the key to upside

With PEG's non-nuclear asset sales progressing and initial interest received for both the solar and the fossil portfolios, we increasingly stress the scarcity value to be obtained from a standalone T&D (admittedly with offshore stake). With NRG's East/West asset sales attracting a 4.3x EV/EBITDA multiple, we perceive some investor concern on merchant gen multiples, even after considerations of fleet quality. That said, we continue to see an ESG premium warranted from a standalone utility biz. Our discussions indicate that PEG is likely still on track to complete sales by its targeted '21 timeline. What appears clear is that the cost dis-synergies contemplated by mgmt. appear to be on track to be offset by this transaction.

What to do with the nuclear portfolio? Changes to ZEC structure & spin/sale too

With nuclear to be the remaining assets in Power (aside from offshore wind, with much longer '24/'25 timeline), mgmt discussed a three-step plan for its approach to these assets. The ZEC (zero emissions certificate) 3-yr extension application is ongoing, and we largely expect the existing $10/MWh economics to be extended given the backdrop of falling power prices. That said, PSE&G continues to see a 3-yr timeline as insufficient with regard to making decisions about its nuclear fleet.

The next step post-ZEC decision (still expected late April) will be to secure the long-term economic viability of the nukes, most likely via special-purpose legislation in NJ (as opposed to less likely options such as federal action or state FRR election, which may ultimately be too cumbersome). *On balance, the 3-year review cycle putting ZECs at risk appears ill aligned with long-lived nature of assets.*

Finally, PEG would be open to selling these assets given the perceived investor benefit of divesting of generation assets. We stress a spin or sale of these assets would truly unlock its embedded scarcity value as a pure-play listed electric & gas LDC with no generation.

LIPA: yes, scrutiny again – but what will happen?

We stress that ongoing challenges in New York cloud the fate of its service agreement to operate LIPA. While the agreement remains for a further six years, we see some potential for reducing the scope of its involvement over time should the state deem its operations as inadequate from last year.

Utility biz strength with largely unchanged rate base CAGR

As the focus increasingly turns to utilities (with ~90% of earnings to come from PSE&G post-asset sales), we highlight PEG's recently updated rate base growth of 6.5-8% off a new 2020 base of $22Mn is relatively in line the prior 7-8% on a pre-rolled forward basis. PSE&G also recently updated its 5-yr capex forecast to $14-$16Bn for '21-25, with confidence by '25 on CEF-EE and GSMP extensions at least at current levels.

With NJ BPU transmission ROE negotiations ongoing, mgmt provided minimal update on negotiations (with transmission ROE change not factored into 1Q21 guidance at a minimum, giving some expectation of timeline for resolution) but we perceive the recent JCP&L settlement at a 10.2% stated ROE (incl. adder) as a positive sign that should guide resolution with others including PSE&G. As a positive, the company plans to finance its capex plan and planned offshore wind investments without the need to issue any equity. LIPA impact in aggregate is estimated to be minimal at roughly -5c/sh.

Further offshore wind opportunities

With PEG's recently confirmed agreement with Orsted to acquire a 25% equity interest in the 1.1GW Ocean Wind project, we still highlight limited contribution on an NPV basis to our SOTP at < $1/sh (no buy-in disclosed), although EPS profile could be upfront-biased. Mgmt noted clear interest in evaluating further opportunities in NJ as well as MD. Recall that Orsted has submitted a bid through Ocean Wind 2 for NJ's second

offshore wind solicitation of up to 2400 MW. While PEG has not directly entered into the bidding process with Orsted, we see it as likely that Orsted could offer to PEG at a later point a JV agreement akin to the one at present.

Spire (SR)

Spire represents the silver lining to gas LDCs relative to Texas events having invested in gas storage assets in the Southeast earlier, when they proved quite out of favor.

Gas LDC biz impact minimal; Gas marketing and off system sales big positive
Mgmt. highlighted that it would expect to use its typical Purchase Gas Account mechanism to recovery the fuel cost from the Texas winter event (with it mostly isolated to W. MO). While it did not specifically quantify the impact, we estimate this in the $200-400mn range; we view this as a clear positive given peers that experienced costs in the multi-billion dollar range and does NOT need securitization/amortization of regulatory asset with the latter that would impact customer bills more meaningfully. In terms of the impact on the gas marketing side, mgmt. is still working through the details although was clearly a beneficiary given the physical flow of gas on its storage assets in the MidCon, Texas, and Gulf. While difficult to quantify the impact, mgmt. highlighted that at a minimum it should reduce future equity needs (currently $100-150mn/yr). The company was also able to benefit on the gas utility side through off system gas sales, which should be a benefit to its gas customers. At the end of the day, we see SR as having a constructive set-up and would expect upside to both '21 guidance and the LT EPS trajectory.

Sunrun (RUN)

Strategic thoughts – but remaining focused on VSLR integration near-term
In light of continued strategic developments across resi solar sector, including peer NOVA (with SunStreet) and ENPH (software tuck-in acquisitions), RUN mgmt provided its perspective on strategic thoughts, emphasizing that it will look at companies that can add significant value to what RUN does in particular in being able to add meaningful capabilities from the acquisition of a leader in the space (as with the VSLR acquisition). Indeed RUN highlighted its past acquisitions having provided it with its Direct Biz capabilities, value for channel partners, proprietary racking technology, and digital lead generation. Specifically, mgmt expressed that RUN will evaluate any potential opportunity that provide bolt-on capabilities. While peer NOVA has expressed that it will remain tech hardware agnostic, RUN expressed that if there were a company that was also a product hardware OEM that mgmt perceived to be strategically important – it would be considered, noting that RUN has acquired a resi solar racking company in the past. Nonetheless, RUN mgmt emphasized focus on organic growth as well as continued integration of VSLR (post acquisition in FY20) – but continues to monitor M&A opportunities.

With the significant attention on cleantech from SPACs of late driving heightened public market activity of late, RUN mgmt expressed its view that sellers would perceive it as a desirable buyer in being able to further value by integrating with the leading resi solar and storage company (no SPAC 'finder's fee' either), though acquisitions are case by case in most suitable buyer (in going public via SPAC vs. strategic acquisition).

Storage inflection through '21 with >100% y/y growth guide
With its latest 4Q20 update, RUN notably guided >100% y/y increase in new storage deployments (~12-14K by our estimates) relative to its cumulative base of 16K storage systems, emphasizing that it is less impacted by higher storage cycle times (relative to solar) vs. long-tail installers given its acute focus on training installers for years within its Direct Biz. Mgmt expressed that FY21 storage guide is constrained by supply still given substantial consumer demand. That said, mgmt expressed being multi-sourced (TSLA and LG) helps with additional supply support from products from high quality

manufacturers near-term in the pipeline (for qualification to approved vendors list, expect ENPH and SEDG given existing relationship on inverters)

Mgmt highlighted significant demand from TX with latest cold snap outages, particularly as its solar+storage customers have been able to stay online with power through this period. RUN expressed it was already in the process of expanding in TX (San Antonio in particular) prior to event driven outages and expects strong traction here. In other markets, RUN expects continued geographic expansion growth organically, which includes working with channel partners/dealers.

Policy-wise, mgmt expects a stand-alone storage ITC as likely given case for meaningful value to the grid from a resiliency perspective for incremental storage assets.

Grid services – potential to expand/partner and further add to network effect

For grid services, RUN mgmt expressed that it would consider expanding beyond PPA/lease assets it owns on B/S to customers that purchase solar+storage via RUN or channel partners (where RUN still provides warranty and servicing) through cash/loan, with enrollment bringing more assets to its partnerships to deliver against its growing grid service contracts (12 awarded already currently). Additionally, mgmt acknowledged that it could potentially partner with product OEMs – here ENPH expressed it could provide customers with ENPH systems that use its app an opt-in option where it could then work with a partner to manage the grid services (such as RUN among others) This would still add $2K NPV per customer on grid service margin even if not a RUN originated or owned system.

Shift towards whole home energy – multi step approach in adding value

Beyond expansion from solar into storage, RUN mgmt expects trends to continue towards whole home energy/power – a focus are for its JV with SK. RUN mgmt expressed a multi-step approach - first electrifying more of the home, for instance electric appliances that have advanced significantly (smart water heaters, electric cooktops, etc) as well as EV additions. This creates more home electric load supporting greater sizing for home solar and storage, with saving potentially paying for much of the improvements. Smart devices such as thermostats (CFO experience as prior CFO of Nest) to support coordination of home DERs as well.

From a grid services perspective, solar+storage is the easiest to dispatch though RUN CFO emphasized experience doing this with thermostats at Nest. Key to consider here is finding the right balance between capacity for grid relative to home owner experience in properly coordinating between loads in home.

Vistra Energy (VST)

We see shares back at among their cheapest levels in the shares history – and at implied multiples that appear akin to the lows since 2008 despite the wider market backdrop. We reiterate our expectation for some degree of reform to materialize. We're surprised by continued fade in shares despite clear market focus on 'reform' and mitigating the supply impacts from recent impacts once more.

Presenting the upside case for market reform

Our discussion principally centered on market reform opportunities following the latest ERCOT severe weather event. With VST and NRG both presenting options to the TX legislature, we see VST as advocating a number of key changes. First, mgmt sees a need to address current market design, with a more defined reliability standard e.g. resource adequacy with potential for higher reserve margins, whether for dispatchable assets or all assets, or with potential changes in the ORDC curve. The question will be whether it makes sense to reduce the $9,000 price cap currently in place. While power forwards have been up of late, it is unclear how much of this can be attribute to likelihood of ERCOT market reform. Other options discussed have been improved coordination

between constituents such as natgas, power/retailers, and TDUs. A re-pricing scenario is also a point of discussion, although we see this as a lower likelihood option.

Nuances to watch in the market reform discussion: Not all reserves are created equal; look for discussion of dispatchable and un-dispatchable resreves each; also look for changes to the ORDC curve of late too. On balance, we stress how quickly ERCOT moved through its reserves was a key point of focus coming out of the events. However we do not see a capacity market as still in the cards. Rather, energy market reforms are the focus.

How much of the $900mn-$1.3bn impact can be mitigated?
With VST's plants largely winterized, mgmt emphasized their resilient business model over the long term with minimal changes necessary despite this one-time event. Notably, as VST had stated previously, the key driver of the $900mn-$1.3bn in estimated losses stemmed from gas suppliers declaring force majeure (*all of them appear to have done so).* While VST emphasized that they feel comfortable on being able to stay within this range on ultimate expected losses, the key question will be how much upside could be achieved in reducing this figure by disputing suppliers' force majeure claims. Separately, we see exposure to ERCOT default allocations as minimal given VST's 6-7% market participant share, in addition to $2.5mn monthly maximum allocations instituted by ERCOT for payments (with an event of this magnitude not previously considered, changes may need to be made).

Still see resilient integrated biz, despite it all
We continue to see a resilient integrated business model with a solid retail book backing the existing generation assets, and reduced earnings volatility aside from the latest event. It will be critical for mgmt to prove out guidance for long-term ~2% EBITDA growth. While VST mgmt made it clear that retail customers would not bear the impact of the February event, we stress that we continue to see a long-term trajectory of improving margins for the company, driven from a variety of angles including ability to capture some benefits from hedging strategies as well as cross-selling and add-on products and services. While questions had arisen of potential retail consolidation with the exit of smaller players, it now appears that this is less likely given the load curtailments seen during the TX Feb event.

What does winterization look like? Costly
Seems principally tied to coal handling systems at coal plants – costing upwards of $50-100 Mn. The question is whether this mandate for winterization will be funded in any explicit way in coming weeks. We suspect investing this level of capital back into coal assets is likely quite challenging to justify under any range of contexts. On balance we perceive few companies as poised to act substantively on winterization of their assets.

Xcel Energy (XEL)

Our update with XEL mgmt. focused on the recent announcement of transmission expansion projects in CO, with $700m of upside to the current plan through 2025, an additional $400m through 2027, and a further $1B of potential incremental investment, among the more ambitious transmission expansions recently seen across our coverage. As expected mgmt. reported that the CO ALJ recommended against the adoption of the wildfire rider while otherwise affirming recovery of wildfire mitigation spending through a reg asset. The proposed CO clean generation plan represents upside beyond the current plan through 2025 though includes a meaningful runway of generation investment. Maintain Neutral on XEL.

$2B transmission upside in CO; resource spend in '25+

The proposed transmission expansion plan calls for $1.3B of investment in 560 miles of 345 kW lines and several new and expanded substations in XEL's CO territory, supporting the buildout of over 5 GW of mostly renewable generation capacity (~4 GW rate base wind and solar, 1.3 GW distributed) as proposed in the recently filed resource plan for the state. While the investment in new generation build is targeted for beyond

2025, the supporting infrastructure buildout represents $700m of upside in XEL's current capex plan through 2025, as well as an additional $400m in the 2026-27 timeframe. A further $0.5-1.0B of incremental opportunities including network upgrades and interconnection work has been flagged but will depend on the ultimate mix and location of resources deployed. While the topic of expanding investment in transmission is not new in our coverage (and indeed has been gaining traction given expectations for infrastructure legislation at the federal level) XEL's update represents one of the more meaningful upticks in transmission investment of late. We note that as this proposal is entirely within Colorado, filings and approvals are at the state level, further reducing the regulatory burden. *On balance look for a constructive 1Q update.*

Rate case looking more likely following wildfire rec

The CO administrative law judge (ALJ) issued an order opposing XEL's proposed wildfire recovery rider which would have allowed for concurrent recovery of wildfire mitigation investment in the state through 2025 as drafted. While rejecting the rider, the ALJ recommended adoption of the investment plan ($325m) through 2025 with a proposed deferral of prudently-incurred spend for recovery in a future rate case. While mgmt. had previously indicated that the wildfire rider outcome is not in itself a driver of whether the company will elect to file a rate case in CO, XEL now expects to make a filing around mid-year.

Fuel cost impacts subject to recovery

XEL mgmt. estimates its incremental fuel costs stemming from severe weather across the country at $1.2B driven by spiking spot gas prices over a several day period. Mgmt. expressed confidence in achieving full recovery and expects an extended recovery period in order to mitigate the impact on customer bills. Based on preliminary calculations, XEL sees a per-customer impact of $250-300 across most of its jurisdictions, suggesting a $10/month or higher individual bill impact assuming recovery is spread over 2-3 years. Mgmt. maintains that its internal hedging policies were followed across all of its jurisdictions and does not expect any incremental impact on future rate case filings given what will likely be meaningful rate pressures in the near term.

Exhibit 1: Stocks mentioned
Prices and ratings for stocks mentioned in this report

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
AEE	AEE US	Ameren Corp	US$ 72.52	A-2-7
ATO	ATO US	Atmos Energy	US$ 90.87	A-1-7
BKH	BKH US	Black Hills	US$ 60.73	B-1-7
CWEN	CWEN US	Clearway Energy	US$ 27.94	B-1-7
CWENA	CWEN/A US	Clearway Energy	US$ 26.09	B-1-7
CMS	CMS US	CMS Energy	US$ 54.91	B-1-7
D	D US	Dominion Energy	US$ 69.53	A-1-8
DTE	DTE US	DTE Energy	US$ 120.65	B-1-7
DUK	DUK US	Duke Energy	US$ 88.61	B-2-7
EIX	EIX US	Edison Intl	US$ 56.27	B-1-8
ETR	ETR US	Entergy Corp.	US$ 87.95	B-1-7
WTRG	WTRG US	Essential Utilities	US$ 41.95	B-1-7
ES	ES US	Eversource Energy	US$ 79.15	B-2-7
FE	FE US	FirstEnergy	US$ 33.45	B-2-8
HASI	HASI US	HASI	US$ 53.95	B-2-7
NI	NI US	NiSource Inc	US$ 21.81	B-1-7
OGS	OGS US	ONE Gas, Inc.	US$ 70.60	A-2-7
PCG	PCG US	PG&E Corp.	US$ 10.75	C-1-9
PNW	PNW US	Pinnacle West Capit	US$ 75.02	B-3-7
PEG	PEG US	Public Service	US$ 55.10	B-1-7
SR	SR US	Spire	US$ 68.56	A-1-7
RUN	RUN US	SunRun	US$ 53.82	C-1-9
VST	VST US	Vistra Energy	US$ 17.08	B-1-7
XEL	XEL US	Xcel Energy	US$ 59.34	B-2-7

Source: BofA Global Research

BofA GLOBAL RESEARCH

Price objective basis & risk

Ameren Corporation (AEE)
Our $76 price objective is predicated on a P/E based sum of the parts, valuing each business subsidiary relative to the 2023E ratebase weighted peer multiple of 15.9x for electric. We apply a 1.0x premium to peers at AEE Missouri to account for the improving prospects of capital spend, supplemented by a regulatory jurisdiction becoming more favorable - but lack of decoupling. We apply a 1.0x premium to peers at AEE Illinois to account for decoupling on the distribution business which aids in earnings predictability. The overall business is expected to grow at a more meaningful clip than that of peers - we see a 10% EPS CAGR at IL 2020-2024. At ATXI, we apply a 1x premium to peers to reflect the FERC ROEs. At the Parent, we assume 1x multiple premium reflecting average of the subs and given the healthy debt metrics with FFO/Debt at 17%+. Electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. The upside (downside) risks to our price objective are the utilities earning their allowed returns or better (worse), a significant increase (decrease) in 30-year U.S. Treasury bond yields, and positive (adverse) regulatory outcomes that could impact mgmt's ability to earn its allowed return

Atmos Energy Corporation (ATO)
Our $99 PO is based on our 2023E sum-of-the-parts (SOTP) analysis, based on the gas LDC peer group multiple of 14.1x. Our gas peer P/E multiple is grossed up to reflect the group's 5% CAGR to reflect capital appreciation across the sector. We then apply a 3x premium to the base gas LDC multiple to reflect the high-quality nature of the assets given a sustainable runway for capex/EPS underpinned by constructive regulatory mechanisms and jurisdictions. For the Pipeline & Storage segment we apply an 8x EV/EBITDA multiple as a base to our '23E EBITDA. We then apply a 2x premium to the assets given their fully regulated nature and unique ability for APT to benefit from the spread differentials.

Upside risks: 1) improving regulatory relationships, 2) decrease in interest rates, 3) incremental capital spending, 4) constructive rate case outcomes, 5) less equity needs.

Downside risks: 1) deteriorating regulatory relationship, 2) increase in interest rates, 3) less or deferred capital spending, 4) poor rate case outcomes, 5) more equity needs.

Black Hills Corporation (BKH)
Our $68 PO is based on a SoTP valuation. Gas Utilities: We apply the 14.7x peer P/E multiple on 2023E EPS. Electric Utilities: We apply the 16.2x peer P/E multiple on 2023E EPS. Both electric and gas peer P/E multiples are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. Coal Mine: We apply an 8x peer EV/EBITDA multiple, which is in line with other PRB coal producers. Based on our view of the strength/maintainability of different coal plant output contracts, we apply a discount/prem multiple to that portion of the mine. IPP Assets: We use the recent sale price and '23/EVEBITDA multiple for Pueblo Airport and Wygen I assets, respectively. Parent Expense, Debt, and Eliminations: We apply an average regulatory P/E multiple to this segments income. This captures some Interco revenues that are double counted as well as parent SG&A drag and debt.

Downside risks: operational errors, increasing interest rates, and difficult regulatory environments.
Upside risks: favorable weather, favorable regulatory outcomes, higher capex deployment

Clearway Energy (CWENA / CWEN)

Our $38/sh PO is based on 75/25 weighted Growth/DCF methodologies. Our Growth value is $42 and our DCF value is $27.

In our DCF, we discount the current portfolio's expected cash flows. Main assumptions include:
- Our cost of equity applies a 1.50% yieldco premium to the 1.87% 30-yr Treasury
- Outstanding corporate debt is refinanced at maturity with amortizing debt with an eight-year term

Main assumptions under our drop-down approach are:
- 1,200 MW of assets are dropped down
- A target payout ratio of 80%
- A 3.8% required yield based on the 2021E dividend yield for the YieldCo peer set.
- A 0.25% premium for CWEN to the yieldco peer yield in our base case as prospects strengthen around the validity of the PPAs which are tied to PG&E

Risks are 1) misalignment between the new sponsor and the company's growth strategy, 2) the inability to purchase high-quality assets at accretive multiples, 3) the failure to successfully develop projects, and 4) the inability to access capital markets at attractive terms 5) PCG related counterparty exposure is among the nearest exposures to watch.

CMS Energy (CMS)
Our PO of $65 is based on a SotP relying on 2023E forward P/E multiples for the utility and banking business and a 2023E forward EV/EBITDA multiple for CMS' IPP assets. For the utility seg we apply a 4.0x prem to the avg regulated multiple P/E of 16.2x for the electric seg and of 14.6x for the gas seg, with the 10-yr capex update providing clear sight on ratebase growth and further upside, as well as cont'd favorable regulatory environment, and finally historically proven ability to consistently perform at the high end of guidance range. Both electric and gas peer P/E multiples are grossed up to 2020 by 5% to reflect capital appreciation across the sector. For CMS' merchant business we apply a 8x EV/EBITDA multiple, in line with current market value of CMS power plants (specifically DIG), moreover DIG has relatively favorable contracts for the near future which strengthen plant earnings. Finally, we apply a 15.5x P/E multiple on CMS' consumer lending subsidiary Enerbank, in line with forward P/Es other smaller regional banks with similar growth profile.

Risks are: 1) earned ROEs declining which reduce CMS utility earnings 2) execution risk on capex and cost cutting which would primarily affect the utility earnings, 3) negatives changes to market energy prices which could affect the DIG plant's ability to re-contract at the assumed prices.

Dominion Energy (D)
We use SOTP to derive our $78/sh PO. Utilities: We value VEPCO at 4x prem multiple to elec. peers of 16.1x '23 P/E and 14.1x w/ 3x prem on our '23E P/E to D's portfolio of gas LDCs (East Ohio, Hope Gas (WVa), and Questar (UT)). Mults are grossed up to by 5% to reflect capital appreciation. We value Wexpro at 10x disc to gas utility peers for declining rate base/ROEs and reg. risks. We ascribe a 3x premium multiple for SCANA legacy utility assets, and a 2x disc. for the NND asset. We also net out NPV of ongoing bill credits. Merchant: We apply an 8x FCF multiple for Millstone and separately apply a 100% wt to our NPV est of the ZCP cash flows. We include the full EBITDA from the contracted renewables with a 11x '23 EV/EBITDA multi w/ 3x prem in line with peers. Cove Point: We apply an NPV approach with to our DCF adjusted for the 50% sell-down in the facility. For remaining debt beyond that allocated to state utilities, we incl a 50% wt towards a str netting of leverage, with the remaining 50% using a P/E multiple on associated interest expense, in line with the methodology employed for more highly levered diversified utilities.

Downside risks: increase in rates, capex below assumptions, unconstructive regulatory outcomes, delays and/or cancellation of key projects vs our expectation.

DTE Energy (DTE)

We value DTE Energy at $133 using an SOTP approach.
We value the utility segment on a 2023E forward P/E multiple basis and the non-utility seg. on a 2023E forward EV/EBITDA multiple basis. For the utility segment we apply a 5x premium to both our reg. electric and gas utility peer multiples (of 16.3x and 13.5x, respectively). Both electric and gas peer P/E multiples are grossed up for a year to 2021 by 5% to reflect capital appreciation across the sector. We subtract out Corp & Other expense excl. interest rate.
For GSP we use a midstream peer group multiple of 9x. P&I, we apply an 8x EV/EBITDA multiple, despite the lower quality of these earnings and opaque disclosures, as mgmt has been able to execute on new project origination. We value the reduced emissions fuel (REF) tax credits separately using a DCF methodology at 6% discount rate.

Upside risks to our PO are capex expansions, higher authorized ROEs, and strong performance in the ET segment. Downside risks are interest rate hikes, execution risk on organic growth initiatives at the nonregulated business, and less favorable regulatory environment.

Duke Energy (DUK)

Our $94 PO is derived from a sum-of-the-parts valuation. We value the Electric and Gas utilities using peer 2023E P/E multiples. We apply a 3.0x multiple premium to Duke's operations in FL and 2x in IN to reflect more favorable regulatory environments (and recent sale valuation marker). We apply a 3x multiple to the Carolinas given upside to spending in improving regulatory construct combined with latest IRP & wider legislative reforms into 2021. We value the other regulated electric utilities at 16.2x and the gas utilities at peer group multiples of 14.7x 2022E P/E, respectively. Both electric and gas peer P/E multiples are grossed up by 5% for the groups CAGR to reflect capital appreciation across the sector. The commercial midstream, and transmission are valued on a 2023E EV/EBITDA basis. We use a 9.0x multiple for midstream and transmission segment. We add the net present value of renewable segment using an 8% discount rate. We subtract out the impact of commercial debt, and add back for the renewable debt.

Upside risks: constructive rate case results, higher capital expenditure additions vs our assumptions, lower interest rates. Downside risks: poor rate case results, operating errors, and negative changes in the regulatory environment, Macro risks: Increases in interest rates and decreases in equity market valuations.

Edison International (EIX)

Our $68 PO is based on SOTP, applying a 4x disc to the FERC and CPUC jurisdictional subsidiaries, and the parent/other segment 16.9x on 2023E (grossed up by 5% to reflect capital appreciation across the sector). The disc reflects CA ongoing wildfire risk despite the improved construct through AB1054. We apply 10x 2023E P/E to the Edison Energy segment to reflect uncertainty in the nascent biz. We net out ongoing contribution to the fund on an NPV basis. We also assume an additional $625mn of equity that we net out of our SOTP at the current share price given uncertainty over timing.

Downside risks: 1) Regulatory outcomes less favorable than expected. 2) Natural disasters or catastrophic events can affect system reliability and are subject to regulatory cost recovery risk. 3) Interest rate risk. 4) Non-reg businesses are inherently more risky and subject to both execution risk and commodity variation. 5) CA has specific risks given the differentiated regulatory regime. 6) CA wildfires.
Upside risks: rate case outcome above what's embedded in companies' guidance and

BofA estimates, lower interest rates, more constructive regulatory / legislative outcomes to address wildfire risk

Entergy (ETR)
Our $107 PO is SOTP based. We assign P/E multiples (peer multiple of 15.9x) for 2023E on most segments, in line with peer multiples (and grossed up by 5% to reflect capital appreciation across the group) due to similar growth, and strip out 50% of the holdco senior notes. The Merchant business is also added as a DCF (10% discount rate, no terminal value). Both electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector.

Downside risks: 1) Regulatory outcomes or earned ROE's could worsen, 2) Rate making mechanisms could change in the future, 3) Failure to get trackers or ROE adjustment mechanisms could hurt realized ROE, 4) weather can affect operations and earnings, 5) Interest rate risk affects cost of capital, 6) Consumer advocates or utility staff may focus more on issues that challenge the company ROE, 7) ETR has had safety issues in the past, which have affected regulatory relationships and company liabilities, 8) Exit from the competitive business could present unforeseen challenges.

Essential Utilities (WTRG)
Our price objective is $49 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. These peer multiples are 25.4x and 14.9x. We apply a 3.0x premium to Peoples Gas given the organic growth opportunities, while applying a variety of premiums to its water (2x previously) subsidiaries: +4x to PA, +3x to IL, +2x to OH, +2x for TX, +2x for OH, and no premium for balance of biz. We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Eversource Energy (ES)
Our sum of the parts based price objective of $89 uses P/E multiples on 2023E earnings. For electric utilities, we attribute a 3x premium NSTAR, 3x premium to PSNH, and in line CL&P to peer 15.9x multiple, reflecting future potential positive revisions to capex and earnings. For gas, we apply a 3x premium to the peer 14.9x multiple, given capex upside particularly in MA and a 2x for Columbia Gas. Both electric and gas peer P/E multiples are grossed up by 5% to reflect capital appreciation across the sector. We value Aquarion at a 1x premium to the 27.9x water multiple. We reflect ES's 50% ownership in Revolution and South Fork offshore wind sites on an NPV basis. We further reflect a devco value with an assumption of an additional 3GW through 2031. We take out 50% of parent debt, and 50% of interest to accurately reflect parent leverage.
Upside risks to our price objective are additional capex announcements on the T&D side, as well as success in offshore wind RFPs.
Downside risks are reduction in authorized ROEs, inability to meet earned ROE expectations, as well as failure to receive permitting on incremental capex opportunities.

FirstEnergy (FE)
Our PO of $32 is based on an SOTP: Multiples are driven by relative P/E premiums/discounts to the 2023E regulated peer multiple of 16.0x. Electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. As for premiums/discounts, we view NJ as at a slight discount -1x given a generally constructive commission despite overhang, PA at -2x as we view our more punitive ests already account for industrial load sensitivity incl O&G royalties, and others as in line. In OH, we apply a -2x P/E discount multiple to account for rate review risk. Finally, we apply a 0x P/E premium to peers 2023E multiple to the Transmission business given some limited ability to invest and FERC ROE difficulties. We removed impact of DMR

payments. We subtract out the holding co debt given the high parent lev. We net out potential liabilities from a potential FES bankruptcy by assuming all known 'extra' potential liabilities.

Downside risks: 1) Reg outcomes may improve/deteriorate, 2) legislative solutions may materialize for challenged parts of biz or FE could lose/fail to gain legislative support in key states, 3) int rates positively/negatively affect cost of cap, 4) reg staff or cons advocates may focus on issues beneficial/detrimental to ROEs, 5) exit from comp power biz may or may not have substantive liabilities accrued to equity holders, 6) negative outcome from any investigations and litigation including the HB6 lawsuit.

Hannon Armstrong (HASI)
Our valuation with a $63/sh price objective using a 75/25 DDM/DCF methodology, with $68 DDM valuation and $48 DCF valuation. For the DCF we apply a cost of equity of 3.0% to value the stream of cash flows from the existing portfolio as well as the growth prospects of the proprietary origination business. We assume a 11.1x P/E multiple on a peer group, with a 5x premium given strong growth prospects vs. peers, including commercial mortgage REITs and business development companies (BDCs).
Our assumptions for 7.7% yield and 3.8% cost of debt arise from analysis of historical and projected portfolio composition (and associated yields by asset class) and expectations for fixed vs. floating rate debt composition.

Upside risks: 1) Origination growth above expectations 2) Acceleration in securitization transactions 3) Dividend growth faster than expected 4) SG&A costs below expectations 5) Faster than expected yield expansion.

Downside risks: 1) Origination growth below expectations 2) Slowdown in securitization transactions 3) Shift towards greater proportion of BTM vs. GC assets may result in drag on portfolio's yield 4) Potential for rapid rise in interest rates 5) Slowing dividend growth may impact relative valuation vs. peers.

NiSource Inc (NI)
Our $26 PO is based on a sum of the parts valuation. We value each gas and electric utility separately using 2023 forward P/E multiples of 15.1 for gas utilities and 15.9x for electric utilities with a 2.0x premium for the electric utility's strong growth rates and incremental renewable buildout with capex beginning in '22, but acknowledge industrial risk. Also, we assign a 3x M&A premium to the VA, KY and MD gas utilities to account for their M&A premium. We note that electric / gas peer P/E multiples are grossed up by 5% to reflect capital appreciation across the sector. We subtract the value of excess holding company debt at the parent not supporting the utility opcos. We believe NI's 5-7% EPS/dividend growth outlook, attractive regulated earnings profile and constructive legislation across NI's service territories are under-estimated given its discounted multiple versus peers.

Downside risks to our PO are a sustained period of economic weakness pressuring customer growth, interest rate increases, high natural gas prices, financing plan updates, unforeseen costs associated with the MA incident, and challenging steel production economics in Indiana.

ONE Gas, Inc. (OGS)
We use a sum-of-the-parts analysis to calculate our $75 for OGS, applying a 23E Gas LDC peer multiple of 14.3x (grossed up by 5% to reflect capital appreciation across the space) with a 1.0x premium to the company's regulated Kansas assets due to upside on earned ROE, and a 2.0x and 3.0x premium for Oklahoma and Texas businesses, respectively, given their location and de-risked nature.

Upside risks: lower interest rates, constructive regulatory outcomes, increased capital

expenditure opportunities.
Downside risks: higher interest rates, unconstructive regulatory outcomes, decreased capex spending, ban on fracking, decarbonization efforts.

PG&E Corporation (PCG)
Our PO of $14 reflects an Electric peer P/E group multiple of 15.5x and gas group P/E multiple of 14.6x (w/ both grossed up by 5% to reflect capital appreciation across the sector) based on 2023E. We reflect a discount on both Electric and Gas group P/E multiple of -5x to PCG shares to reflect a larger fire-prone service territory, lack of dividend payment for 3yr period, and operational risks. Further, we net out the NPV of the ongoing wildfire contribution from valuation. Lastly, we net out 50% weighting of HoldCo debt and add back 50% weighting of interest expense to derive our $14 PO.

Upside risk: Better terms on equity raise or mandatory convert, incremental capex, favorable rate case outcomes, and lower interest rates.

Downside risk: Less favorable terms on further equity raises, selling pressure from unnatural owners including victims, lower capex, triggering the max liability cap for wildfires, unfavorable rate case outcomes, and higher interest rates.

Pinnacle West (PNW)
Our price objective of $74 is based on a peer utility 2023E P/E multiple of 15.8x with a -2.5x discount to account for PNW's risk around its pending rate case as well as headline risk related to disconnect policy review. Electric and gas peer P/E mult is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We ascribe an in-line premium despite clear renewable capex backdrop given ongoing regulatory risk associated with the company's upcoming rate filing and 2020 election risk.

Upside risks: 1) Regulatory relationships/outcomes could improve, including changes at the elected commission 2) load growth in territory above expectations 3) Riders and capital trackers could help achieve ROE 4) positive weather helps earnings 5) interest rate risk changes cost of capital - lower rates could improve 6) Consumer advocates or utility staff could become focused on issues that improve ROE

Downside risks: 1) Regulatory relationships/outcomes could decline, including changes at the elected commission 2) load growth in territory below expectations 3) Riders and capital trackers could hurt ROE 4) negative weather hurts earnings 5) interest rate risk changes cost of capital - higher rates could worsen 6) Consumer advocates or utility staff could become focused on issues that hurt ROE 7) Solar advocates in the state have engaged in public confrontations with the utility, which could change public relations in the future.

Public Service Enterprise Group (PEG)
Our $63 PO is derived from our SOTP valuation. For the electric utility we use a 3x premium to the 15.4x '23E group multiple to value the regulated and parent side of the business. Electric peer P/E multiple is grossed up by 5% to reflect capital appreciation across the sector. For the gas utility we use a 3x prem to the 13.7x '23E peer group multiple. PSE&G has meaningful growth capex planned, and while pressure on earned ROEs exists, the regulatory environment is favorable.
Downside risks to PO 1) interest rate increases, 2) unfavorable regulatory outcome, and 3) weather, all of which could lower PEG's earnings ability, 4) we caution dilutive asset sales, capacity auction uncertainty, and overall power headwinds as potential overhangs on the stock 5) BPU approvals.

Spire (SR)
Our $66 PO for SR is based on a sum-of-the-parts analysis, applying a Gas LDC multiple of 14.3x on '23E with in-line multiple for Missouri, and 2x premium for the

Mississippi/Gulf and 2x for AL assets given their location and de-risked nature (although COVID concerns remain). For the midstream assets, we use a base 8x EV/EBITDA multiple with a 1x premium for the STL pipeline given it is the one of the only new greenfield pipes in-service, a 4x discount for storage given uncertainty, and a 4x discount for marketing due to volatility.

Upside risks: 1) improving regulatory relationships, 2) decrease in interest rates, 3) incremental capital spending, 4) constructive rate case outcomes, 5) less equity needs.

Downside risks: 1) deteriorating regulatory relationship, 2) increase in interest rates, 3) less or deferred capital spending, 4) poor rate case outcomes, 5) more equity needs.

SunRun (RUN)
We arrive at our $95/share price objective as follows. We value the PowerCo portion of the company by taking NPV equal to Net Earnings Assets, equivalent to discounting cash flows from the existing asset by an unlevered 3.5% discount rate (roughly equivalent to 5% levered discount rate). We value the installed assets through 2025 on a DCF basis with cash flows discounted by 5% with an additional 8% discount rate on the NPV given future execution risk. We further include value from solar renewable energy credits beyond the four year contracting window also on a DCF basis at a 12% discount rate. With ITC extension prospects, we value installed assets through 2026 and include a 8x terminal value multiple on 2029 NPV given scale advantages for future growth prospects as a consolidated entity, we weigh '26+ DevCo value at 60%. We lower DevCo value created by annual R&D and non-cash SBC expenses not captured within creation costs and increase value by incremental NPV from storage and grid service contracts. We add value of operational synergies, existing grid service contracts, and upsell opportunities. We attribute credit for 50% of estimated renewal value to reflect incremental customer value.

Downside risks: We see downside risks associated with the ability to meet cost reduction expectations, MW deployment guidance, Net Energy Metering (NEM), debt capital markets given the highly leveraged strategy employed, as well as if the ITC is not extended beyond the current schedule.

Vistra Energy (VST)
Our $20/sh Price Objective is based on a 2021E SOTP valuation. We assign a discount/premium to the peer group EV/FCF multiple of 7.0x for each fuel within each geography, depending on our specific views for the asset type and market: We include the full $275mn of margin-enhancing initiatives as well as $200mn optimization benefits and the $275mn of synergies related to the DYN acquisition. We further capitalize our estimated income tax for the combined entity to reflect the higher tax burden than peers, and we include a $50mn NPV of TRA payments. We reflect accretion from the Moss Landing storage project as well.

Downside risks: 1) declining wholesale power & capacity prices, 2) competitive & regulatory change to retail businesses, principally in Texas, 3) operational issues pertaining to running power assets including Nuclear asset in Texas.

Upside risks: 1) VST may improve its retail margins and retain customers, 2) VST may beat its margin enhancements initiatives, 3) VST may see a decrease in the price of key inputs such as natural gas and coal, and 4) VST may see an increase in wholesale power prices.

Xcel Energy Inc (XEL)
Our PO is $63. We value Xcel Energy using a sum of the parts (SOTP) approach. Given the difference in geography, earnings strength, growth opportunity and risk profile, we divide the segments by subsidiary.

We use 2023E forward P/E multiples to derive a value for the different business segments, including the parent segment. We use a peer multiple of 16.1x . Electric peer P/E multiple is then grossed up for a year to 2021 by 5% to reflect capital appreciation across the sector. We apply a 2x premium to most subsidiaries except in MN where we apply a 3.0x due to additional stimulus upside. We see this multiple as appropriate as the company has growth opportunities, resolving regulatory drag and resolving uncertainty around rate cases. We stripped Mankato as a non-reg asset in our SOTP due to the sale. We also net back 50% of the parent interest expense and instead subtract out 50% of parent debt to more accurately reflect HoldCo leverage.

Downside risks are interest rate increases, regulatory risk such as lower authorized ROEs or less favorable riders/trackers for renewables and transmission, interest rate risk, execution delays, and weather anomalies.

Analyst Certification

We, Julien Dumoulin-Smith and Richard Ciciarelli, CFA, hereby certify that the views each of us has expressed in this research report accurately reflect each of our respective personal views about the subject securities and issuers. We also certify that no part of our respective compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

Special Disclosures

BofA Securities is currently acting as Financial Advisor to Engie SA inconnection with its proposed sale of Portfolio of 2.3 GW portfolio of U.S. wind& solar assets to Hannon Armstrong Sustainable Infrastructure Capital Inc,which was announced on July 2, 2020.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Enphase Energy	ENPH	ENPH US	Aric Li
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Ormat Technologies	ORA	ORA US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
NEUTRAL				
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Atlantica Sustainable Infrastructure	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	TransAlta Renewables Inc.	YRNW	RNW CN	Julien Dumoulin-Smith
	UGI Corp.	UGI	UGI US	Richard Ciciarelli, CFA
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	Southwest Gas Holdings	SWX	SWX US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	AES	AES	AES US	Julien Dumoulin-Smith

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Alternative Energy Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	5	50.00%	Buy	3	60.00%
Hold	3	30.00%	Hold	3	100.00%
Sell	2	20.00%	Sell	1	50.00%

Equity Investment Rating Distribution: Energy Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	90	57.69%	Buy	69	76.67%
Hold	37	23.72%	Hold	24	64.86%
Sell	29	18.59%	Sell	15	51.72%

Equity Investment Rating Distribution: Utilities Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	80	51.61%	Buy	58	72.50%
Hold	37	23.87%	Hold	28	75.68%
Sell	38	24.52%	Sell	22	57.89%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1863	56.90%	Buy	1185	63.61%
Hold	686	20.95%	Hold	426	62.10%
Sell	725	22.14%	Sell	358	49.38%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

INCOME RATINGS, indicators of potential cash dividends, are: 7 - same/higher (dividend considered to be secure), 8 - same/lower (dividend not considered to be secure) and 9 - pays no cash dividend. *Coverage Cluster* is comprised of stocks covered by a single analyst or two or more analysts sharing a common industry, sector, region or other classification(s). A stock's coverage cluster is included in the most recent BofA Global Research report referencing the stock.

Price charts for the securities referenced in this research report are available at https://pricecharts.baml.com, or call 1-800-MERRILL to have them mailed.
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Spire, SunRun, Vistra Energy, Xcel Energy.
BofAS or an affiliate was a manager of a public offering of securities of this issuer within the last 12 months: Atmos Energy, Black Hills Corporat, Dominion Energy, DTE Energy, Duke Energy, Entergy, Essential Utilities, Eversource Energy, NiSource Inc, ONE Gas, Inc., PG&E Corp., Spire, Inc, SunRun, Xcel Energy Inc.
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The issuer is or was, within the last 12 months, a non-securities business client of BofAS and/or one or more of its affiliates: Ameren Corporation, Atmos Energy, Black Hills Corporat, Clearway Energy, CMS Energy, Dominion Energy, DTE Energy, Duke Energy, Edison Intl, Entergy, Essential Utilities, Eversource Energy, FirstEnergy Corp, HASI, NiSource Inc, ONE Gas, Inc., PG&E Corp., Pinnacle West Capita, Public Service, Spire, Inc, SunRun, Vistra Energy, Xcel Energy Inc.
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Essential Utilities

Moving Past the Tax: Ever Clearer 5-year Growth View

Reiterate Rating: BUY | PO: 49.00 USD | Price: 43.25 USD

Contemplating the Latest Developments

WTRG reported full year adjusted EPS of $1.58, a penny above our estimate and at the top end of management's guidance. After the earlier roll forward in January, there were limited financial updates with affirmation of 2021 EPS guidance of $1.64-$1.69 and their LT 5-7% EPS CAGR through 2023 – and while their water biz has a footprint in TX, commentary suggested no material financial impact from the recent cold weather events. After previously announcing plans to file a rate case at Aqua PA this year keeping with their three year rate case cadence for their water biz, a verbal settlement has been reached around the catch up component of Repairs tax accounting for the gas biz with plans to give **all** of the tax benefits back to customers over a five year period. While we view the decision to settle the catch up with the full benefit to the rate payers as an incremental drag on our estimates in '23, we expect rate relief in '24 to reaccelerate earnings for the gas segment and **stress their 5-7% CAGR as intact** (w/further upside support from the midpoint still given the robust muni pipeline). Meanwhile, after the ALJ recommended the PUC deny the DELCORA transaction, the commission is expected to make a decision next month: Given that there are only four commissioners right now in the state, we could very well see a stalemate or see the commission send it back to the ALJ to reconsider add'l evidence as the company works through their concerns. While we see some challenges on the margin, we stress the equity doesn't need to be pulled until August if there is a slight delay of the transaction and the robust muni opp's abound.

Valuation: PO to $49; tax noise is over; reiterate Buy

We tweak our model to reflect lower ROEs at Peoples Gas in '23 given commentary around the verbal settlement and the need to file a formal rate case for rate relief - but see '24 as intact when we would expect new rates to go into effect. We update our valuation to ascribe the current utility peer multiples of 25.4x and 14.9x for water & gas, respectively (vs. 27.4x and 14.2x previously). We reduce our premium for Peoples Gas from 3x to 1x given the need for a rate case in 2023 while our water premiums remain unchanged and continue to reflect confidence in ability to consistently deliver, strong muni acquisition prospects, and an underappreciated ESG angle. Our PO ultimately shifts to $49 (from $54 previously). Reiterate Buy given deep discount and muni upside.

Estimates (Dec) (US$)	2019A	2020A	2021E	2022E	2023E
EPS	1.47	1.58	1.67	1.80	1.87
GAAP EPS	1.47	1.58	1.67	1.80	1.87
EPS Change (YoY)	4.3%	7.5%	5.7%	7.8%	3.9%
Consensus EPS (Bloomberg)			1.54	1.67	1.79
DPS	0.92	0.99	1.06	1.13	1.21
Valuation (Dec)					
P/E	29.4x	27.4x	25.9x	24.0x	23.1x
GAAP P/E	29.4x	27.4x	25.9x	24.0x	23.1x
Dividend Yield	2.1%	2.3%	2.4%	2.6%	2.8%
EV / EBITDA*	35.4x	21.5x	17.8x	16.6x	15.3x
Free Cash Flow Yield*	-2.0%	-4.7%	-3.6%	-2.8%	-1.6%

* For full definitions of *iQmethod℠* measures, see page 8.

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26 February 2021

Equity

Key Changes

(US$)	Previous	Current
Price Obj.	54.00	49.00

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Stock Data

Price	43.25 USD
Price Objective	49.00 USD
Date Established	25-Feb-2021
Investment Opinion	B-1-7
52-Week Range	30.40 USD - 51.22 USD
Mrkt Val (mn) / Shares Out (mn)	10,608 USD / 245.3
Average Daily Value (mn)	48.23 USD
BofA Ticker / Exchange	WTRG / NYS
Bloomberg / Reuters	WTRG US / WTRG.N
ROE (2021E)	8.6%
Net Dbt to Eqty (Dec-2020A)	100.4%

ESG: Environmental Social Governance

DELCORA: Delaware County Regional Water Authority

PUC: Public Utilities Commission

ALJ: Administrative Law Judge

iQprofile℠ Essential Utilities

iQmethod℠ **– Bus Performance***

(US$ Millions)	2019A	2020A	2021E	2022E	2023E
Return on Capital Employed	3.5%	3.9%	5.1%	5.1%	5.2%
Return on Equity	8.9%	9.3%	8.6%	8.8%	8.9%
Operating Margin	38.4%	-15.6%	66.8%	66.8%	68.9%
Free Cash Flow	(212)	(498)	(379)	(300)	(169)

iQmethod℠ **– Quality of Earnings***

(US$ Millions)	2019A	2020A	2021E	2022E	2023E
Cash Realization Ratio	1.3x	1.4x	1.7x	1.7x	1.9x
Asset Replacement Ratio	3.5x	4.2x	2.9x	2.7x	2.5x
Tax Rate	NM	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	31.1%	100.4%	97.9%	105.7%	111.1%
Interest Cover	3.1x	2.4x	3.3x	3.5x	3.2x

Income Statement Data (Dec)

(US$ Millions)	2019A	2020A	2021E	2022E	2023E
Sales	886	886	1,006	1,077	1,126
% Change	6.2%	0%	13.4%	7.1%	4.5%
Gross Profit	890	890	1,661	1,785	1,865
% Change	6.2%	0%	86.7%	7.5%	4.5%
EBITDA	504	831	1,000	1,077	1,164
% Change	-74.1%	64.9%	20.4%	7.6%	8.2%
Net Interest & Other Income	(100)	(183)	(205)	(207)	(242)
Net Income (Adjusted)	**263**	**402**	**430**	**470**	**489**
% Change	**36.9%**	**53.1%**	**7.0%**	**9.2%**	**4.1%**

Free Cash Flow Data (Dec)

(US$ Millions)	2019A	2020A	2021E	2022E	2023E
Net Income from Cont Operations (GAAP)	225	403	431	470	489
Depreciation & Amortization	156	257	376	412	446
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	(10)	(75)	(75)	(75)	0
Other Adjustments, Net	(32)	(33)	(11)	(6)	(5)
Capital Expenditure	(550)	(1,050)	(1,100)	(1,100)	(1,100)
Free Cash Flow	**-212**	**-498**	**-379**	**-300**	**-169**
% Change	**-66.5%**	**-135.1%**	**23.9%**	**20.9%**	**43.4%**

Balance Sheet Data (Dec)

(US$ Millions)	2019A	2020A	2021E	2022E	2023E
Cash & Equivalents	1,869	6	6	7	7
Trade Receivables	108	177	201	216	226
Other Current Assets	36	48	52	55	56
Property, Plant & Equipment	6,346	10,739	11,462	12,150	12,805
Other Non-Current Assets	1,003	1,003	1,003	1,003	1,003
Total Assets	**9,362**	**11,973**	**12,725**	**13,431**	**14,097**
Short-Term Debt	131	129	138	154	167
Other Current Liabilities	188	236	253	263	270
Long-Term Debt	2,943	4,681	5,013	5,592	6,064
Other Non-Current Liabilities	2,219	2,144	2,069	1,994	1,994
Total Liabilities	**5,481**	**7,190**	**7,472**	**8,003**	**8,494**
Total Equity	**3,881**	**4,783**	**5,253**	**5,429**	**5,603**
Total Equity & Liabilities	**9,362**	**11,973**	**12,725**	**13,431**	**14,097**

* For full definitions of ***iQ***method℠ measures, see page 8.

Company Sector

Water Utilities

Company Description

Essential Utilities is a regulated water/gas providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI - along with a natural gas presence through the recently acquired Peoples Gas providing distribution services to 740,000 customers in PA, WV, and KY.

Investment Rationale

We are Buy rated on shares of WTRG, seeing shares as poised to re-rate higher given consistent execution, acquisition upside, and increasing conviction around the premium story.

Stock Data

Average Daily Volume	1,108,464

Quarterly Earnings Estimates

	2020	2021
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NA

LT Story Intact with Muni Acquisitions Abound

After rolling forward the outlook earlier this year, formal financial updates were relatively quiet for WTRG this quarter. Full year adjusted EPS of $1.58 was a penny above our estimate and at the top end of management's guidance, while the company reaffirmed 2021 EPS guidance of $1.64-$1.69 and their LT 5-7% EPS CAGR through 2023. While their water biz has a footprint in TX, they noted no material financial impact to the water biz and no financial impact to the recent cold weather events for the gas biz given the location of their operations.

After previously announcing plans to file a rate case at Aqua PA this year keeping with their three year rate case cadence for their water sub, management noted on the call that a verbal settlement has been reached around the catch up component of Repairs tax accounting for the gas biz – with plans to file the written agreement on March 11th that would give all of the tax benefits back to customers over a five year period. While we view the decision to settle the catch up with the full benefit to the rate payers as an incremental drag on our estimates in '23, we stress the $420Mn in rate base opportunities from signed APAs should generate ~$21Mn in earnings with further muni opportunities still to materialize – and we see opportunities abound to further accelerate water tucks ins. Following the adoption of Fair Market Value legislation in TX and VA, the company now has the constructive legislation in all eight states of their water footprint. We expect this to help further accelerate consolidation in the industry as muni budgets are further flex'd from the crisis.

Dissecting the DELCORA hiccups

After the Delaware County Court of Common Pleas issued an order supporting the pending acquisition of DELCORA by rejecting the county's attempt to block the sale, the county appealed the decision and the ALJ recommended the PUC deny the transaction. Given that there are only four commissioners right now in the state, we could very well see a stalemate or see the commission send it back to the ALJ to reconsider add'l evidence as the company works through their concerns. The commission is expected to issue a decision in March, and we stress the equity doesn't need to be pulled until August if there is a slight delay of the transaction.

We reiterate our Buy rating on shares, seeing value relative to AWK (B-2-7, $145.64) and longer term re-rating potential as management continues to perform and drive incremental growth through municipal acquisitions.

EPS Estimates

The exhibit below reflects our latest EPS Estimates. Our 2023 estimates shift down slightly to reflect a reduction in earned ROEs given the latest developments around the settlement related to the Repairs Tax Deduction. That said, we continue to stress longer dated estimates intact despite just a three year view - and see a long trajectory of tailwinds from an acceleration in muni acquisition opportunities: we continue to model to their 5-7% CAGR longer term.

Considering the tax deal we perceive this as de-risking eventual '23 rate case and positioning co well on track to execution backdrop in '24+. We see latest NI de-risking of its PA rate case as clearly improving backdrop too. Decisive reiteration of our Buy.

Exhibit 1: EPS Estimates
Lowering '23 on repairs tax developments: Still see LT outlook intact with new rates in 2024

EPS Estimates	2019A	2020A	2021E	2022E	2023E	2024E	2025E
PA	$1.05	$0.75	$0.76	$0.88	$0.94	$1.00	$1.05
OH	$0.09	$0.07	$0.07	$0.07	$0.08	$0.08	$0.09
IL	$0.10	$0.07	$0.08	$0.08	$0.09	$0.09	$0.10
TX	$0.09	$0.06	$0.07	$0.07	$0.07	$0.08	$0.08
NC	$0.05	$0.04	$0.04	$0.05	$0.05	$0.05	$0.05
Other States	$0.10	$0.07	$0.07	$0.08	$0.08	$0.09	$0.09
Water Utility	**1.47**	**1.06**	**1.09**	**1.23**	**1.31**	**1.39**	**1.46**
Peoples Gas		**0.62**	**0.67**	**0.71**	**0.71**	**0.81**	**0.86**
Parent & Other		*-0.09*	*-0.09*	*-0.13*	*-0.15*	*-0.17*	*-0.20*
EPS	**1.47**	**1.58**	**1.67**	**1.80**	**1.87**	**2.03**	**2.13**
YoY Growth		*8%*	*6%*	*8%*	*4%*	*8%*	*5%*
Guidance	**1.45-1.50**	**1.53-1.58**	**1.64-1.69**				
Three Year CAGR (off $1.56 in 2020)					***6%***		
Guidance					**5-7%**		
Fully Diluted Shares O/S	*178*	*254*	*258*	*261*	*261*	*261*	*261*
Previous EPS		***$1.57***	***$1.67***	***$1.80***	***$1.92***		
Consensus	**1.48**	**1.54**	**1.67**	**1.79**	**1.89**		
DPS	**0.92**	**0.99**	**1.06**	**1.13**	**1.21**	**1.29**	**1.38**
Payout Ratio	*63%*	*62%*	*63%*	*63%*	*64%*	*64%*	*65%*
Guidance			***60-65%***				
Share Count	**179**	**255**	**258**	**261**	**261**	**261**	**261**

Source: BofA Global Research, Bloomberg

BofA GLOBAL RESEARCH

Valuation: PO Shifts to $49

The exhibit below reflects our latest SOTP. We update our valuation to apply the current peer multiples to our latest estimates: 25.4x for water and 14.9x for gas (vs. 27.4x and 14.2x previously). We reduce our premium for Peoples Gas from 3x to 1x given the need for a rate case in 2023 while our water premiums remain unchanged and continue to reflect confidence in ability to consistently deliver, strong muni acquisition prospects, and an underappreciated ESG angle. Our PO ultimately shifts to $49 (from $54 previously). Reiterate Buy given deep discount and upside catalysts.

Exhibit 2: SOTP
PO Shifts to $49 on Lower Multiples and Gas Premium

Water Utilities	**2023 EPS**		**P/E Multiple**				**Equity Value**		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*25.4x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		27.5x							
Water Utilities									
States	2023E EPS	ROE embedded							
PA	$0.94	10.0%	4.0x	30.5x	31.5x	32.5x	$29	$30	$31
OH	$0.08	9.2%	2.0x	28.5x	29.5x	30.5x	$2	$2	$2
IL	$0.09	9.1%	3.0x	29.5x	30.5x	31.5x	$3	$3	$3
TX	$0.07	10.0%	2.0x	28.5x	29.5x	30.5x	$2	$2	$2
NC	$0.05	9.2%	2.0x	28.5x	29.5x	30.5x	$1	$1	$1
Other (including acquisitions)	$0.08	9.2%	0.0x	26.5x	27.5x	28.5x	$2	$2	$2
Water utilities total (ex-Peoples)	$1.31			*29.9x*	*30.9x*	*31.9x*	$39	$40	$42
Gas Utilities									
Peer Gas P/E		*14.9x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		15.8x							
	2023E EPS	ROE embedded							
Peoples Gas	$0.71	11.9%	1.0x	15.8x	16.8x	17.8x	$11	$12	$13
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			-1099	50%			($550)	($550)	($550)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($475)	($441)	($517)
50/50 Weighted Drag from HoldCo Drag							($1,024)	($990)	($1,067)
Fully Diluted Shares Outstanding							*261*	*261*	*261*
PO							$47.00	$49.00	$51.00
Current Price								$43.31	
Dividend Yield								2.4%	
Total Expected Return								15.57%	

Source: BofA Global Research, Bloomberg

BofA GLOBAL RESEARCH

Price objective basis & risk

American Water Works (AWK)
Our PO for American Water Works is $162. We apply the sector average 28.4x to American Water's 2023E earnings based on the water peer multiple and a 8.1% group EPS CAGR for '18-'23E. We think this multiple is justified as in our view AWK largely drives the peer multiple as the largest publicly traded water utility. We ascribe a 3x premium for NJ, PA, IL & Other given scope of acquisition opportunities. Also a -1x P/E for Cali utility.

Risks to the downside are increase in market interest rates, potential impact of tax reform on utilities, operational errors, changes in valuation levels for water utilities. Risks to the upside are accelerating muni acquisitions, multiple expansion, and constructive legislation in regulatory jurisdictions.

Essential Utilities (WTRG)
Our price objective is $49 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. These peer multiples are 25.4x and 14.9x. We apply a 3.0x premium to Peoples Gas given the organic growth opportunities, while applying a variety of premiums to its water (2x previously) subsidiaries: +4x to PA, +3x to IL, +2x to OH, +2x for TX, +2x for OH, and no premium for balance of biz. We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AES	AES	AES US	Julien Dumoulin-Smith
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Enphase Energy	ENPH	ENPH US	Aric Li
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Ormat Technologies	ORA	ORA US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
NEUTRAL				
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Atlantica Sustainable Infrastructure	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	TransAlta Renewables Inc.	YRNW	RNW CN	Julien Dumoulin-Smith
	UGI Corp.	UGI	UGI US	Richard Ciciarelli, CFA
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	Southwest Gas Holdings	SWX	SWX US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith

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Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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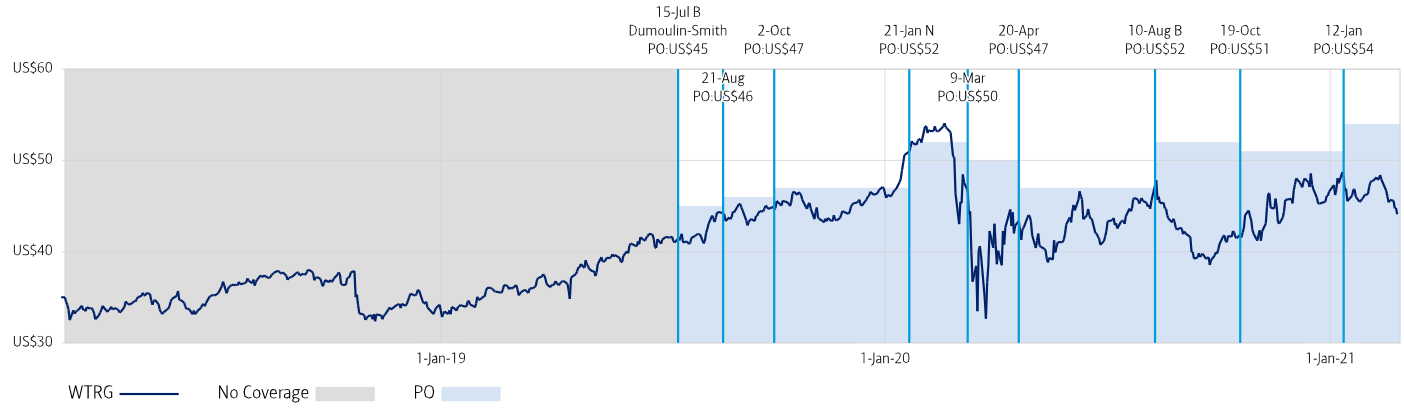
Disclosures

Important Disclosures

Essential Utilities (WTRG) Price Chart



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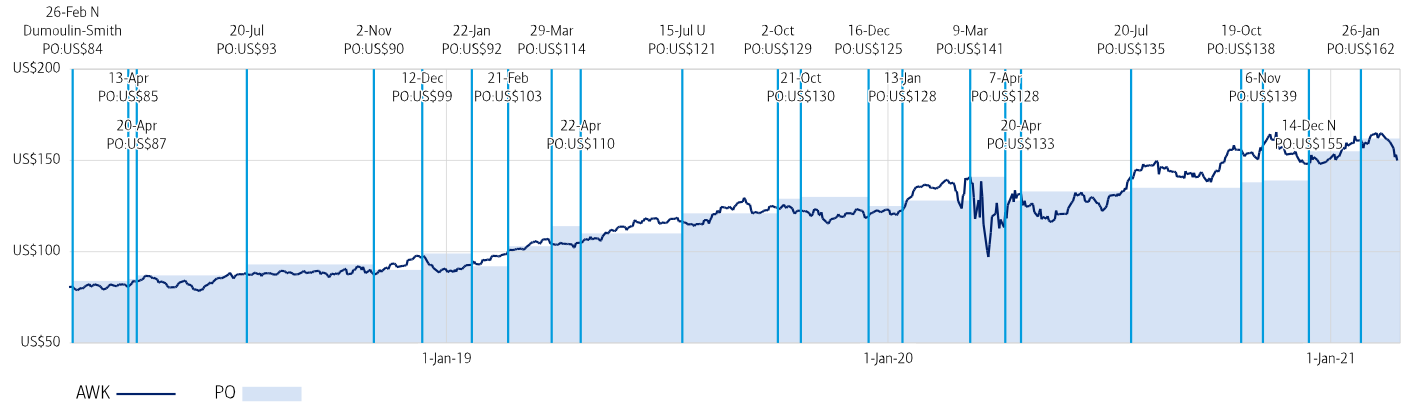
American Water (AWK) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Utilities Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	80	51.61%	Buy	58	72.50%
Hold	37	23.87%	Hold	28	75.68%
Sell	38	24.52%	Sell	22	57.89%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1863	56.90%	Buy	1185	63.61%
Hold	686	20.95%	Hold	426	62.10%
Sell	725	22.14%	Sell	358	49.38%

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
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Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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BARCLAYS

Equity Research
18 November 2020

North America Power & Utilities

Rolling Valuations to 2023

We have initiated 2023 estimates for our coverage and updated all price targets based on 2023 estimates. This update combined with EEI updates and relative price moves has resulted in the following ratings changes:

- Upgrading AEE to Equal Weight, from Underweight, on underperformance and higher projected earnings.
- Upgrading NI to Overweight, from Equal Weight, on higher earnings growth from the increased electric capex in Indiana.
- Downgrading NWE to Equal Weight, from Overweight, on outperformance and lower projected earnings.
- Downgrading PNM to Underweight, from Equal Weight, on low projected return given pending acquisition, along with view that and increased bid is unlikely near term.

With election results and multiple positive COVID-19 vaccine trials, risk appetite appears to be alive and well. In utilities, much like in other sectors, risk has outperformed momentum in recent weeks. This has manifested in a long awaited contraction in the PE disparity in the sector. We believe this trend will continue as investors seek risk and value over defense and momentum. We continue to see names with idiosyncratic risks expecting near term resolution along with utilities possessing higher energy exposure to be in favor given this dynamic. This aligns well with our Overweight ratings on SRE, PCG, SO and PNW and Underweight ratings on ED and WEC.

Based on EEI, Q3 and recent meetings with management, we highlight updates to stock investment theses, where our ratings remain unchanged. COVID-19 load impacts into 2021, rate case expectations, guidance updates, capex updates, corporate actions and more have been discussed recently. We highlight by stock where these changes cause a shift in our investment thesis.

RATING CHANGE

North America Power & Utilities
POSITIVE
Unchanged

For a full list of our ratings, price target and earnings changes in this report, please see table on page 2.

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PLEASE SEE ANALYST CERTIFICATION(S) AND IMPORTANT DISCLOSURES BEGINNING ON PAGE 42.

Summary of our Ratings, Price Targets and Earnings Changes in this Report (all changes are shown in bold)

Company	Rating		Price	Price Target			EPS FY1 (E)			EPS FY2 (E)		
	Old	New	17-Nov-20	Old	New	%Chg	Old	New	%Chg	Old	New	%Chg
North America Power & Utilities	Pos	Pos										
Alliant Energy Corporation (LNT)	EW	EW	54.73	56.00	**65.00**	16	2.40	**2.46**	3	2.58	**2.52**	-2
Ameren Corp. (AEE)	UW	**EW**	80.60	79.00	**95.00**	20	3.41	**3.38**	-1	3.71	**3.73**	1
American Electric Power Company, Inc. (AEP)	OW	OW	86.73	93.00	**107.00**	15	4.33	**4.35**	0	4.65	**4.62**	-1
American Water Works Company, Inc. (AWK)	EW	EW	159.29	138.00	**173.00**	25	3.86	**3.89**	1	4.22	**4.25**	1
CenterPoint Energy, Inc. (CNP)	EW	EW	25.17	21.00	**27.00**	29	1.27	1.27	-	1.36	1.36	-
CMS Energy Corporation (CMS)	EW	EW	63.83	65.00	**75.00**	15	2.67	2.67	-	2.86	**2.84**	-1
Consolidated Edison, Inc. (ED)	UW	UW	79.25	74.00	**83.00**	12	4.24	**4.25**	0	4.52	**4.47**	-1
Duke Energy Corporation (DUK)	EW	EW	92.92	87.00	**102.00**	17	5.08	**5.14**	1	5.18	**5.24**	1
Edison International (EIX)	EW	EW	65.60	57.00	**69.00**	21	4.43	4.43	-	4.58	4.58	-
Essential Utilities, Inc. (WTRG)	EW	EW	44.88	45.00	**50.00**	11	1.56	1.56	-	1.67	**1.62**	-3
Eversource Energy (ES)	EW	EW	91.75	88.00	**100.00**	14	3.70	**3.62**	-2	3.94	**3.89**	-1
FirstEnergy Corp. (FE)	EW	EW	28.74	32.00	**33.00**	3	2.50	2.50	-	2.63	2.63	-
NextEra Energy, Inc. (NEE)	EW	EW	76.61	301.00	**87.00**	-71	9.04	**2.28**	-75	9.87	**2.45**	-75
NiSource, Inc. (NI)	EW	**OW**	24.75	25.00	**29.00**	16	1.33	1.33	-	1.33	**1.38**	4
NorthWestern Corporation (NWE)	OW	**EW**	60.38	59.00	**63.00**	7	3.37	3.37	-	3.62	**3.51**	-3
OGE Energy Corp. (OGE)	EW	EW	34.21	33.00	**36.00**	9	2.14	**2.15**	0	2.20	**2.26**	3
PG&E Corporation (PCG)	OW	OW	11.72	13.00	**14.00**	8	1.62	1.62	-	1.00	1.00	-
Pinnacle West Capital Corporation (PNW)	OW	OW	86.78	89.00	**103.00**	16	4.90	**5.06**	3	4.92	**5.09**	3
PNM Resources, Inc. (PNM)	EW	**UW**	48.90	50.00	50.00	-	2.11	**2.28**	8	2.29	**2.37**	3
Public Service Enterprise Group (PEG)	EW	EW	59.05	59.00	**65.00**	10	3.41	**3.43**	1	3.43	**3.40**	-1
Sempra Energy (SRE)	OW	OW	134.06	146.00	**159.00**	9	7.57	7.57	-	7.99	7.99	-
The Southern Company (SO)	OW	OW	62.36	61.00	**73.00**	20	3.18	3.18	-	3.34	**3.27**	-2
WEC Energy Group, Inc. (WEC)	UW	UW	100.18	94.00	**107.00**	14	3.75	**3.77**	1	3.97	**4.02**	1
Xcel Energy Inc. (XEL)	EW	EW	72.63	70.00	**82.00**	17	2.73	**2.77**	1	2.97	**3.01**	1

Source: Barclays Research. Share prices and target prices are shown in the primary listing currency and EPS estimates are shown in the reporting currency.
FY1(E): Current fiscal year estimates by Barclays Research. FY2(E): Next fiscal year estimates by Barclays Research.
Stock Rating: OW: Overweight; EW: Equal Weight; UW: Underweight; RS: Rating Suspended
Industry View: Pos: Positive; Neu: Neutral; Neg: Negative

FIGURE 1
2023 Barclays EPS Estimates

Ticker	2023 EPS
LNT	$2.94
AEE	$4.28
AEP	$5.28
AWK	$5.01
CNP	$1.38
CMS	$3.25
ED	$4.94
DUK	$5.81
EIX	$5.12
WTRG	$1.82
ES	$4.34
FE	$2.86
NEE	$2.84
NI	$1.55
NWE	$3.79
OGE	$2.46
PCG	$1.25
PNW	$5.56
PNM	$2.68
PEG	$3.58
SRE	$9.05
SO	$3.92
WEC	$4.45
XEL	$3.40

Source: Barclays Research

Ratings Changes

Upgrades

AEE

We upgrade AEE to Equal Weight, as we believe recent underperformance has accounted for risks to future growth weighing on the stock, including energy rules modification in IL and the ability to execute on the preferred MO IRP scenario. At Q3, management narrowed guidance to $3.40-$3.55 (from $3.40-$3.60) and said updates to the 5-year capital plan and 2021 EPS guidance are planned for the Q4 call. We see the potential for incremental spending opportunities from the MO IRP (AEE has 950 MW of renewables opportunities before 2024 not included in current plans) as well as from regional transmission projects, though regulatory approval on a project-by-project basis and the ability to increase regulated capital plans while avoiding significant increases in customer bills will be areas of focus. Management notes the IL legislature's weak appetite for comprehensive energy legislation at this time, though Gov. Pritzker's eight-principled energy reform plan could influence regulatory policy in the future. We now view the risk/reward outlook for the stock as balanced given the uncertainty of the regulatory construct in IL offset by incremental

spending opportunities that could accelerate rate base growth. Our updated price target is $95, which is premised on a 20% premium to the 2023 regulated group average multiple of 18.5x applied to our 2023 EPS estimate of $4.28

NI

After the investor day, we used a 5% premium to the group average to reflect expectations of above-average growth driven by the $1.8-$2.0 bn in renewables investments related to RM Schahfer replacement power. By rolling our valuation forward to 2023, we are able to capture some of the earnings related to this spend via new rates from the anticipated 2022 rate case (rates expected effective mid-2023). We believe the level of cost savings necessary to achieve management's growth guidance is achievable. Additionally, although we do not believe concerns regarding the future of natural gas operations should be materially priced into the stock, we feel the need to reflect the overhang that may weigh on the stock until investors can gain more clarity into the future value of natural gas LDCs. Particularly for those companies operating colder climates, the threat posed by electrification of heating is limited by economic and technological constraints. Thus, for these reasons, we eliminate our premium to the group average, yet we still believe there is enough upside to the current valuation to merit an upgrade to Overweight.

Risks include a higher-than-anticipated skew towards PPAs from procurement results (though management remains on track as of EEI), as well as the ability to control costs and achieve savings from the NI Next initiative in 2021 and beyond. COVID-19 impacts on gas usage during winter months are a source of uncertainty, though most residential gas rate structures have decoupling mechanisms (management estimates that changes in gas usage will comprise a majority of the ($0.05) COVID-19 headwind in 2021). Considering these risks, the current risk/reward backdrop leaves opportunity for upside to the current valuation, in our view. Our updated price target is $29, which is premised on the 2023 regulated group average multiple of 18.5x applied to our 2023 EPS estimate of $1.55.

Downgrades

NWE

At EEI, NEW initiated 2021 guidance of $3.40-$3.60 (below consensus). The wider than normal range was used based on COVID-19 uncertainties and will be narrowed to a $0.15 range on the Q4 call. With the reiteration of a 3-6% growth range and rolling the starting point to a lower than expected 2021 guidance, our 2021 and 2022 numbers have come down and our updated valuation on 2023 combined with the recent outperformance, while providing upside no longer supports an Overweight rating.

We continue to view NWE as a well-managed company with limited growth opportunities compared to peers. The updated capital plan does show a $300M increase as compared to the previous 5-year plan. The updated plan includes $100m of incremental investment for SD generation from the results of a recent competitive solicitation. The Montana generation opportunity is still outstanding, but could add $200M to the capital plan over the next five years. Management had provided commentary previously that $400M/year of capex (new plan is at or above $400M in all years) would allow for growth at the midpoint of the earnings CAGR. While we see longer term opportunity and ability to grow earnings closer to 5% assuming a win in MT capacity RFPs, near term needs to manage O&M between rate cases will drive growth closer to 4% in the near term. We expect a Montana rate case filing in 2022 for new rates in 2023 and expect multiple cases in SD to coincide with commercial operation of the capacity resources to be owned by NWE selected in the competitive solicitation processes.

The current risk/reward feels balanced given the lower current relative growth, recent relative price performance, mixed recent regulatory results in MT and potential for future capex and earnings growth associated with winning MT capacity RFPs. Our updated price target is $63, which is premised on a 10% discount to the 2023 regulated group average multiple of 18.5x applied to our 2023 EPS estimate of $3.79.

PNM

We downgrade PNM to Underweight to reflect the limited upside in the stock given Avangrid's take-out offer of $50.30/share. The acquisition is expected to close in 2H21. We characterize prospects for a superior bid as unlikely given few competitors with the balance sheet capacity for such an acquisition, and none with the strategic alignment or likelihood for regulatory approval as AGR. While regulatory approval of any transaction can never be predicted with absolute certainty, we do not see any significant impediments to approval at this time. Given New Mexico is a net benefit state, AGR's commitment to maintain the PNM workforce and likely willingness to compromise on other factors (HQ location, customer credit, charitable giving, etc.) strengthen the likelihood of transaction approval. Our updated price target is $50, which is premised on the 2023 regulated group average multiple of 18.5x applied to our 2023 EPS estimate of $2.68.

Investment Thesis Updates

AEP

The 5-7% growth rate is maintained and the inclusion of North Central Wind pushes growth above the midpoint for 2022 and 2023, with expected equity to support NCW at 65% financing to be issued commensurate with commercial operation of each of the wind farms. AEP has highlighted a 5 year, $37B capital plan driving 7.4% rate base CAGR which supports the 5-7% EPS CAGR (regulatory lag, holding company debt and equity drive the difference). 2021 guidance was initiated at $3.51-$3.71.

AWK

AWK's resolution of key Pennsylvania and New Jersey rate cases is a strong step forward and should reinforce the market's confidence in AWK's ability to execute. Execution was particularly evident in 2020 as AWK was able to claw back to its original guidance range amidst Covid-19 and the ongoing uncertainty from the two material rate cases in PA and NJ. We see the upcoming 2021 and 2022 fiscal years as de-risked given the rate agreements and expect market focus to turn toward timing of equity in the forecast period, O&M management, and FMVL M&A given the lack of clear challenges ahead. AWK's multiple remains elevated, but near five-year spread averages relative to both the S&P 500 and the broader utility group P/E multiple. Following the rate case conclusions and the clear runway leaves little indication that the multiple will contract in the near term.

CNP

Management's reiteration of the prior 5-7% utility-level EPS CAGR is incrementally positive given our perception that the guidance range contemplates some type of strategic midstream corporate action. The ability to maintain the prior CAGR is viewed favorably as it seemingly overcomes headwinds from a re-allocation of corporate interest previously allocated to the midstream segment and contemplates a roll off of recovery bond equity earnings. We also note that the decision to sell at least one gas LDC business has received a positive reception as it avoids re-levering the holdco after significant debt maturities to come over the next three years. We are also more sanguine on the name following management's inclusion of IN capex in its formal guidance. The IN RFP process is ongoing, but we see the update building confidence that initial stakeholder feedback was positive enough to indicate that CNP wins more renewable build than originally expected. We

continue to model a 'status quo' forecast, but anticipate additional details to come from the December analyst day.

CMS

Management maintained the 6-8% growth rates for EPS and dividend and provided 2021 EPS guidance of $2.84-$2.86. The CMS Gas settlement includes a stay-out provision to avoid a rate case in 2021. CMS has filed for securitization of Karn 1&2 ($703m) and expects to file a new IRP mid-2021. CMS has had marked success at managing costs and work crews to offset any COVID-related headwinds. We expect CMS to refresh capital and financing plans at Q4.

DUK

The 4-6% growth rate is maintained with a bias towards the high end. DUK will provide 2021 guidance on the Q4 call, but has pointed towards expectations at or above $5.15 even with a "Dominion" coal ash outcome in North Carolina. The recent Carolina IRP provides a path to increasing rate base growth from the expected 6.5% CAGR through 2024 to 7% CAGR from 2024 through 2029. We expect earnings growth in the top half of the 4-6% range through 2023 off of a 2021 base.

ED

Management narrowed 2020 EPS guidance to $4.15-$4.30 (from $4.15-$4.35) to reflect COVID-19 impacts. ETRN pushed the expected in-service date for MVP to 2H21 due to pending legal challenges. Management accelerated some clean energy capex from 2021 to 2020 in order to create contingency against deliverables deadlines in planning for a potential second wave (5.5% rate base CAGR through 2022). In 2021 we anticipate more concrete planning regarding onshore and offshore transmission investment opportunities related to offshore wind. Strong execution on cost savings opportunities in 2021 and beyond will be critical to meeting allowed ROEs. We expect an update to financing and capex plans at Q4.

EIX

Focus remains on EIX's ability to settle remaining individual wildfire claims from the 2017 and 2018 seasons and the related equity issuance timing and magnitude. We see the $1bn figure as a helpful marker and should belay overstated credit rating agency concerns about the amount of debt issuance to occur under EIX's capital structure waiver. We still anticipate the individual victim settlement process to be a longer road than most current expectations, but delayed equity issuance and slower ultimate cash outflows could be a silver lining. We think the current discount may subside to some extent as we progress into the latter stages of wildfire season, but note that large fires in EIX's service territory as late as January.

ES

The 5-7% long-term EPS CAGR is maintained, with an expectation of the middle of the range. The CAGR does not reflect the CGMA acquisition, offshore wind, CT/NH grid modernization, or AMI in MA. Management expects to provide EPS commentary on the incremental opportunity from offshore wind at Q4. Management shifted the anticipated commercial operation dates for the three offshore wind projects back by roughly a year, dependant on BOEM review schedules expected to be released in early 2021. The Ørsted/ES partnership has submitted bids into the NY RFP (awards anticipated by EOY). Awards in the MD, NJ and RI RFPs are anticipated mid-2021. Penalties in CT related to Isaias are anticipated mid-2021. ES may be required to file a CT rate case, but otherwise has no plans for rate reviews in 2021.

FE

FE's recent management changes and discussions around financial contingencies to increases flexibility have encouraged us that the Board is moving quickly and taking the

federal investigation seriously. However, the moves could indicate management culpability, or at the least, indelicate ethical violations that could impact FE's ESG perception for the foreseeable future. We expect the FBI investigation to result in negative headlines for some time, but take recent management commentary around potential settlements or announcements in early 2021 at their merit. We look to the 4Q20 call and any investigation announcements for more clarity into financial impacts going forward and continue to monitor regulatory processes for potential impacts. We incorporate the potential for up to $2bn in penalties and fines based on historical precedent. However, with limited balance sheet capacity and our belief that public information regarding the investigation remains in the early stages, we see no reason to expect a re-rating near term.

LNT

LNT's roll forward incorporated some anticipated windfalls from the Iowa Clean Energy Blueprint and reinforced out perception in the achievability of the 5-7% EPS CAGR guidance off the back of strong rate base growth. We believe the capital investment need to hit state targets for renewables and broader sustainability efforts (including electric vehicles) actually affords LNT the ability to grow rate base and earnings at a faster clip, but believe management has concluded that 5-7% is the sweet spot because it allows for palatable customer bill increases under various load scenarios and avoids significant external funding requirements. We continue to value LNT at a 20% premium to the group on LNT's 2023E P/E, reflecting regional peers' valuations that remain above LNT.

NEE

Management expects to achieve 6-8% EPS growth through 2023 off of new adj 2021 guidance, with an assumption of the top of the range, and anticipates 10% dividend growth through at least 2022. NEE increased 2021 guidance due to strength in the renewables pipeline (~1.5 GW added since Q2). Management expects a $60bn 2019-2022 capital plan, an increase of $7.5bn from the previous midpoint.

OGE

The ability to receive approval for a grid modernization rider in OK is a positive step and provides evidence of an improving regulatory climate following years of environmentally-mandated capital. We also maintain a more positive outlook for OGE's ability to consider strategic alternatives to its ENBL stake given its strong balance sheet and ability to weather the loss of cash flows from a sale or other transaction. However, OGE's below-peer rate base and utilities EPS growth rate command a 10% discount P/E to the group average.

PCG

We believe near-term noise around PCG's safety certificate is unlikely to amount to a loss of coverage under the AB 1054 wildfire fund provision, though the proceeding merits close attention as long as there is no ruling beyond the statutory deadline. We also expect heavy investor focus on the securitization process and management appointments. Related to the securitization process, equity issuance timing and magnitude will likely gain increased clarity as we progress toward a May 2021 CPUC decision, per the procedural schedule (earlier with settlement). We see PCG as increasingly attractive as wildfire season nears an end in early 2021. We move PCG's discount to the group average 2023E P/E multiple to 35% to reflect the near-term headwinds and an active wildfire season. We believe the discount embedded in our valuation framework is an easy hurdle given regional peers and would expect PCG to re-rate higher in a risk on environment and see a further tailwind if we move through wildfire season with no additional large-liability fires.

PEG

The near-term focus will continue to be on potential participation in Ørsted's Ocean Wind, offshore wind project, a potential settlement with the NJ BPU on transmission ROE, updates

on the announced intention to divest non-nuclear generation, the NJ BPU report on resource adequacy expected in Q1 2021(will address fixed resource requirement), and a BPU ruling on non-energy efficiency aspects of the clean energy plan. The utility rate base and earnings growth are above average and the utility capital plan does not require equity, nor cashflow from the genco.

PNW

A focus going into 2021, alongside the APS rate case and AZ energy rulemaking, will be the new commissioners joining the AZCC. Commissioner Marquez Peterson (R), Jim O'Connor (R), and Anna Tovar (D), will join Commissioners Kennedy (D) and Olson (R). Though O'Connor was not initially planning on running, Commissioner Olson convinced him to run. We anticipate the two will have similar policy goals, and we look for any early alignment of rhetoric or voting between Commissioners Olson and O'Connor. A new commission chair will be voted on at the first open meeting of 2021, and, if precedent stands, Cmr. Olson would be chair as the most senior majority party member. If Cmrs. Olson and O'Connor have similar philosophies, Commissioner Marquez Peterson may be the deciding vote on contentious issues such as AZ energy rules and retail competition. For more information on the newly elected commissioners, see our note "*Last Bunch of EEI Meetings*," 11/12/20. Management does not plan to initiate FY21 guidance until the current rate case concludes.

SO

Vogtle continues to be the focus. We continue to expect and have modelled regulatory in-service dates for Unit 3 and Unit 4 of 11/21 and 11/22 respectively. Georgia Power will file an integrated resource plan (IRP) in January of 2022, the findings of which will likely be included in a mid-year 2022 rate case filing for new rates (to include Vogtle and the associated fuel savings) in 2023. We believe that the additional free cash flow from Vogtle will drive annual capex increases of $1B, which should increase the EPS CAGR from 4-6% to 5-7%. The dividend payout is expected to drop below 70% in 2023 when Vogtle is on line, providing the opportunity for dividend growth to accelerate from $0.08/share annually to a rate more in line with earnings growth.

SRE

We expect the recent FID decision at ECA to have a limited impact to SRE near term, given the low equity contribution from the SRE balance sheet, but continue to closely monitor the LNG segment as management mulls strategic options for financing future LNG export opportunities and maximize shareholder value as utility companies across the sector opt for pure-play, renewable-driven stories. We think the 'conglomerate discount' currently being ascribed to SRE is too severe and expect a re-rating to occur over the next twelve months as investors gain confidence around the energy outlook for Mexico and Ienova's role in the infrastructure buildout and management continues to seek ways to highlight value for the LNG business and reiterate our Overweight rating.

WEC

Management increased the 5-year capital plan 7.3% to $16.1 bn over 2021-2025 and firmly maintains expectations for 7% rate base growth and 5-7% EPS growth in the long term. Management sees significant bill offsets from O&M and fuel cost savings as legacy generation comes offline in 2023 and 2024 that would keep bill increases at or below the inflation rate. Management estimates legacy generation assets will amount to ~2% of company-estimated total 2025 rate base of $32 billion. Storage has become economic over peaking capacity, and for the first time WEC is adding 600 MW of battery storage to resource plans.

WTRG

WTRG continues to lag the valuation expansion experienced by AWK and other pure-play water peers. One of the drivers, in our view, is a perception of risk around the DELCORA acquisition and we keep a specific focus on the legal proceeding following local election results that flipped party affiliation of the City Council. We also believe WTRG will trade with some correlation to national gas LDC utilities, though we ascribe a 10% premium to the regulated utility group multiple to reflect our perception of People's gas as a higher-quality business mix than most. Finally, we continue to monitor WTRG's catch-up component of the repairs tax election, but remain confident that WTRG will receive an outcome that allows it to maintain its current growth and authorized ROE levels while extending the rate case need out through 2025.

XEL

The 5-7% long-term growth target is maintained. Management initiated 2021 EPS guidance of $2.90-$3.00, consistent with 5-7% long-term growth objective. Electric sales and O&M are both expected to increase 1% while gas sales are expected to remain flat in FY21 relative to FY20. The $22.6bn 2021-2025 capital plan has $1.4bn in upside from incremental renewables investments (mostly from MN Relief and Recovery spending on wind repowering and solar, which would be funded at 50% equity). Average annual capex from 2021-2024 was increased by ~$140 annually over the previous plan. The implied rate base CAGR from 2021-2025 is 6.3% (6.9% including the incremental renewables spending). XEL has requested a MPUC decision on wind repowering by EOY and expects a decision on solar investments in Q2 or Q3 of 2021. PSCo's AGIS rider filing was dismissed on procedural grounds. PSCo can still defer ~80% of AGIS-related costs for future recovery and does not believe there is any read-through to the wildfire rider filing. The MN PUC must decide whether to implement interim rates or approve the stay-out request by EOY (regardless, capital plans will not be impacted).

Relative Group Valuation and PE Disparity

P/E Disparity Starting to Show Signs of Life for Value

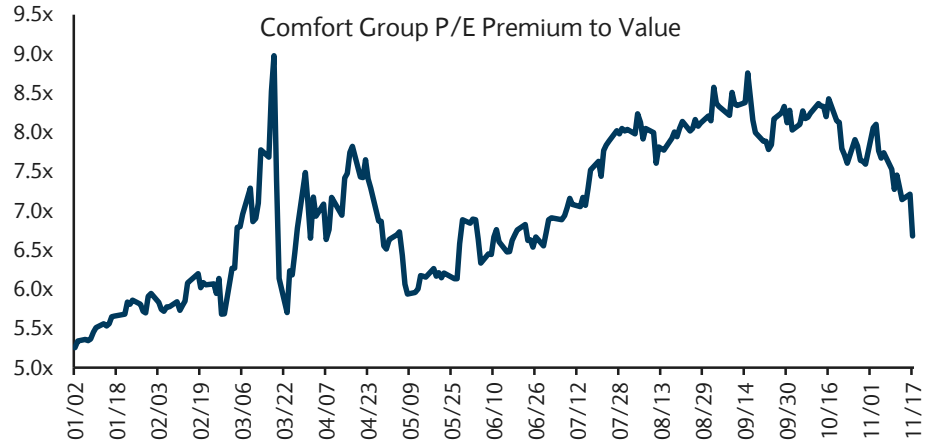
Between the lack of a "blue wave" and positive news on the COVID-19 vaccine front value or 'risk on' names have begun to show evidence of revaluing higher toward 'comfort' names premiums that had increased throughout the year. This contraction has been long-awaited by the market given the historically high spreads and a belief that the spread was unsustainable. We highlight that there is still room to go for the value trade, but are encouraged by signs that fundamentals are beginning to matter as flows move in the direction of more realistic valuation of idiosyncratic risks.

The constituent stocks for our discounted 'value' and high-premium 'comfort' groups displayed in the graphic is broken out below.

Comfort: AEE, CMS, NEE, LNT, ES, WEC, XEL,

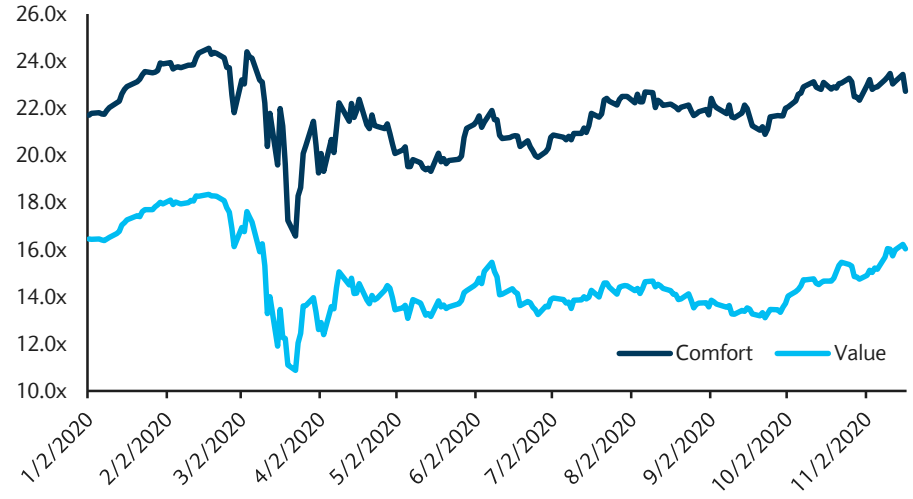
Value: CNP, DUK, EIX, NWE, PCG, PNM, PNW, SO, SRE

FIGURE 2
Spread between Value and Comfort Groups (2yr Blended Fwd P/E)



Source: Bloomberg, Barclays Research

FIGURE 3
Comfort and Value Group P/E (2yr Blended Fwd P/E)



Source: Bloomberg, Barclays Research

Valuation Methodology

We have updated our valuation methodology to use relative premiums and discounts to the 2023 regulated group average PE multiple applied to our 2023 EPS estimates combined with any sum of the parts valuation aspects updated to 2023 expectations.

Our previous valuation methodology used relative premiums and discounts to the 2022 regulated group average PE multiple applied to our 2022 EPS estimates combined with any sum of the parts valuation aspects based on 2022 expectations.

AEE

Our current $95 price target is premised upon a 20% premium applied to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS of $4.28.

Our previous $79 price target was premised upon a 20% premium applied to the 2022 utility group average PE multiple of 17x applied to the prior Barclays 2022E EPS of $3.90.

AEP

Our current $107 price target is premised upon a 10% premium applied to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS of $5.28.

Our previous $93 price target was premised upon a 10% premium applied to the 2022 utility group average PE multiple of 17x applied to the Barclays prior 2022E EPS of $4.97.

AWK

To derive our $173 price target, we utilize a group average water P/E multiple for 2023 earnings and apply a 15% premium to AWK's consolidated 2023 EPS estimate of $5.01. The premium reflects strong management, constructive regulatory exposure, and top-tier growth visibility following key rate case outcomes.

Our previous $138 price target was premised on a 15% premium to the previous 2022 group average water multiple of 27x for AWK applied to our previous 2022 EPS estimate of $4.46

CMS

Our current $75 price target is premised upon a 25% premium applied to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS of $3.25.

Our previous $65 price target was premised upon a 25% premium applied to the 2022 utility group average PE multiple of 17x applied to the Barclays 2022E EPS of $3.09 estimate.

CNP

Our current $27 price target is premised upon a 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E utility EPS estimate of $1.38 after allocating parent debt and operating expenses. We use the current ENBL price of $5 adjusted for CNP's ownership, adjusted for allocated debt – leaving $2 of ENBL value to CNP on a consolidated basis.

Our previous price target of $21 used a group average utility multiple of 17x applied to 2022E prior utility EPS of $1.46 and the prior ENBL share price of $4.

DUK

Our current $102 price target is premised upon a 5% discount applied to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS of $5.81.

Our previous $87 price target was premised upon a 5% discount applied to the 2022 utility group average PE multiple of 17x applied to the Barclays prior 2022E EPS of $5.39.

ES

Our current $100 price target is premised upon a 25% premium to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS of $4.34.

Our previous $88 price target was premised upon a 25% premium to the 2022 utility group average PE multiple of 17x applied to the Barclays prior 2022E EPS of $4.15.

EIX

Our $69 price target is based on a 20% discount to the 2023 group average multiple of 18.5x applied to an adjusted, post wildfire liability and additional funding, Barclays 2023 EPS estimate of $5.12. The 20% discount is based upon perceived wildfire risk absent a test of AB 1054 cost recovery standards and remaining uncertainty on 2017 and 2018 wildfire liabilities.

Our previous $57 price target was premised upon a 25% discount applied to the 2022 utility group average PE multiple of 17x applied to the Barclays prior 2022E EPS of $4.65.

ED

Our current $83 price target is premised upon a 10% discount to the 2023 group average P/E multiple of 18.5x applied to our 2023 EPS estimate of $4.94.

Our prior price target of $74 was premised upon a 10% discount to the 2022 group average P/E multiple of 17x applied to our prior 2022 EPS estimate of $4.73.

FE

Our $33 price target for FE is based on a 30% discount to the group average 2023 multiple of 18.5x applied to our pro forma FY23 EPS estimate, adjusted for an assumed $2bn equity issuance to reflect balance sheet repair following fines or penalties. The 30% discount is based on our expectation that the ongoing Ohio corruption investigation serves as an overhang to the stock valuation regardless of the financial impact.

Our previous $32 price target was premised upon a 30% discount applied to the 2022 utility group average PE multiple of 17x applied to our unchanged 2022E EPS estimate of $2.73.

LNT

Our LNT price target is $65. We utilize a relative target P/E multiple to value LNT shares. We apply a 20% premium to the 18.5x group average 2023 P/E multiple using EPS of $2.94 to reflect LNT's strong track record for execution, visible earnings growth, attractive rate base growth opportunities driven by renewable generation that limit customer bill inflation, and constructive regulatory oversight.

Our previous $56 price target was premised upon a 20% premium to the 2022 group average multiple applied to our prior 2022 EPS estimate of $2.73.

NEE

Our new price target of $87 is premised upon a SOTP with a 20% premium to the 2023 group average PE multiple of 18.5x applied to our 2023 EPS estimate of $1.74, a 17.5x 23E EV/EBITDA for the NEER business – comparable to valuations of renewables developers such as Ørsted. We then add $3 for NEP as we take the Barclays $67 NEP price target and flow it through to represent NEE's ownership.

Our previous price target of $301 was premised upon a SOTP with a 20% premium to the 2022 group average PE multiple of 17x applied to our 2022 EPS estimate of $6.43, a 16x 22E EV/EBITDA for the NEER business – comparable to valuations of renewables developers such as Ørsted. We then add $13 for NEP as we take the Barclays $61 NEP price target and flow it through to represent NEE's ownership.

NI

Our current $29 price target is premised upon the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS estimate of $1.55.

Our prior $25 price target was premised upon a 5% premium to the 2022 regulated utility group average P/E applied to our prior 2022 EPS estimate of $1.42.

NWE

Our current $63 price target is premised upon a 10% discount applied to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS of $3.79.

Our previous $59 price target was premised upon a 10% discount applied to the 2022 utility group average PE multiple of 17x applied to the Barclays prior 2022E EPS of $3.83.

OGE

We derive our $36 price target by applying a 10% discount to the group average multiple of 18.5x applied to our 2023 utility earnings estimate combined with the current ENBL price $5 applied to the 111 units that OGE owns. Our 10% discount reflects below average earnings CAGR compared to the group.

Our previous $33 price target utilized a group average P/E multiple of 17x reflecting our view that earnings growth could expand following the approval of certain regulatory riders and grid modernization opportunities.

PEG

Our current $65 price target is premised upon a 5% premium to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023 utility net parent EPS estimate, resulting in a $62 valuation for the utility. We then use a 5x EV/EBITDA multiple on 2023 generation EBITDA applied to the Barclays 2023 generation EBITDA estimate resulting in $3.25 valuation for PEG Power. Combining the utility $62 valuation and the $3.25 PEG Power valuation yields our $65 price target.

Our previous $59 price target was premised upon a 10% premium to the 2022 utility group average PE multiple of 17x applied to the Barclays 2022 utility net parent EPS estimate, resulting in a $55 valuation for the utility. We then used a 5x EV/EBITDA multiple on 2022 generation EBITDA applied to the Barclays 2022 generation EBITDA estimate resulting in $3.70 valuation for PEG Power. Combining the utility $55 valuation and the $3.70 PEG Power valuation yielded our $59 price target.

PCG

We move PCG's discount to the group average 23E P/E multiple to 35% to reflect the near-term headwinds and an active wildfire season. We believe the discount embedded in our valuation framework is an easy hurdle given regional peers and would expect PCG to re-rate higher in a risk on environment and see a further tailwind if we move through wildfire season with no additional large-liability fires. The P/E multiple is applied to our 2023 EPS estimate of $1.25, which gives a price target of $14.

Our previous $13 price target was premised on a 25% discount to the 2022 utility group average PE of 17x applied to the prior Barclays 2022E EPS of $1.08.

PNM

Our current $50 price target is premised upon the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS estimate of $2.68. Our price target remains consistent with the terms of the AGR acquisition offer.

Our previous $50 price target was premised upon the terms of the AGR acquisition offer.

PNW

Our current $103 price target is premised upon the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS estimate of $5.56.

Our previous $89 price target was premised upon the 2022 utility group average PE multiple of 17x applied to the Barclays 2022E EPS estimate of $5.22.

SO

Our $73 price target is premised on the 2023 group average PE multiple of 18.5x applied to our 2023 earnings estimate of $3.92. The group average multiple is based on a discount for the risk of Vogtle construction offsetting the premium valuation SO deserves based on fundamentals post commercial operation of Vogtle.

Our previous $61 price target was premised on a 5% discount to the 2022 group average PE multiple of 17x applied to our prior 2022 earnings estimate of $3.60 and then add the NPV of the Vogtle earnings uplift of $0.20 and apply 5% discount to the group average 2022.

SRE

We utilize a sum of the parts valuation framework for our $159 price target for SRE. We apply a relative P/E multiple premium / discount to the North American utility businesses a base group average (10% premium for Texas, 15% for SoCalGas, group average for SDG&E). We utilize the Barclays' Ienova price target and adjust for SRE ownership and spot USDMXN for Peso translation. We utilize a probability-weighted DCF approach for the LNG business depending on where each facility is on securing contracting for export capacity.

Our previous $146 price target was derived using the same methodology, but prior 2022 EPS of $8.49 and 2022E P/E multiple of 17x for the group.

WTRG

Our $50 price target is arrived at using our methodology where we value WTRG's water business using a 5% premium to the 2023 water group average P/E multiple. The 5% premium reflects strong regulatory exposure and public M&A opportunities, balanced by growth visibility lower than peers. We value the regulated gas business at a 15% premium to reflect a strong growth profile and familiar regulatory exposure.

Our previous $45 price target was premised on a 5% premium to the 2020 group average water multiple of 27x applied to the $1.24 2022 earnings contribution from the water business combined with a 15% premium to the 2022 regulated utility group average multiple of 17x applied to the $0.72 2022 earnings contribution from the LDC business, less the 2022 parent drag eps of $0.15 at a blended multiple of 25.8x

WEC

Our current $107 price target is premised upon a 30% premium to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS estimate of $4.45.

Our previous $94 price target was premised upon a 30% premium to the 2022 utility group average PE multiple of 17x applied to the prior Barclays 2022E EPS estimate of $4.24.

XEL

Our current $82 price target is premised upon a 30% premium to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS estimate of $3.40.

Our previous $70 price target was premised upon a 30% premium to the 2022 utility group average PE multiple of 17x applied to the Barclays 2022E EPS estimate of $3.15.

North America Power & Utilities **Industry View: POSITIVE**

Ameren Corp. (AEE)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	5,910	5,987	6,242	6,379	2.6%
EBITDA (adj)	2,262	2,389	2,615	2,784	7.2%
EBIT (adj)	1,267	1,364	1,561	1,701	10.3%
Pre-tax income (adj)	1,016	1,087	1,233	1,348	9.9%
Net income (adj)	828	844	953	1,042	8.0%
EPS (adj) ($)	3.35	3.38	3.73	4.00	6.1%
Diluted shares (mn)	247.1	249.4	255.7	260.4	1.8%
DPS ($)	1.92	1.98	2.04	2.10	3.0%

Margin and return data					Average
EBITDA (adj) margin (%)	38.3	39.9	41.9	43.6	40.9
EBIT (adj) margin (%)	21.4	22.8	25.0	26.7	24.0
Pre-tax (adj) margin (%)	17.2	18.2	19.8	21.1	19.1
Net (adj) margin (%)	14.0	14.1	15.3	16.3	14.9
ROIC (%)	7.1	6.3	6.6	6.7	6.7
ROA (%)	3.0	2.9	2.9	3.0	3.0
ROE (%)	10.9	10.5	10.6	10.0	10.5

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	24,376	26,181	28,116	30,021	7.2%
Cash and equivalents	16	1,954	1,919	1,794	382.2%
Total assets	28,933	32,676	34,576	36,356	7.9%
Short and long-term debt	9,797	12,576	13,120	14,102	12.9%
Other long-term liabilities	9,312	9,312	9,312	9,312	0.0%
Total liabilities	20,732	23,511	24,055	25,037	6.5%
Shareholders' equity	8,059	9,023	10,379	11,177	11.5%
Net debt/(funds)	9,781	10,622	11,201	12,308	8.0%
Change in working capital	80	1,690	-613	-57	N/A
Cash flow from operations	2,170	2,381	2,989	2,486	4.6%
Capital expenditure	-2,411	-2,830	-2,988	-2,988	N/A
Free cash flow	-713	-942	-520	-1,048	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	24.1	23.8	21.6	20.1	22.4
EV/EBITDA (adj) (x)	13.0	12.7	11.8	11.5	12.2
EV/EBIT (adj) (x)	23.2	22.2	19.8	18.8	21.0
FCF yield (%)	-2.4	-3.1	-1.7	-3.3	-2.6
P/BV (x)	2.5	2.2	2.0	1.9	2.1
Dividend yield (%)	2.4	2.5	2.5	2.6	2.5
Net debt/EBITDA (adj) (x)	4.3	4.4	4.3	4.4	4.4

Selected operating metrics					Average
Payout ratio (%)	57.3	58.4	54.6	52.4	55.7
Interest cover (x)	3.3	3.3	3.4	3.5	3.4
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 80.60**
Price Target	**USD 95.00**

Why Equal Weight? AEE is a quality name with 5-7% growth that is visible for an extended period of time and we see the name deserving of a 20% premium to the group. Given the current price and premium we see increased uncertainty surrounding the regulatory construct in IL as balanced by incremental potential growth opportunities, resulting in our EW rating.

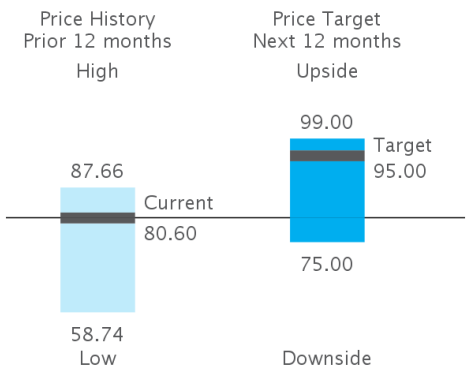
Upside case **USD 99.00**

Our upside case reflects a 25% premium to the 2023 group average P/E multiple applied to our 2023 EPS estimate.

Downside case **USD 75.00**

Our downside case reflects a 5% discount to the 2023 group average P/E multiple applied to our 2023 EPS estimate.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

American Electric Power Company, Inc. (AEP)

Stock Rating: OVERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	15,602	16,968	17,425	17,984	4.8%
EBITDA (adj)	8,504	5,675	5,998	6,516	-8.5%
EBIT (adj)	5,990	3,074	3,247	3,592	-15.7%
Pre-tax income (adj)	2,009	2,336	2,496	2,799	11.7%
Net income (adj)	2,095	2,159	2,308	2,584	7.2%
EPS (adj) ($)	4.23	4.35	4.62	5.00	5.7%
Diluted shares (mn)	494.9	496.0	499.0	516.4	1.4%
DPS ($)	2.68	2.84	3.01	3.19	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	54.5	33.4	34.4	36.2	39.7
EBIT (adj) margin (%)	38.4	18.1	18.6	20.0	23.8
Pre-tax (adj) margin (%)	12.9	13.8	14.3	15.6	14.1
Net (adj) margin (%)	13.4	12.7	13.2	14.4	13.4
ROIC (%)	12.9	6.1	6.0	6.1	7.8
ROA (%)	3.0	3.0	3.0	3.2	3.1
ROE (%)	11.0	10.4	11.0	12.0	11.1

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	79,585	85,385	91,915	99,962	7.9%
Cash and equivalents	311	931	956	855	40.1%
Total assets	72,748	76,567	80,371	85,393	5.5%
Short and long-term debt	25,648	29,166	32,478	37,120	13.1%
Other long-term liabilities	19,338	19,338	19,338	19,338	0.0%
Total liabilities	52,076	55,594	58,906	63,548	6.9%
Shareholders' equity	20,672	20,973	21,464	21,845	1.9%
Net debt/(funds)	25,337	28,236	31,523	36,265	12.7%
Change in working capital	776	14	905	503	-13.4%
Cash flow from operations	5,485	4,889	5,058	5,508	0.1%
Capital expenditure	-6,500	-5,800	-6,530	-8,047	N/A
Free cash flow	-2,341	-2,320	-2,975	-4,187	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	20.5	19.9	18.8	17.3	19.1
EV/EBITDA (adj) (x)	8.0	12.5	12.4	12.1	11.3
EV/EBIT (adj) (x)	11.4	23.1	22.9	22.0	19.8
FCF yield (%)	-3.4	-3.3	-4.0	-5.3	-4.0
P/BV (x)	2.1	2.1	2.0	2.1	2.0
Dividend yield (%)	3.1	3.3	3.5	3.7	3.4
Net debt/EBITDA (adj) (x)	3.0	5.0	5.3	5.6	4.7

Selected operating metrics					Average
Payout ratio (%)	63.3	65.3	65.1	63.8	64.4
Interest cover (x)	5.6	2.6	2.7	2.9	3.5
Regulated (%)	92.9	91.2	92.3	92.2	92.2

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	USD 86.73
Price Target	USD 107.00

Why Overweight? We assign an Overweight rating as we believe AEP should trade at a 10% premium to the average regulated utility multiple. This is supported by top-tier EPS growth target of 5-7% with a bias towards the high end.

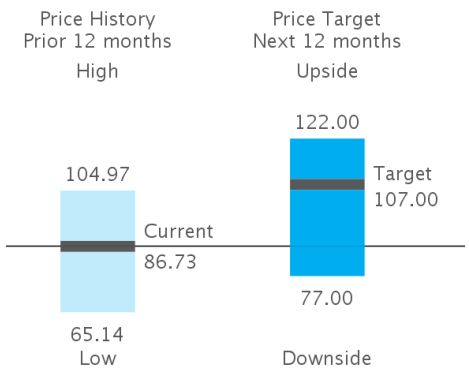
Upside case — **USD 122.00**

Our upside case reflects a 20% premium to the utility group average P/E multiple , applied to higher earnings driven by additional rate base growth and a favorable rate case outcomes.

Downside case — **USD 77.00**

Our downside case reflects a 20% discount to the utility group average P/E multiple, applied to lower earnings driven by slower rate base growth and unfavorable rate outcomes

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

American Water Works Company, Inc. (AWK)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	3,610	3,828	4,054	4,315	6.1%
EBITDA (adj)	2,032	2,231	2,382	2,541	7.7%
EBIT (adj)	1,450	1,606	1,717	1,831	8.1%
Pre-tax income (adj)	833	944	1,034	1,139	11.0%
Net income (adj)	621	705	772	850	11.0%
EPS (adj) ($)	3.77	3.89	4.25	4.63	7.1%
Diluted shares (mn)	181	181	182	184	0.5%
DPS ($)	1.96	2.15	2.34	2.55	9.2%

Margin and return data					Average
EBITDA (adj) margin (%)	56.3	58.3	58.8	58.9	58.1
EBIT (adj) margin (%)	40.2	42.0	42.4	42.4	41.7
Pre-tax (adj) margin (%)	23.1	24.7	25.5	26.4	24.9
Net (adj) margin (%)	17.2	18.4	19.0	19.7	18.6
ROIC (%)	9.3	10.0	10.2	10.3	9.9
ROA (%)	2.9	3.1	3.3	3.5	3.2
ROE (%)	10.6	11.5	11.9	12.3	11.6

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	23,941	25,741	27,496	29,426	7.1%
Cash and equivalents	60	41	47	68	4.1%
Total assets	22,682	23,272	24,369	25,609	4.1%
Short and long-term debt	9,453	9,552	9,971	10,091	2.2%
Other long-term liabilities	0	0	0	0	N/A
Total liabilities	7,917	8,341	8,326	8,605	2.8%
Shareholders' equity	6,121	6,502	6,918	7,749	8.2%
Net debt/(funds)	9,393	9,511	9,923	10,023	2.2%
Change in working capital	504	-585	7	21	-65.6%
Cash flow from operations	1,383	1,441	1,699	1,849	10.2%
Capital expenditure	-1,654	-1,650	-1,555	-1,755	N/A
Free cash flow	-859	-749	-482	-550	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	42.3	40.9	37.5	34.4	38.8
EV/EBITDA (adj) (x)	18.9	17.2	16.3	15.3	16.9
EV/EBIT (adj) (x)	26.4	23.9	22.6	21.3	23.6
FCF yield (%)	-2.2	-1.9	-1.2	-1.4	-1.7
P/BV (x)	4.7	4.4	4.2	3.8	4.3
Dividend yield (%)	1.2	1.3	1.5	1.6	1.4
Net debt/EBITDA (adj) (x)	4.6	4.3	4.2	3.9	4.2

Selected operating metrics					Average
Payout ratio (%)	57.1	55.3	55.2	55.1	55.7
Interest cover (x)	3.8	4.2	4.5	4.9	4.4
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 159.29**
Price Target	**USD 173.00**

Why Equal Weight? AWK presents a strong growth profile with top-tier management and a solid execution track record, however valuation is stretched relative to electric and gas utilties and our valuation framework implies a 15% premium to the water group average P/E multiple, all of which is fully reflected in the current stock price

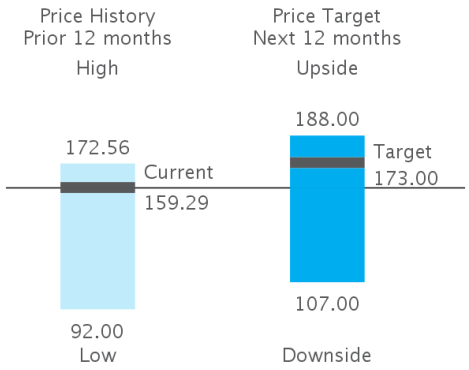
Upside case **USD 188.00**

Our upside case assumes AWK trades at a 25% premium to the group average water utility P/E multiple. We believe this scenario could materialize if ESG flows increase or general utility equity demand rises and disproportionately benefits AWK.

Downside case **USD 107.00**

Our downside case values AWK on the same 15% premium, but applies the group utitlity multiple in lieu of the water group multiple. This could materialize if investors perceive long-term growth opportunities and ESG profiles to be similar to electric and gas.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

CenterPoint Energy, Inc. (CNP)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	11,111	7,551	7,808	7,983	-10.4%
EBITDA (adj)	2,348	2,531	2,725	2,840	6.5%
EBIT (adj)	1,111	1,336	1,472	1,579	12.4%
Pre-tax income (adj)	813	995	1,099	1,204	14.0%
Net income (adj)	587	714	813	957	17.7%
EPS (adj) ($)	1.17	1.27	1.36	1.53	9.3%
Diluted shares (mn)	501.0	560.1	598.4	626.4	7.7%
DPS ($)	1.15	0.74	0.60	0.64	-18.0%

Margin and return data					Average
EBITDA (adj) margin (%)	21.1	33.5	34.9	35.6	31.3
EBIT (adj) margin (%)	10.0	17.7	18.8	19.8	16.6
Pre-tax (adj) margin (%)	7.3	13.2	14.1	15.1	12.4
Net (adj) margin (%)	5.3	9.5	10.4	12.0	9.3
ROIC (%)	4.9	6.8	6.5	7.2	6.4
ROA (%)	1.7	2.0	2.2	2.5	2.1
ROE (%)	7.1	7.2	7.7	8.6	7.7

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	20,650	21,797	23,113	24,472	5.8%
Cash and equivalents	1,124	0	6	11	-78.4%
Total assets	35,263	35,262	36,647	38,071	2.6%
Short and long-term debt	14,244	9,665	12,072	10,695	-9.1%
Other long-term liabilities	8,809	8,809	9,778	10,746	6.9%
Total liabilities	27,012	25,311	26,142	27,724	0.9%
Shareholders' equity	8,251	9,951	10,505	11,113	10.4%
Net debt/(funds)	13,120	9,665	12,066	10,684	-6.6%
Change in working capital	-3,263	-4,023	2,572	-2,005	N/A
Cash flow from operations	1,638	2,051	2,104	2,207	10.4%
Capital expenditure	2,506	2,342	2,569	2,620	1.5%
Free cash flow	3,567	3,978	4,314	4,429	7.5%

Valuation and leverage metrics					Average
P/E (adj) (x)	21.5	19.7	18.5	16.5	19.1
EV/EBITDA (adj) (x)	11.0	8.8	9.1	8.2	9.3
EV/EBIT (adj) (x)	23.2	16.7	16.8	14.8	17.8
FCF yield (%)	13.9	17.9	17.5	19.0	17.1
P/BV (x)	1.5	1.4	1.4	1.4	1.4
Dividend yield (%)	4.6	2.9	2.4	2.5	3.1
Net debt/EBITDA (adj) (x)	5.6	3.8	4.4	3.8	4.4

Selected operating metrics					Average
Payout ratio (%)	98.3	58.0	44.2	41.6	60.5
Interest cover (x)	2.0	2.7	2.6	2.8	2.5
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 25.17**
Price Target	**USD 27.00**

Why Equal Weight? We see upside potential from activist involvement and valuation expansion balanced by uncertainty on asset sales, strategic actions with Enable. We await results of the business review and see reduced risk now that the CEO and CFO positions have been filled with strong candidates.

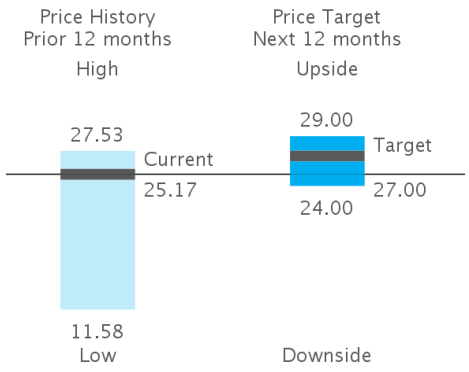
Upside case — **USD 29.00**

Our upside case for CNP values the company's Utility business on a 5% premium to the group average multiple for 2022 and utilizes the Barclays MLP upside case for ENBL.

Downside case — **USD 24.00**

Our downside case for CNP values the Utility business on a 20% discount to the group average multiple for 2022. We use the Barclays MLP team's downside case for ENBL.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

CMS Energy Corporation (CMS)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	6,845	6,949	7,096	7,299	2.2%
EBITDA (adj)	2,231	2,370	2,488	2,663	6.1%
EBIT (adj)	1,239	1,329	1,388	1,510	6.8%
Pre-tax income (adj)	829	935	1,006	1,108	10.2%
Net income (adj)	708	768	825	906	8.6%
EPS (adj) ($)	2.49	2.67	2.84	3.10	7.6%
Diluted shares (mn)	284.3	287.4	290.1	292.4	0.9%
DPS ($)	1.53	1.64	1.75	1.87	7.0%

Margin and return data					Average
EBITDA (adj) margin (%)	32.6	34.1	35.1	36.5	34.6
EBIT (adj) margin (%)	18.1	19.1	19.6	20.7	19.4
Pre-tax (adj) margin (%)	12.1	13.5	14.2	15.2	13.7
Net (adj) margin (%)	10.3	11.0	11.6	12.4	11.4
ROIC (%)	7.3	6.9	7.2	7.2	7.2
ROA (%)	2.5	2.7	2.8	2.9	2.7
ROE (%)	13.5	13.7	13.6	13.8	13.6

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	18,926	20,085	21,685	22,832	6.5%
Cash and equivalents	157	942	97	207	9.6%
Total assets	26,837	28,781	29,536	30,793	4.7%
Short and long-term debt	11,951	13,576	13,186	14,283	6.1%
Other long-term liabilities	383	383	383	383	0.0%
Total liabilities	21,782	23,177	23,462	24,209	3.6%
Shareholders' equity	5,055	5,604	6,073	6,583	9.2%
Net debt/(funds)	11,794	12,634	13,089	14,077	6.1%
Change in working capital	-217	1,015	-1,520	460	N/A
Cash flow from operations	1,790	1,811	1,928	2,061	4.8%
Capital expenditure	-2,104	-2,200	-2,700	-2,300	N/A
Free cash flow	-750	-860	-1,280	-787	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	25.6	23.9	22.4	20.6	23.1
EV/EBITDA (adj) (x)	13.4	13.0	12.5	12.1	12.7
EV/EBIT (adj) (x)	24.1	23.1	22.5	21.3	22.7
FCF yield (%)	-2.5	-2.8	-4.1	-2.4	-3.0
P/BV (x)	3.6	3.3	3.0	2.8	3.2
Dividend yield (%)	2.4	2.6	2.7	2.9	2.7
Net debt/EBITDA (adj) (x)	5.3	5.3	5.3	5.3	5.3

Selected operating metrics					Average
Payout ratio (%)	61.4	61.3	61.6	60.5	61.2
Interest cover (x)	2.8	3.1	3.3	3.5	3.2
Regulated (%)	93.1	93.3	93.4	93.6	93.3

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 63.83**
Price Target	**USD 75.00**

Why Equal Weight? We see the current valuation as fair given a constructive regulatory jurisdiction, 10-year capex backlog, above-average earnings/dividend growth, and a long history of achieveing or exceeding results through capital and O&M managment.

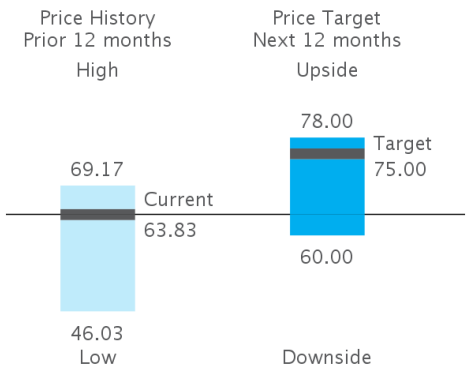
Upside case — **USD 78.00**

Our upside case values CMS at a 30% premium to the regulated utility average multiple applied to our 2023 EPS estimate.

Downside case — **USD 60.00**

Our downside case values CMS at the regulated utility average multiple applied to our 2023 EPS estimate.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Consolidated Edison, Inc. (ED)

Stock Rating: UNDERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	12,574	12,778	13,164	13,642	2.8%
EBITDA (adj)	4,360	4,776	5,041	5,316	6.8%
EBIT (adj)	6,044	6,702	7,094	7,522	7.6%
Pre-tax income (adj)	1,736	1,943	2,080	2,231	8.7%
Net income (adj)	1,438	1,438	1,546	1,666	5.0%
EPS (adj) ($)	4.36	4.25	4.47	4.72	2.7%
Diluted shares (mn)	329.5	338.7	346.0	352.8	2.3%
DPS ($)	2.96	3.06	3.17	3.28	3.5%

Margin and return data					Average
EBITDA (adj) margin (%)	34.7	37.4	38.3	39.0	37.3
EBIT (adj) margin (%)	21.3	22.3	22.7	22.8	22.3
Pre-tax (adj) margin (%)	13.8	15.2	15.8	16.4	15.3
Net (adj) margin (%)	11.5	12.0	12.5	12.9	12.2
ROIC (%)	7.3	7.1	6.8	6.8	7.0
ROA (%)	2.7	2.6	2.7	2.8	2.7
ROE (%)	8.6	8.5	8.6	8.6	8.6

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	43,889	46,355	48,337	50,171	4.6%
Cash and equivalents	1,217	2,050	1,128	1,388	4.5%
Total assets	58,079	61,378	62,438	64,532	3.6%
Short and long-term debt	18,527	20,690	23,230	24,246	9.4%
Other long-term liabilities	4,993	4,993	4,993	4,993	0.0%
Total liabilities	15,052	15,052	15,052	15,052	0.0%
Shareholders' equity	18,022	19,219	20,416	21,670	6.3%
Net debt/(funds)	17,310	18,640	22,102	22,858	9.7%
Change in working capital	139	160	0	0	-100.0%
Cash flow from operations	3,134	3,461	3,696	3,968	8.2%
Capital expenditure	-3,996	-4,392	-4,035	-4,040	N/A
Free cash flow	-1,028	-1,110	-914	-505	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	18.2	18.7	17.7	16.8	17.8
EV/EBITDA (adj) (x)	9.8	9.2	9.4	9.1	9.4
EV/EBIT (adj) (x)	7.1	6.6	6.7	6.4	6.7
FCF yield (%)	-2.4	-2.5	-1.9	-1.0	-2.0
P/BV (x)	1.4	1.4	1.3	1.3	1.4
Dividend yield (%)	3.7	3.9	4.0	4.1	3.9
Net debt/EBITDA (adj) (x)	4.0	3.9	4.4	4.3	4.1

Selected operating metrics					Average
Payout ratio (%)	67.8	72.2	71.0	69.5	70.1
Interest cover (x)	3.0	3.1	3.0	3.0	3.0
Regulated (%)	0.0	0.0	0.0	0.0	0.0

Price (17-Nov-2020)	**USD 79.25**
Price Target	**USD 83.00**

Why Underweight? We rate ED Underweight as we believe the current valuation is stretched based on a lack luster rate outcome for CECONY which drives a lower growth profile. We see the lower than group average growth as driving a 10% discount to the 2023 group average multiple.

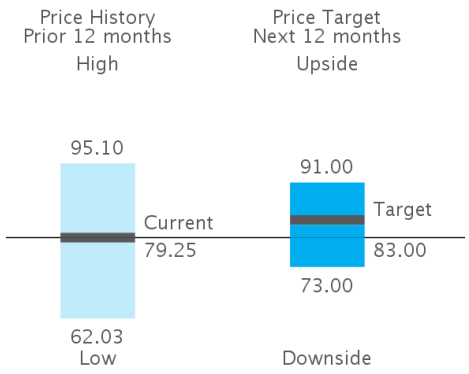
Upside case — **USD 91.00**

Our upside case reflects the utility group average P/E multiple to portray potentially higher earnings from additional rate base growth and a favorable O&R rate case outcome.

Downside case — **USD 73.00**

Our downside case reflects a 20% discount to the regulated group to reflect potentially lower earnings driven by lower sales growth and investment because of REV.

Upside/Downside scenarios



Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

North America Power & Utilities — **Industry View: POSITIVE**

Duke Energy Corporation (DUK)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	25,079	25,577	26,509	27,242	2.8%
EBITDA (adj)	10,257	10,697	11,321	11,941	5.2%
EBIT (adj)	5,709	6,000	6,431	6,861	6.3%
Pre-tax income (adj)	4,097	4,235	4,482	4,765	5.2%
Net income (adj)	3,707	3,792	4,008	4,243	4.6%
EPS (adj) ($)	5.08	5.14	5.24	5.51	2.7%
Diluted shares (mn)	729.5	737.0	765.1	770.3	1.8%
DPS ($)	3.79	3.97	4.17	4.38	5.0%

Margin and return data					Average
EBITDA (adj) margin (%)	40.9	41.8	42.7	43.8	42.3
EBIT (adj) margin (%)	22.8	23.5	24.3	25.2	23.9
Pre-tax (adj) margin (%)	16.3	16.6	16.9	17.5	16.8
Net (adj) margin (%)	14.8	14.8	15.1	15.6	15.1
ROIC (%)	5.3	5.4	5.8	6.1	5.6
ROA (%)	2.5	2.4	2.5	2.6	2.5
ROE (%)	8.5	8.2	8.2	8.8	8.4

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	146,916	156,091	164,766	173,316	5.7%
Cash and equivalents	276	779	549	290	1.8%
Total assets	156,797	161,730	164,898	168,123	2.4%
Short and long-term debt	61,947	63,177	63,714	66,277	2.3%
Other long-term liabilities	40,092	41,413	44,745	46,393	5.0%
Total liabilities	110,553	113,104	116,975	121,188	3.1%
Shareholders' equity	46,292	48,697	48,017	47,052	0.5%
Net debt/(funds)	61,671	62,399	63,165	65,987	2.3%
Change in working capital	95	950	1,202	107	3.8%
Cash flow from operations	9,086	9,220	9,629	10,053	3.4%
Capital expenditure	-11,100	-10,550	-9,675	-9,050	N/A
Free cash flow	-4,775	-4,260	-3,239	-2,372	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	18.3	18.1	17.7	16.9	17.8
EV/EBITDA (adj) (x)	12.4	12.0	11.4	11.0	11.7
EV/EBIT (adj) (x)	22.3	21.4	20.1	19.2	20.7
FCF yield (%)	-3.7	-3.3	-2.5	-1.8	-2.8
P/BV (x)	1.5	1.4	1.5	1.5	1.5
Dividend yield (%)	4.1	4.3	4.5	4.7	4.4
Net debt/EBITDA (adj) (x)	6.0	5.8	5.6	5.5	5.7

Selected operating metrics					Average
Payout ratio (%)	74.5	77.3	79.7	79.6	77.7
Interest cover (x)	2.6	2.6	2.6	2.6	2.6
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020) USD 92.92
Price Target USD 102.00

Why Equal Weight? We view DUK as a solid regulated company with a credible long-term investment plan. We see earnings growth rebounding back to the 4-6% off of a 2021 earnings base given the removal of ACP earnings from 2020 and 2021 earnings

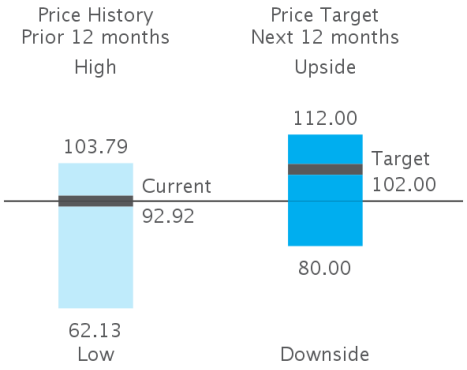
Upside case USD 112.00

Our upside case uses a 5% premium to the 2023 group average P/E multiple applied to our 2021 EPS estimate.

Downside case USD 80.00

Our downside case uses a 10% discount to the 2023 group average P/E multiple applied to our 2021 estimate.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Edison International (EIX)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	12,347	12,967	13,234	13,576	3.2%
EBITDA (adj)	3,505	4,401	4,705	5,083	13.2%
EBIT (adj)	1,775	2,410	2,559	2,762	15.9%
Pre-tax income (adj)	1,127	1,725	1,819	1,924	19.5%
Net income (adj)	1,284	1,644	1,736	1,845	12.8%
EPS (adj) ($)	4.70	4.43	4.58	4.85	1.1%
Diluted shares (mn)	339.7	371.2	378.9	380.1	3.8%
DPS ($)	2.45	2.55	2.58	2.61	2.2%

Margin and return data					Average
EBITDA (adj) margin (%)	28.4	33.9	35.5	37.4	33.8
EBIT (adj) margin (%)	14.4	18.6	19.3	20.3	18.2
Pre-tax (adj) margin (%)	9.1	13.3	13.7	14.2	12.6
Net (adj) margin (%)	10.4	12.7	13.1	13.6	12.4
ROIC (%)	5.2	6.5	6.5	6.6	6.2
ROA (%)	3.6	3.6	3.6	3.8	3.6
ROE (%)	10.1	10.6	10.2	10.4	10.4

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	54,329	59,229	64,629	70,029	8.8%
Cash and equivalents	68	470	2	38	-17.8%
Total assets	64,382	67,335	69,770	72,539	4.1%
Short and long-term debt	18,893	20,395	21,879	23,620	7.7%
Other long-term liabilities	0	0	0	0	N/A
Total liabilities	48,886	50,388	52,102	54,043	3.4%
Shareholders' equity	15,496	16,946	17,668	18,496	6.1%
Net debt/(funds)	18,825	19,925	21,877	23,582	7.8%
Change in working capital	73	-148	-1,180	-32	N/A
Cash flow from operations	-307	4,114	4,353	4,632	N/A
Capital expenditure	-4,877	-4,900	-5,400	-5,400	N/A
Free cash flow	-6,115	-1,900	-2,181	-1,906	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	14.0	14.8	14.3	13.5	14.2
EV/EBITDA (adj) (x)	11.5	9.4	9.2	8.8	9.7
EV/EBIT (adj) (x)	22.6	17.1	16.9	16.3	18.2
FCF yield (%)	-15.2	-4.6	-5.0	-4.2	-7.3
P/BV (x)	1.4	1.4	1.4	1.3	1.4
Dividend yield (%)	3.7	3.9	3.9	4.0	3.9
Net debt/EBITDA (adj) (x)	5.4	4.5	4.7	4.6	4.8

Selected operating metrics					Average
Payout ratio (%)	52.1	57.6	56.4	53.9	55.0
Interest cover (x)	2.1	2.7	2.7	2.7	2.6
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Price (17-Nov-2020)	**USD 65.60**
Price Target	**USD 69.00**

Why Equal Weight? We assign an Equal Weight rating as we believe questions around final net 17/18 liability risk, implementation of improved cost recovery parameters, and equity issuance mean EIX likely continues to trade at a discount for next 12 months.

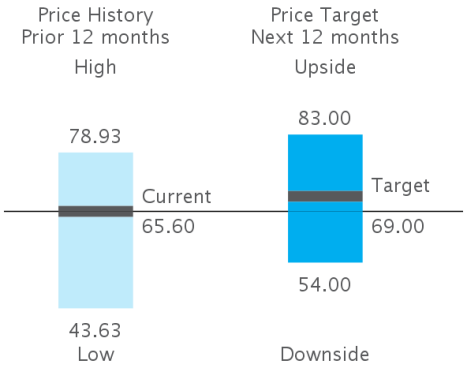
Upside case **USD 83.00**

The upside case applies a group average 2023 P/E multiple and assumes zero wildfire liability for 2017 / 2018 fires.

Downside case **USD 54.00**

Our downside case assumes $3.7bn net 2017 / 2018 wildfire liability and a 20% discount to the group average P/E multiple.

Upside/Downside scenarios



Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

North America Power & Utilities — **Industry View: POSITIVE**

Essential Utilities, Inc. (WTRG)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	890	1,880	2,056	2,315	37.5%
EBITDA (adj)	517	911	980	1,102	28.7%
EBIT (adj)	361	634	675	769	28.7%
Pre-tax income (adj)	261	436	479	551	28.2%
Net income (adj)	263	398	422	446	19.2%
EPS (adj) ($)	1.47	1.56	1.62	1.70	5.1%
Diluted shares (mn)	179	255	260	262	13.5%
DPS ($)	0.91	0.96	1.02	1.08	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	58.1	48.5	47.7	47.6	50.5
EBIT (adj) margin (%)	40.6	33.7	32.9	33.2	35.1
Pre-tax (adj) margin (%)	29.4	23.2	23.3	23.8	24.9
Net (adj) margin (%)	29.6	21.2	20.5	19.3	22.6
ROIC (%)	3.7	7.3	7.3	7.7	6.5
ROA (%)	N/A	3.1	3.1	3.1	3.1
ROE (%)	N/A	8.6	8.9	8.5	8.7

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	10,795	11,745	12,720	13,720	8.3%
Cash and equivalents	32	31	41	0	-100.0%
Total assets	12,929	13,601	14,281	14,907	4.9%
Short and long-term debt	5,225	3,950	4,075	4,572	-4.4%
Other long-term liabilities	766	2,531	2,561	2,423	46.8%
Total liabilities	8,315	8,844	9,055	9,519	4.6%
Shareholders' equity	4,613	4,765	5,226	5,388	5.3%
Net debt/(funds)	5,193	3,919	4,034	4,572	-4.2%
Change in working capital	N/A	0	-1	10	N/A
Cash flow from operations	0	713	784	802	N/A
Capital expenditure	0	-950	-975	-1,000	N/A
Free cash flow	0	-514	-767	-538	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	30.5	28.7	27.6	26.3	28.3
EV/EBITDA (adj) (x)	48.0	29.7	27.9	25.4	32.8
EV/EBIT (adj) (x)	68.8	42.7	40.5	36.4	47.1
FCF yield (%)	0.0	-1.9	-2.8	-1.9	-1.7
P/BV (x)	N/A	N/A	N/A	N/A	N/A
Dividend yield (%)	2.0	2.1	2.3	2.4	2.2
Net debt/EBITDA (adj) (x)	10.0	4.3	4.1	4.1	5.7

Selected operating metrics					Average
Payout ratio (%)	61.9	61.8	62.9	63.6	62.6
Interest cover (x)	3.0	4.6	5.1	5.3	4.5
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 44.88**
Price Target	**USD 50.00**

Why Equal Weight? We assign an Equal Weight rating to reflect transitory overhangs and a historically palatable valuation. We value WTRG on a sum of the parts basis and apply the utility group average P/E multiple, reflecting gas utility peers. The current share price reflects our valuation conclusion.

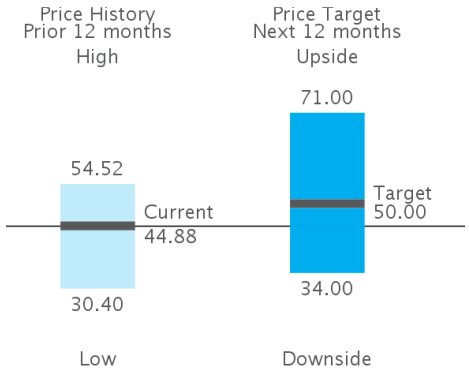
Upside case — **USD 71.00**

Our upside case assumes WTRG is valued using consolidated EPS against a water group P/E multiple. We believe this case could materialize if scarcity value persists and WTRG is deemed a pure-play water utility, despite the gas contribution to earnings.

Downside case — **USD 34.00**

Our downside case values WTRG consolidated EPS on the utility group average P/E multiple, while maintaining a 15% premium for the gas business and a 5% premium for water. We think this could materialize if ESG flows lessen or long-term growth appears unsustainable long term.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Eversource Energy (ES)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	8,526	8,915	9,155	9,413	3.4%
EBITDA (adj)	2,671	3,223	3,466	3,686	11.3%
EBIT (adj)	1,590	2,072	2,241	2,388	14.5%
Pre-tax income (adj)	1,190	1,619	1,776	1,893	16.7%
Net income (adj)	917	1,230	1,350	1,439	16.2%
EPS (adj) ($)	3.45	3.62	3.89	4.13	6.1%
Diluted shares (mn)	322.9	337.9	345.0	346.2	2.3%
DPS ($)	2.12	2.27	2.42	2.57	6.7%

Margin and return data					Average
EBITDA (adj) margin (%)	31.3	36.2	37.9	39.2	36.1
EBIT (adj) margin (%)	18.7	23.2	24.5	25.4	22.9
Pre-tax (adj) margin (%)	14.0	18.2	19.4	20.1	17.9
Net (adj) margin (%)	10.7	13.8	14.7	15.3	13.6
ROIC (%)	6.0	7.0	7.4	7.7	7.0
ROA (%)	2.2	2.8	3.0	3.1	2.8
ROE (%)	7.3	9.3	10.1	10.7	9.3

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	30,000	32,979	34,189	35,938	6.2%
Cash and equivalents	15	884	291	325	176.1%
Total assets	41,124	44,103	45,313	47,062	4.6%
Short and long-term debt	14,098	16,346	16,745	17,603	7.7%
Other long-term liabilities	9,052	9,202	9,352	9,502	1.6%
Total liabilities	28,494	30,858	31,968	33,617	5.7%
Shareholders' equity	12,630	13,245	13,345	13,445	2.1%
Net debt/(funds)	14,083	15,462	16,454	17,278	7.1%
Change in working capital	96	-1	112	110	4.7%
Cash flow from operations	2,010	2,300	2,493	2,650	9.7%
Capital expenditure	-2,911	-3,071	-2,834	-2,817	N/A
Free cash flow	-1,565	-1,538	-1,175	-1,058	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	26.6	25.4	23.6	22.2	24.4
EV/EBITDA (adj) (x)	16.4	14.0	13.3	12.7	14.1
EV/EBIT (adj) (x)	27.5	21.8	20.6	19.6	22.4
FCF yield (%)	-3.6	-3.4	-2.6	-2.3	-2.9
P/BV (x)	2.3	2.3	2.4	2.4	2.4
Dividend yield (%)	2.3	2.5	2.6	2.8	2.6
Net debt/EBITDA (adj) (x)	5.3	4.8	4.7	4.7	4.9

Selected operating metrics					Average
Payout ratio (%)	61.4	62.8	62.2	62.3	62.2
Interest cover (x)	5.0	5.4	5.6	5.6	5.4
Regulated (%)	100.0	100.0	200.0	200.0	150.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020) **USD 91.75**
Price Target **USD 100.00**

Why Equal Weight? We believe ES's diverse, high quality regulated business will grow base earnings at the midpoint of its 5-7% target through the forecast period. We apply a 25% valuation premium to reflect the above average growth, reasonable regulatory mechanisms that are in place, allowing the company to earn a prompt return on its regulatory investing.

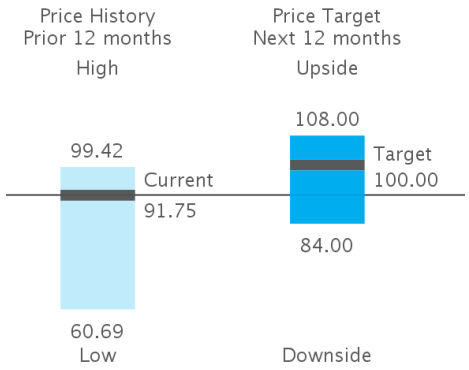
Upside case **USD 108.00**

We believe there are a number of large projects that could boost ES's earnings power and growth rate in the medium to long term. Offshore wind projects, the CGMA acquisition, grid mod, and elevated ESG fund flows could justify a 35% premium.

Downside case **USD 84.00**

An adverse change in regulation or legislation, while not expected, could result in a discount valuation for ES. We impute a 5% group discount to arrive at our downside case valuation.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

FirstEnergy Corp. (FE)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	11,035	11,733	12,076	12,365	3.9%
EBITDA (adj)	3,730	4,025	4,261	4,442	6.0%
EBIT (adj)	2,510	2,730	2,883	2,981	5.9%
Pre-tax income (adj)	1,117	1,750	1,838	1,923	19.9%
Net income (adj)	912	1,338	1,408	1,475	17.4%
EPS (adj) ($)	2.58	2.50	2.63	2.73	1.8%
Diluted shares (mn)	535.0	535.0	535.0	540.7	0.4%
DPS ($)	1.46	1.48	1.52	1.52	1.4%

Margin and return data					Average
EBITDA (adj) margin (%)	33.8	34.3	35.3	35.9	34.8
EBIT (adj) margin (%)	22.7	23.3	23.9	24.1	23.5
Pre-tax (adj) margin (%)	10.1	14.9	15.2	15.6	14.0
Net (adj) margin (%)	8.3	11.4	11.7	11.9	10.8
ROIC (%)	9.2	9.4	9.3	9.3	9.3
ROA (%)	5.1	5.0	5.1	5.0	5.1
ROE (%)	13.4	19.4	17.1	16.4	16.6

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	42,421	45,321	48,371	51,441	6.6%
Cash and equivalents	95	313	901	629	87.8%
Total assets	41,454	43,269	45,522	46,852	4.2%
Short and long-term debt	20,400	20,745	21,993	22,249	2.9%
Other long-term liabilities	11,260	11,429	11,647	11,888	1.8%
Total liabilities	34,541	35,055	36,520	37,018	2.3%
Shareholders' equity	6,913	8,214	9,002	9,835	12.5%
Net debt/(funds)	20,305	20,432	21,091	21,620	2.1%
Change in working capital	-148	223	598	-272	N/A
Cash flow from operations	2,139	3,439	3,049	3,231	14.7%
Capital expenditure	-2,952	-2,900	-3,050	-3,070	N/A
Free cash flow	-1,627	-296	-877	-769	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	11.1	11.5	10.9	10.5	11.0
EV/EBITDA (adj) (x)	9.5	8.9	8.5	8.3	8.8
EV/EBIT (adj) (x)	14.2	13.1	12.6	12.4	13.0
FCF yield (%)	-4.6	-0.8	-2.4	-2.1	-2.5
P/BV (x)	2.2	1.9	1.7	1.6	1.8
Dividend yield (%)	5.1	5.1	5.3	5.3	5.2
Net debt/EBITDA (adj) (x)	5.4	5.1	4.9	4.9	5.1

Selected operating metrics					Average
Payout ratio (%)	56.5	59.2	57.8	55.7	57.3
Interest cover (x)	2.4	2.3	2.3	2.4	2.3
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	USD 28.74
Price Target	USD 33.00

Why Equal Weight? We assign a 30% discount to the group average 23E PE against our pro forma EPS estimate, to account for potential penalties and fines along with a challenging ESG profile.

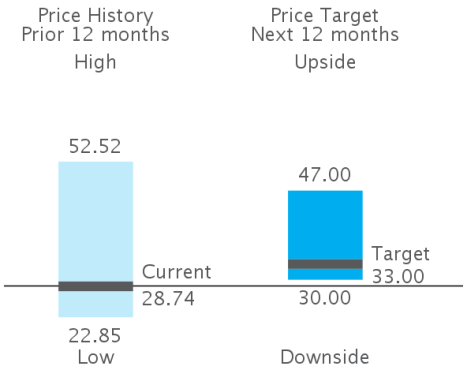
Upside case — **USD 47.00**

We apply a group average 23E PE multiple applied to our pro forma EPS estimate.

Downside case — **USD 30.00**

We apply a 35% discount to the group average 23E PE multiple applied to our pro forma EPS estimate.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

NextEra Energy, Inc. (NEE)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	19,204	19,827	20,284	20,613	2.4%
EBITDA (adj)	10,301	10,358	10,653	10,757	1.5%
EBIT (adj)	6,085	6,209	6,668	6,937	4.5%
Pre-tax income (adj)	4,568	4,609	4,934	5,208	4.5%
Net income (adj)	4,062	4,446	4,768	5,088	7.8%
EPS (adj) ($)	2.09	2.28	2.45	2.61	7.7%
Diluted shares (mn)	1,940	1,947	1,947	1,947	0.1%
DPS ($)	5.00	5.65	6.38	7.21	13.0%

Margin and return data					Average
EBITDA (adj) margin (%)	53.6	52.2	52.5	52.2	52.6
EBIT (adj) margin (%)	31.7	31.3	32.9	33.7	32.4
Pre-tax (adj) margin (%)	23.8	23.2	24.3	25.3	24.2
Net (adj) margin (%)	21.2	22.4	23.5	24.7	22.9
ROIC (%)	7.1	7.4	8.0	8.5	7.7
ROA (%)	3.9	4.0	4.2	4.5	4.1
ROE (%)	11.9	12.6	14.6	18.9	14.5

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	92,220	104,275	116,420	128,550	11.7%
Cash and equivalents	-6,221	-12,122	-20,894	-31,580	N/A
Total assets	111,836	114,089	113,734	111,620	-0.1%
Short and long-term debt	40,506	45,357	50,780	55,855	11.3%
Other long-term liabilities	22,941	22,941	22,941	22,941	0.0%
Total liabilities	71,705	76,556	81,979	87,054	6.7%
Shareholders' equity	35,289	32,691	26,913	19,724	-17.6%
Net debt/(funds)	46,727	57,479	71,674	87,435	23.2%
Change in working capital	5,402	-5,783	-10,170	-10,686	N/A
Cash flow from operations	7,747	7,147	7,227	7,263	-2.1%
Capital expenditure	-11,945	-11,680	-11,780	-11,780	N/A
Free cash flow	-13,170	-15,909	-17,348	-18,914	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	36.6	33.5	31.3	29.3	32.7
EV/EBITDA (adj) (x)	19.0	19.9	20.7	22.0	20.4
EV/EBIT (adj) (x)	32.2	33.3	33.1	34.1	33.2
FCF yield (%)	-6.7	-7.7	-7.9	-8.0	-7.6
P/BV (x)	4.2	4.6	5.5	7.6	5.5
Dividend yield (%)	6.5	7.4	8.3	9.4	7.9
Net debt/EBITDA (adj) (x)	4.5	5.5	6.7	8.1	6.2

Selected operating metrics					Average
Payout ratio (%)	238.8	247.4	260.7	276.0	255.7
Interest cover (x)	2.4	2.8	2.8	2.9	2.7
Regulated (%)	61.9	62.9	62.4	60.6	61.9

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 76.61**
Price Target	**USD 87.00**

Why Equal Weight? Top industry growth combined with an above-average regulatory environment drive the 20% premium valuation. Above-average growth provides for a larger increase to our expected price target, providing a compelling risk reward.

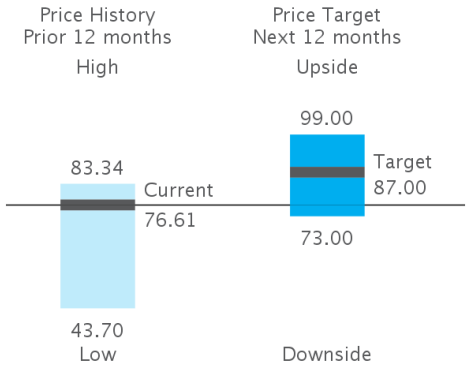
Upside case — **USD 99.00**

Our upside case applies a 30% premium multiple to the 2023 EPS estimates for the regulated utilities and assumes a 25% greater contribution from NEP and 20% greater contribution from NEER.

Downside case — **USD 73.00**

Our downside case applies an industry average multiple to 2023E earnings and assumes a 25% lower NEP value and a 15% lower contribution from NEER.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

NiSource, Inc. (NI)

Stock Rating: OVERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	5,209	5,250	5,173	5,387	1.1%
EBITDA (adj)	2,028	1,914	2,031	2,183	2.5%
EBIT (adj)	1,316	1,167	1,235	1,306	-0.2%
Pre-tax income (adj)	507	771	816	877	20.1%
Net income (adj)	495	518	551	597	6.4%
EPS (adj) ($)	1.32	1.33	1.38	1.43	2.9%
Diluted shares (mn)	376.0	389.5	400.4	415.8	3.4%
DPS ($)	0.80	0.85	0.90	0.95	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	38.9	36.5	39.3	40.5	38.8
EBIT (adj) margin (%)	17.1	22.0	23.7	24.1	21.7
Pre-tax (adj) margin (%)	9.7	14.7	15.8	16.3	14.1
Net (adj) margin (%)	9.5	9.9	10.6	11.1	10.3
ROIC (%)	5.7	7.1	7.1	7.4	6.8
ROA (%)	2.3	2.3	2.3	2.4	2.3
ROE (%)	8.6	8.6	8.5	8.5	8.6

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	16,912	18,023	19,385	21,816	8.9%
Cash and equivalents	139	-83	-295	-2,263	N/A
Total assets	22,660	23,548	24,698	25,161	3.6%
Short and long-term debt	9,629	9,840	10,332	10,038	1.4%
Other long-term liabilities	5,071	5,189	5,307	5,425	2.3%
Total liabilities	16,673	17,057	17,700	17,646	1.9%
Shareholders' equity	5,987	6,492	6,999	7,515	7.9%
Net debt/(funds)	9,490	9,923	10,627	12,301	9.0%
Change in working capital	89	1,496	-244	-2,091	N/A
Cash flow from operations	1,583	1,470	1,552	1,678	1.9%
Capital expenditure	-1,802	-1,750	-2,050	-3,200	N/A
Free cash flow	-219	-280	-498	-1,522	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	18.8	18.6	18.0	17.2	18.2
EV/EBITDA (adj) (x)	9.2	10.0	9.8	9.9	9.7
EV/EBIT (adj) (x)	14.2	16.4	16.1	16.5	15.8
FCF yield (%)	-1.2	-1.5	-2.5	-7.1	-3.1
P/BV (x)	1.6	1.5	1.4	1.4	1.5
Dividend yield (%)	3.2	3.4	3.6	3.8	3.5
Net debt/EBITDA (adj) (x)	4.7	5.2	5.2	5.6	5.2

Selected operating metrics					Average
Payout ratio (%)	60.8	63.8	65.3	66.4	64.1
Interest cover (x)	2.4	3.0	3.0	3.1	2.9
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 24.75**
Price Target	**USD 29.00**

Why Overweight? We view NI as a quality utility with a well-defined rate base growth strategy from gas and electric infrastructure modernization, which we see as relatively low risk. We believe opportunities for accelerated growth from legacy generation replacement power investments result in upside to the current valuation.

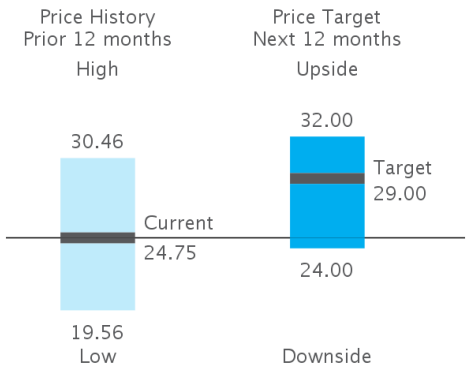
Upside case **USD 32.00**

Our upside case reflects a 5% premium to the 2023 utility group average P/E multiple applied to higher earnings driven by additional rate base growth and favorable rate case outcomes.

Downside case **USD 24.00**

Our downside case reflects a 10% discount to the 2023 utility group average P/E multiple applied to lower earnings driven by slower rate base growth and unfavorable rate case outcomes.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Northwestern Corporation (NWE)

Stock Rating: EQUAL WEIGHT

Income statement ($k)	2019A	2020E	2021E	2022E	CAGR
Revenue	1,250,610	1,256,145	1,278,443	1,296,992	1.2%
EBITDA (adj)	442,886	448,007	472,048	497,949	4.0%
EBIT (adj)	246,650	265,054	275,100	288,081	5.3%
Pre-tax income (adj)	174,895	168,261	179,547	193,468	3.4%
Net income (adj)	173,820	171,626	179,547	187,664	2.6%
EPS (adj) ($)	3.42	3.37	3.51	3.65	2.1%
Diluted shares (mn)	50.8	50.9	51.2	51.5	0.5%
DPS ($)	2.30	2.40	2.51	2.63	4.5%

Margin and return data					Average
EBITDA (adj) margin (%)	35.4	35.7	36.9	38.4	36.6
EBIT (adj) margin (%)	19.7	21.1	21.5	22.2	21.1
Pre-tax (adj) margin (%)	14.0	13.4	14.0	14.9	14.1
Net (adj) margin (%)	13.9	13.7	14.0	14.5	14.0
ROIC (%)	4.2	3.9	3.9	4.0	4.0
ROA (%)	3.1	2.9	2.9	3.0	3.0
ROE (%)	8.9	8.4	8.5	8.6	8.6

Balance sheet and cash flow ($k)					CAGR
Tangible fixed assets	N/A	N/A	N/A	N/A	N/A
Cash and equivalents	5,145	-5,215	-59,843	-163,534	N/A
Total assets	5,910,702	6,117,549	6,321,053	6,469,094	3.1%
Short and long-term debt	2,233,281	2,353,281	2,473,281	2,533,281	4.3%
Other long-term liabilities	1,638,327	1,655,982	1,668,637	1,684,292	0.9%
Total liabilities	3,871,608	4,009,263	4,141,918	4,217,573	2.9%
Shareholders' equity	2,039,094	2,108,286	2,179,135	2,251,520	3.4%
Net debt/(funds)	2,228,136	2,358,496	2,533,124	2,696,815	6.6%
Change in working capital	36,784	-28,015	-67,283	-119,346	N/A
Cash flow from operations	296,720	365,874	385,070	404,587	10.9%
Capital expenditure	-316,016	-398,800	-451,000	-456,000	N/A
Free cash flow	-134,423	-155,360	-194,628	-186,691	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	17.6	17.9	17.2	16.6	17.3
EV/EBITDA (adj) (x)	12.0	12.1	11.9	11.6	11.9
EV/EBIT (adj) (x)	21.5	20.5	20.4	20.0	20.6
FCF yield (%)	-2.5	-2.9	-3.5	-3.2	-3.0
P/BV (x)	1.4	1.4	1.3	1.3	1.3
Dividend yield (%)	3.8	4.0	4.2	4.4	4.1
Net debt/EBITDA (adj) (x)	5.0	5.3	5.4	5.4	5.3

Selected operating metrics					Average
Payout ratio (%)	67.2	71.3	71.7	72.1	70.6
Interest cover (x)	2.6	2.7	2.8	2.9	2.7
Regulated (%)	100.0	100.0	100.0	200.0	125.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 60.38**
Price Target	**USD 63.00**

Why Equal Weight? We believe a 10% discount to the group multiple is appropriate given below average growth and regulatory (although regulatory is improving). The current valuation shows the balanced risk reward profile.

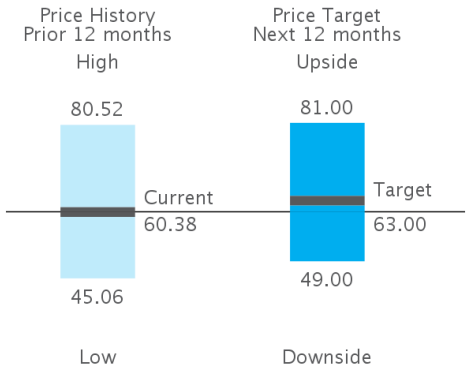
Upside case — **USD 81.00**

Our upside case assumes a 15% premium to the group average regulated utility multiple assuming a positive shift in regulatory framework and significant improvement to ratebase growth and visibility driven by self build of generation in support of capacity needs.

Downside case — **USD 49.00**

Our downside case assumes a 15% discount to the group average regulated utility multiple if regulatory issues persist and capacity needs are filled via purchased power contracts and not self build.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

OGE Energy Corp. (OGE)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	2,232	2,219	2,279	2,354	1.8%
EBITDA (adj)	859	913	961	1,025	6.1%
EBIT (adj)	504	538	569	615	6.9%
Pre-tax income (adj)	463	480	514	543	5.5%
Net income (adj)	434	432	453	467	2.5%
EPS (adj) ($)	2.16	2.15	2.26	2.33	2.5%
Diluted shares (mn)	201	201	201	201	0.0%
DPS ($)	1.51	1.59	1.65	1.72	4.4%

Margin and return data					Average
EBITDA (adj) margin (%)	38.5	41.2	42.2	43.5	41.3
EBIT (adj) margin (%)	22.6	24.2	25.0	26.1	24.5
Pre-tax (adj) margin (%)	20.8	21.6	22.6	23.1	22.0
Net (adj) margin (%)	19.4	19.5	19.9	19.8	19.6
ROIC (%)	7.0	7.4	7.7	8.2	7.6
ROA (%)	3.9	3.8	3.9	3.9	3.9
ROE (%)	10.5	10.2	10.4	10.4	10.3

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	9,045	9,244	9,578	9,898	3.1%
Cash and equivalents	0	86	6	45	N/A
Total assets	11,024	11,325	11,621	12,018	2.9%
Short and long-term debt	3,307	3,495	3,670	3,945	6.1%
Other long-term liabilities	3,032	3,032	3,032	3,032	0.0%
Total liabilities	6,885	7,073	7,248	7,523	3.0%
Shareholders' equity	4,140	4,253	4,374	4,496	2.8%
Net debt/(funds)	3,307	3,409	3,664	3,900	5.7%
Change in working capital	N/A	N/A	N/A	N/A	N/A
Cash flow from operations	682	792	802	839	7.2%
Capital expenditure	-636	-575	-725	-730	N/A
Free cash flow	46	217	77	109	33.3%

Valuation and leverage metrics					Average
P/E (adj) (x)	15.8	15.9	15.2	14.7	15.4
EV/EBITDA (adj) (x)	11.8	11.2	10.9	10.5	11.1
EV/EBIT (adj) (x)	20.1	19.1	18.5	17.5	18.8
FCF yield (%)	0.5	2.1	0.7	1.0	1.1
P/BV (x)	1.7	1.6	1.6	1.5	1.6
Dividend yield (%)	4.4	4.6	4.8	5.0	4.7
Net debt/EBITDA (adj) (x)	3.8	3.7	3.8	3.8	3.8

Selected operating metrics					Average
Payout ratio (%)	69.9	73.8	73.2	73.9	72.7
Interest cover (x)	5.7	5.9	6.0	5.9	5.9
Regulated (%)	80.8	81.5	81.7	82.8	81.7

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 34.21**
Price Target	**USD 36.00**

Why Equal Weight? While there recent developments for OK regulatory lag and ENBL options. The combination of Enable Midstream and Oklahoma Gas and Electric, while synergistic from a utility financing standpoint, is ultimately dilutive to the corporate growth rate. Fair and timely regulatory recovery remains a risk as OG&E's earned returns show a meaningful regulatory lag.

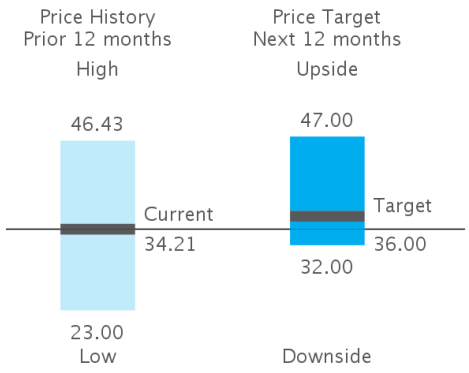
Upside case **USD 47.00**

Our upside case factors in a 10% utility P/E premium based on 2023 utility EPS combined with ENBL valued at $5/unit ($2 to OGE).

Downside case **USD 32.00**

Our downside case factors in a 20% discount to the group average at the utility, for higher regulatory risk and uncertainty. We value ENBL at $5 per unit ($2 to OGE).

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

PG&E Corporation (PCG)

Stock Rating: OVERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	17,129	18,698	19,498	19,769	4.9%
EBITDA (adj)	-6,860	6,500	6,945	7,394	N/A
EBIT (adj)	-10,094	2,977	3,149	3,341	N/A
Pre-tax income (adj)	-11,042	2,042	2,205	2,381	N/A
Net income (adj)	-7,656	2,021	2,184	2,360	N/A
EPS (adj) ($)	3.92	1.62	1.00	1.08	-35.0%
Diluted shares (mn)	528	1,250	2,180	2,190	60.7%
DPS ($)	0.00	0.00	0.00	0.00	N/A

Margin and return data					Average
EBITDA (adj) margin (%)	-40.0	34.8	35.6	37.4	16.9
EBIT (adj) margin (%)	-58.9	15.9	16.2	16.9	-2.5
Pre-tax (adj) margin (%)	-64.5	10.9	11.3	12.0	-7.5
Net (adj) margin (%)	-44.7	10.8	11.2	11.9	-2.7
ROIC (%)	-18.1	31.4	22.8	20.8	14.2
ROA (%)	-9.1	3.5	3.5	3.6	0.4
ROE (%)	-59.3	37.5	28.0	22.5	7.2

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	61,635	66,812	71,216	74,863	6.7%
Cash and equivalents	1,570	180	16	41	-70.3%
Total assets	85,196	89,013	93,253	98,025	4.8%
Short and long-term debt	52,046	1,850	3,350	3,350	-59.9%
Other long-term liabilities	21,631	19,901	19,901	19,901	-2.7%
Total liabilities	79,808	28,182	29,682	30,032	-27.8%
Shareholders' equity	5,388	7,811	10,476	12,767	33.3%
Net debt/(funds)	50,476	1,670	3,334	3,309	-59.7%
Change in working capital	-2,010	-1,664	-325	14	N/A
Cash flow from operations	4,816	5,858	6,812	5,595	5.1%
Capital expenditure	-6,313	-8,700	-8,200	-7,700	N/A
Free cash flow	-1,497	-2,842	-1,388	-2,105	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	3.0	7.2	11.7	10.9	8.2
EV/EBITDA (adj) (x)	-8.3	1.2	1.4	1.3	-1.1
EV/EBIT (adj) (x)	-5.6	2.6	3.0	2.8	0.7
FCF yield (%)	-2.6	-36.1	-14.6	-22.1	-18.9
P/BV (x)	1.1	1.9	2.4	2.0	1.9
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Net debt/EBITDA (adj) (x)	-7.4	0.3	0.5	0.4	-1.5

Selected operating metrics					Average
Payout ratio (%)	0.0	0.0	0.0	0.0	0.0
Interest cover (x)	-7.3	6.9	7.3	7.7	3.7
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	USD 11.72
Price Target	USD 14.00

Why Overweight? We expect PCG's discount to close over the coming twelve months following resolution of the safety certification process, conclusion of the CPUC securitization regulatory proceeding, and eventual equity issuance in 2021.

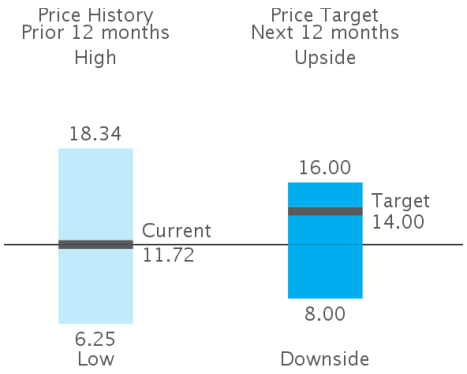
Upside case — **USD 16.00**

Our upside case assumes a group average multiple if PG&E is able to avoid large wildfires, reinstate the dividend, and execute at its guided growth rate for multiple years.

Downside case — **USD 8.00**

Our downside case assumes a 50% discount to the group average multiple. We would expect this draconian outcome to emerge if a large-scale wildfire is caused in a negligent manner without AB 1054 coverage if PCG cannot obtain a safety certificate.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Pinnacle West Capital Corporation (PNW)

Stock Rating: OVERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	3,471	3,576	3,694	3,788	3.0%
EBITDA (adj)	1,263	1,445	1,521	1,613	8.5%
EBIT (adj)	672	828	862	911	10.7%
Pre-tax income (adj)	542	679	735	770	12.4%
Net income (adj)	558	592	597	625	3.9%
EPS (adj) ($)	4.77	5.06	5.09	5.32	3.7%
Diluted shares (mn)	113	113	113	114	0.3%
DPS ($)	3.00	3.17	3.37	3.57	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	36.4	40.4	41.2	42.6	40.1
EBIT (adj) margin (%)	19.4	23.2	23.3	24.0	22.5
Pre-tax (adj) margin (%)	15.6	19.0	19.9	20.3	18.7
Net (adj) margin (%)	16.1	16.5	16.1	16.5	16.3
ROIC (%)	6.0	6.7	6.5	6.5	6.4
ROA (%)	2.9	2.9	2.8	2.8	2.8
ROE (%)	9.5	9.7	9.4	9.5	9.5

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	16,752	17,245	17,891	18,882	4.1%
Cash and equivalents	10	328	320	166	152.7%
Total assets	19,397	20,367	21,372	22,262	4.7%
Short and long-term debt	6,233	7,333	7,833	8,333	10.2%
Other long-term liabilities	N/A	N/A	N/A	N/A	N/A
Total liabilities	13,398	14,128	14,896	15,546	5.1%
Shareholders' equity	5,876	6,116	6,353	6,593	3.9%
Net debt/(funds)	6,222	7,005	7,513	8,167	9.5%
Change in working capital	2,190	107	627	49	-71.9%
Cash flow from operations	957	1,209	1,255	1,327	11.5%
Capital expenditure	-1,191	-1,263	-1,650	-1,725	N/A
Free cash flow	-504	-413	-776	-804	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	18.2	17.2	17.1	16.3	17.2
EV/EBITDA (adj) (x)	12.6	11.6	11.3	11.1	11.7
EV/EBIT (adj) (x)	23.7	20.2	20.0	19.6	20.9
FCF yield (%)	-3.2	-2.5	-4.5	-4.5	-3.7
P/BV (x)	1.7	1.6	1.5	1.5	1.6
Dividend yield (%)	3.5	3.7	3.9	4.1	3.8
Net debt/EBITDA (adj) (x)	4.9	4.8	4.9	5.1	4.9

Selected operating metrics					Average
Payout ratio (%)	62.7	62.8	66.2	67.0	64.7
Interest cover (x)	5.4	5.7	5.7	5.5	5.6
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 86.78**
Price Target	**USD 103.00**

Why Overweight? We rate PNW as Overweight based on current relative value within our regulated utility group. The price target is based on a group average 2023 EPS multiple.

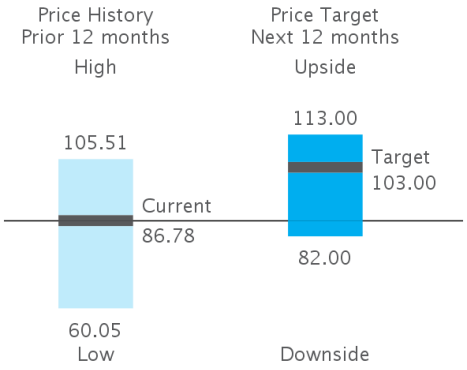
Upside case — **USD 113.00**

A 10% premium to the group P/E multiple is attributed to potential for above-average earnings and dividend growth, pending regulatory outcomes and economic conditions.

Downside case — **USD 82.00**

A 20% discount to the group P/E premised on lower-than-expected load growth combined with sub-optimal rate case, IRP, and retail competition outcomes.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

PNM Resources, Inc. (PNM)

Stock Rating: UNDERWEIGHT

Income statement ($k)	2019A	2020E	2021E	2022E	CAGR
Revenue	1,458,600	1,520,053	1,575,559	1,627,226	3.7%
EBITDA (adj)	592,681	659,408	710,685	755,341	8.4%
EBIT (adj)	324,873	369,625	399,052	427,233	9.6%
Pre-tax income (adj)	203,857	226,424	252,347	278,280	10.9%
Net income (adj)	172,540	183,665	203,623	223,103	8.9%
EPS (adj) ($)	2.16	2.28	2.37	2.60	6.4%
Diluted shares (k)	79,990	80,588	85,969	85,969	2.4%
DPS ($)	1.18	1.25	1.33	1.41	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	40.6	43.4	45.1	46.4	43.9
EBIT (adj) margin (%)	22.3	24.3	25.3	26.3	24.5
Pre-tax (adj) margin (%)	14.0	14.9	16.0	17.1	15.5
Net (adj) margin (%)	11.8	12.1	12.9	13.7	12.6
ROIC (%)	6.6	6.4	6.8	6.9	6.7
ROA (%)	2.5	2.5	2.5	2.7	2.6
ROE (%)	10.2	10.9	9.9	10.4	10.4

Balance sheet and cash flow ($k)					CAGR
Tangible fixed assets	7,918,601	8,724,601	9,700,601	10,460,601	9.7%
Cash and equivalents	3,833	301,081	-253,500	-403,382	N/A
Total assets	7,298,774	8,112,239	8,222,025	8,504,035	5.2%
Short and long-term debt	3,192,817	3,633,643	3,654,043	3,834,043	6.3%
Other long-term liabilities	2,060,565	2,060,565	2,060,565	2,060,565	0.0%
Total liabilities	5,557,024	5,997,850	6,018,250	6,198,250	3.7%
Shareholders' equity	1,678,698	2,051,337	2,140,723	2,242,733	10.1%
Net debt/(funds)	3,188,984	3,332,562	3,907,543	4,237,425	9.9%
Change in working capital	-463,542	63,016	355,018	-204,881	N/A
Cash flow from operations	503,163	488,217	530,025	565,980	4.0%
Capital expenditure	-616,273	-806,000	-976,000	-760,000	N/A
Free cash flow	-206,036	-419,337	-560,741	-315,640	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	22.7	21.5	20.6	18.8	20.9
EV/EBITDA (adj) (x)	12.0	11.0	11.0	10.8	11.2
EV/EBIT (adj) (x)	21.8	19.6	19.6	19.0	20.0
FCF yield (%)	-2.9	-5.8	-7.2	-3.9	-4.9
P/BV (x)	2.3	1.9	2.0	1.9	2.0
Dividend yield (%)	2.4	2.6	2.7	2.9	2.6
Net debt/EBITDA (adj) (x)	5.4	5.1	5.5	5.6	5.4

Selected operating metrics					Average
Payout ratio (%)	54.8	55.0	56.1	54.3	55.1
Interest cover (x)	4.9	4.6	4.8	5.1	4.9
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 48.90**
Price Target	**USD 50.00**

Why Underweight? We expect average to above-average earnings/dividend growth through the close of the transaction and believe management has provided adequate information to be confident they can achieve growth through the forecast period. Our price target and UW rating reflect the per share purchase price according to the terms of the AGR merger agreement.

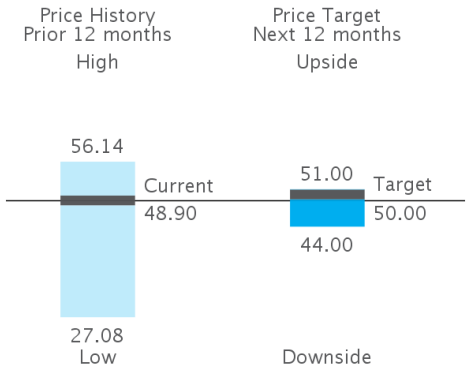
Upside case — **USD 51.00**

Our upside case comprises the small likelihood a topping bid from a competitor is seriously considered.

Downside case — **USD 44.00**

Our downside case assumes that the merger falls through and growth proceeds at a slower pace and the regulatory and/or economic landscape in NM does not improve. PNM could trade down to a 10% discount in this environment.

Upside/Downside scenarios



North America Power & Utilities **Industry View: POSITIVE**

Public Service Enterprise Group (PEG)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	10,076	8,660	8,778	8,768	-4.5%
EBITDA (adj)	3,191	3,583	3,729	3,873	6.7%
EBIT (adj)	1,943	2,272	2,344	2,418	7.6%
Pre-tax income (adj)	2,008	1,922	1,955	2,039	0.5%
Net income (adj)	1,666	1,742	1,726	1,759	1.8%
EPS (adj) ($)	3.28	3.43	3.40	3.46	1.8%
Diluted shares (mn)	508.0	508.0	508.0	508.0	0.0%
DPS ($)	1.88	1.96	2.04	2.12	4.1%

Margin and return data					Average
EBITDA (adj) margin (%)	31.7	41.4	42.5	44.2	39.9
EBIT (adj) margin (%)	19.3	26.2	26.7	27.6	25.0
Pre-tax (adj) margin (%)	19.9	22.2	22.3	23.3	21.9
Net (adj) margin (%)	16.5	20.1	19.7	20.1	19.1
ROIC (%)	6.7	7.6	7.7	7.2	7.3
ROA (%)	3.5	3.5	3.3	3.3	3.4
ROE (%)	10.9	10.9	10.3	10.1	10.6

Balance sheet and cash flow ($mn)					CAGR
Net PP&E	35,868	37,707	39,558	41,026	4.6%
Cash and equivalents	489	584	715	957	25.1%
Total assets	48,048	49,981	51,964	53,674	3.8%
Short and long-term debt	16,248	17,529	20,234	18,166	3.8%
Other long-term liabilities	13,689	13,917	13,795	16,194	5.8%
Total liabilities	32,779	33,966	35,258	36,286	3.4%
Shareholders' equity	15,269	16,016	16,705	17,387	4.4%
Net debt/(funds)	15,759	16,946	19,519	17,209	3.0%
Change in working capital	390	652	1,067	2,156	76.8%
Cash flow from operations	3,496	3,200	3,260	3,361	-1.3%
Capital expenditure	-3,149	-3,115	-3,203	-2,888	N/A
Free cash flow	-608	-910	-980	-604	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	18.0	17.2	17.4	17.1	17.4
EV/EBITDA (adj) (x)	14.3	13.1	13.3	12.2	13.2
EV/EBIT (adj) (x)	23.5	20.7	21.1	19.5	21.2
FCF yield (%)	-1.3	-1.9	-2.0	-1.3	-1.6
P/BV (x)	2.0	1.9	1.8	1.7	1.8
Dividend yield (%)	3.2	3.3	3.5	3.6	3.4
Net debt/EBITDA (adj) (x)	4.9	4.7	5.2	4.4	4.8

Selected operating metrics					Average
Payout ratio (%)	57.3	57.2	60.0	61.2	58.9
Interest cover (x)	5.6	5.8	5.7	6.0	5.7
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020) **USD 59.05**
Price Target **USD 65.00**

Why Equal Weight? PEG is a quality company that should be able to support 6%+ utility growth in our view based on current capital expenditure projections. As the merchant arm results in lower total EPS growth and the utility has risks on transmission ROE and the clean energy plan, we see PEG as an Equal Weight investment.

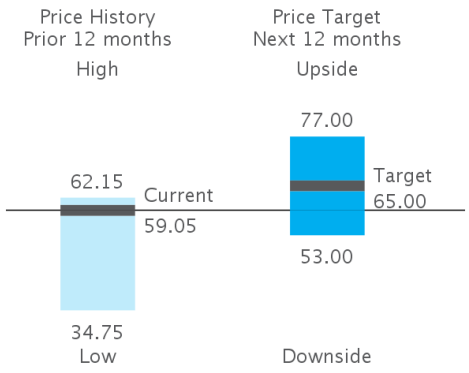
Upside case **USD 77.00**

This is a 20% premium to the 23 group average PE applied to our 23 eps estimate and a 7.5x EBITDA multiple applied to our 23 Power EBITDA.

Downside case **USD 53.00**

This is a 15% discount to the 23 group average PE applied to our 23 eps estimate, discounted to reflect lower transmission ROE and lower capital spending approved by the BPU estimate and a 5.0x EBITDA multiple applied to our 23 Power EBITDA.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Sempra Energy (SRE)

Stock Rating: OVERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	10,829	11,705	11,995	12,226	4.1%
EBITDA (adj)	4,380	4,640	4,789	5,071	5.0%
EBIT (adj)	2,811	2,994	2,992	3,131	3.7%
Pre-tax income (adj)	1,734	2,022	1,998	2,109	6.7%
Net income (adj)	2,055	2,237	2,505	2,683	9.3%
EPS (adj) ($)	7.29	7.57	7.99	8.49	5.2%
Diluted shares (mn)	282	295	313	316	3.9%
DPS ($)	3.87	4.20	4.56	4.94	8.5%

Margin and return data					Average
EBITDA (adj) margin (%)	40.4	39.6	39.9	41.5	40.4
EBIT (adj) margin (%)	26.0	25.6	24.9	25.6	25.5
Pre-tax (adj) margin (%)	16.0	17.3	16.7	17.2	16.8
Net (adj) margin (%)	19.0	19.1	20.9	21.9	20.2
ROIC (%)	6.1	6.8	6.4	6.4	6.4
ROA (%)	5.3	5.1	5.1	5.1	5.1
ROE (%)	12.0	11.2	12.0	12.2	11.8

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	36,452	40,466	44,219	46,079	8.1%
Cash and equivalents	108	993	949	1,973	163.4%
Total assets	65,665	65,864	69,573	72,456	3.3%
Short and long-term debt	25,816	23,215	25,055	26,055	0.3%
Other long-term liabilities	0	0	0	0	N/A
Total liabilities	43,860	41,259	43,099	44,099	0.2%
Shareholders' equity	19,929	20,926	22,003	23,124	5.1%
Net debt/(funds)	25,708	22,222	24,106	24,082	-2.2%
Change in working capital	-1,933	3,231	1,817	1,173	N/A
Cash flow from operations	3,088	3,566	5,111	5,405	20.5%
Capital expenditure	-3,708	-5,660	-5,550	-3,800	N/A
Free cash flow	-1,755	-3,480	-1,887	32	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	18.4	17.7	16.8	15.8	17.2
EV/EBITDA (adj) (x)	22.4	20.9	21.1	20.0	21.1
EV/EBIT (adj) (x)	34.9	32.3	33.7	32.3	33.3
FCF yield (%)	-1.8	-3.6	-1.9	0.0	-1.8
P/BV (x)	1.9	1.9	1.9	1.8	1.9
Dividend yield (%)	2.9	3.1	3.4	3.7	3.3
Net debt/EBITDA (adj) (x)	5.9	4.8	5.0	4.7	5.1

Selected operating metrics					Average
Payout ratio (%)	53.1	55.4	57.0	58.2	55.9
Interest cover (x)	2.6	3.1	3.0	3.1	2.9
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 134.06**
Price Target	**USD 159.00**

Why Overweight? We think SRE represents an attractive thematic investment opportunity to invest with a top-tier management team with exposure to the best parts of the North American energy story. We also see the CA utilities' rate case outcomes as constructive to support utility growth and stability. We believe recent sensitivity to weak global LNG prices is overdone.

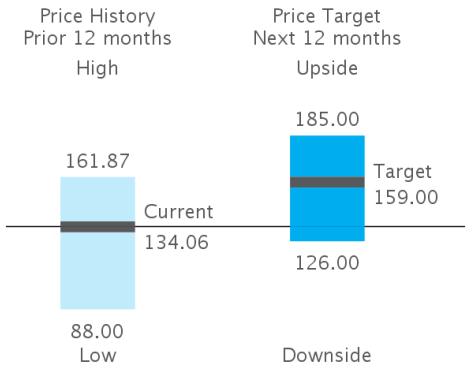
Upside case — **USD 185.00**

Our upside case assumes all LNG projects are FID'd and applies a 10% premium to SDG&E, a 15% premium in TX, and increases the SoCalGas premium to 15%.

Downside case — **USD 126.00**

Our downside case assumes no future LNG projects are FID'd, assumes the current Ienova stock price (mxn), and lowers SDG&E to a 20% discount, SoCalGas and Texas to a 10% and 15% discount, respectively.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

The Southern Company (SO)

Stock Rating: OVERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	21,419	21,943	22,397	23,008	2.4%
EBITDA (adj)	10,774	8,469	8,832	9,359	-4.6%
EBIT (adj)	7,736	5,408	5,614	5,962	-8.3%
Pre-tax income (adj)	6,542	3,951	4,057	4,447	-12.1%
Net income (adj)	4,739	3,353	3,443	3,775	-7.3%
EPS (adj) ($)	4.53	3.18	3.27	3.53	-8.0%
Diluted shares (mn)	1,046.0	1,054.0	1,054.0	1,068.4	0.7%
DPS ($)	2.30	2.38	2.46	2.54	3.4%

Margin and return data					Average
EBITDA (adj) margin (%)	50.3	38.6	39.4	40.7	42.3
EBIT (adj) margin (%)	36.1	24.6	25.1	25.9	27.9
Pre-tax (adj) margin (%)	30.5	18.0	18.1	19.3	21.5
Net (adj) margin (%)	22.1	15.3	15.4	16.4	17.3
ROIC (%)	10.8	8.0	7.7	8.1	8.6
ROA (%)	4.7	3.1	3.2	3.5	3.6
ROE (%)	12.2	9.0	9.0	9.3	9.9

Balance sheet and cash flow ($mn)					CAGR
Net PP&E	73,695	75,925	78,474	81,621	3.5%
Cash and equivalents	1,978	2,661	1,176	467	-38.2%
Total assets	109,000	106,002	109,025	113,492	1.4%
Short and long-term debt	29,834	25,295	27,728	27,529	-2.6%
Other long-term liabilities	19,063	20,552	20,851	22,249	5.3%
Total liabilities	67,393	63,447	64,038	65,922	-0.7%
Shareholders' equity	37,291	38,301	40,433	42,716	4.6%
Net debt/(funds)	27,856	22,634	26,552	27,062	-1.0%
Change in working capital	-1,567	-3,232	2,742	464	N/A
Cash flow from operations	5,781	6,418	6,664	7,175	7.5%
Capital expenditure	-7,555	-7,200	-6,900	-6,200	N/A
Free cash flow	-181	-3,291	-2,828	-1,739	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	13.8	19.6	19.1	17.7	17.6
EV/EBITDA (adj) (x)	8.4	10.1	10.1	9.6	9.6
EV/EBIT (adj) (x)	11.8	15.9	16.0	15.1	14.7
FCF yield (%)	-0.2	-3.8	-3.2	-1.9	-2.3
P/BV (x)	1.7	1.7	1.6	1.6	1.7
Dividend yield (%)	3.7	3.8	3.9	4.1	3.9
Net debt/EBITDA (adj) (x)	2.6	2.7	3.0	2.9	2.8

Selected operating metrics					Average
Payout ratio (%)	50.8	74.8	75.3	71.9	68.2
Interest cover (x)	-6.2	-4.3	-4.4	-4.6	-4.9
Regulated (%)	94.0	94.0	194.0	294.0	169.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 62.36**
Price Target	**USD 73.00**

Why Overweight? Southern is a high-quality company with above-average dividend payments, which has traded to a discount based on construction risk for Vogtle. With schedule and cost risks still lessening and the risks being schedule and cost, not technology, we see SO as rerating over the next 12 months, thus justifying our Overweight rating.

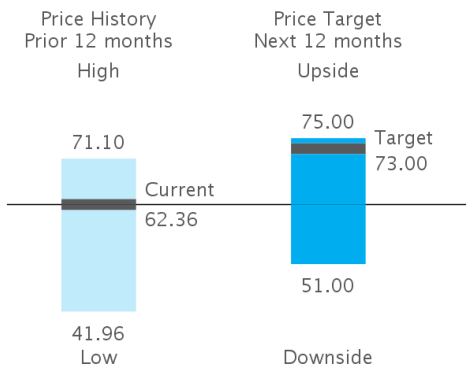
Upside case **USD 75.00**

We apply a 15% premium to group average 2023 P/E multiple on our 2023 EPS which includes the assumption that both Vogtle are in commercial operation in 2022

Downside case **USD 51.00**

We apply a 15% discount to the 2022 group average multiple applied to our 2022 EPS estimate and give no credit for future Vogtle earnings uplift

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

WEC Energy Group, Inc. (WEC)

Stock Rating: UNDERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	7,523	7,795	7,975	8,132	2.6%
EBITDA (adj)	2,458	2,701	2,840	2,971	6.5%
EBIT (adj)	1,531	1,734	1,805	1,870	6.9%
Pre-tax income (adj)	1,260	1,494	1,593	1,693	10.4%
Net income (adj)	1,134	1,195	1,273	1,353	6.1%
EPS (adj) ($)	3.58	3.77	4.02	4.27	6.1%
Diluted shares (mn)	316.7	316.7	316.7	316.7	0.0%
DPS ($)	2.36	2.53	2.68	2.84	6.3%

Margin and return data					Average
EBITDA (adj) margin (%)	32.7	34.7	35.6	36.5	34.9
EBIT (adj) margin (%)	20.4	22.2	22.6	23.0	22.1
Pre-tax (adj) margin (%)	16.7	19.2	20.0	20.8	19.2
Net (adj) margin (%)	15.1	15.3	16.0	16.6	15.8
ROIC (%)	5.0	4.9	4.9	5.0	4.9
ROA (%)	3.4	3.4	3.3	3.3	3.4
ROE (%)	11.6	11.8	12.1	12.4	12.0

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	32,751	35,725	38,817	41,866	8.5%
Cash and equivalents	38	427	303	-146	N/A
Total assets	34,952	38,473	40,598	42,190	6.5%
Short and long-term debt	12,692	14,048	15,122	15,710	7.4%
Other long-term liabilities	10,304	12,184	12,810	13,359	9.0%
Total liabilities	24,838	27,964	29,664	30,801	7.4%
Shareholders' equity	10,113	10,508	10,934	11,389	4.0%
Net debt/(funds)	12,654	13,621	14,819	15,857	7.8%
Change in working capital	-5	-569	615	-1,149	N/A
Cash flow from operations	2,346	2,763	2,909	3,055	9.2%
Capital expenditure	-2,261	-2,974	-3,093	-3,048	N/A
Free cash flow	-660	-1,011	-1,032	-892	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	28.0	26.6	24.9	23.4	25.7
EV/EBITDA (adj) (x)	18.1	16.8	16.4	16.0	16.8
EV/EBIT (adj) (x)	29.0	26.2	25.8	25.4	26.6
FCF yield (%)	-1.5	-2.2	-2.2	-1.9	-2.0
P/BV (x)	3.1	3.0	2.9	2.8	3.0
Dividend yield (%)	2.4	2.5	2.7	2.8	2.6
Net debt/EBITDA (adj) (x)	5.1	5.0	5.2	5.3	5.2

Selected operating metrics					Average
Payout ratio (%)	65.9	67.0	66.6	66.4	66.5
Interest cover (x)	3.1	3.4	3.5	3.5	3.4
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	USD 100.18
Price Target	USD 107.00

Why Underweight? We rate WEC as Underweight on its group high valuation, though meaningful dividend growth, significant free cash flow, and steady ratebase growth in a constructive regulatory jurisdiction provide a lower risk profile. We give WEC a 30% premium to the 2023 group average P/E multiple.

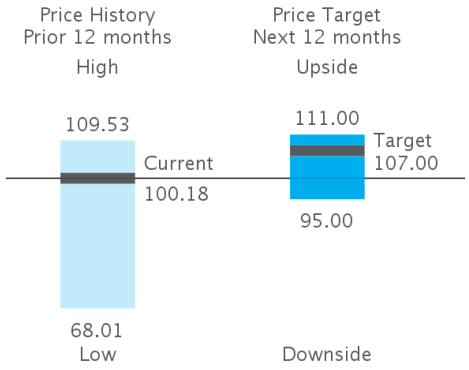
Upside case — **USD 111.00**

Our upside case assumes a 35% premium to the 2023 group average P/E multiple applied to our 2023 EPS estimate.

Downside case — **USD 95.00**

Our downside case assumes a 15% premium the group average multiple on our 2023 EPS estimate.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Xcel Energy Inc. (XEL)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	11,529	11,482	11,932	12,376	2.4%
EBITDA (adj)	4,038	4,154	4,463	4,800	5.9%
EBIT (adj)	2,273	2,243	2,417	2,602	4.6%
Pre-tax income (adj)	1,500	1,457	1,604	1,737	5.0%
Net income (adj)	1,372	1,455	1,604	1,737	8.2%
EPS (adj) ($)	2.64	2.77	3.01	3.21	6.8%
Diluted shares (mn)	520	526	533	541	1.3%
DPS ($)	1.62	1.72	1.82	1.93	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	35.0	36.2	37.4	38.8	36.8
EBIT (adj) margin (%)	19.7	19.5	20.3	21.0	20.1
Pre-tax (adj) margin (%)	13.0	12.7	13.4	14.0	13.3
Net (adj) margin (%)	11.9	12.7	13.4	14.0	13.0
ROIC (%)	4.1	4.2	4.2	4.1	4.1
ROA (%)	3.0	2.9	3.1	3.1	3.0
ROE (%)	9.5	8.7	10.8	9.0	9.5

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	39,483	42,291	45,325	48,785	7.3%
Cash and equivalents	248	-880	-65	1,077	63.1%
Total assets	50,448	52,125	55,993	60,615	6.3%
Short and long-term debt	18,704	19,804	21,405	22,775	6.8%
Other long-term liabilities	13,739	14,797	14,434	14,106	0.9%
Total liabilities	33,765	37,209	36,604	38,415	4.4%
Shareholders' equity	16,683	14,916	19,389	22,200	10.0%
Net debt/(funds)	18,456	20,684	21,471	21,698	5.5%
Change in working capital	-88	750	-704	1,161	N/A
Cash flow from operations	3,263	3,370	3,513	3,544	2.8%
Capital expenditure	-4,225	-4,800	-4,450	-4,900	N/A
Free cash flow	-1,753	-2,333	-1,907	-2,398	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	27.5	26.3	24.1	22.6	25.1
EV/EBITDA (adj) (x)	13.9	14.1	13.3	12.4	13.4
EV/EBIT (adj) (x)	24.7	26.1	24.5	22.9	24.5
FCF yield (%)	-3.1	-4.0	-3.2	-4.0	-3.6
P/BV (x)	2.3	2.6	2.0	1.8	2.1
Dividend yield (%)	2.2	2.4	2.5	2.7	2.4
Net debt/EBITDA (adj) (x)	4.6	5.0	4.8	4.5	4.7

Selected operating metrics					Average
Payout ratio (%)	61.3	62.0	60.4	60.0	60.9
Interest cover (x)	2.9	2.9	3.0	3.0	2.9
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 72.63**
Price Target	**USD 82.00**

Why Equal Weight? We rate XEL as Equal Weight as it is a well-run core large-cap utility whose mix of businesses and locations, coupled with solid operating results and visible growth, supports a 30% premium to the group average 2023 P/E multiple. XEL has rerated close to our expected premium.

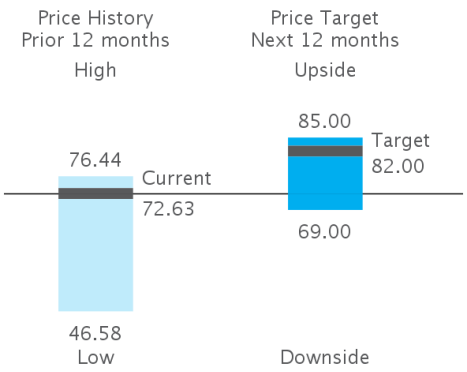
Upside case — **USD 85.00**

We use a 35% premium to the 2023 group average multiple applied to our 2023 EPS estimate.

Downside case — **USD 69.00**

We use a 10% premium to the 2023 group average multiple applied to our 2023 EPS estimate.

Upside/Downside scenarios



North America Power & Utilities **Industry View: POSITIVE**

Alliant Energy Corporation (LNT)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	3,648	3,678	3,780	3,890	2.2%
EBITDA (adj)	1,345	1,356	1,446	1,549	4.8%
EBIT (adj)	777	737	782	826	2.1%
Pre-tax income (adj)	635	553	567	625	-0.5%
Net income (adj)	556	610	630	695	7.7%
EPS (adj) ($)	2.33	2.46	2.52	2.78	6.1%
Diluted shares (mn)	239.0	247.5	250.0	250.0	1.5%
DPS ($)	1.41	1.52	1.61	1.71	6.5%

Margin and return data					Average
EBITDA (adj) margin (%)	36.9	36.9	38.3	39.8	38.0
EBIT (adj) margin (%)	21.3	20.0	20.7	21.2	20.8
Pre-tax (adj) margin (%)	17.4	15.0	15.0	16.1	15.9
Net (adj) margin (%)	15.3	16.6	16.7	17.9	16.6
ROIC (%)	6.6	5.7	5.7	5.6	5.9
ROA (%)	3.7	3.7	3.6	3.8	3.7
ROE (%)	12.1	11.7	10.4	10.5	11.2

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	13,527	14,263	14,870	15,749	5.2%
Cash and equivalents	16	346	511	809	267.5%
Total assets	16,701	17,791	18,587	19,788	5.8%
Short and long-term debt	6,528	6,776	6,974	7,514	4.8%
Other long-term liabilities	0	0	0	0	N/A
Total liabilities	11,296	11,544	11,742	12,282	2.8%
Shareholders' equity	5,205	6,048	6,645	7,306	12.0%
Net debt/(funds)	6,511	6,430	6,463	6,705	1.0%
Change in working capital	1,155	-165	193	-275	N/A
Cash flow from operations	660	1,239	1,304	1,428	29.3%
Capital expenditure	-1,640	-1,380	-1,295	-1,625	N/A
Free cash flow	-1,328	-527	-404	-634	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	23.5	22.2	21.7	19.7	21.8
EV/EBITDA (adj) (x)	14.8	14.6	13.7	13.0	14.0
EV/EBIT (adj) (x)	25.6	26.9	25.4	24.3	25.6
FCF yield (%)	-6.7	-2.7	-2.0	-3.2	-3.6
P/BV (x)	2.5	2.2	2.1	1.9	2.2
Dividend yield (%)	2.6	2.8	2.9	3.1	2.9
Net debt/EBITDA (adj) (x)	4.8	4.7	4.5	4.3	4.6

Selected operating metrics					Average
Payout ratio (%)	60.7	61.7	63.9	61.4	61.9
Interest cover (x)	2.8	2.7	2.8	2.7	2.8
Regulated (%)	92.5	92.5	92.3	92.4	92.4

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020) **USD 54.73**
Price Target **USD 65.00**

Why Equal Weight? We assign an Equal Weight rating to LNT given our view that the current premium to the 2023E group average multiple is appropriate for a name with strong renewable growth potential and an improving regulatory profile.

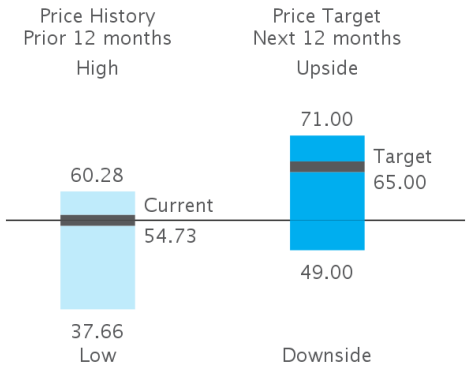
Upside case **USD 71.00**

Our upside case assumes a 25% premium to the group average 2023 utility P/E multiple, which we believe can be realized if LNT receives additional renewable capex approval, translates rate base growth to EPS growth more efficiently, or consistently beats guidance for 4-6 quarters.

Downside case **USD 49.00**

Our downside case assumes a 10% discount to the group average multiple, which we believe may occur if the WPL rate case is unfavorable or sales volumes are lower than expected and cash flow and earnings are put at risk.

Upside/Downside scenarios



Valuation Methodology and Risks

North America Power & Utilities
Alliant Energy Corporation (LNT)
Valuation Methodology: Our LNT price target is $65. We utilize a relative target P/E multiple to value LNT shares. We apply a 20% premium to the 18.5x group average 2023 P/E multiple to reflect LNT's strong track record for execution, visible earnings growth, attractive rate base growth opportunities driven by renewable generation that limit customer bill inflation, and constructive regulatory oversight.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Upside risks to our estimates and price target include better-than-expected regulatory outcomes, defensive equity flows, and increased M&A activity. Downside risks include inflation (commodity and PCE- leading to higher interest rates), adverse regulatory outcomes, project execution issues, or broad economic slowdown in LNT's service territories.
Ameren Corp. (AEE)
Valuation Methodology: Our $95 price target is derived by applying a 20% premium to the group average multiple of 18.5x to our 2023 EPS estimate of $4.28/share. We believe a premium multiple is appropriate at this time given the favorable regulatory structures AEE operates under in its primary jurisdictions of Missouri and Illinois.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Volatility of the US 30 Year Treasury Bond given formulaic rates in IL adds upside and downside risk. Threats to the IL QIP and uncertainty regarding the regulatory construct in IL and MO provide downside risk. Incremental spending opportunities from the MO IRP or clean energy legislation providing for higher levels of capex provide upside risk
American Electric Power Company, Inc. (AEP)
Valuation Methodology: Our price target for AEP is $107. We use a 10% premium to the 2023 regulated group average multiple of 18.5x applied to our 2023 estimate of $5.28 to reflect above average regulatory and long-term growth.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the company are: fair and timely rate recovery, regional economic impacts resulting in lower-than-expected usage, execution on cost controls to manage customer bill impacts.
American Water Works Company, Inc. (AWK)
Valuation Methodology: We utilize a group average water P/E multiple for 2023 earnings and apply a 15% premium to AWK's consolidated 2023 EPS estimate of $5.01. The premium reflects strong management, constructive regulatory exposure, and top-tier growth visibility.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to AWK include rate case outcomes, public system M&A deals and integration, external financing needs, and general interest rate environments.
CenterPoint Energy, Inc. (CNP)
Valuation Methodology: Our $27 price target is premised upon the 2023 utility group average P/E multiple of 18.5x against our 2023 EPS estimate. We use the current ENBL unit price adjusted for CNP's owned shares to account for the midstream segment value.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Equity needs if ENBL cuts its distribution, reaching EPS guidance through 2023, and realizing capex opportunities in IN remain as material upside/downside risks. Broader items that could also impact the shares: 1) economic growth impacting sales volumes, 2) constructive gubernatorial and commission changes benefiting regulation and legislation, and 3) cost control to manage customer bill impacts.
CMS Energy Corporation (CMS)
Valuation Methodology: Our $75 price target is derived by applying a 25% premium to the group average multiple of 18.5x to our 2023 EPS estimate of $3.25. CMS has a constructive regulatory relationship in Michigan and above-average earnings/dividend growth forecast.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major company risks are: broad economic impact slowing sales growth, inability to gain fair and timely regulatory recovery, gubernatorial and commission changes impacting regulation and legislation, Ability to control costs in order to manage customer bill impacts.
Consolidated Edison, Inc. (ED)
Valuation Methodology: Our ED price target is $83. We use a 10% discount to the 2023 group average P/E multiple of 18.5x applied to our 2023 EPS estimate of $4.94 to reflect an average regulatory environment, a more challenged earnings outlook, and low-risk profile.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the upside are: ED being able to achieve the full allowed ROE at CECONY, competition for growing NY transmission opportunities, and competition for behind-the-meter infrastructure based on REV.
Duke Energy Corporation (DUK)
Valuation Methodology: We derive our $102 price target for DUK by applying a 5% discount to the 2023 regulated group average multiple of 18.5x to 2023E regulated utility earnings for DUK of $5.81 per share. We believe a discount to the group average multiple is appropriate given the lack of earnings growth historically.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the company are: the ability to obtain fair and timely rate recovery,and recovery of coal ash costs. The ability to maintain credit metrics in order to avoid equity needs, regional economic impacts driving lower-than-expected usage, lower than expected regulatory recovery
Edison International (EIX)

Valuation Methodology and Risks

Valuation Methodology: Our $69 price target is based on a 20% discount to the 2023 group average multiple of 18.5x applied to an adjusted, post wildfire liability and additional funding, Barclays 2023 EPS estimate of $5.12. The 20% discount is based upon perceived wildfire risk absent a test of AB 1054 cost recovery standards and remaining uncertainty on 2017 and 2018 wildfire liabilities.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major upside/downside risks to the company are: final wildfire liability for 17/18 fires, ultimate legislation on inverse condemnation, and regulatory outcomes in pending and future rate cases.

Essential Utilities, Inc. (WTRG)

Valuation Methodology: We value WTRG's water business using a 5% premium to the group average water multiple. The 5% premium reflects strong regulatory exposure and public M&A opportunities, balanced by growth visibility lower than peers. We value the regulated gas business at a 15% premium to reflect a strong growth profile and familiar regulatory exposure.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to WTRG include rate case outcomes and general regulatory treatment, gas price inflation impacts on customer bills, and general interest rate environments.

Eversource Energy (ES)

Valuation Methodology: We derive our $100 price target by applying a 25% premium to the group average P/E multiple of 18.5x, to our 2023 earnings estimate of $4.34 per share. We believe a premium multiple is appropriate at this time given the nature of ES's growth profile, regulatory relationships, accretion from the Columbia Gas of MA acquisition and recovery mechanisms.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: The primary risk to our investment thesis is a change in regulation. We don't expect significant regulatory change in any of ES's jurisdictions at this time.

FirstEnergy Corp. (FE)

Valuation Methodology: Our $33 price target for FE is based on a 30% discount to the group average 2023 multiple of 18.5x applied to our pro forma FY23 EPS estimate, adjusted for an assumed $2bn equity issuance to reflect balance sheet repair following fines or penalties. The 30% discount is based on our expectation that the ongoing Ohio corruption investigation serves as an overhang to the stock valuation regardless of the financial impact.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major company risks are: OH corruption investigation, regulatory recovery in pending and future cases as well as prudency of spending associated with rate riders and formulaic rates; the ability to finance and execute on capital investment plans; broad economic impacts driving customer usage trends; and cost control execution to manage customer bill increases.

NextEra Energy, Inc. (NEE)

Valuation Methodology: Our price target of $87 is premised upon a SOTP with a 20% premium to the 2023 group average PE multiple of 18.5x applied to our 2023 EPS estimate of $1.74, a 17.5x 23E EV/EBITDA for the NEER business – comparable to valuations of renewables developers such as Ørsted. We then add $3 for NEP as we take the Barclays $67 NEP price target and flow it through to represent NEE's ownership.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: The major company risks are: ability to achieve fair and timely rate recovery, competition for renewable energy projects at NEER, federal legislation impacting profitability or competition of renewable generation, and regional economic impacts resulting in lower-than-expected usage.

NiSource, Inc. (NI)

Valuation Methodology: Our $29 price target is derived using the 2023 regulated utility group average P/E of 18.5x applied to our 2023 EPS estimate of $1.55. This reflects our view that NiSource, despite near-term headwinds, is a quality utility with a above-average medium-term rate base growth strategy from coal replacement power and gas and electric infrastructure modernization.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the company are: the ability to obtain fair and timely rate recovery, regional economic impacts driving lower-than-expected usage, and cost controls to manage customer rates.

NorthWestern Corporation (NWE)

Valuation Methodology: Our $63 price target is derived using the 2023 regulated utility group average P/E of 18.5x discounted by 10% to account for lower than average growth, applied to our 2023 EPS estimate of $3.79. We believe favorable geographic attributes of the state are outweighed by regulatory challenges and uncertainties in Montana.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the company are: fair and timely rate recovery; regional economic impacts; potential ability to manage customer bill impacts. Upside risks include positive regulatory outcomes and potential for new build of capacity resources in Montana.

OGE Energy Corp. (OGE)

Valuation Methodology: We derive our $36 price target by applying a 10% discount to the group average multiple of 18.5x applied to our 2023 utility earnings estimate combined with the current ENBL price $5 applied to the 111 units that OGE owns.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: OGE's capital plans impute less than 5% rate base growth. This is lower than the group average and is indicative of a below average regulatory jurisdiction. The upside is that as most companies grow earnings at or below the rate base growth level, OGE has the opportunity to grow regulated earnings in the 4-6% level on solid customer growth combined with potential to close the earned to allowed ROE gap that exists. The key (upside and downside risk) to enhancing growth lies in gaining rider approvals in Oklahoma. As significant generation and environmental spending is winding down, grid modernization, reliability, resiliency and technology are the next set of major spending programs.

PG&E Corporation (PCG)

Valuation Methodology and Risks

Valuation Methodology: Our $14 price target is based on a 35% discount to the group average 2023E P/E multiple of 18.5x against a $1.25 EPS estimate, reduced by the NPV of wildfire fund contributions, assuming the fund lasts 15 years.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: There is additional downside risk if capital structure changes lead to additional equity, future wildfires occur, or earnings are negatively impacted by regulatory outcomes.

Pinnacle West Capital Corporation (PNW)

Valuation Methodology: Our $103 price target is derived by applying the group average multiple of 18.5x, to our 2023 EPS estimate of $5.56. We expect the company to deliver average EPS and above-average dividend growth through 2023. In our view, the current regulatory uncertainty and geographic attributes justify a discount to the group average P/E multiple on a 2023 utility earnings.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major company risks to the downside include: 1) poor regulatory outcome of current APS rate case, 2) economic impact of lower sales growth, 3) ability to control costs in order to manage customer bill impacts and potential to allow retail choice, 4) deterioration of the regulatory construct.

PNM Resources, Inc. (PNM)

Valuation Methodology: Our $50 price target is premised upon the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E eps $2.68 estimate. Our price target is consistent with the terms of the AGR acquisition offer.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Events and outcomes that could result in under performance are: lack of regulatory support for the acquisition or a change in management sentiment regarding the acquisition.

Public Service Enterprise Group (PEG)

Valuation Methodology: Our price target for PEG is $65. We use a sum of the parts methodology, where we use a 5% premium to the 2023 regulated group average PE multiple of 18.5x applied to our 2023 EPS estimate for the utility and parent earnings of $3.18 and apply a 5X EBITDA multiple to the 2023 genco earnings.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Volatility in power prices, changes to the structure of the PJM, NYISO of NEPOOL capacity or energy markets. FERC ROE changes, or NJ BPU approval or changes to the pending Clean Energy Future capital spending plans.

Sempra Energy (SRE)

Valuation Methodology: We utilize a sum of the parts valuation framework for SRE. We apply a relative P/E multiple premium / discount to the North American utility businesses a base group average (10% premium for Texas, 15% for SoCalGas, group average for SDG&E). We utilize the Barclays Ienova Price Target and adjust for SRE ownership and spot USDMXN for Peso translation. We utilize a probability-weighted DCF approach for the LNG business depending on where each facility is on securing contracting for export capacity.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks include incremental equity needs, FIDs at LNG projects, construction problems, and negative regulatory outcomes.

The Southern Company (SO)

Valuation Methodology: We derive our $73 price target by applying the 2023 regulated group average P/E multiple of 18.5x to our 2023 EPS estimate of $3.92 for SO

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the company are: Adverse regulatory outcomes for Vogtle or the upcoming Georgia rate case; additional, unexpected delays to the plant Vogtle schedule; economic impacts that would drive lower electric usage; competition for renewable and contract generation impacting Southern Power's growth; and ability to drive O&M lower in order to earn the allowed ROE in each jurisdiction.

WEC Energy Group, Inc. (WEC)

Valuation Methodology: Our price target of $107 represents a 30% premium valuation relative to the utility peer group P/E multiple of 18.5x on our 2023 EPS estimate of $4.45. We believe this premium valuation is justified by the strong performance record the company has achieved and our belief that its forward growth goals are both realistic and achievable.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to the upside are: Continued load growth; higher than regulated returns from nonregulated renewable investments; ability to get fair and timely rate recovery; execution on cost controls; continued flight to safety and flows into the "comfort" group of utilities.

Xcel Energy Inc. (XEL)

Valuation Methodology: Our $82 price target is based on a 30% premium to the group average multiple of 18.5x applied to our 2023 EPS estimate of $3.40. We believe this premium valuation fairly reflects the quality, strength, and potential endurance of the company's growth.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the company are: ability to obtain fair and timely rate recovery, execution on coal to renewable generation transformation, ability to maintain credit metrics while financing its long-term capital plan, and execution on cost control to manage customer bill impact.

Source: Barclays Research.

ANALYST(S) CERTIFICATION(S):

I, Eric Beaumont, CFA, hereby certify (1) that the views expressed in this research report accurately reflect my personal views about any or all of the subject securities or issuers referred to in this research report and (2) no part of my compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this research report.

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Primary Stocks (Ticker, Date, Price)

Alliant Energy Corporation (LNT, 17-Nov-2020, USD 54.73), Equal Weight/Positive, CE/J/K/M

Ameren Corp. (AEE, 17-Nov-2020, USD 80.60), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

American Electric Power Company, Inc. (AEP, 17-Nov-2020, USD 86.73), Overweight/Positive, A/CD/CE/D/E/J/K/L/M/N

American Water Works Company, Inc. (AWK, 17-Nov-2020, USD 159.29), Equal Weight/Positive, CE/J

CenterPoint Energy, Inc. (CNP, 17-Nov-2020, USD 25.17), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

CMS Energy Corporation (CMS, 17-Nov-2020, USD 63.83), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

Consolidated Edison, Inc. (ED, 17-Nov-2020, USD 79.25), Underweight/Positive, A/CD/CE/D/J/K/L/M

Duke Energy Corporation (DUK, 17-Nov-2020, USD 92.92), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

Edison International (EIX, 17-Nov-2020, USD 65.60), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

Essential Utilities, Inc. (WTRG, 17-Nov-2020, USD 44.88), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

Eversource Energy (ES, 17-Nov-2020, USD 91.75), Equal Weight/Positive, A/CD/CE/D/E/J/K/L/M

FirstEnergy Corp. (FE, 17-Nov-2020, USD 28.74), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

NextEra Energy, Inc. (NEE, 17-Nov-2020, USD 76.61), Equal Weight/Positive, A/CD/CE/D/E/J/K/L/M

NiSource, Inc. (NI, 17-Nov-2020, USD 24.75), Overweight/Positive, A/CD/CE/D/J/K/L/M

NorthWestern Corporation (NWE, 17-Nov-2020, USD 60.38), Equal Weight/Positive, CD/CE/J

OGE Energy Corp. (OGE, 17-Nov-2020, USD 34.21), Equal Weight/Positive, CE/J

PG&E Corporation (PCG, 17-Nov-2020, USD 11.72), Overweight/Positive, A/CD/CE/D/J/K/L/M

Pinnacle West Capital Corporation (PNW, 17-Nov-2020, USD 86.78), Overweight/Positive, A/CD/CE/D/E/J/K/L/M

PNM Resources, Inc. (PNM, 17-Nov-2020, USD 48.90), Underweight/Positive, CD/CE/FA/J

Public Service Enterprise Group (PEG, 17-Nov-2020, USD 59.05), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

Sempra Energy (SRE, 17-Nov-2020, USD 134.06), Overweight/Positive, A/CD/CE/D/J/K/L/M

The Southern Company (SO, 17-Nov-2020, USD 62.36), Overweight/Positive, A/CD/CE/D/J/K/L/M

WEC Energy Group, Inc. (WEC, 17-Nov-2020, USD 100.18), Underweight/Positive, A/CD/CE/D/J/K/L/M

Xcel Energy Inc. (XEL, 17-Nov-2020, USD 72.63), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

Materially Mentioned Stocks (Ticker, Date, Price)

NextEra Energy Partners LP (NEP, 17-Nov-2020, USD 64.77), Equal Weight/Neutral, CE/J

IMPORTANT DISCLOSURES

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Enviva Partners LP (EVA)	First Solar (FSLR)	GFL Environmental (GFL)
GFL Environmental (GFL.TO)	NextEra Energy Partners LP (NEP)	Plug Power, Inc. (PLUG)
SolarEdge Technologies Inc. (SEDG)	SunPower (SPWR)	Sunrun Inc. (RUN)
North America Power & Utilities		
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Dominion Energy (D)	DTE Energy (DTE)	Duke Energy Corporation (DUK)
Edison International (EIX)	Essential Utilities, Inc. (WTRG)	Eversource Energy (ES)
Exelon Corporation (EXC)	FirstEnergy Corp. (FE)	NextEra Energy, Inc. (NEE)
NiSource, Inc. (NI)	NorthWestern Corporation (NWE)	OGE Energy Corp. (OGE)
PG&E Corporation (PCG)	Pinnacle West Capital Corporation (PNW)	PNM Resources, Inc. (PNM)
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BARCLAYS

Equity Research
22 April 2021

North America Power & Utilities

Straight from the Tap: US Water Utility Monthly

INDUSTRY UPDATE

North America Power & Utilities
POSITIVE
Unchanged

For a full list of our ratings, price target and earnings changes in this report, please see table on page 2.

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In this month's Straight from the Tap, we preview 1Q21 earnings for AWK and WTRG and discuss recent regulatory updates and potential implications of forthcoming water infrastructure legislative efforts.

AWK 1Q21 preview summary - 1Q21E EPS: $0.73. We expect a very straightforward 1Q21E earnings release for AWK as the company enters a relative quiet period now that PA, NJ, and MO rate cases are in the rear view mirror. We expect management commentary to highlight the strong regulated M&A execution YTD following the York deal (*AWK: Regulated M&A Train Rolls Through York, PA*, published 4/7/21), in line with upsized guidance on the 4Q20 call in February. We also anticipate commentary on potential legislative packages at the federal and state level. AWK's New York divestiture is the only remaining overhang, albeit unlikely to prove material in our view, as Governor Cuomo's efforts to push for municipalization as part of a larger budget bill seemingly stalled in the legislature. We reiterate our Equal Weight rating for AWK given our view that the sizable premium to the regulated utility group captures growth upside from regulated M&A amidst a broader ESG prioritization in both politics and financial markets.

WTRG 1Q21 preview summary - 1Q21E EPS: $0.66. We expect a cleaner 1Q21 EPS print as YoY comps now reflect the Peoples deal, though regulatory and legal updates could prove to be more nuanced. We are interested to hear management's perspective on the recent Delcora ALJ stay order, legal case progress, and how the process interacts with financing planning. We expect additional color on Peoples Gas rate case timing following WTRG's commitment to file a base rate case by year-end 2023. The company made the commitment as part of its repairs tax settlement to placate intervenor concerns about potential overearning from ongoing tax benefits above forecast. We expect management to provide a summary of the settlement terms and how the flow-through regulatory accounting interacts with earnings given the agreement compensates customers for 100% of catch-up benefits via a fixed annual surcredit for five years, while WTRG will not monetize the tax benefits as long as it retains an NOL position. We reiterate our Equal Weight rating on WTRG and believe the discount to AWK reflects a lower growth outlook and AWK's pure-play water scarcity. We do not expect near-term Delcora uncertainty to have a material impact longer term, but acknowledge risk that a protracted process serves as an overhang. With repairs tax nearly complete, we think a simplified profile with upside potential from regulated M&A should resonate with investors after Delcora is resolved.

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Completed: 22-Apr-21, 01:26 GMT Released: 22-Apr-21, 04:10 GMT Restricted - External

Summary of our Ratings, Price Targets and Earnings Changes in this Report (all changes are shown in bold)

Company	Rating		Price	Price Target			EPS FY1 (E)			EPS FY2 (E)		
	Old	New	21-Apr-21	Old	New	%Chg	Old	New	%Chg	Old	New	%Chg
North America Power & Utilities	Pos	Pos										

Source: Barclays Research. Share prices and target prices are shown in the primary listing currency and EPS estimates are shown in the reporting currency.
FY1(E): Current fiscal year estimates by Barclays Research. FY2(E): Next fiscal year estimates by Barclays Research.
Stock Rating: OW: Overweight; EW: Equal Weight; UW: Underweight; RS: Rating Suspended
Industry View: Pos: Positive; Neu: Neutral; Neg: Negative

AWK 1Q21 Earnings Expectations

1Q21E EPS Bridge

Our $0.73 1Q21E EPS estimate contemplates various rate increases from infrastructure surcharges, limited issue trackers, and partial realization of rate relief following GRC decisions at AWK's largest operating companies in PA and NJ. Surcharges and general rate relief is expected to provide more than enough offset to incremental financing and operational costs throughout FY21, though rate relief pacing shifts much of the cash benefit post 1Q21. We note that AWK's guidance basis EPS now includes DD&A benefits associated with the NY sale, the impact on Q1 is de minimis, as only $0.01 is added back to reported 1Q20 adjusted EPS.

FIGURE 1

AWK 1Q21E YoY Drivers

AWK EPS Walk	
1Q20A	**$0.67**
Rates and Customer Growth	$0.05
Infrastructure	$0.03
NY DD&A	$0.01
MBB	$0.01
Weather	$0.01
Additional DD&A	-$0.02
Interest Drag	-$0.03
1Q21E	**$0.73**

Source: Barclays Research

Expected Call Topics:

Regulated M&A Execution

We are expecting management to highlight the York wastewater deal and the general market strength for regulated M&A across AWK's national footprint (FMV laws cover 10 states and water quality accountability laws cover 3). We do not anticipate changes to the guidance provided during AWK's combined 4Q20 earnings and Investor Day in February, but expect a reiteration of confidence amidst strong early execution.

Sentiment on regulated M&A has been strong in recent months as muni budgets are strained following Covid-19 and environmental compliance costs are expected to rise as EPA enforcement rates increase under President Biden's administration. However, numerous federal policy proposals being floated to provide direct investment or bolster funding access for municipal water infrastructure could, all else equal, reduce the impetus to sell to AWK.

We believe it is too early to predict final terms of any water infrastructure package, as Republicans have not presented a counter proposal, but President Biden's proposal indicates that lead pipe replacement and water quality standards (contaminant regulations, PFAS monitoring and remediation) are going to be prioritized (see: *link*). While specific earmarks for rural and disadvantaged communities could help, we note that major cities and large municipal systems have historically received the bulk of federal funding versus smaller systems that AWK tends to prefer as acquisition opportunities. Regardless of likely concession and compromises, the President's proposal allocates $45bn for lead pipe replacement (WIIN grants), $56bn for disadvantaged and rural communities (upsize existing programs), and $10bn to remediate PFAS in drinking water and upgrade small rural systems. $110bn compares to the American Society of Civil Engineers estimate that $1tn of water

infrastructure investment is needed in the US over the coming 25 years. The infrastructure package is light on wastewater systems, which we anticipate will continue to make up the bulk of regulated M&A moving forward. Thus, we see plenty of opportunities for AWK in small to medium wastewater systems (5,000-30,000 average customer systems).

NYAW Exit Headaches Persist

At Governor Cuomo's direction, on March 29, 2021, the New York Department of Public Service (DPS) presented a municipalization feasibility study that concluded a public takeover of AWK's Nassau County system is the optimal and least cost option. The primary concern from lawmakers is the outsized customer bill (a result of high local property and franchise taxes that make up 38%-60% of total bills) and an upcoming rate increase (26% increase in some rate classes) set to take effect on May 1, 2021. The DPS report found that municipalization was the optimal path because the inefficient tax collection structure creates numerous inequities and inefficiencies, including paying higher federal taxes when compared to a scenario where NYAW becomes tax exempt and those tax revenues are replaced with higher property taxes. The recommendations from the DPS were to immediately pass legislation to remove the property tax burden on NYAW and create a public authority to acquire NYAW and operate the assets as a public provider.

There was a push to include municipalization authority in the 2021-2022 budget, however efforts stalled in the Assembly on concerns about how special franchise taxes might be absorbed by Long Island utilities under the proposed process. Standalone bills to defer the rate increase and authorize a public takeover were introduced after the budget efforts collapsed, and the Senate passed a version on Tuesday (4/20/21) as negotiations are ongoing with the Assembly.

We see the outcome of the NYAW process as highly uncertain, but remain confident that the PSC will stand by the authorized rate increase if needed and do not see a scenario where AWK receives less than the Liberty offer. However, we stress that the size of the system likely means AWK will comfortably absorb any near-term financial impacts from a delay. The DPS study assumes the $608mn sale price that Liberty agreed to, plus $84.5mn in rate base investment in 2022, less ~$25mn for upstate assets that would be retained and deferrals owed to customers, resulting in a net purchase price of $669.2mn. However, the study is explicit that the math is illustrative and likely inflated (maintaining negotiating options).

CA American Water Cost of Capital

CA water utilities will file updated cost of capital proceedings by May 1, 2021, to determine authorized ROE and capital structures for test years 2022-2024. CA American Water is currently authorized a 9.2% ROE on 55.39% equity layer from a 2018 CPUC decision. It is worth noting that the ALJ proposed decision suggested an 8.23% ROE (avg US water ROE was 9.5%), which was met with significant industry backlash before commissioners decided on the higher 9.20%. It is also important to note that the WRAM decoupling mechanism was a critical element that the ALJ relied upon to justify below industry returns given lower risk. In 2020, the CPUC decided that the WRAM decoupling mechanism used by CA American Water will be replaced by a new structure to be determined during the next rate case covering test years 2024-2026. It is unclear how the cost of capital proceeding will handle the overlap and uncertainty around a replacement. For additional thoughts on the WRAM decision, see our Straight from the Tap note published 9/8/2020 (*link*).

WTRG 1Q21 Earnings Expectations

1Q21E EPS Bridge

Our 1Q21E EPS estimate of $0.66 accounts for small rate relief via water infrastructure surcharges and a full year of Peoples integration. Our estimate is in line with management's projections for first quarter earnings weighting of 35%-45% of $1.64-$1.69 FY21E EPS

guidance (implicit 1Q21 guidance range of $0.58-$0.74 using the FY21 guidance midpoint). We anticipate a small amount of volumetric help YoY given customer growth (guidance 2%-3% annually) and degree day comps for gas usage in PA. We also note residential water usage trends have been strong during the covid-19 shutdowns and margin help may continue to pace favorably relative to 1Q20, providing additional flexibility to meet FY21 guidance. We also forecast small organic growth and operational efficiencies for Peoples relative to the early days of the integration in 1Q20, in line with WTRG's O&M initiatives across the business.

FIGURE 2
WTRG 1Q21E YoY Drivers

WTRG EPS Walk	
1Q20A	**$0.60**
Water Rates	$0.01
Weather and Usage	$0.03
Peoples	$0.02
1Q21E	**$0.66**

Source: Barclays Research

Expected Call Topics:

Peoples Rate Case Timing

As part of WTRG's settlement on the catch-up component of repairs tax, Peoples committed to filing a general rate case no later than December 31, 2023 (Peoples will also likely implement the DSIC mechanism in 2023). Under the initial proposal, WTRG proposed a sharing mechanism that would have allowed Peoples Gas to stay out through 2026.

The settlement effectively provides customers 100% of $381mn catch-up deduction tax savings benefits via a $27.9mn annual surcredit over five years (true up in sixth year). The settlement acknowledges that Peoples is operating in an NOL position and thus cannot monetize the benefit near term, thus justifying the five-year deferral and includes various true up and reconciliation terms to ensure surcredits track actual tax benefits flowing through to Peoples.

Taking Steps Forward at Delcora but Stuck in Regulatory and Legal Maze

We discussed the ALJ PD calling for the PA PUC to reject the Delcora acquisition in the January 22 monthly, *Straight from the Tap*. The PD had three main concerns; 1) commercial customer objections to the deal, 2) the effective rate stabilization plan creation via trust refunds on bills, and 3) the ongoing legal challenge to the sale contract. The Commission took into account new settlements with numerous customers and clarifying comments from WTRG around its willingness to provide trust benefits off of customer bills to avoid being a 'de facto' rate stabilization plan and decided not to adopt the ALJ PD.

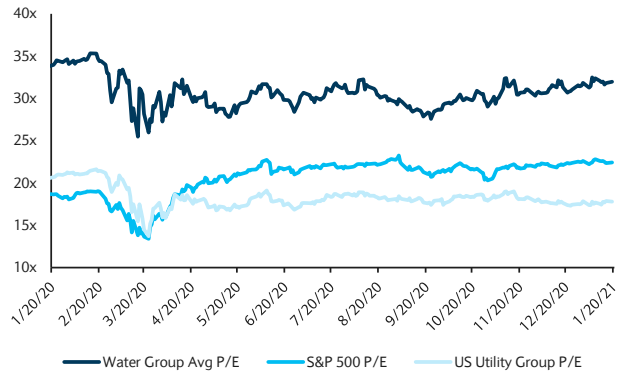
The PUC vacated the PD and remanded back to the ALJ level to reopen the docket. Importantly, as part of the reopening of the docket WTRG agreed to waive the statutory timeline requirements for a decision. The new ALJ on April 16 issued a stay order for the PA PUC proceeding until a final, un-appealable decision is reached in the county court case on whether an enforceable contract exists. Our understanding is that the appeals process could be lengthy and that WTRG will likely seek to have the ALJ order changed to allow for approval while legal appeals on contract validity play out.

We view the Delcora situation as bureaucratically complicated but the deal remains achievable if WTRG continues to execute settlements and legal decisions are upheld, however the timeline remains unclear. WTRG's $300mn forward equity mechanism must be pulled

down by August. We still believe WTRG is likely to issue all authorized equity regardless of whether Delcora is approved in time. We also see the guidance range as intact regardless of the deal given strong M&A activity outside of Delcora. We anticipate management will highlight the strength of their deal backlog and general market activity.

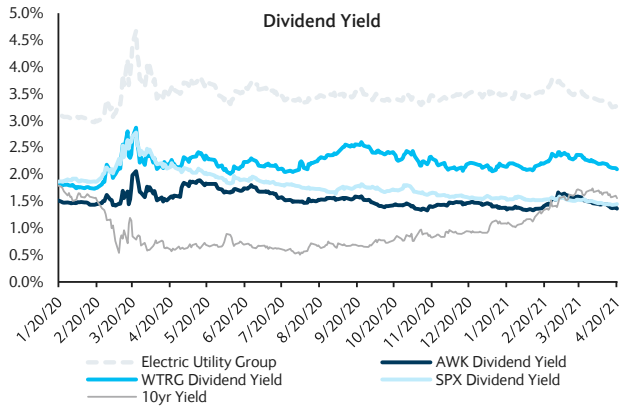
Monthly Valuation Trends

FIGURE 3
Group P/E Trends



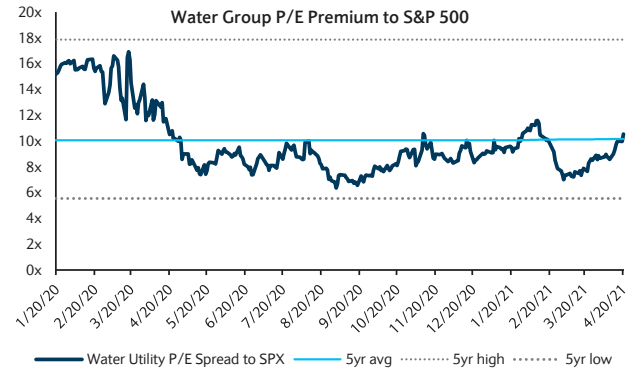
Source: Barclays Research, Bloomberg

FIGURE 4
Group Yield Trends



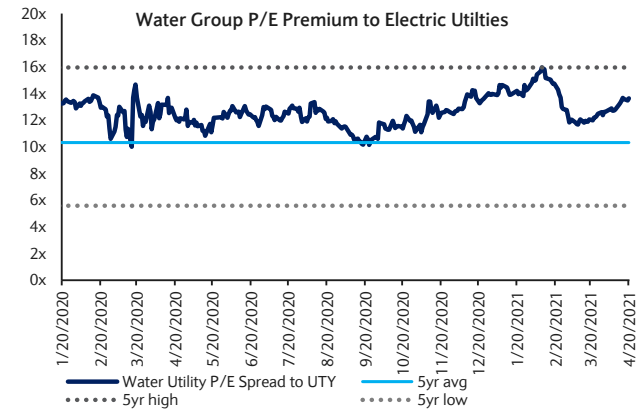
Source: Barclays Research, Bloomberg

FIGURE 5
Water Group Premium to S&P 500



Source: Barclays Research, Bloomberg

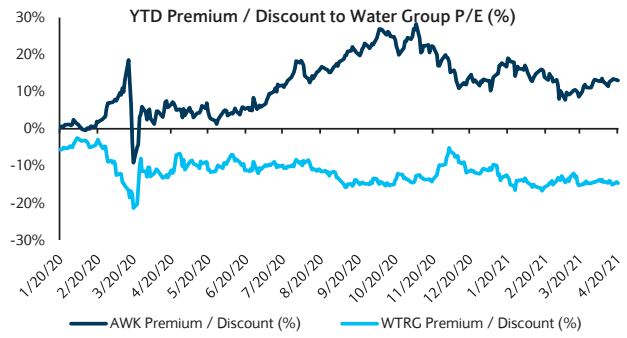
FIGURE 6
Water Group Premium to Regulated Utility Group



Source: Barclays Research, Bloomberg

FIGURE 7

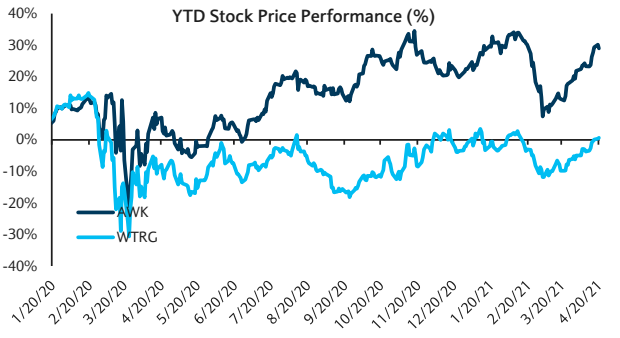
AWK and WTRG Premium (Discount) to Water Group



Source: Barclays Research, Bloomberg

FIGURE 8

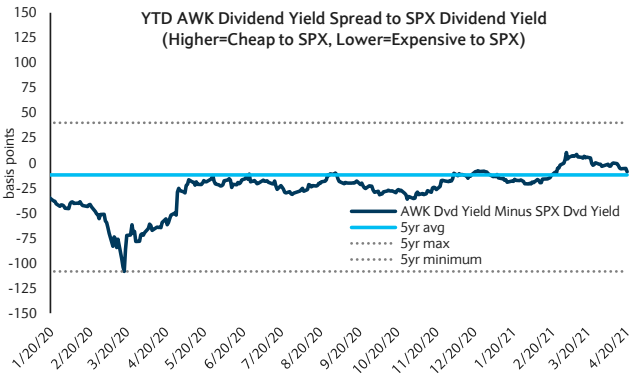
AWK and WTRG YTD Stock Performance



Source: Barclays Research, Bloomberg

FIGURE 9

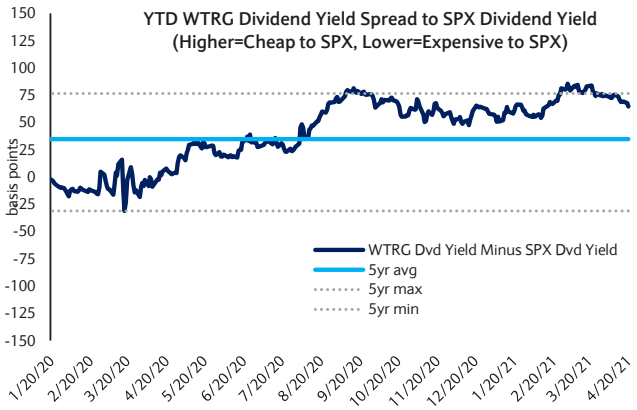
AWK Dividend Spread



Source: Barclays Research, Bloomberg

FIGURE 10

WTRG Dividend Spread



Source: Barclays Research, Bloomberg

North America Power & Utilities — **Industry View: POSITIVE**

American Water Works Company, Inc. (AWK)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2020A	2021E	2022E	2023E	CAGR
Revenue	3,777	4,111	4,405	4,658	7.2%
EBITDA (adj)	2,155	2,338	2,507	2,681	7.6%
EBIT (adj)	1,551	1,687	1,810	1,939	7.7%
Pre-tax income (adj)	924	1,017	1,124	1,230	10.0%
Net income (adj)	709	770	851	930	9.5%
EPS (adj) ($)	3.91	4.24	4.64	4.99	8.5%
Diluted shares (mn)	182	182	184	187	0.9%
DPS ($)	2.15	2.34	2.55	2.78	9.0%

Margin and return data					Average
EBITDA (adj) margin (%)	57.1	56.9	56.9	57.6	57.1
EBIT (adj) margin (%)	41.1	41.0	41.1	41.6	41.2
Pre-tax (adj) margin (%)	24.5	24.7	25.5	26.4	25.3
Net (adj) margin (%)	18.8	18.7	19.3	20.0	19.2
ROIC (%)	8.9	9.6	10.1	10.3	9.7
ROA (%)	3.1	3.1	3.4	3.5	3.3
ROE (%)	11.6	11.9	12.4	12.1	12.0

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	25,614	27,369	29,299	31,229	6.8%
Cash and equivalents	547	35	78	173	-31.9%
Total assets	24,766	25,357	26,634	27,917	4.1%
Short and long-term debt	10,940	10,671	10,291	10,265	-2.1%
Other long-term liabilities	0	0	0	0	N/A
Total liabilities	8,979	9,165	9,478	10,262	4.6%
Shareholders' equity	6,454	6,868	7,701	8,562	9.9%
Net debt/(funds)	10,393	10,636	10,214	10,092	-1.0%
Change in working capital	621	-512	43	95	-46.4%
Cash flow from operations	1,426	1,668	1,821	1,971	11.4%
Capital expenditure	-1,822	-1,555	-1,755	-1,755	N/A
Free cash flow	-920	-513	-578	-478	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	41.2	38.0	34.7	32.3	36.5
EV/EBITDA (adj) (x)	18.6	17.1	15.8	14.7	16.5
EV/EBIT (adj) (x)	25.9	23.7	21.8	20.4	22.9
FCF yield (%)	-2.3	-1.3	-1.5	-1.2	-1.6
P/BV (x)	4.5	4.3	3.8	3.5	4.0
Dividend yield (%)	1.3	1.5	1.6	1.7	1.5
Net debt/EBITDA (adj) (x)	4.8	4.5	4.1	3.8	4.3

Selected operating metrics					Average
Payout ratio (%)	55.0	55.3	55.1	55.8	55.3
Interest cover (x)	3.9	4.3	4.7	5.1	4.5
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (21-Apr-2021)	**USD 161.00**
Price Target	**USD 154.00**

Why Equal Weight? AWK presents a strong growth profile with top-tier management and a solid execution track record, however valuation is stretched relative to electric and gas utilties and our valuation framework implies a 15% premium to the water group average P/E multiple, all of which is fully reflected in the current stock price

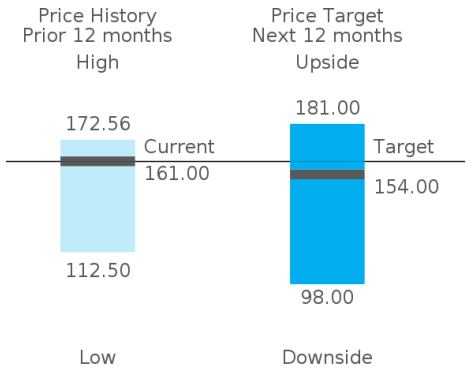
Upside case **USD 181.00**

Our upside case assumes AWK trades at a 25% premium to the group average water utility P/E multiple. We believe this scenario could materialize if ESG flows increase or general utility equity demand rises and disproportionately benefits AWK.

Downside case **USD 98.00**

Our downside case values AWK on the same 15% premium, but applies the group utitlity multiple in lieu of the water group multiple. This could materialize if investors perceive long-term growth opportunities and ESG profiles to be similar to electric and gas.

Upside/Downside scenarios



Valuation Methodology and Risks

North America Power & Utilities
American Water Works Company, Inc. (AWK)
Valuation Methodology: We utilize a group average water P/E multiple for 2023 earnings and apply a 10% premium to AWK's consolidated 2023 EPS estimate of $5.01 to arrive at our $154 price target. The premium reflects strong management, constructive regulatory exposure, and top-tier growth visibility.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to AWK include rate case outcomes, public system M&A deals and integration, external financing needs, and general interest rate environments.

Source: Barclays Research.

ANALYST(S) CERTIFICATION(S):

I, Eric Beaumont, CFA, hereby certify (1) that the views expressed in this research report accurately reflect my personal views about any or all of the subject securities or issuers referred to in this research report and (2) no part of my compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this research report.

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Primary Stocks (Ticker, Date, Price)

American Water Works Company, Inc. (AWK, 21-Apr-2021, USD 161.00), Equal Weight/Positive, CE/J

Materially Mentioned Stocks (Ticker, Date, Price)

Essential Utilities, Inc. (WTRG, 21-Apr-2021, USD 47.84), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

Unless otherwise indicated, prices are sourced from Bloomberg and reflect the closing price in the relevant trading market, which may not be the last available price at the time of publication.

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In addition to the stock rating, we provide industry views which rate the outlook for the industry coverage universe as Positive, Neutral or Negative (see definitions below). A rating system using terms such as buy, hold and sell is not the equivalent of our rating system. Investors should carefully read the entire research report including the definitions of all ratings and not infer its contents from ratings alone.

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Overweight - The stock is expected to outperform the unweighted expected total return of the industry coverage universe over a 12-month investment horizon.

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Below is the list of companies that constitute the "industry coverage universe":

North America Power & Utilities

Alliant Energy Corporation (LNT)	Ameren Corp. (AEE)	American Electric Power Company, Inc. (AEP)
American Water Works Company, Inc. (AWK)	Brookfield Infrastructure Partners LP (BIP)	Brookfield Infrastructure Partners LP (BIP_u.TO)
CenterPoint Energy, Inc. (CNP)	CMS Energy Corporation (CMS)	Consolidated Edison, Inc. (ED)

IMPORTANT DISCLOSURES

Dominion Energy (D)	DTE Energy (DTE)	Duke Energy Corporation (DUK)
Edison International (EIX)	Essential Utilities, Inc. (WTRG)	Eversource Energy (ES)
Exelon Corporation (EXC)	FirstEnergy Corp. (FE)	NextEra Energy, Inc. (NEE)
NiSource, Inc. (NI)	NorthWestern Corporation (NWE)	OGE Energy Corp. (OGE)
PG&E Corporation (PCG)	Pinnacle West Capital Corporation (PNW)	PNM Resources, Inc. (PNM)
Portland General Electric Company (POR)	Public Service Enterprise Group (PEG)	Sempra Energy (SRE)
The Southern Company (SO)	WEC Energy Group, Inc. (WEC)	Xcel Energy Inc. (XEL)

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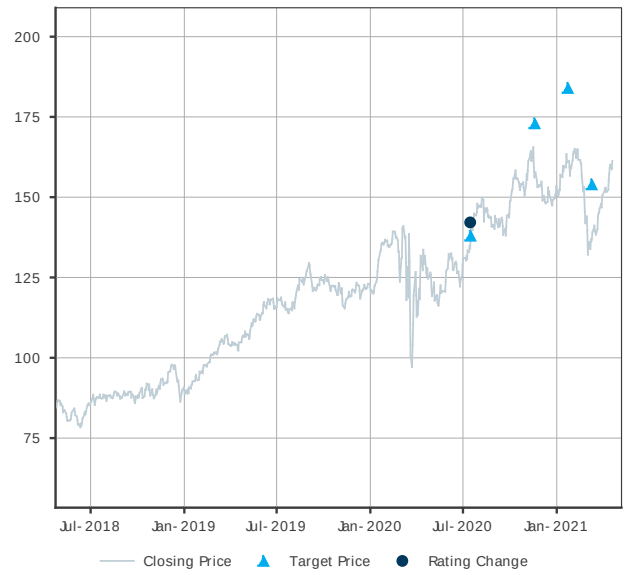
IMPORTANT DISCLOSURES

American Water Works Company, Inc. (AWK / AWK)

Stock Rating	Industry View
EQUAL WEIGHT	**POSITIVE**

USD 161.00 (21-Apr-2021)

Rating and Price Target Chart - USD (as of 21-Apr-2021)



Source: IDC, Barclays Research

Currency=USD

Publication Date	Closing Price	Rating	Adjusted Price Target
10-Mar-2021	136.38		154.00
22-Jan-2021	160.91		184.00
18-Nov-2020	156.19		173.00
15-Jul-2020	134.06	Equal Weight	138.00

Source: Bloomberg, Barclays Research

Historical stock prices and price targets may have been adjusted for stock splits and dividends.

Link to Barclays Live for interactive charting

CE: Barclays Bank PLC and/or an affiliate is a market-maker in equity securities issued by American Water Works Company, Inc..

J: Barclays Bank PLC and/or an affiliate is a liquidity provider and/or trades regularly in the securities by American Water Works Company, Inc. and/or in any related derivatives.

Valuation Methodology: We utilize a group average water P/E multiple for 2023 earnings and apply a 10% premium to AWK's consolidated 2023 EPS estimate of $5.01 to arrive at our $154 price target. The premium reflects strong management, constructive regulatory exposure, and top-tier growth visibility.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to AWK include rate case outcomes, public system M&A deals and integration, external financing needs, and general interest rate environments.

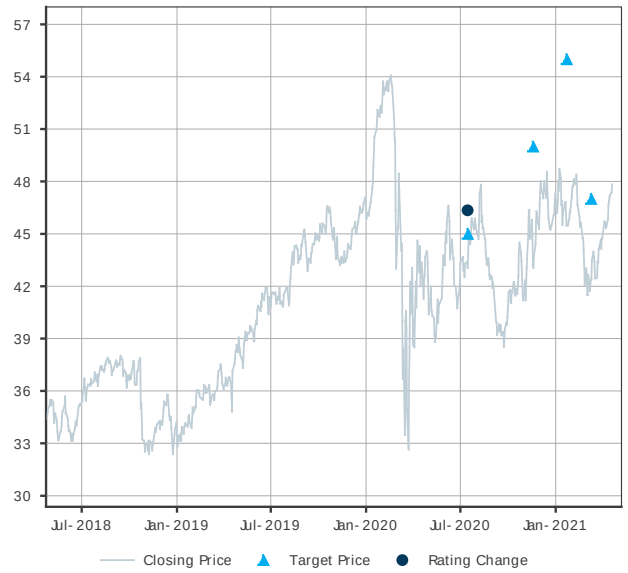
IMPORTANT DISCLOSURES

Essential Utilities, Inc. (WTRG / WTRG)

USD 47.84 (21-Apr-2021)

Stock Rating	Industry View
EQUAL WEIGHT	**POSITIVE**

Rating and Price Target Chart - USD (as of 21-Apr-2021) **Currency=USD**



Publication Date	Closing Price	Rating	Adjusted Price Target
10-Mar-2021	42.39		47.00
22-Jan-2021	45.46		55.00
18-Nov-2020	43.18		50.00
15-Jul-2020	43.04	Equal Weight	45.00

Source: Bloomberg, Barclays Research

Historical stock prices and price targets may have been adjusted for stock splits and dividends.

Source: IDC, Barclays Research

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Valuation Methodology: We have a $47 price target for WTRG. We value WTRG's water business using a group average water multiple of 28x. The valuation reflects strong regulatory exposure and public M&A opportunities, balanced by growth visibility lower than peers and near-term risk from closing recent public M&A deals. We value the regulated gas business at a 5% premium to the average 2023 multiple of 17x for our electric and gas group coverage, reflecting a strong growth profile and familiar regulatory exposure.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to WTRG include rate case outcomes and general regulatory treatment, gas price inflation impacts on customer bills, and general interest rate environments.

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BARCLAYS

Equity Research
15 July 2020

North America Power & Utilities

Water valuations are hot, but have they boiled over?

We initiate coverage on AWK and WTRG with Equal Weight ratings: Water valuations have seemingly lost all correlation to electric and gas utilities, as the group P/E multiple has expanded to a ~10-turn premium. However, we see little evidence of the spread contracting near term, as we view investor expectations as reasonable and near-term earnings headwinds as scarce. Increasing reliance on rate cases throughout the forecast period represent the largest sector-wide risk factor through our 2022 forecast horizon, but customer bill offsets exist for some, and overall customer bill inflation appears palatable.

Scarcity value and ESG narrative likely to drive premium for foreseeable future, in our view: Regardless of fundamental similarities to electric and gas utility counterparts, we expect the water premium to persist as scarcity and index composition drive ownership diversity and support water valuations for the foreseeable future. Water utilities also benefit from their lack of electric generation exposure that disqualifies some utilities on ESG screens, and we see increased environmental regulation on water quality coupled with fair market value legislation as adding a compelling qualitative ESG narrative as investor-owned water utilities provide needed financing for cash-strapped public agencies, particularly following the impact of COVID-19 on public budgets.

Recent execution and industry tailwinds likely mean EPS CAGRs moderate somewhat, but growth backlog and visibility still exceed electric peers: AWK and WTRG possess unique scale that position both to play leading roles in a national water infrastructure replacement cycle in the US. Chronic under-investment in water infrastructure has led the American Society of Civil Engineers to estimate that $1tn of total infrastructure spending is needed over the coming 25 years to repair and replace aging infrastructure. The market position dominance is unmatched in the electric utility space (NEE is probably closest with NEER). We see the scale advantage and reputation for best-in-class management providing greater confidence and visibility into capital deployment and growth. External financing needs likely increase relative to previous years given cash tax positions and balance sheet limitations; we see modest ROE lag between cases as possible, but still believe EPS and rate base growth exceed the average electric utility.

Valuation framework: We arrive at a $138 price target for AWK and a $45 price target for WTRG and rate both Equal Weight. We utilize a 27x 2022 P/E group average multiple base for water utilities and a 17x general utility group average multiple for WTRG's gas business. We apply our standard premium and discount valuation framework to arrive at a 15% water premium for AWK and a 5% and 15% premium for WTRG's water and gas business, respectively.

INITIATING COVERAGE

North America Power & Utilities
POSITIVE
Unchanged

For a full list of our ratings, price targets and earnings in this report, please see table on page 2

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PLEASE SEE ANALYST CERTIFICATION(S) AND IMPORTANT DISCLOSURES BEGINNING ON PAGE 30.

Summary of our Ratings, Price Targets and Earnings Estimates in this Report

Company	Rating		Price	Price Target			EPS FY1 (E)			EPS FY2 (E)		
	Old	New	13-Jul-20	Old	New	%Chg	Old	New	%Chg	Old	New	%Chg
North America Power & Utilities	Pos	Pos										
American Water Works Company, Inc. (AWK)	N/A	**EW**	132.97	N/A	**138.00**	-	N/A	**3.86**	-	N/A	**4.22**	-
Essential Utilities, Inc. (WTRG)	N/A	**EW**	43.37	N/A	**45.00**	-	N/A	**1.56**	-	N/A	**1.67**	-

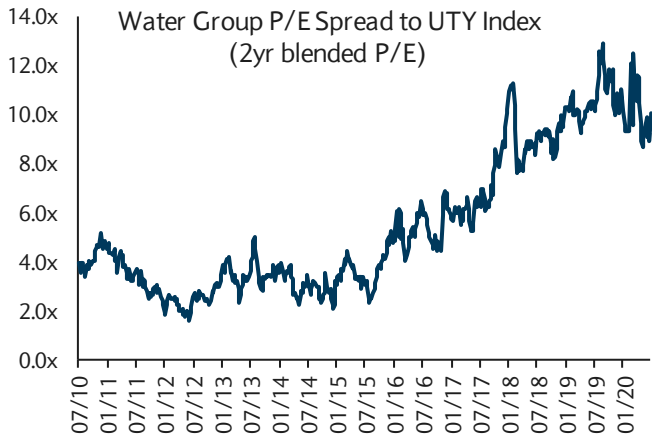
Source: Barclays Research. Share prices and target prices are shown in the primary listing currency and EPS estimates are shown in the reporting currency.
FY1(E): Current fiscal year estimates by Barclays Research. FY2(E): Next fiscal year estimates by Barclays Research.
Stock Rating: OW: Overweight; EW: Equal Weight; UW: Underweight; RS: Rating Suspended
Industry View: Pos: Positive; Neu: Neutral; Neg: Negative

Is Water Just Worth More Than Electricity?

Water Valuation Premium Continues to Expand

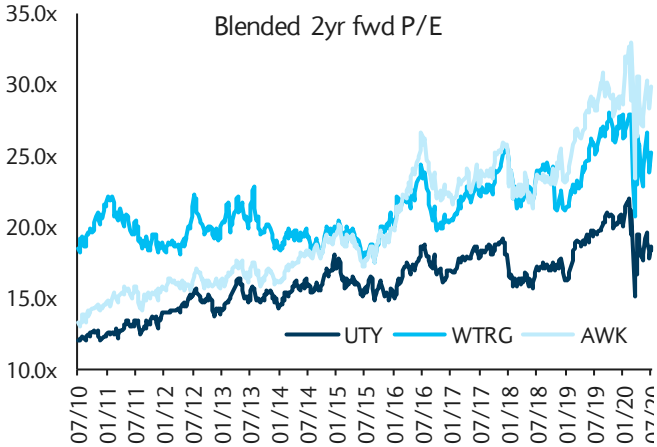
Water utilities have seemingly broken free of any tether to electric and gas utilities in recent years and there are no signs that the gap will close. We use AWK, WTRG, CWT, and AWR as our water utility basket for all group average calculations. The premium would screen even greater, but we exclude securities with a market cap below $2bn (MSEX, SJW, YORW), as we believe limited trading liquidity and embedded takeout premiums would misrepresent comparisons to the traditional US utility under coverage. The pace of the expansion has been particularly notable as the group hovered between 2x-4x premium from 2010 through 2015 before expanding to >10x since early 2019. AWK currently trades at a record 11.5x premium to the UTY.

FIGURE 1
Water P/E Spread to UTY Index



Source: Bloomberg, Barclays Research

FIGURE 2
AWK and WTRG P/E Spread to UTY Index



Source: Bloomberg, Barclays Research

Is That Premium Justified?

Valuation has dominated the debate for the water sector as a whole for the last few years. The duration and apparent sustainability of the premium is notable, in our view, and cannot be dismissed as irrational or transient.

We present our view of current market sentiment on water utilities in the following "Bulls say, Bears say, Barclays says" section before going into additional detail on what we view as the three most compelling justifications for the premium.

Bulls, Bears, Barclays

Bulls say: *Water utilities are advantaged to electric and gas given a more visible long-term capital deployment and earnings growth opportunity, lower earnings and operational risk, and cleaner ESG attributes.*

- **1) Long-term EPS and dividend growth are more than enough to justify price:** AWK's 7-10% growth guidance is ongoing and sustainable long term and justify prices when applied to DCF and dividend-based valuation frameworks. If recently authorized ROE decisions made by state regulatory commissions are correct (most use some derivation of CAPM), the cost of equity capital for most US utilities like AWK and WTRG is ~9.0-9.5x. Assuming AWK can maintain a 7-10% CAGR, the current <2.0% dividend yield is more than adequate for equity investors.
- **2) Rate base growth opportunity is larger and more visible than electric and gas:** Average system age indicates the US is approaching a multi-generational water infrastructure replacement cycle. The investment need is larger than electric and gas, and AWK and WTRG have the scale to become the 'first call' from public officials and legislators when towns are unable to afford upgrades required to stay in compliance. The recent wave of fair market value legislation (FMVL) that passed state legislatures is evidence that public officials understand the need for and support private investment in water systems. The economic impact of COVID-19 on public tax revenues and financial positions will also increase the likelihood of reaching agreement with systems previously unwilling. Additionally, water utilities have greater residential customer bill headroom to pursue rate base growth compared to typical residential electric and gas bills.
- **3) Water utility ESG profiles are more attractive than electric or gas:** Water utilities provide ESG-constrained funds, which may be barred from owning generation or gas assets, an opportunity to gain utility sector exposure. The core growth driver of a water utility is to deploy capital that ensures reliable, efficient, and safe delivery of drinking water and treatment of wastewater, which sustainability-focused funds should find attractive (particularly as water scarcity issues grow). There is also an environmental angle for water utilities, as they could benefit from a wave of environmental regulations (emerging contaminants, like PFAS, are a near-term focus as capex / rate base growth will increase and local municipalities turn to investor-owned utilities with greater capital access and operational expertise.
- **4) Lower operational and earnings risk:** Water infrastructure compares favorably to common electric and gas utility risk factors such as workplace safety, environmental violations and related lawsuits, wildfires, and cost recovery uncertainty as renewable replacement accelerates. Earnings are also more predictable, as revenues are less reliant on weather than electric and gas. Water capex plans consist of thousands of small, diverse projects, lacking the large project risk (execution, environmental permitting, legal challenges) that electric and gas utilities are often exposed to.

Bears say: *Valuations are overdone, equity capital raises will be larger and more frequent, regulated acquisitions are becoming more challenging, ROE lags, and rate case exposure presents greater risk.*

- **1) Current valuations are unapproachable:** All-time high valuations are pricing in unsustainable long-term growth assumptions based on earnings outperformance over the past five years that will settle closer to consensus electric EPS CAGRs over time. With no other apparent distinctions between an electric and water utility with similar regulatory exposure, water stocks carry a 10-turn 'air pocket' on a P/E basis that will fall out as long-term growth assumptions converge.
- **2) Future equity needs will be higher than the past few years:** Debt metrics and parent leverage will approach rating agency thresholds given cash flow projections relative to the size of current capex and regulated M&A plans, requiring greater and more frequent reliance on equity capital markets. The equity need will be amplified as utilities become cash taxpayers (AWK sees payments starting in modest ~2021; $~200mn annual cash source currently). Early evidence can be seen with AWK's inclusion of $500mn of equity in its five-year capital plan and WTRG's $300mn planned issuance in late 2020/1Q21 (timing depends on Delcora outcomes).
- **3) Municipal acquisitions are not the panacea that some think they are:** M&A executed immediately following passage of fair market value bills likely attracted public systems that needed financing most desperately and were most motivated to sell. Recent complications and community pushback relates primarily to concerns about losing both control over freshwater supply and public tax revenues. Negotiating leverage will continue to strengthen over time and municipalities will likely require more onerous terms like customer bill commitments and employee retention, in addition to a pure financial contribution. Regulatory commissions that employ single-tariff ratemaking structures have also limited the ability for utilities to get 'back door' rate recovery without a new general rate case (GRC).
- **4) Rate case reliance and risk of under-earning is higher for water than for electric or gas:** The public M&A component (driven by fair market value legislation discussed in greater detail on page 9) of rate base growth means water companies often carry newly-acquired assets for a time before integrating the assets in rate calculations (leads to regulatory lag). As noted above, the negotiating table for public M&A is likely to become more competitive and investor-owned utilities will often compete for deals with commitments on customer bill increases.

***Barclays says**: Valuations are objectively high, but there is no clear catalyst for compression; scarcity value is likely the main rationale for valuation premium; long-term earnings and rate base growth could moderate somewhat but still outpace electric and gas growth, and visibility clearly leads peers.*

1) Water utilities are still utilities, but valuation premium shows little: We believe any new fundamentals-driven investment in US water utilities requires a long time horizon and the view that the infrastructure replacement cycle will drive EPS growth in excess of most electric utilities. However, there are non-financial factors (e.g. ESG, thematic) attracting capital to the sector. We note AWK's spread to the UTY has been at or near all-time highs since diverging in 2013 (including the current all-time high). We see no imminent catalyst for water valuations to compress to electric utility levels, and thus we utilize a water group average P/E multiple of 27x for our valuation framework.

2) Earnings execution and outlook is strong, but scarcity value is the most compelling justification for the premium: We see scarcity value for publicly traded water equities as a large component of the premium that AWK and other regulated water utilities command. AWK represents ~10% of the S&P Global Water Index and security-specific shareholder composition implies a broader base of investors for both AWK and WTRG than the typical electric utility (both in geography and fund style).

3) Recent execution and industry tailwinds likely mean EPS CAGRs moderate somewhat, but growth backlog and visibility still exceeds electric peers: AWK and WTRG possess unique scale that position both to play leading roles in any water infrastructure replacement programs in the US. The American Society of Civil Engineers estimates that $1tn of total infrastructure spending is needed over the coming 25 years to repair and replace aging infrastructure. The market position dominance is unmatched in the electric utility space (NEE is probably closest with NEER). We also see the scale advantage and reputation for best-in-class management providing greater confidence and visibility into capital deployment and growth. External financing needs likely increase relative to previous years given cash tax positions and we see modest ROE lag between cases as possible, but overall we still believe EPS and rate base growth exceed the average electric utility.

4) ESG is often highlighted as a justification for higher valuations – we agree that the lack of generation allows some funds to own water utilities that cannot own electric and that a strong sustainability narrative exists, however there are material ESG risks inherent to the water utility business model that must be weighed by ESG-focused investors. The ESG pitch for water utilities is that a water utility's core business model is to invest capital in a chronically under-invested US water infrastructure system in order to enhance of an increasingly scarce resource and ensure safe drinking water and more environmentally-responsible wastewater treatment and management. The infrastructure investment embedded in water utility capex plans is based on the need to update pipelines that can be centuries old, improving both water quality (replace lead pipes and lower total effluents) and leakage (water scarcity issues should increase scrutiny on 'treated but not delivered' volumes). We also see a 'social' benefit when classifying customer disposable income as a social benefit, as investor-owned utilities have the unique opportunity to socialize and smooth community and customer financial impacts by utilizing single-tariff ratemaking and longer amortization periods given stronger capital market access. However, for all the positive ESG narratives that water utilities have exposure, there are material ESG risks inherent to doing business as a water utility – including spills, chemical usage, politicized under-investment and customer bill impacts, potential bribery, and workplace safety. The risk exposure to potential ESG disasters make management competency, ethics, Board oversight, and technical expertise critical to any ESG analysis.

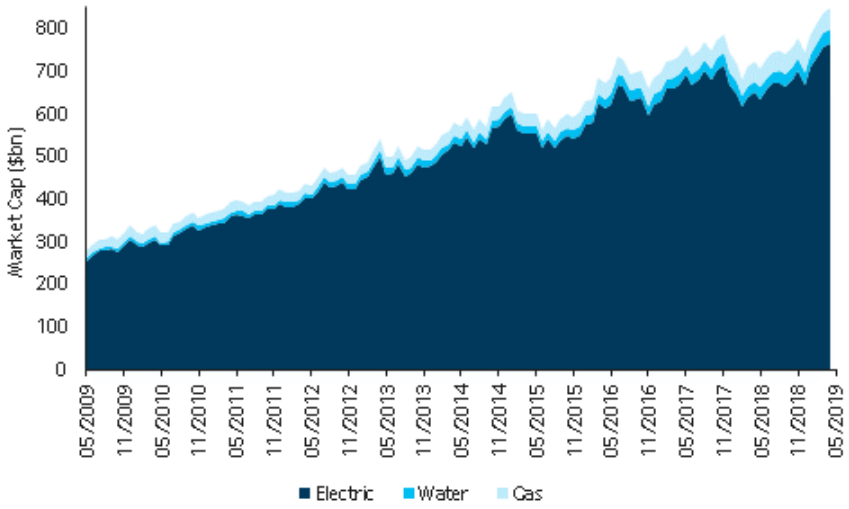
Diving Deeper on Valuation Premium Drivers

Scarcity Value

Scarcity value for water-focused equity securities likely plays a significant role in driving premiums for water utilities when compared to electric utilities with similar growth and regulatory profiles. The market capitalization of each sector directionally illustrates investable supply (Figure 3), but the true float should be adjusted for insider and passive/index stakes.

ETFs (e.g. CGW) tracking the S&P Global Water Index are popular vehicles for investors to gain broad equity exposure to the global water industry. The index, as described by S&P, seeks to provide liquid and tradable exposure to growing global demand for water and ancillary services (infrastructure, equipment, and materials).

FIGURE 3
US Utility Market Cap by Sub-Sector



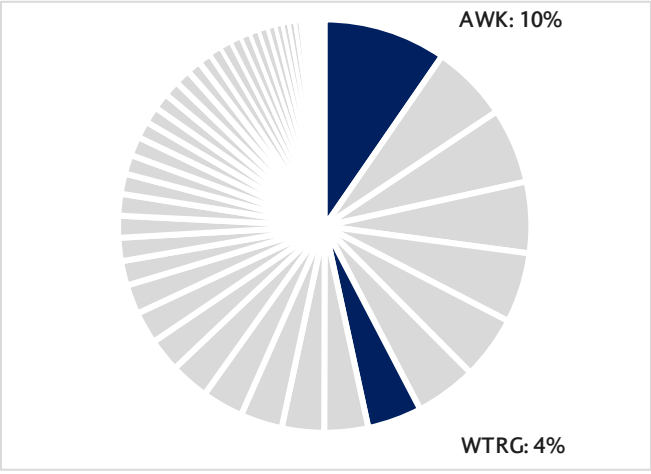
Source: Bloomberg, Barclays Research

FIGURE 4
Top 10 Holding in S&P Global Water Index

Company	Weight (%)
American Water Works Co Inc	10
Xylem Inc/NY	6
Danaher Corp	6
Geberit AG	6
Halma PLC	5
Veolia Environnement SA	5
IDEX Corp	5
Essential Utilities Inc	4
United Utilities Group PLC	3

Source: Bloomberg, Barclays Research

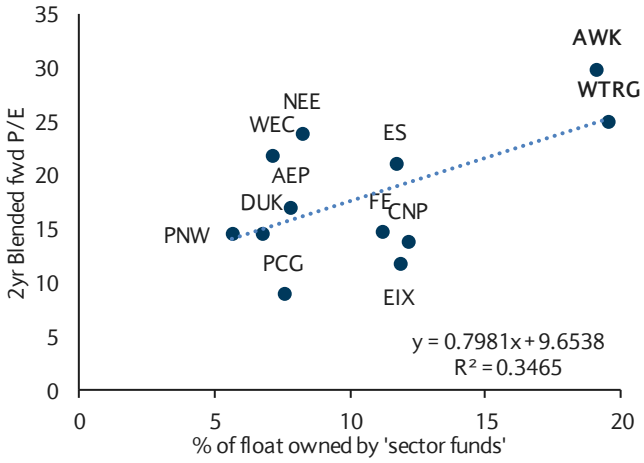
FIGURE 5
S&P Global Water Index



Source: Bloomberg, Barclays Research

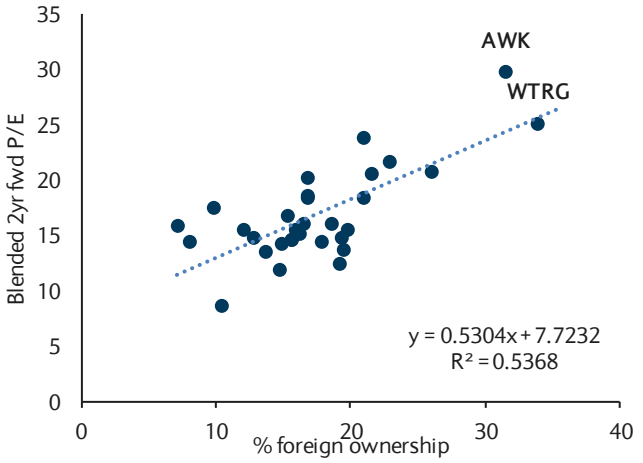
This global index exposure is unique to water utilities when compared to electric and gas utilities who receive passive ownership in US utility benchmark indices (AWK and WTRG are also present in most) and is reflected in AWK and WTRG's sector fund and ETF ownership displayed in figures 6 and 9 below. We also believe this added index exposure is reflected in AWK and WTRG's foreign ownership (ESG also likely plays a role) levels. AWK's recent and projected EPS and rate base growth further qualifies the company for growth fund mandates that help broaden the stocks appeal to industry generalists and help to explain the valuation spread between AWK and WTRG (figure 10).

FIGURE 6
% of shares owned by 'sector funds' vs P/E



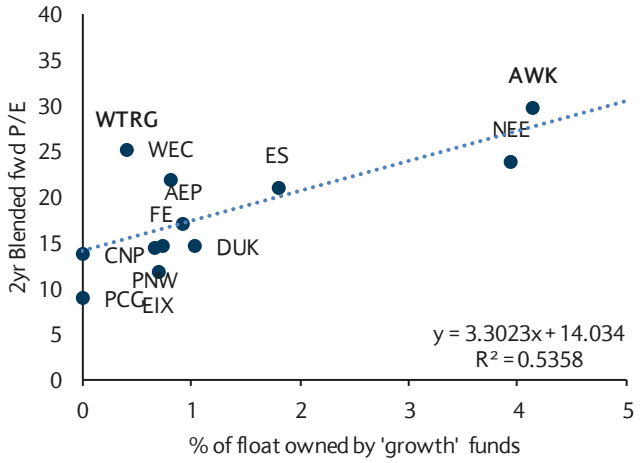
Source: Bloomberg, Barclays Research

FIGURE 7
% of shares owned by investors outside of US vs P/E



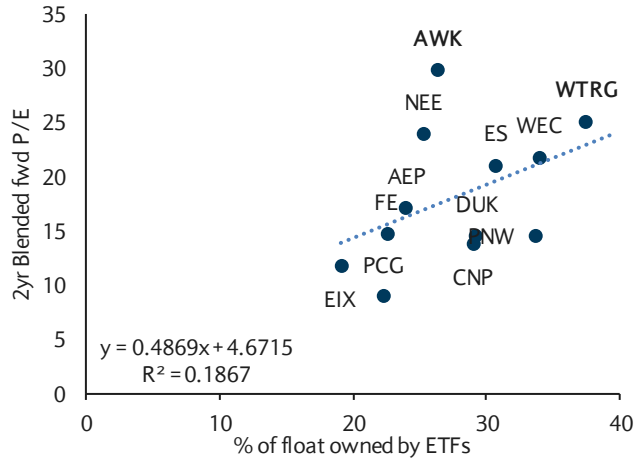
Source: Bloomberg, Barclays Research

FIGURE 8
% of shares owned by 'growth funds' vs P/E



Source: Bloomberg, Barclays Research

FIGURE 9
% of shares owned by ETFs



Source: Bloomberg, Barclays Research

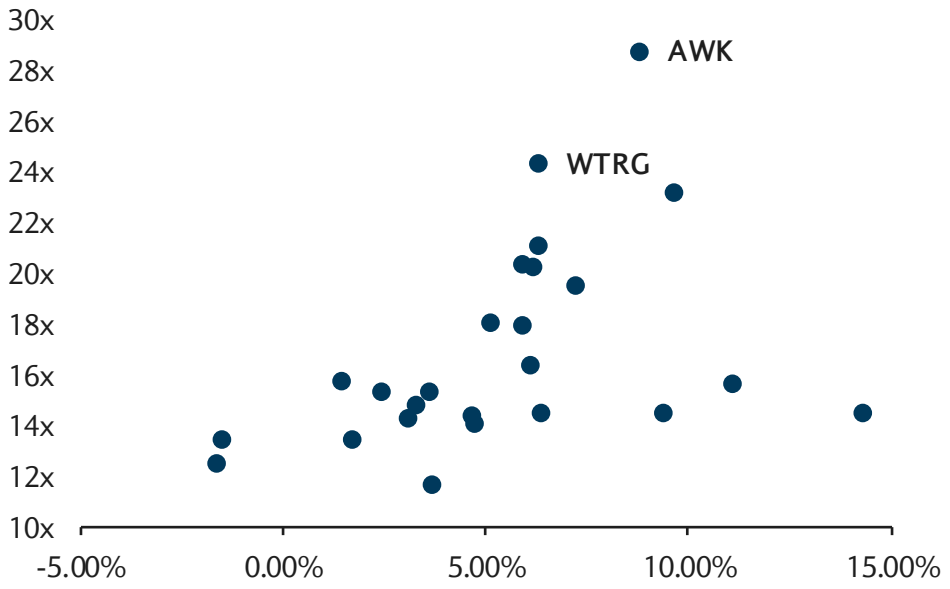
Long-term Growth Outlook

With an average asset age of ~50 years for water and wastewater pipes, the water industry appears to be nearing a generational replacement cycle that should drive capital deployment and rate base growth for the foreseeable future. This opportunity is bolstered by fair market value legislation passed in twelve states (including Virginia as of April 2020 and Texas as of 2019).

There is clearly a strong correlation between realized and expected long-term EPS growth and relative P/E multiples, as investors attempt to ascertain the sustainability of realized growth and CAGR guidance beyond forecast periods and estimate terminal growth assumptions for DCF-based valuation frameworks.

FIGURE 10

EPS CAGR Estimate through 2022 (2018 Base) vs 22E P/E



Source: Barclays Research, Bloomberg

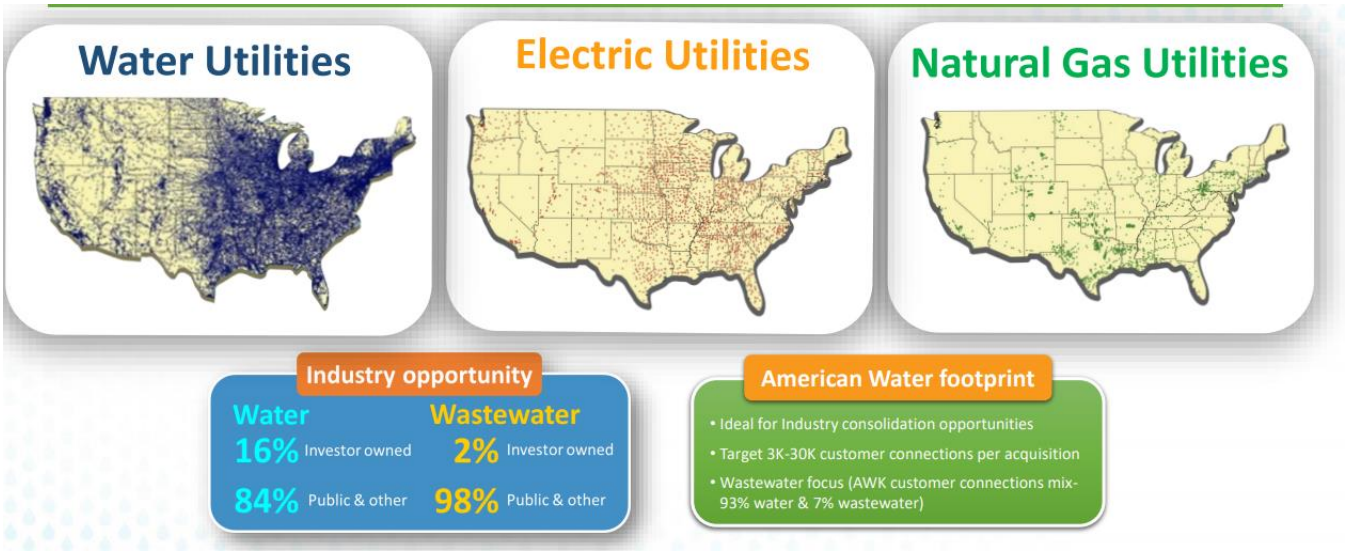
Fair Market Value Laws for Public System Acquisitions

Fair Market Value Legislation (FMVL) allows water utilities to purchase fresh water and wastewater systems from public municipalities and add the total cost of the transaction to rate base, rather than the traditional accounting-based asset cost standards held by many regulatory commissions. The opportunity provides incentive for private industry to financial support to public entities and provides water utilities a streamlined way to grow rate base and often provides outsized ongoing capital deployment opportunities given public systems are often under-invested or face strict environmental regulations that require investment that the public agency does not have financial means to make.

The nation-wide asset replacement narrative is bolstered by water utilities' unique opportunity provided by fair market value legislation, allowing IOUs like AWK and WTRG to participate via public system acquisitions. To date, fair market value legislation has passed in twelve states (including Virginia as of April of this year). The FMVL opportunity is unique to water given the far more fragmented nature of public water and waste water systems in the US when compared to electric or gas. While instances of heavy pushback to private acquisitions of public water distribution systems has been seen in recent years, 98% of US wastewater systems are owned by municipalities or other public entities and generally do not carry the same anxieties associated with freshwater distribution assets, making the public

perception and path to acquisition approval less burdensome. As such, we expect wastewater acquisitions to dominate transaction volume moving forward.

FIGURE 11
Industry Fragmentation



Source: American Water June Investor Presentation

Can FMVL Start to Really Flow?

There are three key recent and ongoing dynamics driving a view that regulated M&A will increase. The first is the significant capital investments required. The second is a reaction to COVID-19 impacts on tax revenues and local government budgets and the need for alternative and external means for municipalities to finance water and wastewater system investment. The third is an outlook for increasing environmental regulation and legislation to address emerging contaminant treatment (primarily PFAS and aging / lead pipelines).

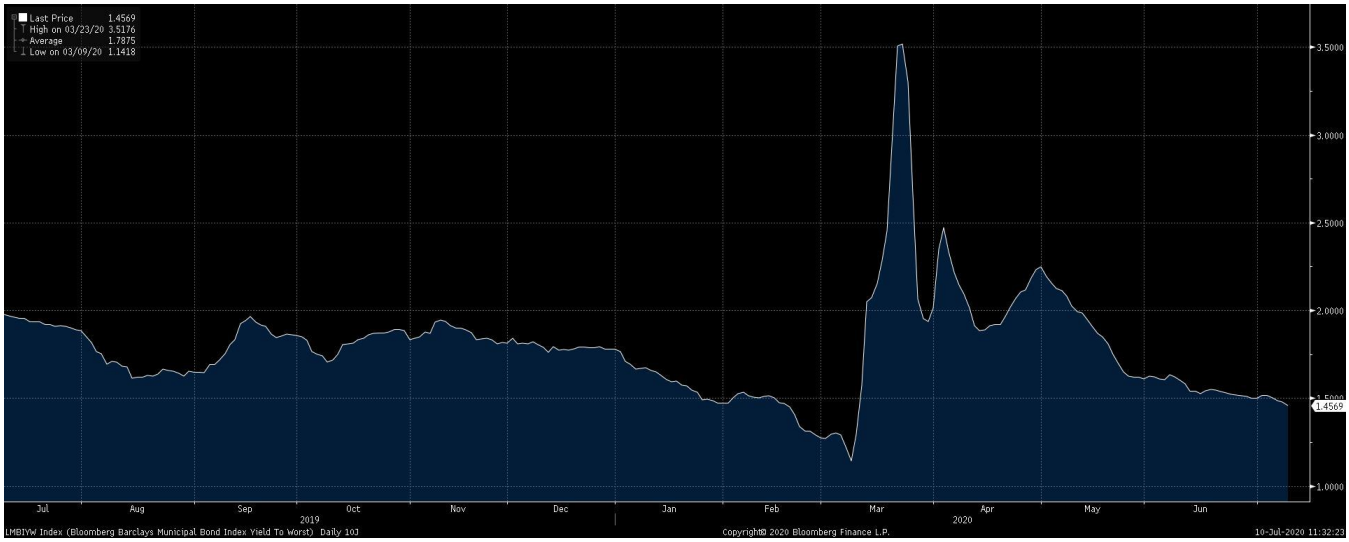
1) **Significant capital investment required**

   A majority of the water and waste-water systems in the US are approaching or beyond their useful lives. This results in increasing annual capital needs, which if not met put reliability, resiliency and public health and safety at risk. The chronic under investment is generally a function of available tax bonding authority combined with pressured municipality budgets.

2) **Municipal financing cost:**

   We view the pressure from COVID-19 related shutdowns on local government finances as a potential driver of increased M&A. Investor-owned utilities can provide capital to execute needed system investments, and public budgets can receive relief in the form of immediate cash inflows (while losing a long-term revenue source). However, all-in financing costs appear to have avoided worst-case scenarios, as evidenced by municipal bond yields as a proxy for total municipal financing costs.

FIGURE 12
Barclays Bloomberg Municipal Bond Index Yield to Worst



Source: Bloomberg

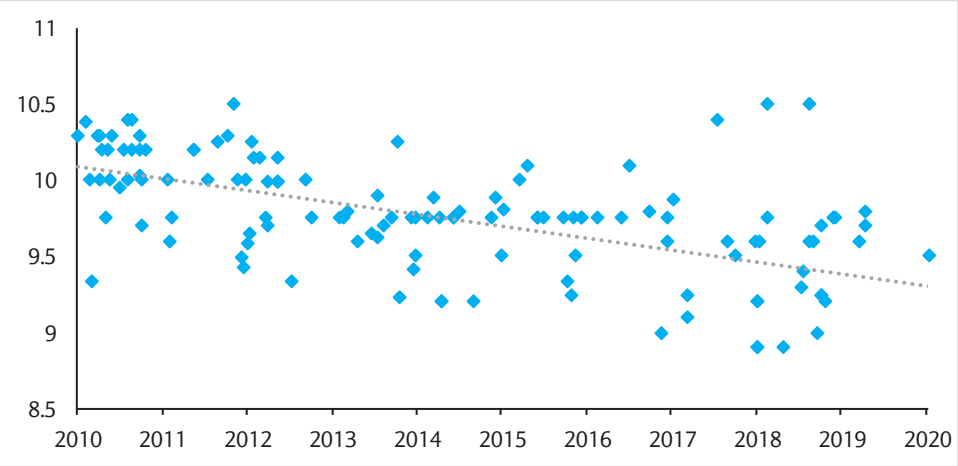
3) Environmental Regulations:

Emerging contaminants like PFAS or 1,4-dioxane have received increased regulatory and legislative attention recently. Numerous new state laws have been introduced over the past few years and national efforts have taken shape to introduce PFAS legislation at a federal level. Emerging contaminants like PFAS are only a health advisory at the EPA, but states have recently chosen to regulate these 'forever chemicals' through state legislatures. Local towns and municipalities with aging infrastructure are already challenged to make investments needed to remain in compliance with many existing environmental regulations and could face further financial pressure given requirements to install water treatment facility upgrades necessary to address new contaminants. Many water companies have already implemented PFAS standards across all systems (~13 parts per trillion seems to be industry standard), but there has been increased pressure from groups like National Association of Water Companies (NAWC) to apply legal requirements to require similar treatment across state and federal jurisdictions.

Trade Off: Added Rate Case Reliance

The nature of the opportunity provides a strong rate base growth avenue; however, it increases water utility reliance on rate cases. It increases susceptibility to ROE lag as larger acquisitions often under-earn until added rate base can be reflected in the revenue requirement recovered in customer bill. This dynamic could be further stretched depending on whether public entities include terms on bill increases as part of the acquisition terms. We assume an average 300bp net lag to authorized for newly-acquired systems, slowly moving back to authorized ROE within three years of the acquisition date after the system is reflected through broader general rate cases. As nationwide ROEs remain under pressure from low interest rates (CAPM), water utilities face more frequent rate cases.

FIGURE 11
Authorized Water ROEs



Source: S&P Market Intelligence, Barclays Research

ESG Analysis

As discussed on page 6, ESG is often viewed as a differentiator for water utilities when compared to their electric and gas counterparts given the lack of generation-related GHG emissions and a perception that operations are safer and more immune to environmental disasters (wildfires, workplace safety, fossil and nuclear waste management). While we agree that water utilities often screen better than electric and gas on scope 1 greenhouse gas emissions and do not directly utilize or transport fossil fuels, they are by no means immune to significant ESG risk exposures from emerging contaminants, wastewater and stormwater chemical use and treatment shortcomings, and potential environmental and safety disasters from spills. This exposure makes management competence and oversight crucial to any ESG-focused investment analysis.

We view the following ESG risks as most critical to discuss with management teams:

- Emerging contaminant standards: Emerging contaminants like PFAS and other effluents are regulated by a rapidly evolving state and federal framework. Top-tier management teams deploy significant research and internal resources to identify risks and play an active role in policy discussions. Best-in-class management teams have scenario planning completed for a variety of regulatory paths and abide by effluent standards that often exceed legally mandated levels to ensure safe drinking water. Utilities should publicly disclose the number of EPA violations related to effluents in annual reporting material.
- Chemical usage and wastewater treatment standards: Wastewater treatment requires heavy chemical usage that can lead to adverse environmental impacts when improperly managed and disposed. Incident histories and internal policies can be supplemented by analyzing EPA violation trends to approximate the relative risk.
- Board oversight: Given the high exposure to potential bribery inherent to any heavily regulated industry and the political nature of public system M&A, the Board should be directly involved in business ethics decisions.
- Energy consumption: Water transportation and treatment is an energy-intensive operation, requiring high levels of electricity usage. Water utilities should disclose total consumption and electricity sources. Analysis of electricity usage and sources can help quantify indirect GHG emission contributions.
- Bill affordability and outlook: We classify customer affordability as a social attribute given the non-discretionary nature of water consumption. With a robust capital outlook, customer affordability and the pace of bill inflation will be critical. The EPA guidelines suggest keeping water bill costs to 2.5% of average family income for residential customers.
- Emergency management plans: Risk of water and chemical spills are inherent to any water utility. We believe strong mitigation systems and quantified risk exposure must be supplemented by a robust and frequently updated environmental response plan to spill events. The plan should be designed to mitigate environmental and social impacts while maintaining safe water services to communities impacted.
- Workplace safety: Workplace safety trends DART rates and OSHA reportable incidents should be analysed to gauge safety program efficacy in recent years.

American Water Works (AWK)

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Company description – American Water Works Co., Inc. provides drinking water, wastewater, and other water-related services in multiple states and Ontario, Canada. The company's primary business involves the ownership of regulated water and wastewater utilities that provide water and wastewater services to residential, commercial, and industrial customers.

American Water Works Company, Inc.

Blocks show how a company is scored by ESG providers (one block is worst, five are best). Icons show the dispersion of those views (no bars indicates only one score provider, two bars indicate dispersion between providers, full bars indicate aligned views). Source: Barclays Research, Sustainalytics, Vigeo Eiris

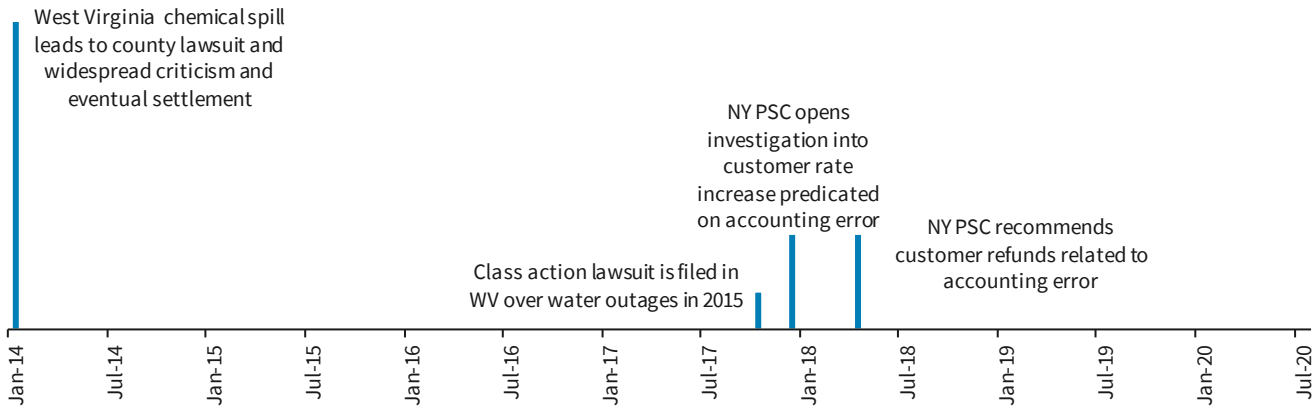
Key conclusions

E AWK receives average environmental ratings, which may be lower than how the average investor thinks about environmental attributes, but accurately reflects negative risk factors balanced by the positive environmental treatment services provided by the company's core operating function, in our view. Said differently, we believe E scores provided by ESG ratings agencies reflect risk factors, rather than the environmental attributes of the business itself. AWK is exposed to environmental risk from effluents that may be insufficiently addressed at AWK's wastewater treatment facilities or leaks and ruptures could lead to environmental disasters when storm water and wastewater contaminate nearby watercourses. American Water has faced minor fines related to improper chemical and hazardous waste, but fewer than industry peers. AWK has experienced no major releases of untreated wastewater or storm water in recent years, while other industry participants have. The risk of large spills of untreated wastewater or storm water remains a material environmental consideration given the impact such releases have on nearby wildlife and water supply.

S AWK's social scores screen as average. We view the social category as inclusive of water waste and water quality. Water scarcity has grown in terms of public knowledge and attention and AWK's (along with the entire water pipeline industry's) lost water amounts could come under increased scrutiny. Lost water can be defined as water that is treated for consumption, but is never delivered to the end use customer due to leakage. This issue is likely to both drive investment capital and risk as average pipe age increases (some pipes are over 100 years old). Our perception is that AWK leads the industry on emerging contaminants, evidenced by environmental policies that often exceed legal requirements and the number of PhD-level specialists and dedicated research labs focused on mitigating potentially harmful particulates not yet regulated directly. However, with growing attention paid to lead levels and other water quality metrics, freshwater delivery quality will remain a risk. Other standard social considerations also apply to American Water, including workplace diversity, community giving, and community relations. Customer bills are a material consideration as water infrastructure ramps up in the United States. AWK highlights average residential bill costs of ~1.9% of average customer family income, versus EPA guidance to keep water bills ~2.5%, however AWK appears to lag WTRG on average customer bill rates.

G American Water's governance scores are above average, which we agree with. As previously noted, our perception is that AWK takes the aggressive and proactive approach necessary to prepare and combat significant safety and environmental risks inherent to the water delivery and treatment business. AWK's Board composition, management compensation structure, and audit quality are consistently ranked among the best in the country. Combined with strong shareholder voting rights and transparent disclosure, we believe governance should be viewed as a differentiator for AWK.

Past and present ESG issues



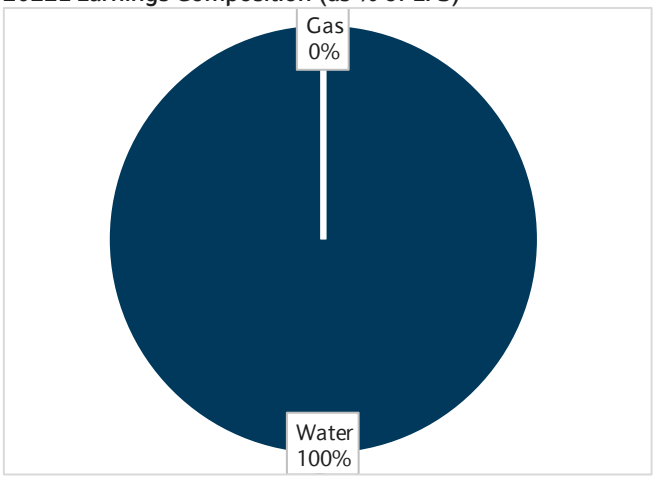
Source: Barclays Research

Risks and management

Category	Risk	Mitigant
E	Wastewater/storm water management	Has effectively avoided major releases of untreated storm and wastewater in prior years.
S	Employee diversity and experience	AWK has workplace diversity working groups and has won numerous inclusion and diversity awards and is recognized in the Bloomberg gender equality index.
S	Health and safety	Has reduced DART rates to 1.13 in 2018 from 2.19 in 2015. Has reduced high-consequence injury rate from 5.26 in 2015 to 3.1 in 2018.
G	Incentive alignment	American Water has published explicit targets tied to ESG performance targets at a board level and has compensation metrics linked to ESG performance.

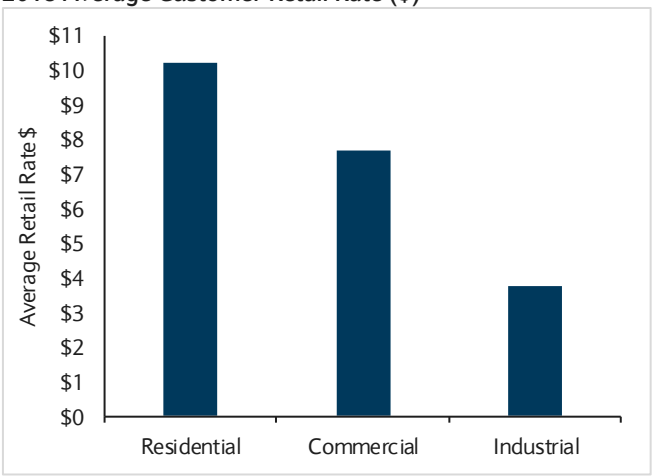
Source: Barclays Research

2022E Earnings Composition (as % of EPS)



Source: Company reports, Barclays Research

2018 Average Customer Retail Rate ($)



Source: Company reports, Barclays Research

Essential Utilities (WTRG)

Equity Research
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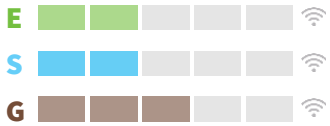
BCI, US

Company description – Essential Utilities, Inc. operates as a water utility company. The company supplies water to residential, commercial, industrial, and public customers. Essential Utilities serves residents through its water and wastewater operations in the Northeastern, Southeastern, and Midwestern United States.

Essential Utilities, Inc.



Blocks show how a company is scored by ESG providers (one block is worst, five are best). Icons show the dispersion of those views (no bars indicates only one score provider, two bars indicate dispersion between providers, full bars indicate aligned views). Source: Barclays Research, Sustainalytics, Vigeo Eiris

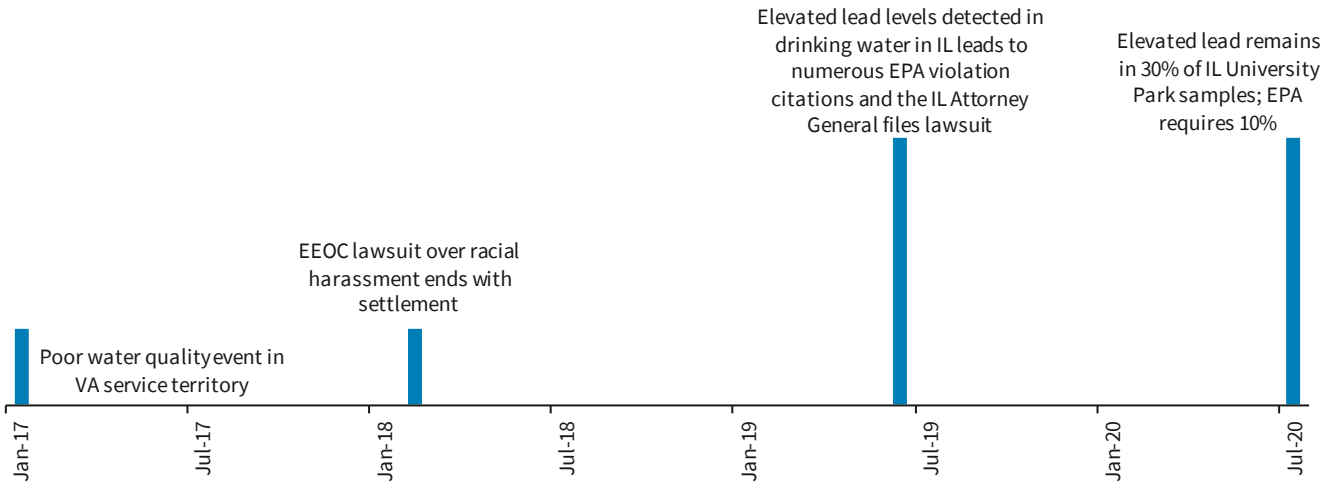
Key conclusions

E Essential receives slightly below average scores for environmental risk factors given below average preparedness and management of potential disasters. We view the ratings as somewhat dated as ratings providers do not contemplate the Peoples natural gas business. WTRG is negatively impacted by a view that the hazardous waste management program lacks management oversight, seemingly from WTRG's lack of EMS certification and emergency response program. While ratings providers take specific issue with the management of environmental risks, we see little evidence that WTRG is lacking relative to other management teams in the water industry. Overall, we view WTRG as equally exposed to environmental risks inherent to the water industry as any other industry participant and applaud WTRG for a robust data disclosure on environmental issues.

S Essential receives below average social ratings due to similar management issues as discussed in the environmental section. We note WTRG has disclosed a fairly robust effluent management system with data supporting its claim that it takes emerging contaminants seriously (citing 95.5% of days in compliance and 272 effluent quality 'events' in 2019). We also highlight that WTRG's average retail rate is lower than the average industry rate on a consolidated average basis across its service territory. DART rates hover around 2.1, slightly higher than industry average. Similar to industry peers, community giving is also prioritized.

G WTRG's Governance ratings are average. Governance risk factors material to WTRG's ratings include a high susceptibility to bribery concerns given the public regulated nature of operations and previous reliance on municipality O&M contracts (though largely divested now). We view the ratings as somewhat stale given the immaterial contribution of municipal O&M contracts. Balancing the downside risks, we note significant management compensation incentives aligned with shareholder and public stakeholder interests. WTRG has explicit long-term and short-term incentives linked to realized ROE, public M&A growth, and O&M inflation management, all of which we view as material to the holistic stakeholder value proposition for a consolidated WTRG.

Past and present ESG issues



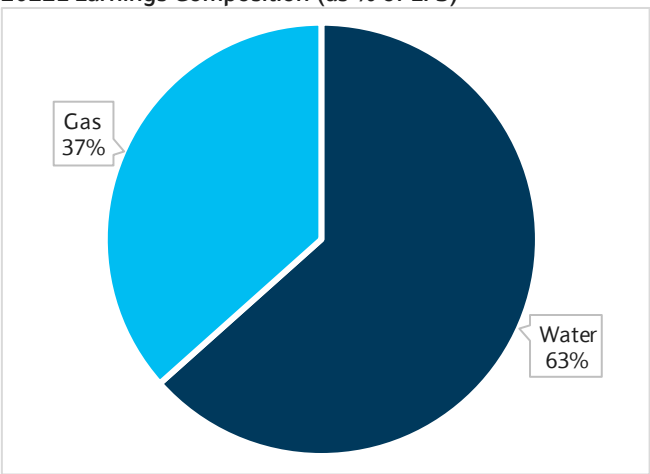
Source: Barclays Research

Risks and management

Category	Risk	Mitigant
E	Wastewater/storm water management	Has effectively avoided major releases of untreated storm and wastewater in prior years.
S	Employee diversity and experience	WTRG has workplace diversity working groups.
S	Health and safety	Has maintained DART rates near 2.1 in 2016-2018. Has reduced lost workdays rate to 102 in 2019 from 568 in 2017.
G	Incentive alignment	We view WTRG's compensation incentives as strongly transparent and well aligned with all stakeholders, with explicit ROE, O&M, public M&A financial targets and strong community involvement and safety targets also embedded.

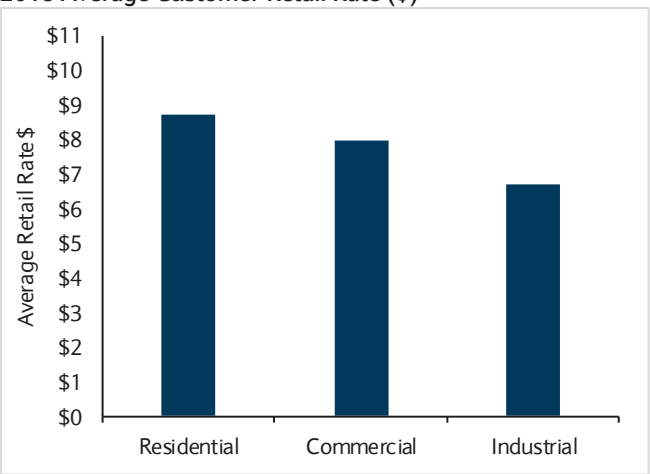
Source: Barclays Research

2022E Earnings Composition (as % of EPS)



Source: Company reports, Barclays Research

2018 Average Customer Retail Rate ($)



Source: Company reports, Barclays Research

Applying Views to Individual Stocks

Barclays Valuation Framework Refresher:

We apply our standard valuation framework used for electric and gas utilities to derive a premium or discount to a group average multiple (in this case we use a water group average multiple of 27x). Our valuation framework takes into account regulatory jurisdiction exposure (capital trackers, ROE trends, other recent commission decisions), geographic trends (population growth, GDP per capita, other general economic activity), long-term growth guidance and visibility, and a qualitative assessment of investor sentiment. The qualitative investor sentiment attribute seeks to encapsulate ESG characteristics and general risk exposures to idiosyncratic issues potentially impacting earnings and providing added earnings variability relative to published financial estimates.

Barclays Water Valuation Framework:

We apply a 15% premium to the group average water multiple for AWK and a 5% premium for WTRG. AWK's premium reflects diversified regulatory and geographic exposure, disproportionate exposure to jurisdictions with DSIC and other constructive capital recovery mechanisms, strong management and competitive position as industry leader, ESG exposure, peer-leading EPS CAGR and multi-decade capex visibility.

WTRG receives a 5% premium to the group average multiple also reflecting disproportionate exposure to strong PA regulatory environment and capital recovery mechanisms, balanced by lower EPS growth, capital guidance visibility and some risk around current M&A deals (namely Delcora). We apply a 15% premium to the 17x utility group average multiple used for all other utility valuation for the regulated gas business (Peoples acquisition) in PA, strong EPS and rate base growth, and our view that constructive regulatory relationships will translate to stable earnings growth in PA.

FIGURE 12

Water Valuation and Price Targets

WTRG PT Methodology	
Regulated Water Business	
22E EPS	$1.24
Group P/E	27.0x
Premium / Discount	5%
Effective 22 P/E	28.4x
PT Contribution	$35
Regulated Gas Business	
22E EPS	$0.72
Group P/E	17.0x
Premium / Discount	15%
Effective 22 P/E	19.6x
PT Contribution	$14
Parent drag	
22E EPS	-$0.15
Blended 22 P/E	25.8x
PT Contribution	-$4
Total Price Target	
Price Target	**$45**
Current Price	$42.90
Price Return	5.8%
Dividend Yield	2.4%
Total Return	**8.2%**

AWK PT Methodology	
Regulated Water Business	
22E EPS	$4.46
Group P/E	27.0x
Premium / Discount	15%
Effective 22 P/E	31.1x
PT Contribution	$138
Regulated Gas Business	
22E EPS	N/A
Group P/E	N/A
Premium / Discount	N/A
Effective 22 P/E	N/A
PT Contribution	N/A
Parent drag	
22E EPS	N/A
Blended 22 P/E	N/A
PT Contribution	N/A
Total Price Target	
Price Target	**$138**
Current Price	$131.00
Price Return	5.7%
Dividend Yield	1.7%
Total Return	**7.4%**

Source: Barclays Research

Upside Scenario:

For our upside scenario we apply the same relative premium / discount framework for WTRG, but we assume all of WTRG earnings receive a consolidated water group multiple and we assume AWK's premium expands to trade at a 25% premium to the water group average multiple.

FIGURE 13
Upside Scenario

WTRG Upside Scenario	
Regulated Water Business	
22E EPS	$1.82
Group P/E	27.0x
Premium / Discount	5%
Effective 22 P/E	28.4x
Contribution	$52
Regulated Gas Business	
22E EPS	$0.00
Group P/E	17.0x
Premium / Discount	15%
Effective 22 P/E	19.6x
Value	$0
Parent drag	
22E EPS	$0.00
Blended 22 P/E	28.4x
Value	$0
Upside Value	
Upside Value	**$52**
Current Price	$43.44
Price Return	18.8%
Dividend Yield	2.3%
Total Return	**21.1%**

AWK Upside Scenario	
Regulated Water Business	
22E EPS	$4.46
Group P/E	27.0x
Premium / Discount	25%
Effective 22 P/E	33.8x
Value	$151
Regulated Gas Business	
22E EPS	N/A
Group P/E	N/A
Premium / Discount	N/A
Effective 22 P/E	N/A
Value	N/A
Parent drag	
22E EPS	N/A
Blended 22 P/E	N/A
Value	N/A
Upside Value	
Upside Value	**$151**
Current Price	$132.92
Price Return	13.2%
Dividend Yield	1.7%
Total Return	**14.9%**

Source: Barclays Research

Downside Scenario:

For our downside scenario, we apply the same relative premium / discount framework for both names, but assume AWK and WTRG trade back to the US utility group average multiple.

FIGURE 14
Downside Scenario

WTRG Downside Scenario	
Regulated Water Business	
22E EPS	$1.25
Group P/E	17.0x
Premium / Discount	5%
Effective 22 P/E	17.9x
Value	$22
Regulated Gas Business	
22E EPS	$0.72
Group P/E	17.0x
Premium / Discount	15%
Effective 22 P/E	19.6x
Value	$14
Parent drag	
22E EPS	-$0.15
Blended 22 P/E	18.5x
Value	-$3
Downside Value	
Downside Value	**$34**
Current Price	$43.44
Price Return	-22.6%
Dividend Yield	2.3%
Total Return	**-20.3%**

AWK Downside Scenario	
Regulated Water Business	
22E EPS	$4.46
Group P/E	17.0x
Premium / Discount	15%
Effective 22 P/E	19.6x
Value	$87
Regulated Gas Business	
22E EPS	N/A
Group P/E	N/A
Premium / Discount	N/A
Effective 22 P/E	N/A
Value	N/A
Parent drag	
22E EPS	N/A
Blended 22 P/E	N/A
Value	N/A
Downside Value	
Downside Value	**$87**
Current Price	$132.92
Price Return	-34.4%
Dividend Yield	1.7%
Total Return	**-32.7%**

Source: Barclays Research

American Water Works (AWK)

Investment Thesis:

AWK provides a peer-leading 7-10% EPS CAGR through 2024 (off of 2018 EPS) driven by regulated investment (5-7% annual contribution to EPS growth), public M&A (likely weighted more toward wastewater; 1-2% annual contribution to EPS growth), and market-based businesses (homeowner services and military services provide 1-2% contribution to annual EPS growth).

We expect AWK to continue to identify accretive capex and public system acquisition opportunities throughout the forecast period, balanced by $500mn of block equity financing weighted toward the middle of the forecast period (we reflect $450mn in 2022 in our model assumptions, but see optionality to delay to 2023), which helps to address increasing parent leverage. Customer bills remain a material consideration as needed investment and public acquisition costs are recovered in rates. O&M efficiency should remain the center of focus for management, and we expect bills to be managed at or below inflation, while also seeking to keep total water bills <2.5% of average family income, per EPA best practices (AWK current avg ~1.9%).

We concede that AWK screens expensive on a P/E basis to any water, electric and gas comps. However, we do not get the impression that earnings expectations are unreasonable, nor do we expect any material unconsidered risk factors to emerge. ESG factors (lack of generation primarily) and scarcity value have led to a sustainable demand premium to electric equities, requiring the use of a water group multiple separate from electric and gas. We apply a 15% premium to the group average multiple (discussed in greater detail in valuation section) to reflect AWK's strong long-term growth visibility, peer-leading EPS CAGR, and constructive regulatory treatment.

Key Regulatory Proceedings:

Pennsylvania: PA represents ~28% of AWK's regulated rate base and benefits from strong capital tracking mechanisms via Distribution System Improvement Charges (DSIC). ROE for the DSIC investment rider is updated via the state's quarterly earnings review. PA's most-recent update held water ROEs at 9.9%. American Water's current Pennsylvania general rate case requests a $92mn rate step up effective January 1, 2021, and a step-up of $46mn in 2022 reflecting a 10.8% ROE (current 10%) and a rate base of $3.98bn in 2021 and $4.29bn in 2022. We assume the 10% ROE currently reflected in rates remains in place and rate increases sufficient to allow PA to earn its allowed returns in 2021 and 2022.

New Jersey: AWK's New Jersey general rate case is seeking an $88mn base rate increase in 2021, reflecting a $3.63bn rate base, 10.5% ROE (current 9.6% authorized), and an assumed 54% equity layer. We note that the $88mn request is incremental to an expected $35mn rate increase contribution from the NJ DSIC mechanism. We assume NJ receives a 9.6% ROE and comparable cap structure, with rate increases adequate to earn implied authorized returns against a $3.6bn rate base as of year-end 2020.

California: CA benefits from forward-looking rate cases with strong precedent of including attrition and capital cost adjustments and a disaggregated cost of capital proceeding reducing general rate case risk (current ROE set at 9.2% with 55.39% equity layer). AWK's current CA rate case requests a $27mn increase effective 1Q21 and a $9.8mn step-up in 2022.

Virginia: AWK's current VA rate case reflects only $196mn of total rate base and requests a $5.6mn rate increase. Interim rates became effective on May 19, 2020, and the case contemplates ~$100mn of infrastructure investments since 2017.

Missouri: AWK's most-recently filed rate case is in Missouri, where the company is requesting a $74mn rate increase to reflect $490mn of investment since the last filing.

Earnings Estimates and Rate Base Model:

FIGURE 15
AWK EPS Model Summary

	2017A	2018A	2019A	2020E	2021E	2022E
Average Shares Outstanding - Diluted	179.0	180.0	181.0	181.3	181.8	183.5
Earnings per Share	**$2.38**	**$3.15**	**$3.43**	**$3.86**	**$4.22**	**$4.60**
Guidance CAGR Implied EPS - Midpoint		*$3.30*	*$3.58*	*$3.88*	*$4.22*	*$4.57*
Guidance CAGR Implied EPS - Low		*$3.30*	*$3.53*	*$3.78*	*$4.04*	*$4.33*
Guidance CAGR Implied EPS - High		*$3.30*	*$3.63*	*$3.99*	*$4.39*	*$4.83*
Regulated Utility EPS	**$3.12**	**$3.34**	**$3.61**	**$3.92**	**$4.20**	**$4.46**
% of total AWK EPS	*94%*	*96%*	*93%*	*91%*	*90%*	*89%*
Market-Based EPS	**$0.21**	**$0.16**	**$0.25**	**$0.39**	**$0.45**	**$0.53**
% of total AWK EPS	*6%*	*4%*	*7%*	*9%*	*10%*	*11%*
Parent EPS	**($0.99)**	**($0.38)**	**($0.51)**	**($0.44)**	**($0.43)**	**($0.38)**
Dividend per share	$1.62	$1.78	$1.96	$2.15	$2.34	$2.55
Payout - target 50-60%	*68%*	*57%*	*57%*	*56%*	*56%*	*56%*
Growth Yoy - target top end of 7-10%		*9.9%*	*10.1%*	*9.7%*	*9.0%*	*9.0%*

Source: Barclays Research, Company presentations

FIGURE 16
Rate Base Summary

Rate Base ($mn)	2020E	2021E	2022E
Total American Water			
Starting Year Rate Base	13,700	14,731	15,625
Capex	1,600	1,500	1,700
Capex Guidance (8.2bn 20-24)	*1,600*	*1,500*	*1,600*
DD&A	569	607	649
Ending Year Rate Base	14,731	15,625	16,676
7-8% Guidance CAGR Implied	*14,445*	*15,529*	*16,693*
Growth YoY (%)	*7.5%*	*6.1%*	*6.7%*
Average Rate Base	**14,216**	**15,178**	**16,150**
Equity Layer (%)	52.65%	52.65%	52.65%
Authorized ROE (%)	9.77%	9.77%	9.77%
Implied Net Income	731	781	831
Below the line items / adjustments	(21)	(17)	(13)
Modeled Net Income	710	763	818

Source: Barclays Research

Risks:

Upside

AWK will likely outperform if M&A opportunities outpace current expectations and EPS grows faster than expected. AWK will also likely outperform if ESG flows increase, general demand for utility equities increase and disproportionately benefit water utilities, O&M reductions are above expectations, or ROE trends benefit earnings.

Downside

AWK will likely underperform if interest rates remain low or decline and impact authorized ROEs, volumes decline materially as a result of COVID-19, heightened M&A activity and competitiveness result in increased ROE lag, FFO metrics deteriorate and require increased equity financing contributions, or operational and environmental accidents impact ESG scores and flows.

Essential Utilities (WTRG)

Investment Thesis:

Essential Utilities closed its transformative acquisition of Peoples Gas in March 2020. The transaction is likely to be accretive to earnings and long-term rate base growth, but it took WTRG from a pure-play water utility to a combined water and natural gas LDC company. The impact from an ESG perspective will be fully reflected over time, but we believe the earnings and growth accretion from the deal helps to put WTRG on a financial trajectory more competitive with industry leaders like AWK. The deal provides gas rate base growth of 8-10%, versus 6-7% water rate base growth through the same forecast period. We view the backlog of necessary gas system investment as providing a strong runway of capital eligible for recovery under the DSIC mechanism, and we highlight the updated pipe replacement programs that provide visibility into 15+ years of investment opportunity and assumes ~200 miles of pipe per year is sustained.

Near-term focus for the investment community is on repairs tax implications to earnings and the closing of the Delcora water system acquisition. While repairs tax election (discussed below) is already helping to support financials in 2020, the remaining catch-up portion remains a key point of debate. We see repairs tax as less likely to provide material upside to estimates, but moreso as a useful tool to upcoming rate case negotiations in PA that should allow WTRG to earn its allowed ROE moving forward while limiting customer bill impacts from otherwise necessary rate increases.

Key Regulatory Proceedings:

Repairs tax and PA rate case outlook: - Repairs tax allows immediate expensing of capex deployed for infrastructure repairs for tax purposes, providing significant tax savings relative to tax rates assumed in ratemaking. The repairs tax situation has two components that contribute to the expected earnings outlook for WTRG. The initial component of repairs tax election is already flowing through financials and is expected to provide $0.08-$0.12 of EPS help for FY20. The second component is the 'catch up' component of repairs tax election – or how much income tax saving is passed through to customers versus retained for shareholders. The prior commission precedent allocated shareholders seven of the ten total years of amortization benefits from the tax savings to shareholders. We view that prior decision as a very constructive outcome. While we do not assume the same treatment in the current round, we again view the repair tax situation as a helpful tool that WTRG possesses for purposes of negotiation in the context of its PA rate case plans (likely to allows for rate case stay outs and other customer commitments rather than purely incremental to growth guidance and assumptions).

DELCORA: - WTRG signed with the Delaware County Regional Water Control Authority (DELCORA) to purchase its wastewater system serving 42 municipalities and ~500k customers for $277mn. DELCORA has line of sight to ~$700mn capex through 2028; however, increasing environmental requirements with the Philadelphia Water Department (one of DELCORA's wastewater offtake and treatment facilities) imply potential investment requirements of >$1bn will be needed ahead of contract renewal in 2028. The investment would require significant customer bill increases and heavy financing strain on the public authority.

WTRG's purchase agreement effectively takes the $277mn of transaction proceeds and allocates it to a customer bill trust that would mitigate customer bill impacts following system investment. As part of WTRG's solution, the wastewater would be directed away from the Philadelphia Water Department facility to one of its own treatment facilities, avoiding worst-case environmental-related capex requirements and providing WTRG opportunities to

acquire other fragmented local wastewater systems that currently send wastewater through the DELCORA system.

The process has become heavily politicized, as some Delaware County representatives seek to block the transaction and restructure the customer bill trust established in the binding sale agreement. The county officials have intervened in the PUC approval process and have filed a lawsuit alleging the transaction is not permitted under current legal provisions. We expect the transaction to remain 'noisy' given the politicized nature, but ultimately we expect the deal to go through without significant changes. We note delays and ultimate approval are not material to financial estimates throughout the forecast period.

Earnings Estimates and Rate Base Model:

FIGURE 17
WRTG: Water Rate Base Summary

Water Summary	2020E	2021E	2022E
Capex ($mn)			
Pennsylvania	376	393	410
Ohio	38	39	41
Illinois	39	41	43
Texas	33	34	36
New Jersey	22	23	24
North Carolina	25	26	27
Indiana	9	10	10
Virginia	9	9	9
Total Regulated Capex	**550**	**575**	**600**
Year End Rate Base ($mn)			
Pennsylvania	3,691	3,962	4,243
Ohio	370	397	425
Illinois	385	413	442
Texas	321	345	369
New Jersey	215	231	247
North Carolina	247	265	284
Indiana	90	97	104
Virginia	84	90	97
Total Year End Water Rate Base	**5,402**	**5,800**	**6,211**
Implied Earnings (($mn)			
Rate Base Implied Net Income	277	293	309
Net Income from Acquisitions	1	8	16
Implied Total Regulated Water Net Income	**278**	**301**	**326**
Modeled Regulated Net Income	*286*	*302*	*328*

Source: Barclays Research

FIGURE 18
WRTG: Gas Rate Base Summary

Gas Summary	2020E	2021E	2022E
Capex ($mn)			
Pennsylvania	376	380	374
West Virginia	20	16	16
Kentucky	4	4	4
Total Regulated Capex	**400**	**400**	**394**
Year End Rate Base ($mn)			
Pennsylvania	2,405	2,666	2,906
West Virginia	131	139	146
Kentucky	28	30	32
Total Year End Gas Rate Base	**2,565**	**2,834**	**3,083**
Implied Earnings (($mn)			
Rate Base Implied Net Income	152	170	186
Modeled Regulated Net Income	*142*	*166*	*188*

Source: Barclays Research

Risks:

Upside

WTRG would likely outperform if repairs tax accretion exceeds expectations and results in incremental growth relative to guidance, currently contemplated M&A is approved in an expedited timeframe, or new M&A deals are announced and provide greater-than-anticipated accretion to growth. WTRG could also outperform if ESG flows increase, general demand for utility equities increases and disproportionately benefits water utilities, O&M reductions are above expectations, or ROE trends benefit earnings.

Downside

WTRG would likely underperform if Peoples integration faces operational challenges, volumes decline materially as a result of COVID-19 or mild weather in gas service territories, rate case outcomes negatively impact earnings, M&A deals face increased scrutiny and legal challenges, deal competitiveness results in increased ROE lag, FFO metrics deteriorate and require increased equity financing contributions, or operational and environmental accidents impact ESG scores and flows.

North America Power & Utilities — **Industry View: POSITIVE**

American Water Works Company, Inc. (AWK)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	3,610	3,817	4,041	4,303	6.0%
EBITDA (adj)	2,032	2,222	2,373	2,532	7.6%
EBIT (adj)	1,450	1,598	1,708	1,822	7.9%
Pre-tax income (adj)	833	937	1,027	1,131	10.7%
Net income (adj)	621	700	766	844	10.8%
EPS (adj) ($)	3.77	3.86	4.22	4.60	6.9%
Diluted shares (mn)	181	181	182	184	0.5%
DPS ($)	1.96	2.15	2.34	2.55	9.2%

Margin and return data					Average
EBITDA (adj) margin (%)	56.3	58.2	58.7	58.8	58.0
EBIT (adj) margin (%)	40.2	41.9	42.3	42.3	41.7
Pre-tax (adj) margin (%)	23.1	24.6	25.4	26.3	24.8
Net (adj) margin (%)	17.2	18.3	19.0	19.6	18.5
ROIC (%)	9.3	10.0	10.1	10.2	9.9
ROA (%)	2.9	3.1	3.3	3.5	3.2
ROE (%)	10.6	11.4	11.8	12.2	11.5

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	23,941	25,741	27,496	29,426	7.1%
Cash and equivalents	60	34	33	46	-8.4%
Total assets	22,682	23,265	24,355	25,588	4.1%
Short and long-term debt	9,453	9,552	9,971	10,091	2.2%
Other long-term liabilities	0	0	0	0	N/A
Total liabilities	7,917	8,339	8,322	8,599	2.8%
Shareholders' equity	6,121	6,496	6,907	7,733	8.1%
Net debt/(funds)	9,393	9,518	9,938	10,045	2.3%
Change in working capital	504	-592	-1	13	-70.3%
Cash flow from operations	1,383	1,434	1,691	1,841	10.0%
Capital expenditure	-1,654	-1,650	-1,555	-1,755	N/A
Free cash flow	-859	-756	-490	-558	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	35.3	34.4	31.5	28.9	32.5
EV/EBITDA (adj) (x)	28.4	26.1	24.6	23.2	25.6
EV/EBIT (adj) (x)	39.8	36.2	34.2	32.2	35.6
FCF yield (%)	-1.5	-1.3	-0.8	-0.9	-1.1
P/BV (x)	3.9	3.7	3.5	3.2	3.6
Dividend yield (%)	1.5	1.6	1.8	1.9	1.7
Net debt/EBITDA (adj) (x)	4.6	4.3	4.2	4.0	4.3

Selected operating metrics					Average
Payout ratio (%)	57.1	55.7	55.6	55.5	56.0
Interest cover (x)	3.8	4.2	4.5	4.9	4.3
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (13-Jul-2020)	**USD 132.97**
Price Target	**USD 138.00**

Why Equal Weight? AWK presents a strong growth profile with top-tier management and a solid execution track record, however valuation is stretched relative to electric and gas utilties and our valuation framework implies a 15% premium to the water group average P/E multiple, all of which is fully reflected in the current stock price

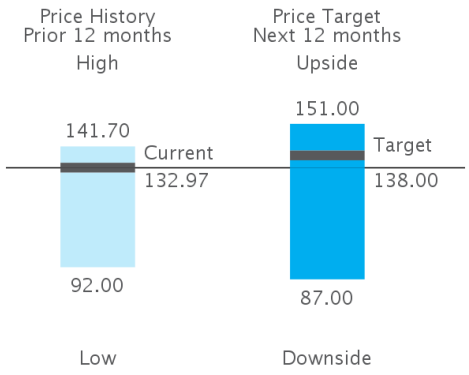
Upside case **USD 151.00**

Our upside case assumes AWK trades at a 25% premium to the group average water utility P/E multiple. We believe this scenario could materialize if ESG flows increase or general utility equity demand rises and disproportionately benefits AWK.

Downside case **USD 87.00**

Our downside case values AWK on the same 15% premium, but applies the group utitlity multiple in lieu of the water group multiple. This could materialize if investors perceive long-term growth opportunities and ESG profiles to be similar to electric and gas.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Essential Utilities, Inc. (WTRG)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	890	1,880	2,081	2,312	37.5%
EBITDA (adj)	517	911	995	1,100	28.6%
EBIT (adj)	361	634	690	767	28.6%
Pre-tax income (adj)	261	436	493	551	28.3%
Net income (adj)	263	398	433	476	21.9%
EPS (adj) ($)	1.47	1.56	1.67	1.82	7.4%
Diluted shares (mn)	179	255	260	262	13.5%
DPS ($)	0.91	0.96	1.02	1.08	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	58.1	48.5	47.8	47.6	50.5
EBIT (adj) margin (%)	40.6	33.7	33.2	33.2	35.2
Pre-tax (adj) margin (%)	29.4	23.2	23.7	23.8	25.0
Net (adj) margin (%)	29.6	21.2	20.8	20.6	23.0
ROIC (%)	3.7	7.3	7.4	7.7	6.5
ROA (%)	N/A	3.1	3.2	3.3	3.2
ROE (%)	N/A	8.6	9.1	9.1	8.9

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	10,795	11,745	12,720	13,720	8.3%
Cash and equivalents	32	31	55	0	-100.0%
Total assets	12,929	13,601	14,295	14,907	4.9%
Short and long-term debt	5,225	3,950	4,075	4,572	-4.4%
Other long-term liabilities	766	2,531	2,561	2,423	46.8%
Total liabilities	8,315	8,844	9,058	9,492	4.5%
Shareholders' equity	4,613	4,765	5,236	5,429	5.6%
Net debt/(funds)	5,193	3,919	4,020	4,572	-4.2%
Change in working capital	N/A	0	-1	24	N/A
Cash flow from operations	0	713	798	884	N/A
Capital expenditure	0	-950	-975	-1,000	N/A
Free cash flow	0	-514	-753	-456	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	29.5	27.8	26.0	23.8	26.8
EV/EBITDA (adj) (x)	46.3	28.4	26.3	24.4	31.3
EV/EBIT (adj) (x)	66.2	40.8	38.0	35.0	45.0
FCF yield (%)	0.0	-2.0	-2.9	-1.7	-1.6
P/BV (x)	N/A	N/A	N/A	N/A	N/A
Dividend yield (%)	2.1	2.2	2.4	2.5	2.3
Net debt/EBITDA (adj) (x)	10.0	4.3	4.0	4.2	5.6

Selected operating metrics					Average
Payout ratio (%)	61.9	61.8	61.4	59.5	61.1
Interest cover (x)	3.0	4.6	5.2	5.3	4.5
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (13-Jul-2020)	**USD 43.37**
Price Target	**USD 45.00**

Why Equal Weight? We believe the recent Peoples acquisition is constructive given its accretion to growth and EPS, however we value WTRG on a sum of the parts basis and apply the utility group average P/E multiple, reflecting gas utility peers. The current share price reflects our valuation conclusion.

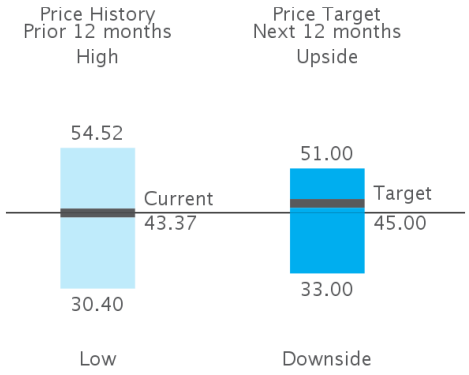
Upside case — **USD 51.00**

Our upside case assumes WTRG is valued using consolidated EPS against a water group P/E multiple. We believe this case could materialize if scarcity value persists and WTRG is deemed a pure-play water utility, despite the gas contribution to earnings.

Downside case — **USD 33.00**

Our downside case values WTRG consolidated EPS on the utility group average P/E multiple, while maintaining a 15% premium for the gas business and a 5% premium for water. We think this could materialize if ESG flows lessen or long-term growth appears unsustainable long term.

Upside/Downside scenarios



Valuation Methodology and Risks

North America Power & Utilities
American Water Works Company, Inc. (AWK)
Valuation Methodology: We utilize a group average water P/E multiple for 2022 earnings and apply a 15% premium to AWK's consolidated 2022 EPS estimate. The premium reflects strong management, constructive regulatory exposure, and top-tier growth visibility.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to AWK include rate case outcomes, public system M&A deals and integration, external financing needs, and general interest rate environments.
Essential Utilities, Inc. (WTRG)
Valuation Methodology: We value WTRG's water business using a 5% premium to the group average water multiple. The 5% premium reflects strong regulatory exposure and public M&A opportunities, balanced by growth visibility lower than peers. We value the regulated gas business at a 15% premium to reflect a strong growth profile and familiar regulatory exposure.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to WTRG include rate case outcomes and general regulatory treatment, gas price inflation impacts on customer bills, and general interest rate environments.

Source: Barclays Research.

ANALYST(S) CERTIFICATION(S):

I, Eric Beaumont, CFA, hereby certify (1) that the views expressed in this research report accurately reflect my personal views about any or all of the subject securities or issuers referred to in this research report and (2) no part of my compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this research report.

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Primary Stocks (Ticker, Date, Price)

American Water Works Company, Inc. (AWK, 13-Jul-2020, USD 132.97), Equal Weight/Positive, CE/J

Essential Utilities, Inc. (WTRG, 13-Jul-2020, USD 43.37), Equal Weight/Positive, A/CD/CE/D/E/J/K/L/M

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In addition to the stock rating, we provide industry views which rate the outlook for the industry coverage universe as Positive, Neutral or Negative (see definitions below). A rating system using terms such as buy, hold and sell is not the equivalent of our rating system. Investors should carefully read the entire research report including the definitions of all ratings and not infer its contents from ratings alone.

Stock Rating

Overweight - The stock is expected to outperform the unweighted expected total return of the industry coverage universe over a 12-month investment horizon.

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Positive - industry coverage universe fundamentals/valuations are improving.

Neutral - industry coverage universe fundamentals/valuations are steady, neither improving nor deteriorating.

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Below is the list of companies that constitute the "industry coverage universe":

North America Power & Utilities

Alliant Energy Corporation (LNT)	Ameren Corp. (AEE)	American Electric Power Company, Inc. (AEP)
American Water Works Company, Inc. (AWK)	Brookfield Infrastructure Partners LP (BIP)	Brookfield Infrastructure Partners LP (BIP_u.TO)
CenterPoint Energy, Inc. (CNP)	CMS Energy Corporation (CMS)	Consolidated Edison, Inc. (ED)
Dominion Energy (D)	DTE Energy (DTE)	Duke Energy Corporation (DUK)
Edison International (EIX)	Essential Utilities, Inc. (WTRG)	Eversource Energy (ES)
Exelon Corporation (EXC)	FirstEnergy Corp. (FE)	NextEra Energy, Inc. (NEE)
NiSource, Inc. (NI)	NorthWestern Corporation (NWE)	OGE Energy Corp. (OGE)
PG&E Corporation (PCG)	Pinnacle West Capital Corporation (PNW)	PNM Resources, Inc. (PNM)

IMPORTANT DISCLOSURES CONTINUED

Portland General Electric Company (POR)	Public Service Enterprise Group (PEG)	Sempra Energy (SRE)
The Southern Company (SO)	WEC Energy Group, Inc. (WEC)	Xcel Energy Inc. (XEL)

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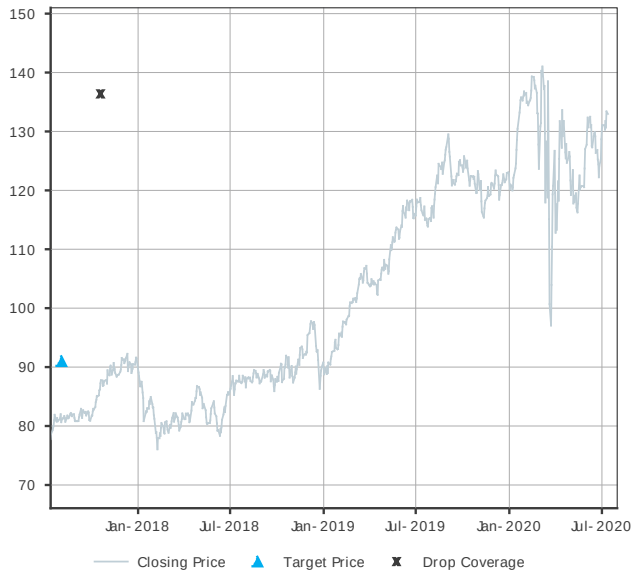
IMPORTANT DISCLOSURES CONTINUED

American Water Works Company, Inc. (AWK / AWK)

	Stock Rating	Industry View
USD 132.97 (13-Jul-2020)	**EQUAL WEIGHT**	**POSITIVE**

Rating and Price Target Chart - USD (as of 13-Jul-2020) **Currency=USD**



Publication Date	Closing Price	Rating	Adjusted Price Target
13-Oct-2017	85.02	Coverage Dropped	
03-Aug-2017	80.65		91.00

Source: Bloomberg, Barclays Research

Historical stock prices and price targets may have been adjusted for stock splits and dividends.

Source: IDC, Barclays Research

Link to Barclays Live for interactive charting

CE: Barclays Bank PLC and/or an affiliate is a market-maker in equity securities issued by American Water Works Company, Inc..

J: Barclays Bank PLC and/or an affiliate is a liquidity provider and/or trades regularly in the securities by American Water Works Company, Inc. and/or in any related derivatives.

Valuation Methodology: We utilize a group average water P/E multiple for 2022 earnings and apply a 15% premium to AWK's consolidated 2022 EPS estimate. The premium reflects strong management, constructive regulatory exposure, and top-tier growth visibility.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to AWK include rate case outcomes, public system M&A deals and integration, external financing needs, and general interest rate environments.

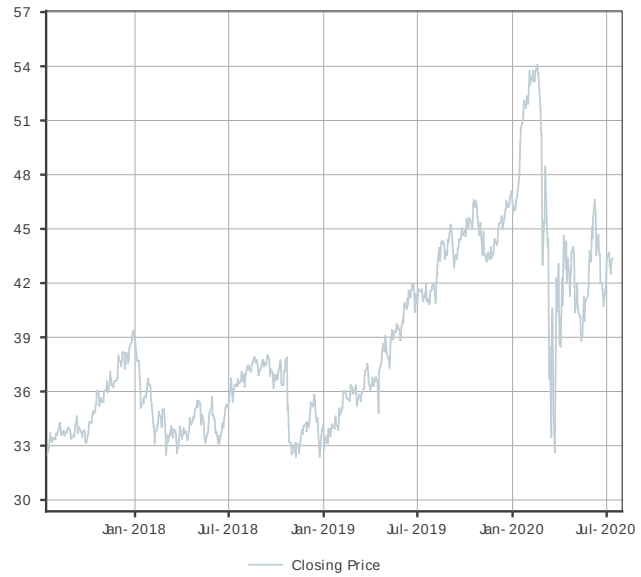
IMPORTANT DISCLOSURES CONTINUED

Essential Utilities, Inc. (WTRG / WTRG)

USD 43.37 (13-Jul-2020)

Stock Rating	Industry View
EQUAL WEIGHT	**POSITIVE**

Rating and Price Target Chart - USD (as of 13-Jul-2020) **Currency=USD**



Publication Date	Closing Price	Rating	Adjusted Price Target

Source: Bloomberg, Barclays Research

Historical stock prices and price targets may have been adjusted for stock splits and dividends.

Source: IDC, Barclays Research

Link to Barclays Live for interactive charting

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Valuation Methodology: We value WTRG's water business using a 5% premium to the group average water multiple. The 5% premium reflects strong regulatory exposure and public M&A opportunities, balanced by growth visibility lower than peers. We value the regulated gas business at a 15% premium to reflect a strong growth profile and familiar regulatory exposure.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to WTRG include rate case outcomes and general regulatory treatment, gas price inflation impacts on customer bills, and general interest rate environments.

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North American Utilities & IPPs

The ESG Antidote: Why Water is a Win/Win

Industry Overview

Takeaways from our 2nd Annual Water on Wall Street

Late last week, we hosted our Second Annual Water on Wall Street conference with ARTNA, AWK, AWR, CWT, ES, MSEX, SJW, WTRG, as well as a number of state regulators, industry experts and water equipment makers. There were a variety of panels throughout both days with updates from company management teams and a wide range of perspectives on the latest trends and the state of the water industry. We left our latest conference increasingly bullish on the water sector, seeing elevated EPS and DPS growth well into the future along with ESG tailwinds that seem unlikely to abate. We prefer WTRG- with its similarly elevated EPS growth to AWK – and very much intact view of EPS despite tax nuance; mgmt. could very well extend out growth targets over time as water & gas normalized (expect 'normal' 3-yr view in Jan still). Bottom line, this remains our 'go to' in the space- even *after* its recent recovery trade. Finally, while the loss of California decoupling provides varying degrees of exposure across the sector, we perceive protracted implementation enables appeal process & mitigating processes to work their way into planning. We see continued positive bias for water utilities alongside renewable energy investments earning renewable returns as among the more desirable opportunities for investors seeking compounding, sustainable earnings and div growth while desiring clean attributes. See parallel AWK upgrade to Neutral today here.

LT visibility to elevated growth & ESG tailwinds

We came away particularly impressed by the elevated EPS and dividend trajectories for the sector, and see visibility to long term organic rate base and accelerating acquisition prospects as municipal budget deficits and FMV legislation drive further privatization efforts (appears '20 acceleration already). With ~44% of all of the water pipe across the US currently classified as poor (up from ~10% in 1980), we see no shortage of investment opportunities and discussions highlighted that about a trillion dollars in spend is currently needed to bring all of the systems up to date. Meanwhile, relative to more carbon-heavy electric and gas peers, we think water remains the clear cut way to play ESG themes as a utility investor. That said, the water sector has materially underperformed relative to other ESG friendly US renewable names (vs. FSLR, BE, RUN, NOVA, and ENPH; see table one in the full note for latest stock performance). Aside from the unfavorable decoupling decision by the CPUC likely to increase rate base contention and drive earnings volatility for companies exposed to the state (a small part of AWK's consolidated biz) , discussions around regulatory treatment for the sector were generally constructive and we don't see particular discrete concerns looking forward. Bottom line, we see increasing merit to premiums for the water sector well above electric and gas peers – due to both sustainable earnings growth justifying P/E-to-G ratios & comps across Clean & YieldCo spaces. If anything else, expanded est of elevated multiples in adjacent clean spaces (well above that of Water & AWK) – justifies valuations, in our view. We believe the water sector *overall* could perform relatively well – and could still eek out a further bid vs electric peers.

14 December 2020

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North America
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Timestamp: 14 December 2020 05:19PM EST

Why are we so constructive on water utilities *now?*

We bullet out the key factors in our mind below but stress for those investors who have only looked at just AWK and WTRG, the entire sector is full of consistent EPS and DPS growth (even if lumpy at times due to discrete rate cases). The outsized growth of the two largest peers in the space understates the consistent trend of growth across the wider sector. We include historical table below; bottom line, while this trend is exceptional relative to the ~5% growth achieved in utilities, the elevated P/E multiple that is 60% higher on average could be explained by its relative P/E-to-G multiple at a minimum (an *increasingly* employed metric given growth co's involved), but ever more supported by emerging high multiple clean alternatives across sector.

Our growing confidence in long-term compounding prospects alongside what is an increasingly supported multiple offer our improved confidence against what is otherwise an admittedly elevated peer group multiple. While it is difficult to have a more positive view on AWK given its 30x+ P/E on '23 EPS, we perceive WTRG as a key opportunity given its compounding re-rating and what should prove meaningfully less contentious EPS growth trajectory. While we acknowledge dilutive effect of its gas LDC acquisition, we stress its ability to drive a consistent 3-year EPS CAGR (irrespective of what happens on repairs tax true-up) and growing ability to articulate a longer term growth outlook (perhaps in future updates beyond Jan '21 release of latest guidance). As integration is fully reflected, we see a normalized outlook without adjustments and clean baseline for growth. On balance, this remains our favorite name in the Water sector at just 25x '23 P/E.

COVID just the latest push for industry consolidation

The latest conference highlighted the incredibly fragmented nature of the water industry, with over 50K community water systems & 15K wastewater systems relative to ~3200 electric and ~1000 gas LDCs (Local Distribution Company). This remains particularly glaring given 16% of water systems are Investor owned (with an even more notable ~2% investor owned for wastewater) and with 92% of systems serving less than 10K customers. Even prior to COVID, the industry was ripe for consolidation against a backdrop of favorable legislation and higher compliance burdens around emerging contaminants. Twelve states have now adopted FMV legislation with both Consolidated Tariff and Water Quality Legislation also continuing to gain momentum. The EPA has currently established health advisory levels for PFA at 70 parts per trillion, but we perceive a broader mandate for the industry as on the horizon amid some discrete state-level requirements already. That said, the latest pressures put on munis from the ongoing pandemic are just another factor in the perfect storm to accelerate the consolidation trend. Meanwhile, a further environmental push under a Biden administration could provide additional capital opportunities as compliance costs with PFAs (per- and polyfluoroalkyl substances) and water quality concerns have already started contributing to the push away from muni owned water systems

Contemplating the Setup for the Sector

We left our Second Annual Water on Wall Street Conference increasingly constructive on prospects for the sector for the foreseeable future. We see visibility well into the future for earnings trajectory given both organic opportunities and the clear cut industry consolidation trends that we expect to continue to accelerate amid the lingering pandemic.

Meanwhile, we stress the water utility sector as the clear cut way for utility investors to play the ESG theme over the coming years given their lack of carbon exposure vs. both electric and gas utility peers. Despite this, the sector has materially underperformed other ESG friendly US renewable names (vs. FSLR, BE, RUN, NOVA, and ENPH). The exhibit below reflects water utilities stock performance on a one week, one month, three month, and YTD vs. US solar plays, with the sector materially underperforming despite a much better proven track record.

Table 1: Stock Performance: Water Utilities Materially Underperforming US Renewables by a good bit…

Water Utilities	Ticker	One Week	One Month	Three Month	YTD
American Water	AWK	-1.4%	-8.1%	3.3%	20.7%
Essential Utilities	WTRG	0.7%	6.4%	20.8%	1.4%
American States Water	AWR	3.7%	-0.1%	6.4%	-11.0%
SJW Group	SJW	3.7%	4.8%	15.4%	-2.4%
Artesian Water	ARTNA	2.2%	0.8%	15.0%	5.8%
Middlesex Water Company	MSEX	6.1%	5.0%	15.6%	17.3%
California Water Services	CWT	4.9%	-0.2%	21.0%	1.4%
York Water	YORW	5.9%	6.8%	13.5%	7.0%
US Renewables	Ticker	One Week	One Month	Three Month	YTD
First Solar Inc	FSLR	-2.7%	8.0%	18.5%	54.3%
SunPower Corp	SPWR	2.1%	13.2%	95.1%	321.0%
Bloom Energy	BE	-10.7%	36.7%	70.6%	230.4%
SunRun	RUN	-0.6%	5.2%	-4.5%	322.0%
Sunnova Energy	NOVA	1.5%	20.4%	48.8%	252.2%
Enphase	ENPH	8.2%	20.0%	93.9%	435.4%

Source: BofA Global Research, Bloomberg

But just how fast has the sector actually grown?

Consistently better than Utility alternatives: we provide comments provided by companies across the sector on both historical and prospective growth commitments. Bottom line, we see nearly uniform high single digits ratebase growth across the sector (rather than AWK being the unusually elevated company). We perceive ratebase growth as still in the midst of execution – rather than reaching the 'end' of its reinvestment cycle. We perceive few specific regulatory consternations – with in fact many pointing to the need for more consolidation to enable greater scale. If anything what remains critical to the industry is ensuring cost efficiencies to offset otherwise bill inflation. This remains critical as FMV acquisitions drive shifts in tariffs across customers as well.

Table 2: Contrasting commitments on EPS, DPS, and Ratebase across sector: mixed disclosures – but trajectory is clear

Companies	EPS (CAGR)	DPS (CAGR)	Rate Base
American Water Works (AWK)	2020-2024 expected 7-10%	2020-2024 projected high end of 7-10%	NA
American States Water (AWR – Not Rated)	2009-2019: 10.7%	2010-2020: 9.4%, guiding 7% going forward	Planned capex going forward remains at 3.5-4x depreciation
Aquarion – Eversource (ES)	NA	NA	2017-2024 expected 8% rate base CAGR
Artesian Resources (ARTNA – Not Rated)	NA	Expected 3%	NA
California Water Service Group (CWT – Not Rated)	NA	NA	2008-2019: 9.7%
Essential Utilities (WTRG)	Expected 5-7% through 2022	NA	NA
Middlesex Water (MSEX - Not Rated)	NA	NA	Capex forecast of $295Mn in 2020 through 2022
SJW Group (SJW – Not Rated)	5% LT	Committed to a dividend payout ratio of 50-60%	2016-2021 projected: 13%

Source: BofA Global Research estimates & Bloomberg; industry presentations & commentary from conference for uncovered companies

We also include the existing historical EPS growth rates across the sector to provide a bit more perspective across the peers- admittedly AWK stands out clearly vs. peers on its ability to consistently execute and explains its notable premium. If anything, we perceive re-acceleration of growth underway across peers beyond just AWK's consistency.

Table 3: EPS Growth over Time Across the Water Industry: entire sector's performance is well in excess of trends elsewhere

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Average EPS Growth - over decade	EPS CAGR - over decade	EPS Growth 2019-2020E	EPS CAGR - 5YR - 2015-2020E
AWK	22%	18%	17%	4%	10%	9%	8%	7%	9%	9%	8%	9%	7%	11%	11%	8%	8%
WTRG	17%	4%	40%	10%	3%	5%	5%	4%	3%	4%	6%	6%	9%	10%	9%	6%	4%
SJW	60%	-28%	27%	-5%	121%	-25%	39%	11%	-12%	-29%	16%	16%	7%	16%	8%	16%	2%
ARTNA	3%	-17%	36%	-17%	14%	18%	12%	7%	2%	4%	11%	4%	na	6%	5%	11%	7%
CTWS	-5%	14%	19%	8%	16%	6%	2%	2%	-35%	na	na	na	na	3%	na	na	na
MSEX	33%	-13%	7%	14%	10%	8%	13%	0%	42%	3%	6%	4%	3%	12%	11%	6%	12%
CWT	-7%	-6%	37%	-13%	17%	-21%	7%	39%	-3%	-4%	28%	1%	7%	5%	3%	28%	12%
Avg	18%	-4%	26%	0%	27%	0%	12%	10%	1%	-2%	13%	7%	7%	9%	6%	13%	3%

Source: BofA Global Research, Bloomberg; consensus applied for uncovered names (we only cover AWK and WTRG)

Contemplating the Regulatory & Legislative Backdrop

Aside from the unfavorable decoupling decision by the CPUC likely to increase rate base contention and drive earnings volatility for companies exposed to the state, discussions around regulatory treatment for the sector were generally constructive. We perceive continued support in surcharges like the DSIC (Distribution System Improvement Charge) to drive critical investment spend longer term and see commissions as continuing to engage with companies around COVID challenges and navigating through as the pandemic continues to linger. As we await a broader mandate around PFAs and water quality, regulatory support across states will remain critical to watch: We don't expect it to be too controversial. Meanwhile, we perceive legislation such as Fair Market Value legislation, Single Tariffs, and the Water Quality Accountability Act will all continue to gain momentum, setting up opportunities for further consolidation.

Company Highlights

We include our latest company takeaways below:

Essential Utilities (WTRG)

Latest discussions with WTRG management stressed confidence around execution of their strategy with the company successfully navigating the pandemic while integrating their Peoples Gas acquisition. Despite COVID, the company previously noted expectations to be at the top end of the 2020 range and affirmation of their 5-7% EPS growth through '22. The company is poised to roll forward their guidance on January 11th, and we perceive more announcements to come on the acquisition front. Recall the company has elected to use Repairs Tax accounting treatment and has effectively implemented the last several months – with guidance of $0.08-$0.12 benefit annually. We await developments around the regulatory process of the catch up component after the earlier filing, with resolution expected early in April of 2021. Rather than drive incremental upside to their 5-7% EPS CAGR, the filing seeks to extend the growth without a need for a rate case. As opposed to going in for new rates in 2023 to take effect in 2024, a constructive outcome from the catch up filing would benefit '23, with incremental benefits in '24, and '25 to help drive earned returns for the segment in outer years without any rate relief until 2026: the repairs tax debate boils down to Peoples Gas ROE lag in '23 likely to a modest degree. On balance we are comfortable in mgmt's ability to manage lag around its ROEs at core water utilities including PA into a potential water filing next year.

With FMV legislation now in all eight water & wastewater states in WTRG's footprint following the passage in Virginia earlier this year, the company continues to execute on tuck in acquisitions and discussions continue to highlight a robust pipeline of opportunities. Management remains confident on the DELCORA process, with a regulatory approval expected in mid-March. This would put the company on track to

potentially close the transaction in April or May after the 30 day appeal window. Meanwhile, a decision is expected from a judge within 60 days after the recent hearing regarding the litigation around the trust. Recall the company has until August to pull on the ~$300Mn equity forward to be used for DELCORA and other acquisitions.

We reiterate our Buy rating, seeing upside risk in the event of better than expected execution on their long-term growth rate.

American Water Works (AWK)

Ahead of their upcoming 2021 guidance and outlook roll forward, AWK management continued to highlight confidence across their business and around their ability to execute on their strategy through both the lingering pandemic and the longer term. Despite the ongoing impact of COVID, latest disclosures with their 3Q update brought the midpoint of full year 2020 guidance back to the original 2020 guidance on an adjusted basis – and we see the company as poised to extend expectations another year: We don't perceive a pivot from the strategy with management seemingly committed to their growth triangle and the largely regulated portfolio. As such, we expect continued guide towards 7-10% EPS growth through 2025 with their full year results.

As the largest publicly traded water utility with a regulated footprint across 14 states, AWK is poised to benefit from enabling legislation and the continuing acceleration in consolidation across the industry. FMV legislation has been enacted in ten of their states including the top 7 (which make up 88 % of their biz by revenue).

95% of their acquisitions over the last five years have been in states that have enacted the legislation. Meanwhile, the company now enjoys consolidated tariffs in 12 states and water accountability legislation in three. We see the latest pressures from both COVID and water quality standards as likely to further accelerate the trends. After our event, the company announced the latest completed tuck in acquisition of Four Lakes Water Distribution System in Illinois American Water's Chicago Metro Area ($900K and 1300 households). With a line of sight to $20-$22Bn of investment over the ten year period, we see no slowdown in opportunities even through the longer term, particularly given the consolidation backdrop. The earlier decision to de-lever the balance sheet should further provide additional flexibility to pursue acquisitions.

We upgrade AWK shares to Neutral following the latest constructive conference and a more fairly balanced risk/reward. Click here for the parallel upgrade.

Aquarion – Eversource (ES)

We hosted meetings with Aquarion Water, ES' regulated water utility subsidiary that comprises 5% of the company's rate base. The company is one of the ten largest privately-owned water utilities in the US and the largest investor-owned water utility in NE serving ~214K customers in NH, MA, and CT. Following the sale to ES, Aquarion's rate base is expected to grow nearly 3x faster than before the acquisition to a rate base of ~1.3Bn in 2024, reflecting an 8% rate base CAGR off the 2017 base. We perceive opportunities beyond this as the industry continues to consolidate from the 50,000+ water systems that are in the US today. Since 2011, Aquarion has closed 24 transactions, with two small acquisitions currently before regulators – and discussions stressed the constructive regulatory backdrop to further promote muni deals. We see the M&A focus going forward on larger opportunities over a thousand connections in both water & wastewater. Maintain our Neutral rating on ES given balanced risk/reward.

American States Water (AWR – Not Rated)

American States Water Company (AWR) is a consolidated low volatility water company that operates through 3 subsidiaries: 1) Golden State Water Company (GSWC), Bear Valley Electric Service, Inc. (BVESI), and 3) American States Utility Services (ASUS). The company recently spun out BVESI to insulate it from the rest of the company, but stressed the higher elevation (7000ft) and stronger build to whether ice and snow required above 3000ft – stressing the differences in risk relative to some other parts of

California. The regulated water and electric utility serves 261,000 and 24,000 customers across California, respectively, while ASUS is a contracted service for water/wastewater systems that serves military bases under 50-year contracts, largely competing with AWK.

The EPS breakdown is comprised 72% from GSWC, 7% from BVESI, and 21% from ASUS with the company growing earnings at a ten year CAGR of 10.7% through 2019. Going forward, the company is guiding to dividend growth of 7%, stressing potential room to grow from the company's earnings prospects: planned capex going forward remains at 3.5-4x depreciation. Given the rate case filing in July, the company doesn't expect to lose decoupling until 2025 (after the commission subsequently opted to eliminate it on August 27th) and view the language in the decision as supporting Golden State Water's position that it does not apply to its general rate case application filed earlier this summer (which will set new rates for '22-24). The company may still have the ability to use the Monterey-style WRAM for partial price adjustment protection.

Artesian Resources (ARTNA – Not Rated)

ARTNA is a $400Mn market cap water utility headquartered in Newark, DE providing water services in parts of Delaware, Maryland, and PA. The company services more than 118K metered customers and supplies over 8.3Bn gallons of water per year through more than 1,331 miles of water mains. Through public-private partnerships, the company provides a variety of water and wastewater-related services to several municipalities with latest discussions suggesting the primarily resi based business as not materially impacted by COVID. The company continues to focus on organic growth on the Delmarva Peninsula and growth has been around 1-2% across their footprint in addition to several recent acquisitions. The company alluded to 3% dividend growth.

California Water Service Group (CWT – Not Rated)

We hosted meetings with management of CWT – the second largest ($2.5Bn market cap) pure play water company in the US. The latest 2018 California GRC adopted on Dec 3rd allows 3-year CapEx of $828m, adopting a $1.5bn rate base in 2020, with the company growing investment at a ten year CAGR of 9.7% through 2019. As they appeal the recent CPUC decision to eliminate decoupling in California, discussions stressed any overturn as unlikely before the next GRC and they expect the shift to make rate cases more contentious and drive rate design changes, potentially reducing conservation incentives and increasing volatility. COVID has increased the number of delinquencies with 60,000 customers behind on payments - raising the company's bad debt reserve to $2.7Mn (albeit the state has provided an emergency memo account for COVID related expenses). Overall, the capital program remains robust and running 3x depreciation, while acquisition opportunities remain strong with five more acquisitions in progress after closing the Rainier View deal in June.

Middlesex Water (MSEX - Not Rated)

We hosted meetings with MSEX, a $1.3Bn regulated water utility with operations in NJ and DE. Discussions emphasized robust investment opportunities, with a capex forecast of $295Mn in 2020 through 2022, including a $70Mn CJO plant upgrade in New Jersey anticipated to complete in mid-2021. MSEX is subject to a Distribution System Improvement Charge (DSIC) in both its NJ and DE jurisdictions which allows accelerated recovery of certain pre-approved investments subject to a cap. While favorable legislation such as FMV is helping drive consolidation across the industry, MSEX doesn't currently enjoy such legislation in their states at this point in time. Nonetheless, discussions still suggested muni opportunities materializing with the Water Quality Act in NJ and as more and more munis look to get help from IOUS. The company has not articulated a formal EPS target.

SJW Group (SJW – Not Rated)

We hosted meetings with SJW, the second-largest pure-play water/wastewater utility by rate base in the US. Discussions emphasized the company's growth strategy including Capex, constructive regulatory relations, and acquisitions. After the earlier transformative M&A, the footprint now includes San Jose Water (regulated utility in California), Conneticut Water, Maine Water, SJWTX (regulated utility in TX), and SJW Land Company (unregulated biz in California). The company is committed to a dividend payout ratio of 50-60% and seeks to grow earnings around 5% longer term – and stressed additional capital opportunities above plan including further municipal acquisitions. The company estimated over $230m of Capex in 2021, implying 5 year CAGR of 13% through 2021. Despite the latest decoupling setbacks for the water industry in the state of California with the CPUC's decision to eliminate it, SJW didn't employ the mechanism and instead remains well protected with the Monterey-style WRAM in place. After earlier issues with guidance, the company noted that guidance will be released after the rain season going forward in order to more accurately reflect any water costs.

The Tech Angle: AQUA, BMI, Ionic Water & XYL

We held meetings with AQUA, BMI, Ionic Water, and XYL for perspective and latest updates from technology providers.

Ionic: Start-up company by same developer of EOS stationary batteries. Focused on PFOA solution with regenerative (reusable) activated carbon solution. See potentially material cost reductions to cost of water purification along with substantial reductions in use of activated carbon (presently consumed in large quantities).

AQUA: Evoqua is a $2.8Bn market cap company that provides water treatment equipment and services through two segments, Integrated Solutions and Services and 2) Applied Product Technologies. Discussions stressed that COVID had led to rapid growth in outsourced water, creating short term revenue challenges but paving a way for long term success as projects take 12-24 months until they are fully operational. Looking forward, their base case guidance into 2021 is flat to slightly up sales and adjusted EBITDA y/y as the pandemic continues to linger.

BMI: Badger Meter is a $2.6Bn market cap company that manufactures and markets flow measurement and control products focused on smart meters in the water sector. Latest discussions stressed that after a very challenging second quarter, business bottomed in April and organic growth has started to resume. While the company doesn't provide formal guidance, they expect 5% growth on the utility business longer term on higher average selling prices, and expect software as a service to grow to 10% of their biz. Only ~60% of the US market currently has some form of AMR/AMI (automated meter reading / advanced metering infrastructure), and while likely slow to adopt, this provides a long runway of potential growth along with upgrades from AMR to AMI. Meanwhile, with 80% of their utility biz in the US, discussions noted potential for international tailwinds through the strategic cycle. While small, their recent acquisition of S:CAN has an installed base in 50 countries to help further accelerate their international push.

XYL: Xylem Inc is an $18Bn market cap designer, manufacturer, equipment, and service provider for water and wastewater applications addressing the full-cycle of water from collection, distribution, and use to the return of water to the environment. By geography, the bulk of revenue is generated in the US (45%) while Western Europe, Emerging Markets, and the rest of the world comprise 26%, 21%, and 8%, respectively, while end markets are broken down by utilities at 50%, industrial at 35%, commercial at 10%, and resi at 5%. Discussions stressed the company as well positioned to grow faster than the market the next several years and a likely pickup in growth in 2H as we start to recover from the pandemic – with signed contracts building up given the delay in work.

Table 4: Stocks mentioned

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
AWK	AWK US	American Water	US$ 148.55	B-2-7
WTRG	WTRG US	Essential Utilities	US$ 47.07	B-1-7
ES	ES US	Eversource Energy	US$ 85.46	B-2-7

Source: BofA Global Research

Price objective basis & risk

American Water Works (AWK)

Our PO for American Water Works is $155. We apply the sector average 27.8x to American Water's 2023E earnings based on the water peer multiple and a 8.1% group EPS CAGR for '18-'23E. We think this multiple is justified as in our view AWK largely drives the peer multiple as the largest publicly traded water utility. We ascribe a 3x premium for NJ, PA, and IL, and a -3x discount to the non-regulated Retail biz. Also a -1x P/E for Cali utility. no prem/discount for 'Other' segment with smaller state exposures.

Risks to the downside are increase in market interest rates, potential impact of tax reform on utilities, operational errors, changes in valuation levels for water utilities. Risks to the upside are accelerating muni acquisitions, multiple expansion, and constructive legislation in regulatory jurisdictions.

Essential Utilities (WTRG)

Our price objective is $51 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. These peer multiples are 25.5x and 13.9x. We apply a 3.0x premium to Peoples Gas given the organic growth opportunities, while applying a variety of premiums to its water (2x previously) subsidiaries: +4x to PA, +3x to IL, +2x to OH, +2x for TX, +2x for OH, and no premium for balance of biz. We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Eversource Energy (ES)

Our sum of the parts based price objective of $93 uses P/E multiples on 2023E earnings. For electric utilities, we attribute a 4x premium NSTAR, and 3x premium to PSNH and CL&P to peer 16.6x multiple, reflecting future potential positive revisions to capex and earnings. For gas, we apply a 3x premium to the peer 15.0x multiple, given capex upside particularly in MA and a 2x for Columbia Gas. Both electric and gas peer P/E multiples are grossed up by 5% to reflect capital appreciation across the sector. We value Aquarion at a 1x premium to the 26.5x water multiple. We reflect ES's 50% ownership in Revolution and South Fork offshore wind sites on an NPV basis. We further reflect a devco value with an assumption of an additional 3GW through 2031. We take out 50% of parent debt, and 50% of interest to accurately reflect parent leverage.

Upside risks to our price objective are additional capex announcements on the T&D side, as well as success in offshore wind RFPs.

Downside risks are reduction in authorized ROEs, inability to meet earned ROE expectations, as well as failure to receive permitting on incremental capex opportunities

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also

certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AES	AES	AES US	Julien Dumoulin-Smith
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Enphase Energy	ENPH	ENPH US	Aric Li
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
NEUTRAL				
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	TransAlta Renewables Inc.	YRNW	RNW CN	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith

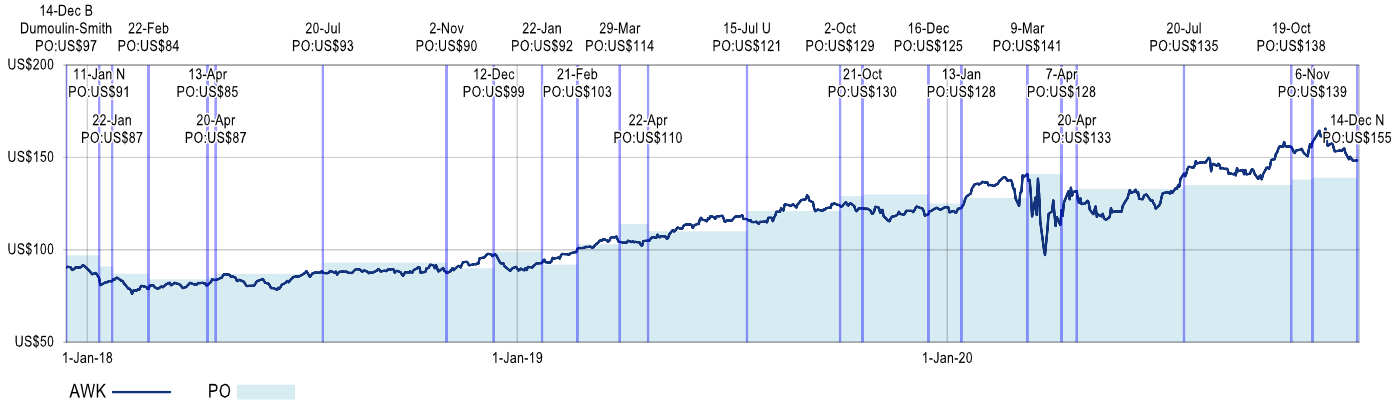
North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	Southwest Gas Holdings	SWX	SWX US	Richard Ciciarelli, CFA
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	Atlantica Sustainable Infrastructure	AY	AY US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith

Disclosures

Important Disclosures

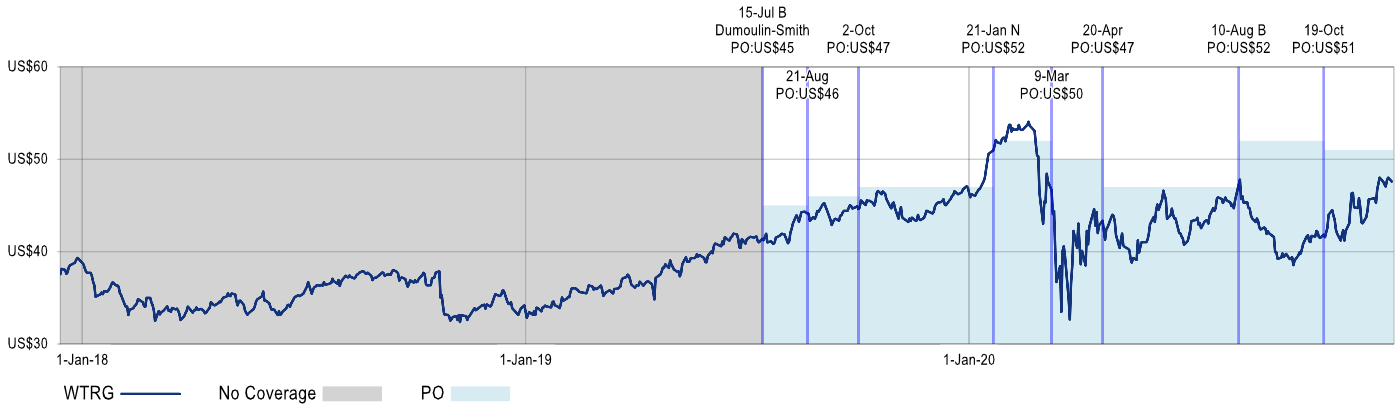
American Water (AWK) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Essential Utilities (WTRG) Price Chart



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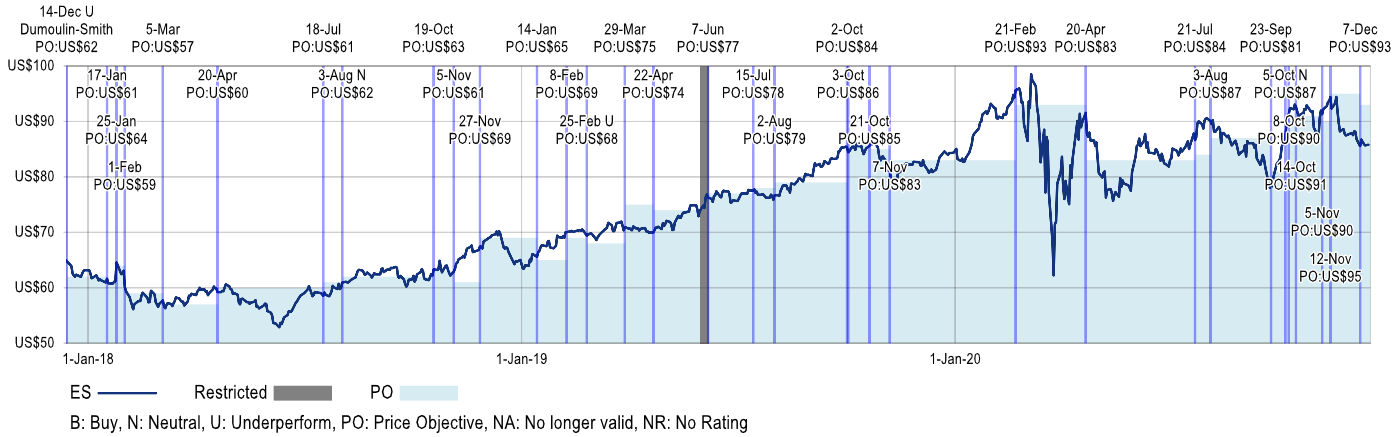
Eversource Energy (ES) Price Chart



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Equity Investment Rating Distribution: Utilities Group (as of 30 Sep 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	79	51.63%	Buy	59	74.68%
Hold	36	23.53%	Hold	24	66.67%
Sell	38	24.84%	Sell	25	65.79%

Equity Investment Rating Distribution: Global Group (as of 30 Sep 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1749	54.79%	Buy	1114	63.69%
Hold	677	21.21%	Hold	415	61.30%
Sell	766	24.00%	Sell	386	50.39%

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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Essential Utilities

We Are Confident on the Near & 3-Yr View

Reiterate Rating: BUY | PO: 54.00 USD | Price: 48.18 USD

Latest Guide Intact Indeed – But Only Rolls to 3-yr view

On Monday morning, WTRG management provided 2021 EPS expectations of $1.64-1.69 - with the midpoint a touch above our prior estimate of $1.65 and prior consensus of $1.66 – while rolling forward their 5-7% EPS CAGR through 2023 (vs. '22 earlier). While the three year look is admittedly less than other utility peers, we expect a consistent roll forward of the outlook beyond '23 as well despite all the noise around tax credits and rate case timing. We perceive few meaningful impediments for shares despite perceived noise around tax credits this is simply rate case timing issue. See upside from further deals not contemplated in the plan, with only a ~$60Mn annual run rate considered outside of the known transactions, providing support for a water rate base CAGR well above their organic 6-7%. Discounted ESG opportunity remains clear among water peers

No Shortage of Muni Opportunities

With no shortage of municipal acquisition opportunities, we see the company as a prime beneficiary of further consolidation across the industry as COVID continues to pressure muni budgets and against a backdrop of favorable legislation: recall WTRG currently enjoys FMV legislation in all eight of their legacy water states. Following the acquisition of ~$63Mn in rate base in 2020, the company has five signed APAs totaling over $420Mn in rate base with another two winning bids totally ~$30Mn waiting a formal agreement. We see a long trajectory of further deals and suspect a potential run rate well above historical norms going forward given the increasingly constructive backdrop.

PO Shifts to $54 on Latest Multiples

Our 2021 estimate comes up slightly to the midpoint of management's guidance. We update our valuation to apply the current peer multiples to our latest estimates: 27.4x for water and 14.2x for gas (vs. 25.5x and 13.9x previously). Our premiums remain unchanged and continue to reflect confidence in ability to consistently deliver, strong muni acquisition prospects, and an underappreciated ESG angle. Our PO is raised to $54 (from $51 previously). Bottom line, see shares as poised to re-rate higher alongside wider water sector: The ESG Antidote: Why Water is a Win/Win.

Estimates (Dec)

(US$)	2018A	2019A	2020E	2021E	2022E
EPS	1.41	1.47	1.57	1.67	1.80
GAAP EPS	1.41	1.47	1.57	1.67	1.82
EPS Change (YoY)	3.7%	4.3%	6.8%	6.4%	7.8%
Consensus EPS (Bloomberg)			1.58	1.67	1.80
DPS	0.86	0.92	0.99	1.06	1.13

Valuation (Dec)

	2018A	2019A	2020E	2021E	2022E
P/E	34.2x	32.8x	30.7x	28.9x	26.8x
GAAP P/E	34.2x	32.8x	30.7x	28.9x	26.5x
Dividend Yield	1.8%	1.9%	2.0%	2.2%	2.3%
EV / EBITDA*	9.6x	37.1x	20.3x	18.6x	17.2x
Free Cash Flow Yield*	-1.1%	-1.8%	-3.6%	-3.2%	-2.5%

* For full definitions of *iQmethod*℠ measures, see page 9.

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Timestamp: 12 January 2021 06:08AM EST

12 January 2021

Equity

Key Changes

(US$)	Previous	Current
Price Obj.	51.00	54.00

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Stock Data

Price	48.18 USD
Price Objective	54.00 USD
Date Established	12-Jan-2021
Investment Opinion	B-1-7
52-Week Range	30.40 USD - 54.52 USD
Mrkt Val (mn) / Shares Out (mn)	11,817 USD / 245.3
Average Daily Value (mn)	48.16 USD
BofA Ticker / Exchange	WTRG / NYS
Bloomberg / Reuters	WTRG US / WTRG.N
ROE (2020E)	8.6%
Net Dbt to Eqty (Dec-2019A)	31.1%

ESG: Environmental Social Governance

PFA: Perfluoroalkoxy Polymer-Chemical Compound

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iQprofile℠ Essential Utilities

*iQ*method℠ – Bus Performance*

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Return on Capital Employed	3.9%	3.5%	5.4%	5.0%	5.1%
Return on Equity	9.7%	8.9%	8.6%	8.1%	8.6%
Operating Margin	38.7%	38.4%	64.7%	66.8%	67.0%
Free Cash Flow	(127)	(212)	(425)	(375)	(300)

*iQ*method℠ – Quality of Earnings*

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Cash Realization Ratio	1.9x	1.3x	1.7x	1.8x	1.7x
Asset Replacement Ratio	3.4x	3.5x	3.1x	2.9x	2.7x
Tax Rate	NM	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	127.1%	31.1%	98.3%	95.5%	103.1%
Interest Cover	2.8x	3.1x	3.4x	3.4x	3.6x

Income Statement Data (Dec)

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Sales	835	886	959	1,006	1,077
% Change	3.7%	6.2%	8.2%	4.8%	7.1%
Gross Profit	838	890	1,555	1,661	1,785
% Change	3.5%	6.2%	74.8%	6.8%	7.5%
EBITDA	1,941	504	920	1,006	1,084
% Change	-86.4%	-74.1%	82.6%	9.4%	7.8%
Net Interest & Other Income	(99)	(100)	(181)	(200)	(202)
Net Income (Adjusted)	192	263	373	410	464
% Change	-19.9%	36.9%	42.1%	9.8%	13.1%

Free Cash Flow Data (Dec)

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Net Income from Cont Operations (GAAP)	192	225	400	429	470
Depreciation & Amortization	147	156	338	376	412
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	(15)	(10)	(75)	(75)	(75)
Other Adjustments, Net	45	(32)	(38)	(6)	(6)
Capital Expenditure	(496)	(550)	(1,050)	(1,100)	(1,100)
Free Cash Flow	-127	-212	-425	-375	-300
% Change	-31.5%	-66.5%	-100.5%	11.6%	20.1%

Balance Sheet Data (Dec)

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Cash & Equivalents	4	1,869	6	6	7
Trade Receivables	101	108	188	201	216
Other Current Assets	42	36	50	52	55
Property, Plant & Equipment	5,930	6,346	10,657	11,381	12,069
Other Non-Current Assets	887	1,003	1,003	1,003	1,003
Total Assets	6,964	9,362	11,905	12,644	13,350
Short-Term Debt	160	131	126	135	151
Other Current Liabilities	239	188	244	253	263
Long-Term Debt	2,398	2,943	4,594	4,909	5,485
Other Non-Current Liabilities	2,158	2,219	2,144	2,069	1,994
Total Liabilities	4,955	5,481	7,108	7,366	7,893
Total Equity	2,009	3,881	4,797	5,278	5,457
Total Equity & Liabilities	6,964	9,362	11,905	12,644	13,350

* For full definitions of *iQ*method℠ measures, see page 9.

Company Sector

Water Utilities

Company Description

Essential Utilities is a regulated water/gas providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI - along with a natural gas presence through the recently acquired Peoples Gas providing distribution services to 740,000 customers in PA, WV, and KY.

Investment Rationale

We are Buy rated on shares of WTRG, seeing shares as poised to re-rate higher given consistent execution, acquisition upside, and increasing conviction around the premium story.

969,084

Quarterly Earnings Estimates

	2019	2020
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NAE

Rolling Forward the EPS CAGR with More Muni Upside

WTRG management provided 2021 EPS expectations of $1.64-1.69 - with the midpoint a touch above our prior estimate of $1.65 and prior consensus of $1.66 – while rolling forward their 5-7% EPS CAGR through 2023 (vs. '22 earlier). While the three year look is admittedly less than other utility peers, we expect a consistent roll forward of the outlook beyond '23 as well despite all the noise around tax credits and rate case timing.

With the latest update, management noted plans to file a rate case at Aqua Pennsylvania later this year, keeping with their three year rate case cadence for their water biz in the state while the company continues to implement Repairs Tax accounting treatment at Peoples Gas: recall earlier guidance of $0.08-$0.12 benefit annually from the repairs election. After the earlier subsequent filing of the catch up component, hearings are scheduled for the end of this month with resolution expected in the second quarter. Rather than drive incremental upside to their 5-7% EPS CAGR, the filing seeks to extend the growth without a need for a rate case. As opposed to going in for new rates in 2023 to take effect in 2024, a constructive outcome from the catch up filing would benefit '23, with incremental benefits in '24, and '25 to help drive earned returns for the segment in outer years without any rate relief until 2026. On balance, we feel comfortable in management's ability to manage around lag, particularly if the company is able to opt out of going in for rates longer.

Muni opportunities Increasingly Robust

We expect the growing pipeline of municipal opportunities to provide a long term tailwind for the water biz. Following the adoption of Fair Market Value legislation in TX and VA, the company now has the constructive legislation in all eight states of their water footprint. We expect this to help further accelerate consolidation in the industry as muni budgets are further flex'd from the crisis - and any further resulting acquisitions would be upside to mgmt.'s latest extended targets with guidance *only assuming ~$60Mn* in annual tuck ins through the forecast period (this is relative to ~$420 Mn of ratebase acquisitions pending). We stress clear positive re-rating potential within this guide range – and see this as also helping to take pressure off execution at Delcora too.

De-risking DELCORA

Late last year, the Delaware County Court of Common Pleas issued an order supporting the pending acquisition of DELCORA by rejecting the county's attempt to block the sale. The order ruled the asset purchase agreement is fully binding and enforceable and that the funds to offset DELCORA customer bills is legal – helping derisk the deal and mitigating prior concerns about the ability for the transaction to close. While we perceive there could still yet be a potential appeal around the decision, the order supports the anticipated closing timeline for the transaction: the Recommended Decision from the PA ALJ is anticipated next week (1/20/21), setting up a decision by the commission in early March and a transaction close in early 2Q. Final resolution should help alleviate some overhang given the forward that needs to be pulled by August.

Overall, we think the $420Mn in rate base opportunities from signed APAs is should generate ~$21Mn in earnings with further muni opportunities still to materialize (*this is roughly +4% to EPS and should help mgmt. execute towards upper end of targeted range*). We see upside to the plan given the more conservative approach to guide, and expect shares to rerate higher relative to AWK as investors continue to appreciate the premium story amid consistent management execution.

We reiterate our Buy rating on shares of WTRG following the latest guidance update. We have increasing conviction in management's ability to consistently deliver and see the company as a prime beneficiary of further consolidation across the water industry. – while the ongoing docket for the catch up component of Repairs Tax treatment in PA should provide further latitude to stay out of rate cases for the gas segment. We struggle to reconcile the sharp discount to peer AWK and see the overhang from gas as nearsighted, particularly given the pipeline of water opp's to further dilute gas as a percentage of their biz. With a growing focus on ESG – and mgmt.'s proactive action around PFAs and emission reductions – we see this an underappreciated angle not reflected at the current valuation.

WTRG 4Q20 Earnings Walk

We forecast 4Q20 adjusted EPS of $0.45 compared to 4Q19 adjusted results of $0.34 and consensus of $0.45.

• **Key Drivers:** The primary driver of the quarter is the contribution from the Peoples Gas acquisition after closing the transaction earlier this year with additional dilution offsetting growth at the legacy water biz.

Table 1: 4Q20 EPS Walk

WTRG 4Q20 Earnings Walk		EPS
WTRG 4Q19 EPS	$	0.34
Aqua		0.03
Peoples Gas		0.11
Dilution		-0.03
4Q20 BofAe Adjusted EPS	$	0.45
Consensus		$0.45
WTRG Guidance		$1.53-$1.58
2020 Consensus		$1.58
4Q20 Adjusted Shares Outstanding		254
4Q19 Adjusted Shares Outstanding		233

Source: BofA Global Research estimates, company report, Bloomberg

EPS Estimates: already towards top end of 5-7%

The exhibit below reflects our latest EPS Estimates. Our 2021 estimates come up slightly to the midpoint of management's newly rolled out guidance of $1.64-$1.69. Longer term, we continue to model to the high end of their 5-7% EPS CAGR. We perceive further upside from a likely acceleration in industry consolidation out of the pandemic as municipal budgets are further stretched and constructive legislation continues to enable transactions. With prospective EPS growth likely more consistent than earlier trajectory (which proved more 'lumpy,' we perceive the trajectory as ever more appealing for those seeking a de-risked outlook).

We continue to see positive bias on EPS execution as 5-7% could be implicitly reset off high end of '20 EPS guide – and see our estimates already at the top end of the EPS CAGR without the full inclusion of contemplated acquisitions (~$1.90 is high end of 5-7% for '23 off $1.55 midpoint). While financing details are pending, we see clear latitude to achieve high end and even re-base slightly higher too.

Table 2: EPS Estimates

EPS Estimates	2020E	2021E	2022E	2023E
PA	$0.75	$0.76	$0.88	$0.94
OH	$0.07	$0.07	$0.07	$0.08
IL	$0.07	$0.08	$0.08	$0.09
TX	$0.06	$0.07	$0.07	$0.07
NC	$0.04	$0.04	$0.05	$0.05
Other States	$0.07	$0.07	$0.08	$0.08
Water Utility	1.06	1.09	1.23	1.31
Peoples Gas	0.62	0.67	0.71	0.76
Parent & Other	*-0.10*	*-0.10*	*-0.13*	*-0.14*
EPS	1.57	1.67	1.80	1.92
YoY Growth	*7%*	*6%*	*8%*	*7%*
Guidance	1.53-1.58	1.64-1.69		
Fully Diluted Shares O/S	*254*	*258*	*261*	*261*
Previous EPS	*$1.56*	*$1.65*	*$1.80*	
Consensus	1.58	1.66	1.80	
DPS	0.99	1.06	1.13	1.21
Payout Ratio	*63%*	*63%*	*63%*	*63%*
Guidance		*60-65%*		

Source: BofA Global Research, Bloomberg

Valuation: PO Raised to $54 on Multiples

The exhibit below reflects our latest SOTP. We update our valuation to apply the current peer multiples to our latest estimates: 27.4x for water and 14.2x for gas (vs. 25.5x and 13.9x previously). Our premiums remain unchanged and continue to reflect confidence in ability to consistently deliver, strong muni acquisition prospects, and an underappreciated ESG angle. Our PO ultimately shifts to $54 (from $51 previously). Reiterate Buy given deep discount and upside catalysts.

Table 3: SOTP

Water Utilities	2023 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*27.4x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		29.7x							
Water Utilities									
States	2023E EPS	ROE embedded							
PA	$0.94	10.0%	4.0x	32.7x	33.7x	34.7x	$31	$32	$33
OH	$0.08	9.2%	2.0x	30.7x	31.7x	32.7x	$2	$2	$3
IL	$0.09	9.1%	3.0x	31.7x	32.7x	33.7x	$3	$3	$3
TX	$0.07	10.0%	2.0x	30.7x	31.7x	32.7x	$2	$2	$2
NC	$0.05	9.2%	2.0x	30.7x	31.7x	32.7x	$1	$2	$2
Other (including acquisitions)	$0.08	9.2%	0.0x	28.7x	29.7x	30.7x	$2	$2	$3
Water utilities total (ex-Peoples)	$1.31			*32.1x*	*33.1x*	*34.1x*	$42	$43	$45
Gas Utilities									
Peer Gas P/E		*14.2x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		15.0x							
	2023E EPS	ROE embedded							
Peoples Gas	$0.76	11.9%	3.0x	17.0x	18.0x	19.0x	$13	$14	$14
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			-985	50%			($492)	($492)	($492)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($444)	($412)	($482)
50/50 Weighted Drag from HoldCo Drag							($937)	($904)	($975)
Fully Diluted Shares Outstanding							*261*	*261*	*261*
PO								$54.00	
Current Price								$48.18	
Dividend Yield								2.2%	
Total Potential Return								14.27%	

Source: BofA Global Research, Bloomberg

Price objective basis & risk

Essential Utilities (WTRG)
Our price objective is $54 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. These peer multiples are 27.4x and 14.2x. We apply a 3.0x premium to Peoples Gas given the organic growth opportunities, while applying a variety of premiums to its water (2x previously) subsidiaries: +4x to PA, +3x to IL, +2x to OH, +2x for TX, +2x for OH, and no premium for balance of biz. We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AES	AES	AES US	Julien Dumoulin-Smith
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Enphase Energy	ENPH	ENPH US	Aric Li
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Ormat Technologies	ORA	ORA US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
NEUTRAL				
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Atlantica Sustainable Infrastructure	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	TransAlta Renewables Inc.	YRNW	RNW CN	Julien Dumoulin-Smith
	UGI Corp.	UGI	UGI US	Richard Ciciarelli, CFA
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	Southwest Gas Holdings	SWX	SWX US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith

iQmethod℠ **Measures Definitions**

Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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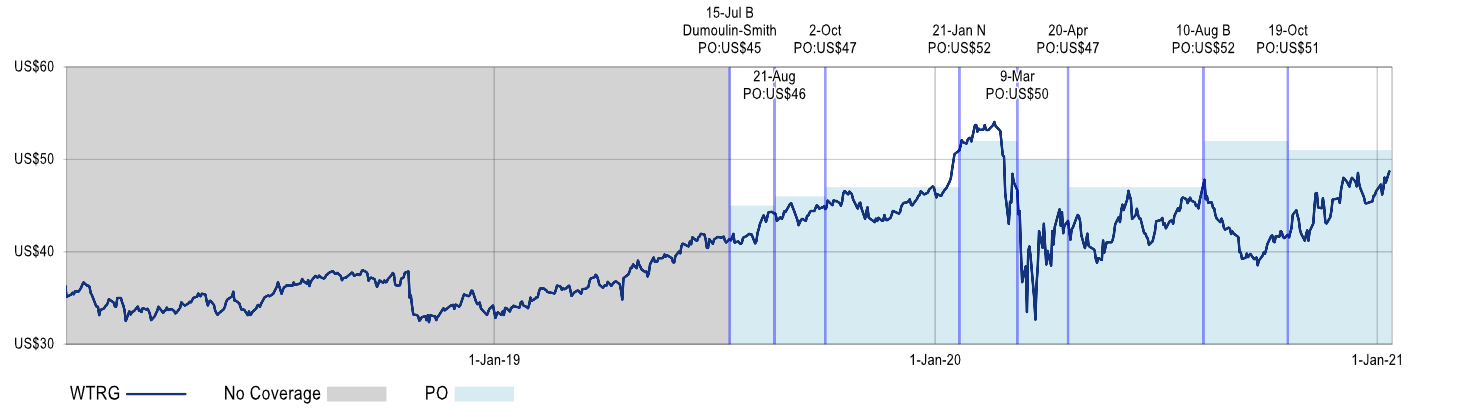
Disclosures

Important Disclosures

Essential Utilities (WTRG) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Utilities Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	80	51.61%	Buy	58	72.50%
Hold	37	23.87%	Hold	28	75.68%
Sell	38	24.52%	Sell	22	57.89%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1863	56.90%	Buy	1185	63.61%
Hold	686	20.95%	Hold	426	62.10%
Sell	725	22.14%	Sell	358	49.38%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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North American Utilities & IPPs

2Q20 Regulated Utility Preview: The Covid Compendium Condensing What We Know

Price Objective Change

20 July 2020

Equity
North America
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'20 looks intact for most across Regulated space

We provide our 2Q20 Regulated utility preview for AEE, AEP, AWK, CMS, DTE, DUK, EIX, LNT, WTRG, EVRG, FE, PNW, PPL, WEC, and XEL. The group trod water during Q2 with the IXU index returning +1.8% from Mar 31 through June 30, a tough comp against the broader market with the S&P 500 rallying +20% in the same period. Nonetheless, we see a more constructive story across the board than one quarter ago with weather largely serving as a cushion on Q2 results, offsetting expected losses linked to COVID. If Anything those with pitfalls into 2Q are largely of their own discrete nature, rather than wider (unknown) Covid concerns – along with a handful who didn't update earlier.

Q2 shaping up (much) better than initially feared

For **EIX** we see a miss on 2Q, although comparability continues to remain outside of reach given pending O&M recovery; instead, expect focus to remain on the upcoming fire season and mitigation efforts (PSPS, Blackhawks, fire retardants) as well as updates on '17/18 liabilities (where we remain biased to the upside on the $4.9bn low-end range) although could see further clarity on B/S help w/ re-rating potential. For **DUK**, we see a weak 2Q given more material COVID impacts with O&M offsets back half weighted; we remain concerned around mgmt.'s messaging *of re-base its growth trajectory* given an expected weak '21 outlook following cancelation of ACP and capex backfilled in the later part of the program; longer-term the IRP presents a clear opportunity for further capex deployment (post-21 given litigated process) as well as legislation stemming from the NC clean energy agenda. With large resi compositions and constructive recovery mechanisms/orders across most jurisdictions, we see **AWK** and **WTRG** as relatively protected from COVID challenges. After electing not to reset expectations with 1Q results, *we see more risk to **PPL**'s 2020 guidance* – albeit our latest model still suggests the low end of their range: full quarter impact and ongoing expectations around UK in particular will prove critical given two year lag with true up mechanism. **LNT** continues to move ahead with its WI solar filing with an expected order in '21, while the rate stabilization filing in the state should be decided in Q3 with unchanged ROE and equity and escrow treatment for pension and bad debt. **DTE** appears to have largely offset Covid impacts (among the higher Industrial sales declines posted in Apr) thanks to a strong weather uplift in the quarter (across MIS); we also see approval for rate case filing delay until Q2 202; among best for 2Q outlook. We expect similar benefits for CMS with further details and confidence in cost savings to support a firmer reaffirmation of FY20 guidance. **EVRG** received approval of its accounting order in KS (historically its more difficult jurisdiction) and has a pending request in MO; we see a largely in-line quarter though the focus remains on the outcome of its strategic process with committee recommendation in late July and Board decision in August. **PNW** has a tricky regulatory setup in 2H with rate case staff testimony due in early August, though mgmt. recently affirmed that they do not see a path to settlement in '20, with likely decision coming from a new bench of commissioners after Nov elections; we do expect capex clarity as unexpected angle into 2Q to drive partial offset to outlook; pos '20 affirmation too. We expect **WEC** to post a Q2 print at the top of its already-increased guide range on the back of warm June weather, and see their '20 guidance as very much intact (we raise ests to high range); here too pos framing ahead.

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2Q Summary and PO Changes

We include a brief summary of our 2Q estimates compared vs Street as well as PO changes reflected in this report.

Table 1: PO Changes

Regulated		New PO	Old PO
Alliant Energy Corp	LNT	$54.50	$52.00
Ameren Corp.	AEE	$79.00	$79.00
American Electric Power, Inc	AEP	$88.00	$80.00
American Water	AWK	$135.00	$133.00
DTE Energy Co.	DTE	$115.00	$115.00
Duke Energy	DUK	$87.00	$84.00
Edison International	EIX	$65.00	$65.00
Essential Utilities	WTRG	$47.00	$47.00
Evergy, Inc	EVRG	$68.00	$63.00
FirstEnergy Corp.	FE	$45.50	$45.50
Pinnacle West Capital Co.	PNW	$78.00	$78.00
PPL Corporation	PPL	$27.00	$27.00
WEC Energy Group Inc.	WEC	$83.00	$83.00
Xcel Energy Inc.	XEL	$62.50	$62.50

Source: BofA Global Research

Table 2: 2Q Estimate Summary

Regulated		2Q20 - BofAe	2Q20 - Cons	Delta
Alliant Energy Corp	LNT	$0.51	$0.44	16%
Ameren Corp.	AEE	$0.86	$0.86	0%
American Electric Power, Inc	AEP	$1.07	$1.02	5%
American Water	AWK	$0.97	$0.96	1%
DTE Energy Co.	DTE	$1.27	$1.19	7%
Duke Energy	DUK	$1.01	$1.01	0%
Edison International	EIX	$0.95	$1.15	-17%
Essential Utilities	WTRG	$0.24	$0.22	4%
Evergy, Inc	EVRG	$0.70	$0.68	3%
FirstEnergy Corp.	FE	$0.54	$0.55	-2%
Pinnacle West Capital Co.	PNW	$1.55	$1.43	8%
PPL Corporation	PPL	$0.54	$0.56	-4%
WEC Energy Group Inc.	WEC	$0.69	$0.67	3%
Xcel Energy Inc.	XEL	$0.43	$0.49	-12%

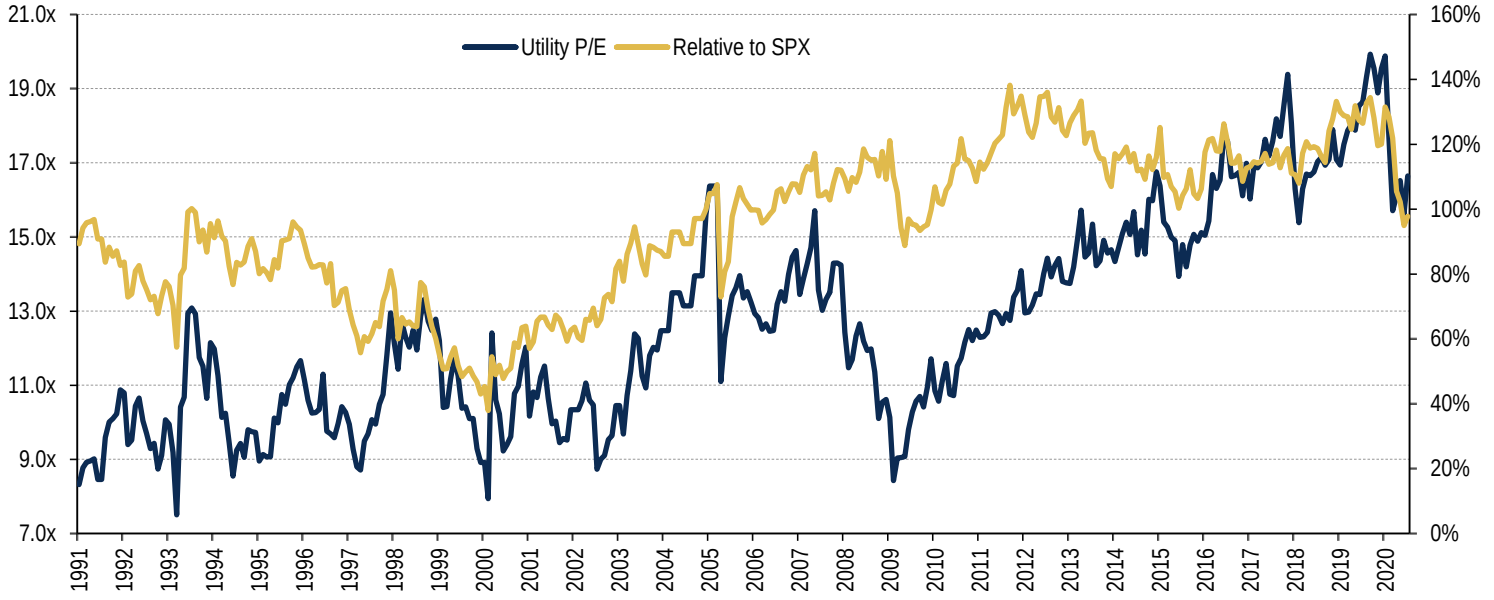
Source: BofA Global Research, Bloomberg

Macro Backdrop

We perceive investors are generally skeptical of current sector valuations – and see the continued upward trajectory of the sector as still showing an expensive backdrop from a high level perspective. The chart below shows the latest mark-to-market of the group on an absolute basis and against the SPX; utilities continue to trade near their all-time highs on both a relative and absolute basis.

We continue to see the backdrop as among the single most intriguing backdrops in recent memory with the sector having traded off relative to its historic relationship between rates and the S&P to its lowest levels since the 2000 tech bubble – off its highest relative trading levels in 3Q19 (almost -60% under-performance), making the sector incredibly compelling against historic valuation metrics. With few material risks to estimates, dividends, or outlook, the question is just whether the market will remain oriented towards growth equities with elevations. Much of this is dependent on recovery from recession ironically – where recovery has historically driven a bid towards value relative to growth (per our Equity strategist Savita Subramanian).

Chart 1: Utility PE relative to SPX

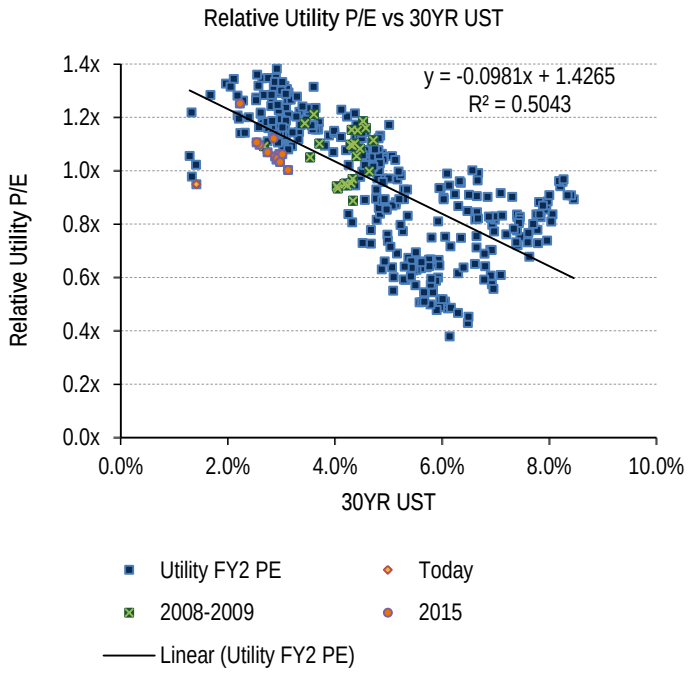


Source: Bloomberg

When adjusting for the S&P itself *and* the treasury environment: different story

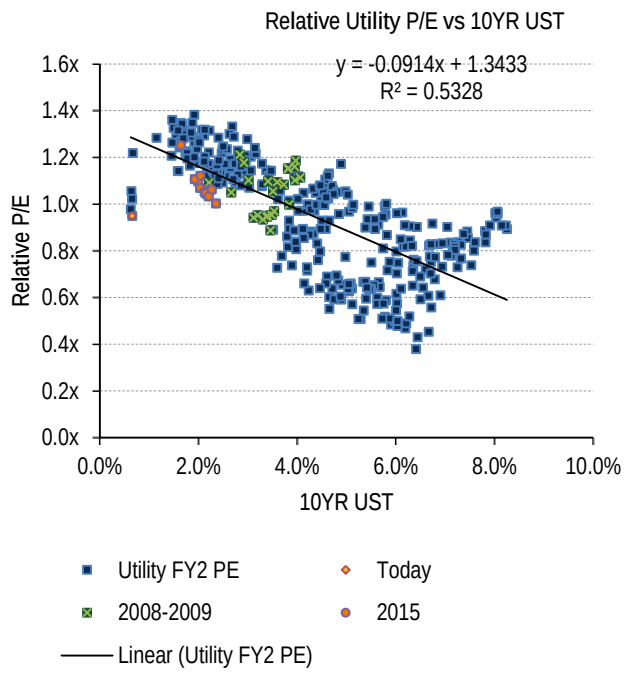
In the exhibits below, we show a time series of where the sector has traded relative to the linear regression on a relative and absolute basis for Treasuries to illustrate the premium; the group has started to trade more in line with its historical linear relationship with 10Yr and 30 Yr Treasuries on a relative basis.

Chart 2: Relative Utility PE vs 30YR UST



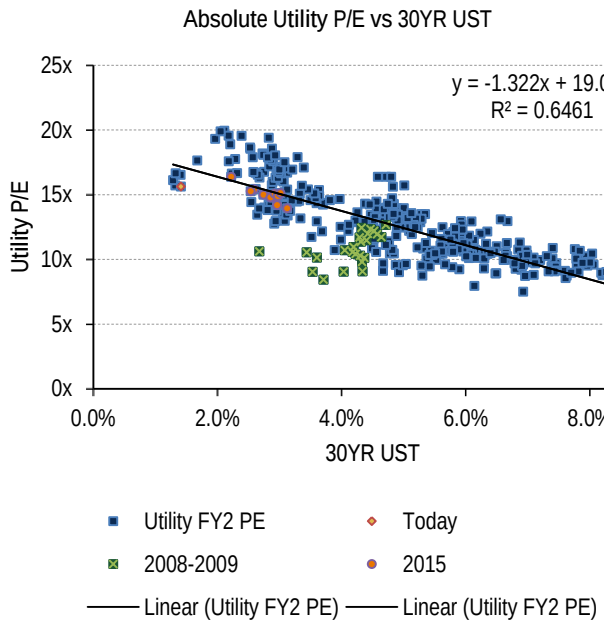
Source: BofA Global Research, Bloomberg

Chart 3: Relative Utility PE vs 10YR UST



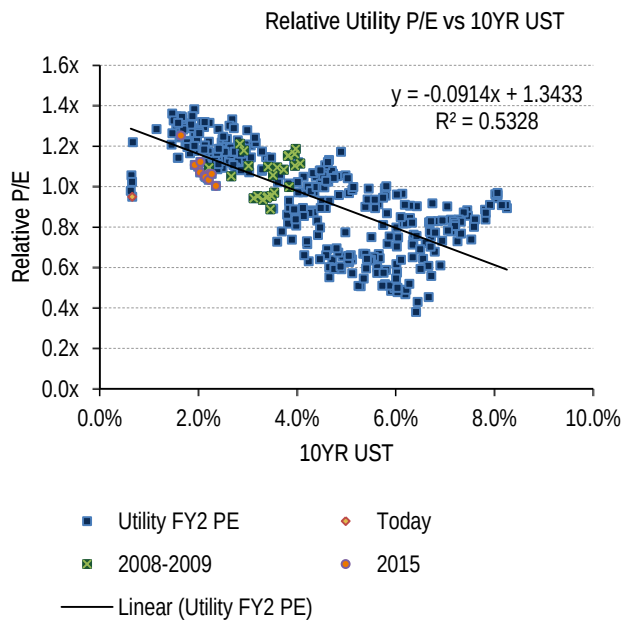
Source: BofA Global Research, Bloomberg

Chart 4: Absolute Utility PE vs 30YR UST



Source: BofA Global Research, Bloomberg

Chart 5: Absolute Utility PE vs 10YR UST



Source: BofA Global Research, Bloomberg

Tax Reform Perspectives For Utilities In Brief

Tax Reform & Utilities: Not as Concerned as Investors

We recently hosted a call with our BofA Public Policy expert regarding potential tax reform with Biden as President. Critically, our expert asserts only if there is a Democratic sweep in November (Biden wins, and Democrats regain control of both the House and Senate) would it be likely for Democrats move to pass a meaningful tax bill in 2021. Many utility investors have been concerned about tax reform prospects and focusing on this scenario as if this was directly tied to a Biden win of late- rather than appreciating the very more narrow under which comprehensive tax reform would once again pass. Note the budget reconciliation vehicle, allows Congress to move tax legislation with only a bare majority in the Senate (cannot be filibustered); this remains a critical vehicle seeing it being used for the last tax reform effort. Notably, Biden's platform currently has three major likely tax proposals, which include: 1) raising the U.S. corporate tax rate from 21% to 28%, 2) implementing a new minimum tax on companies' GAAP earnings, and 3) tightening of the Global Intangible Low Tax Income (GILTI). The first two matter to utilities, while the third really would only apply to AES among utilities/IPPs. Think tanks and private revenue estimators believe raising the tax rate (the most likely of the three proposals) would lead to government revenue of $1.3 trillion over ten years, the highest potential revenue source of the three proposals. The exact rate increase is still subject to change, but 28% is the current proposal. We address many of the tax reform debates in latest election note. The minimum tax on GAAP earnings specifically impacts U.S. corporations that currently do not pay taxes of at least 15% of their GAAP earnings. The proposal would bring the tax level up to 15% for the companies that currently "habitually pay less" than this rate; this could very well still allow for renewable tax credits to be netted even against this minimum requirement (hence giving reprieve to much of the utility industry, albeit this remains unclear). A tightening of GILTI impacts multinational corporations where a company's rate would be increased from 10.5% (current as of 2017) to 21%, effectively doubled. It remains unclear just how this would manifest itself for AES (B-1-7; $14.44). Overall, we see utilities as net beneficiaries under a tax reform context given the muted impact vs other industries despite what is likely delayed ability to recoup the higher tax rates from customers given the need to file rate cases (and likely suffer ROE drops too).

But the real low prob kicker is dividend tax rate hike risk

Separately on the income tax front, but critical for utility investors, Biden has also proposed to tax capital gains and dividends at the same rate as ordinary income, which would go back up to 39.6% in the top income bracket (above $1mn/year). However, we acknowledge that this would be a relatively dramatic proposal, and it is unclear if moderate democrats would support this or even move in the context of a Democratic sweep according to our internal expert. Bottom line, although it is unlikely there is desire to move legislation on capital gains and dividends, and a democratic sweep presents notable vulnerability for utilities under this proposal in addition to the three aforementioned major tax proposals.

King Coal: How Much Exposure is Left?

Measuring the value of remaining coal across the sector

We present our analysis of estimated rate base, earnings, and in turn, value of coal as a % of market cap across our Wider Power & Utilities universe. While disclosures vary with most companies under our coverage (explicitly) disclosing coal rate base many provide some very helpful clues enabling us to estimate ratebase (particularly of more recently built) scrubbers, leveraging FERC Form 1 data and estimates around deferred tax and related adjustments. We also highlight the impact on rate base of scrubber and other pollution control retrofits that have left many utilities with the challenge of dealing with undepreciated plant in what are increasingly uncompetitive generation assets - though some states such as MI have addressed the challenge head on with existing securitization laws, we see opportunities for acceleration of retirements in other jurisdictions such as WI, KS, MO among others where securitization is yet on the books.

Leaders and laggards among our coverage

Our analysis shows that on average Regulated and SMID-cap names have earnings exposure linked to coal in rate base of 10-15% while Diversified peers are meaningfully lower with the exception of SO, although w/ constructive regulatory relationships. EVRG stands out w/ 2019 EPS estimated at 39% derived from its coal-heavy fleet given an estimated ~$5B of coal in rate base. We continue to see this as a key angle to watch in the ongoing strategic process given a largely undepreciated amount w/an estimated $1-$1.5B in rate base linked to scrubber retrofits (highlights need for securitization in both the KS and MO). Elsewhere, we continue to see ETR's unscrubbed fleet as representing a significant renewable investment opportunity with minimal rate base remaining - though the overall share of coal-fired generation in the company's portfolio remains 9% by nameplate capacity. CNP screens as the single highest exposure to coal by % of its portfolio at 83% of nameplate, but the small size of its overall fleet and minimal ratebase associated with its assets (including scrubbers on all assets) mitigate its overall exposure. Meanwhile we expect DTE's relatively high exposure estimated at 19% of EPS to decline in coming years with scheduled 2022 retirements of three facilities - while we estimate some undepreciated rate base associated with the assets, the regulatory environment is broadly supportive of transitioning away from coal with securitization legislation in place in the state since 2000. NEE is unsurprisingly a leader in terms of minimizing exposure among utilities, with less than 1% of rate base tied to coal on our estimates. PNW provides particularly limited (no) disclosure on the composition of its coal rate base (we estimate modest exposure), although is seeking to meaningfully add to its coal rate base. DUK too stands out given ~13% of EPS made up of coal where it also intends to add through coal ash clean-up on one hand, although is looking to make strides through the IRP w/ coal retirements and potential for securitization/accelerated D&A in legislation/rate cases: only DUK, SO, and PNW are still really adding to coal (ash) ratebase. While AES' earnings are ~35% coal and our SOTP indicates ~30% value (among highest for entire sector) are from coal, co is rapidly selling & de-carbonizing (anticipate closer to ~20% end of year): more here. With ESG investors focused on this question of exposure typically from a revenue perspective we thought it appropriate to reposition the debate on a more relevant set of metrics. Please refer the link for full details here.

ESG in the Utility Sector: The Inaugural Diversity Handbook

Diversity & inclusion across the utilities

We provide an inaugural deep dive on diversity and inclusion efforts across our coverage universe. We perceive the issue of diversity in its various forms as increasingly relevant to the investor community, with a growing body of evidence linking financial performance to an inclusive and equitable business environment. We highlight our BofA ESG Research Team's recent report, Womentum! Our report on company initiatives and efforts covers nearly 60 companies across the Diversified, Regulated, SMID Utilities, Gas Utility, Water Utility, Power, LNG, and Residential Solar sectors.

Selecting our diversity metrics

We compiled data and information to assess D&I practices using a range of relevant diversity metrics. In particular, our analysis is focused on: 1) board representation of women & minorities, 2) senior leadership representation of women & minorities, 3) supplier diversity programs and % diverse spend, 4) availability of Employee Resource Groups, and 5) LGBTQ equality policies and practices. Based on public data regarding gender equality, we note a major push across the sector in recent years: on average, women now comprise ~30% of Board members and ~25% of executive leadership roles. Racial/ethnic minority representation is slightly lower with ~20% BoD and 15-20% executive leadership representation in companies in our coverage universe; these averaged statistics also fall slightly below company-reported workforce percentages. Further, fewer disclosures were provided on POC representation than on gender, suggesting that these figures may be even lower. We also provide LGBTQ equality ratings as assessed by the Human Rights Campaign's Corporate Equality Index. While the majority of companies with CEI ratings received full scores (100), a handful of companies scored below, a couple did not respond to repeated requests, and a few of the smaller-cap names were not included given their size. On supplier diversity, nearly all companies stated that they had supplier diversity programs but many did not disclose % spend; on the high end; we note that some companies had up to 30-40% diverse spend. Finally, we include company summaries with more qualitative information (e.g. ERGs, other initiatives).

How did the companies stack up? Stocks in focus...

After examining the quantitative/qualitative metrics, we highlight the companies which stood out within each subsector. SRE has 38% female and 31% POC Board representation, has signed on to the "Paradigm for Parity" for full gender parity in senior executive roles by 2030, and maintains ~40% diverse spend at SoCalGas and SDG&E. ETR has 40% female representation on its BoD, with 30% female executives and 20% POC executives. For 2020, ETR has a diverse spend target of 14% of managed spend. EIX has 36%/36% representation on the BoD by women and POC, respectively, with 35%/34% women and POC in executive roles. Edison is part of the Paradigm for Parity effort. Diverse spend comprises ~40% of total spend. PCG has 34% and 35% female and POC executives, respectively. Total diverse supplier spend represents ~41% of total purchases. CMS has 45% female representation and 27% POC representation on its Board. Women and POC comprise 32% and 18% of executive roles, respectively. Please refer the link for full details here.

Contrasting US Utility Performance Against Global Peers

A Sector Trip Around the Globe

Our macro series continues, with our latest analysis providing some color around BofA utility performance vs regional markets relative to the US Outlook. We include perspectives from our colleague's from Asia, Australia, Europe, and LatAm in an attempt to contrast against the latest backdrop for US utilities. Across the world, we have seen wide dispersions in performance by geography, subsector, and company - with our included tables highlighting performance on a one week, one month, three month, and YTD basis and reflecting averages by subsector across the durations (on a market-cap weighted basis). Most geographies show *relative performance similar or even out-performing their regional markets (admittedly what would be expected in a global defensive pivot*). See each relative performance trends below by region.

So how Does this Stack up with the US?

In our full note, we include the latest stock performance for our core US utility coverage (Diversified, Regulated, SMIDs, Gas, and Water) along with the latest charts showing utility valuations vs. risk free rates & bond yields - with discrepancies recently reached having not been seen in the last several decades. We view US Utilities as substantially intact despite earlier fears of widespread Covid impacts. While admittedly revisions could still prove slightly downwards (2-3%) on '21 given delayed rate recovery & under-earning vs. authorized returns, we see this as much more intact than peer S&P sectors. While a potential 'twin' headwind remains around corporate tax reform into '21, this admittedly is a factor for all utilities. On a market cap weighted basis, Diversified Utilities and Large CapRegulated Utilities remain down low double digits YTD, while SMIDs and Gas utilities are off a more material 25% and 14%, respectively. Water utilities are down a more modest 1% for the year. More specifically, with the utility sector primed for the return of the value cycle, we see SMIDs particularly well positioned to recover from the underperformance this year. With the economy reopening in many states across the nation, we could see a reversal of the 2Q liquidity environment that has favored growth stocks, with value stocks starting to outperform with the latest improving data trends amid re-openings and estimate revisions. With the BofA strategy team calling for value stocks to outperform at least for the next quarter, we believe this bodes well for the sector going forward. Into the next several months. We continue to see the most opportunity in **ETR** and **AEE** among larger-cap regulated names. We also highlight **AES** with its global footprint; down -33% YTD, we perceive this as outsized relative to any relevant geography for the company globally (with even Latam Utilities only down on average -8%). The wider under-performance of the US utilities as part of a near record downtick in 'Value' allocations (see macro note on this trend in US) is also highlighted by the near record relative dispersions *among* utilities, seeing near all-time highs in P/E spreads between 'quality' (those have a record of stable & consistent EPS growth) and 'value' (those with historically lower & less consistent EPS growth alongside higher leverage).

Please refer the link for full details here.

Why are US Utes so Cheap? Let's Look at the Balance Sheet- and P/BV

Tackling the Price/Book Value Debate for Utilities

With the evolving backdrop and strong market comeback more recently, we continue to analyze the US utilities sector against the latest macro data and trends. We continue to see utilities trading at a wide valuation gap on a relative basis to historical relationships to risk free rates and bond yields - with discrepancies recently reached having not been seen in the last several decades. Our latest analysis dives deeper by looking at Price/Book Values across our coverage at both a sector (vs. SPX and other S&P sectors) and company specific level vs. historical norms. Broadly speaking, the group is trading at a ~1.2x discount on this metric, slightly above the -1.0x discount to the S&P over the last decade while the majority of sectors (ex. Financials, Materials, and Energy) are all elevated from an absolute level vs historic norms but off their peaks. While admittedly P/BV value trends don't show the sector trading as cheap as comparisons vs yields (both risk-free and corporate IG bond yield relationships) would otherwise indicate, it admittedly is still wider than historical norms by -20%, this metric controversially shows the sector trading at one of its most elevated levels in recent years in absolute terms (see full tables below). Critically, his has been one of the arguments from bears or those otherwise Neutral on Utility sector valuation, suggesting it just doesn't 'screen' well for a hard asset sector. Admittedly, most sectors are already trading at near record historical levels on a P/BV basis (likely with tech & other growth sectors reflecting an increasing premium for intangible assets). Looking at the spread between the wider S&P and Utilities, the discount on a P/BV basis today is at its widest (eg-utility discount) since the GFC. Altogether, while not quite as bullish a characterization we still see even this valuation metric as meriting an investment case in utilities. Meanwhile looking at sector balance sheet more holistically, metrics have seen a steady uptick in leverage in recent years (both net Debt/EBITDA and FFO/debt) reflecting wider de-risking (fewer non-reg subs, etc) and acceptance of greater leverage by rating agencies

EV to Ratebase yields similar outcomes

In our latest analysis, we also highlight EV/Rate base as a further proxy of P/BV valuation: notable companies on EV/Ratebase metric include DUK, FE, ES, WEC, LNT among others with larger non-regulated/tax items.

So What are Our Top Picks these Days?

We see the utility sector as primed for the return of the value cycle, with SMIDs particularly well positioned to recover from the underperformance this year. With the economy reopening in many states across the nation, we could see a reversal of the 2Q liquidity environment that has favored growth stocks, with value stocks starting to outperform with the latest improving data trends amid re-openings and estimate revisions. With the BofA strategy team calling for value stocks to outperform at least for the next quarter, we believe this bodes well for the sector going forward. Into the next several months. Our favorite opportunities remain ETR and AEE among larger-cap regulated opportunities.

Please refer the link for full details here.

The ABC's of Utilities: ROE, leverage, debt capital, and capex tell the story

Evaluating GAAP ROEs and ratio trends

Below we compile a series of ratios to show aggregate trends for sector wide returns and balance sheet metrics. We find this a useful compilation for investors to gauge wider sector trends on largely sustained balance sheet metrics and consistent ROEs across the space in spite of sector gyrations from year to year & provides a baseline for comparison across each of the sub-sectors against 'normal'. We include full tables of both projected and historical earned ROEs and balance sheet metrics below for review. Credit metrics are intact, despite continued acceleration in capex in recent years. We anticipate 2020 could prove a pause on this accelerating trend.

Risks to sector linger as Corp Tax & Covid Combined

We increasingly see some risks of compounding rate case delays given consumer impacts of Covid (& low rates at that) exacerbated by the prospects of higher corporate taxes through a change in administration: this could drive more meaningful rate lag. This could specifically impact '22 and '23 ests as years of rate stay outs eventually take their toll on earned ROEs despite cost cutting efforts. While earlier (lower) corporate taxes were readily passed through to consumers, the reverse could be reflected potentially in a delayed fashion through new rate cases (unclear if trued up) and would present potentially unpalatable rate increases despite covid sensitivities. This could also serve to reduce authorized equity ratios.

Subsector breakdown: Regulated have higher GAAP ROEs

We find that Diversifieds, SMIDS, and gas utes have roughly an average of 9% GAAP ROEs, while Water and Regulateds are higher at 10%, and 11%, respectively. Canadian utes are at 7% - reflecting non-regulated segments and commodity risk. In '20 we see 40-100bps YoY decreases in all subsectors but gas (flat) & Canadian names (increasing).

Could we see more capex shifts?

In response to balance sheet pressures, a number of co's reduced capex in '20, shifted capex from '20 into later years, or reduced capex overall in the next few years; we adjusted capex in our models for co's including CNP, EXC, AEP, CMS, EIX, POR, NI, EMA and AQN. Not all companies reduced '20 capex; some have upside potential including co's positioned to benefit from replacing generation with ratebase opps (AEE, ETR) working with states in what we see as stimulus (i.e. accelerate or increase capex to create jobs) (XEL, PEG), and pursing renewables opps that benefit from the PTC continuity safe harbor guideline expansion (NEE, AQN). Across our coverage, we find a net $419mn capex reduction in '20 and a $1.5bn capex reduction for '20-25 - a mere -0.3% reduction in total spending but indicative of co-level differences. Looking forward this year, we believe there remains risk of negative capex revisions still for the sector, given potential further balance sheet pressure going into 2Q (what many expect is the hardest quarter on sales) and apparent delays in rate case timing (as companies are rightfully sensitive of the economic backdrop to not file too soon). We see this risk as largely overlooked.

Please refer the link for full details here.

Alliant Energy (LNT)

We forecast 2Q20 adjusted EPS of $0.53 vs. consensus of $0.40 (we note upside to Street estimates as these are not updated yet) and 2Q19 results of $0.40. We reflect a 2020 EPS estimate of $2.44/sh, above the midpoint of mgmt.'s $2.34-2.48/sh guidance range as LNT continues to respond to Covid-related sales impacts, though we note that Q2 provided an estimated weather-related uplift, in contrast with Q1. We expect an update on LNT's WI rate stabilization filing which is currently making its way through the PSC process with staff recommendations forthcoming. With this approval expected sometime in Q3 and the recent solar filing, we see the LNT story as increasingly de-risked and set up for continued execution into '21with our forecast EPS CAGR at 6-7% off 2019 vs. mgmt. range of 5-7% .

Key Drivers: Weather is expected to be a benefit of $0.05/sh as we normalize for the negative effects of 2Q19 (2 cents) and account for milder weather in 2Q20 that drove the number of CDDs across LNT's service area higher than normal – in particular in the month of June which sees a heavier weighting toward its degree days. We estimate a Covid-related impact (sales and O&M offsets) of approximately -3 cents for the quarter as LNT reported residential sales up 4% with C&I down 12% for the first 2 months of Q2. We also note a tax timing item which we estimate at+4 cents in Q2 related principally to PTCs, which along with the 8 cent gain reported by LNT in Q1 is expected to reverse during the balance of the year.

Unknowns: Weather is expected to be a benefit to LNT – we estimate a 3 cent uplift – thought given the shoulder quarter he exact impact is difficult to ascertain. We note the relative weighting of degree days varies from Apr-Jun, though with Q2 CDDs weighted toward June for LNT, this trend should provide a tail wind. Additionally, we note that while most states have lifted strict stay-at-home orders, higher-margin residential sales may have benefitted as more people remained indoors than during a 'normal' year. While the tax timing impact related mostly to PTCs is expected to be flat for the year, it is difficult to estimate the precise impact though we expect it to be directionally lower in Q2 relative to 8 cents in Q1.

Table 3: LNT Q2 EPS walk: a nice beat off lowered expectations from 1Q

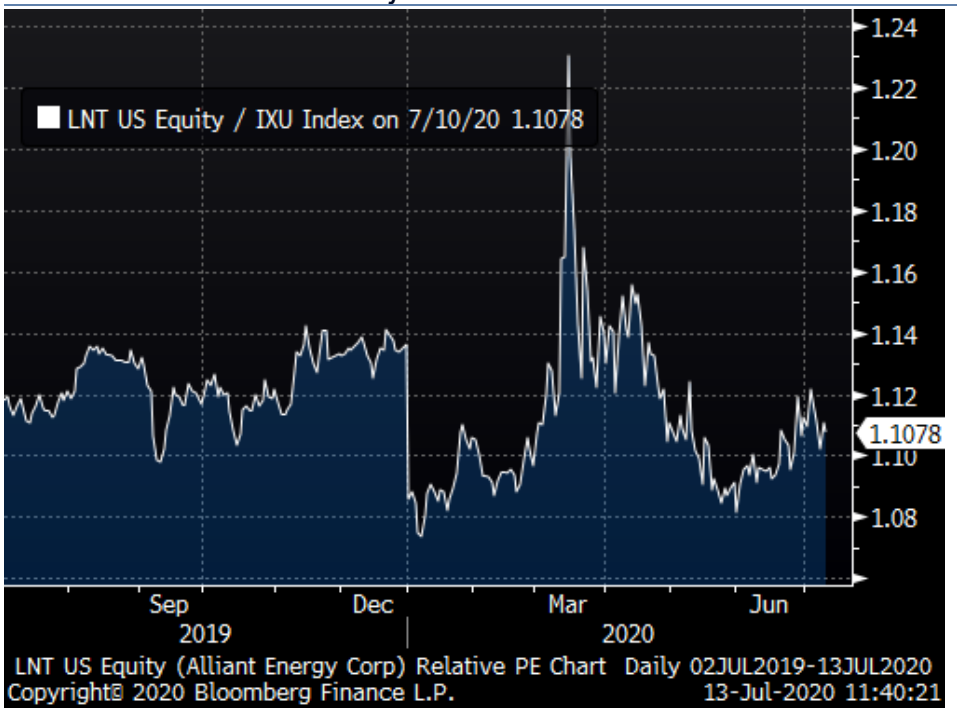
2Q20 EPS Walk	Notes	EPS Impact
2Q19 Starting Point		$0.40
Weather impact 2Q19		$0.02
Weather impact 2Q20	*June CDDs higher than normal*	$0.03
IPL Base rate increase	*IPL Electric effective 1/8/20; IPL Gas effective 12/18/19*	$0.09
WPL Electric	*New rates at WPL*	$0.05
Depreciation	*-$0.18/sh for full year; weighted more heavily later in yr*	($0.03)
AFUDC increases	*-$0.13/sh for full year*	($0.02)
Other items / O&M / ATC	*-$0.08/sh for full year*	($0.02)
Int Expense	*Debt issuance at WPL and IPL*	($0.01)
COVID	*Stay at home mid-March*	($0.03)
Tax timing	*Related mostly to PTCs – flat for the year*	$0.04
Dilution	*Incremental equity dilution*	($0.02)
2Q20 EPS		$0.51
Consensus		$0.40
2020 EPS		$2.44
2020 Consensus EPS		$2.40
2020 Guidance		2.34-2.48
2Q19 Sharecount		238
2Q20 Sharecount		250

Source: BofA Global Research, Quick, Bloomberg

Stock trading dynamics

Shares of LNT have traded up in recent weeks relative to the electric utility peer group, exceeding the relative trading levels of pre-Covid Q1. We note several constructive developments of late including the filing of the company's first tranche of its intended 1 GW solar projects in WI – the company's request for 675 MW continues to move through the permitting process in the state where we note appetite for renewables is strong with ample precedent for including utility-scale projects in rate base, as MGEE has done. Mgmt. has also recently affirmed that it is not seeking to expand its non-reg business aside from a small wind footprint and transport business. We see LNT as offering above-peer EPS growth in its regulated biz of 6-7%, among the more constructive Midwest utility stories among our coverage.

Exhibit 1: LNT shares relative to IXU on 2yr forward PE



Source: Bloomberg

Covid impact: Q2 trending in the right direction

We note the most recent Covid sales update from mgmt. indicates an uptick in C&I sales in the month of May. While weather-normalized Residential sales held steady at +4% for the Apr-May period (in-line with prior Apr reporting), C&I ticked up to -12% from -13% previously reported in April, indicative of a modest though encouraging uptick. We note this trend largely supports MISO data which shows electricity demand bottoming in Apr and then beginning a gradual and somewhat uneven recovery. We note that LNT's service territory highlights the different state-level approaches to handling the pandemic, with IA having never issued a statewide shelter-in-place order (leaving this to the county level) while WI initially issued a lockdown order which has since been lifted, following by gradual re-introduction of distancing measures. We received further comfort from mgmt. on our recent fireside chat where the company affirmed the recent uptick in sales – a notable positive given one of the more conservative sales guidance outlooks and further bolstering what we expect to be a reaffirmation of full-year guidance as we remain above the midpoint. Among the other positive developments of late, the WI commission lifted the moratorium on disconnections effective Jul 25, after IA had issued a similar order effective Jul 1. WI utilities are likewise able to resume charging late payment fees on accounts in arrears effective Jul 15, all factors that are trending toward gradual normalization – though the PSC had previously issued an order

for deferral of Covid-related costs included those associated with bad debts and the disconnect moratorium.

Table 4: LNT sales earnings sensitivity

	EPS sens to 1% move	Apr	Apr-May
All Classes		-9%	-8%
Residential	$0.02	4%	4%
Commercial	$0.01	-13%	-12%
Industrial	$0.01	-13%	-12%

Source: Company report

WI stabilization in Q3, Solar approval expected in 1H21

LNT's rate WI stabilization asks for the same ROE & Equity layer, and escrow treatment of pension & bad debt. With ~$500mn in rate base additions, 1/3 will be offset with lower fuel costs and the remainder related to taxes. The decision on the stabilization plan is expected to come down in Q3, with staff recommendations to the PSC the next meaningful milestone.

During Q2 announced plans for the initial 675MW tranche of its eventual 1 GW solar portfolio at a purchase consideration of $900m of which tax equity partner would sponsor 35-40% of the investment outlay with the rest being financed by LNT's Wisconsin subsidiary - $780m is included in the capex plan across the full 1 GW portfolio. The company indicated to purchase tax equity's ownership in the projects within 10 years of operation. We note that LNT already signed purchase and sale agreements with the developers, subject to pending approval from the regulators, however, none of the projects are currently under construction. The company anticipates 425MW to be placed in service by 2022 and 250MW in 2023 – see below. We note positive signs toward eventual approval given the state PSC's pro-renewables stance (recently appointed third commissioner comes from a renewable advocacy group) and overall constructive utility-regulator relationships across the state.

Table 5: LNT initial 675 MW solar projects

Name	Capacity (MW)	In Service
Crawfish River	75	2022
Onion River	150	2022
Richland County	50	2022
Wood County	150	2022
Grant County	200	2023
North Rock	50	2023

Source: Company report

Estimates

We had previously forecast Covid impact into our '20 estimates for LNT and remain 1 cent below the midpoint of the $2.34-2.48 guidance range at $2.40, tweaking our forecast incrementally to reflect updated ATC ROE following the FERC's MISO ruling. We note that positive weather trends in late Q2 and early Q3 bode well for a sales tailwind during the peak cooling season, with encouraging sales trends as previously highlighted by the mgmt. team further de-risking the near-term outlook. We remain near the upper end of mgmt.'s 5-7% EPS range looking out further ahead.

UPDATE TABLE

Table 6: LNT updated ests

EPS by Segment	2017A	2018A	2019A	2020E	2021E	2022E	2023E
IPL	$0.94	$1.13	$1.19	$1.35	$1.43	$1.50	$1.52
WPL	$0.80	$0.89	$0.97	$0.95	$1.04	$1.13	$1.21
ATC	$0.11	$0.13	$0.13	$0.14	$0.14	$0.15	$0.15
Parent/Other	$0.09	$0.02	$0.01	-$0.04	-$0.04	-$0.03	-$0.03
Total	$1.93	$2.17	$2.31	$2.40	$2.58	$2.75	$2.86
Prior Estimates	$1.93	$2.17	$2.31	$2.40	$2.57	$2.74	$2.85
EPS Guidance							
IPL +WPL		*2.04 - 2.07*	*2.21 - 2.23*				
ATC		*0.10 - 0.12*	*0.11 - 1.13*				
Parent/Other		*(0.01) - 0.00*	*(0.05) - (0.03)*				
Guidance	$1.89-$1.97	$2.13-$2.19	2.27-2.33	2.34-2.48			
Non-GAAP EPS Growth Off $2.26 in '19 (5-7%)				6.35%	6.82%	6.78%	6.04%
Consensus	$1.95	$2.16	$2.30	$2.40	$2.58	$2.71	$2.85
Consensus CAGR					6.86%		
Mid				$2.41	$2.56	$2.71	$2.87
High				$2.48	$2.65	$2.84	$3.04
Low				$2.34	$2.46	$2.58	$2.71
Model Embedded ROEs / Equity	2017A	2018A	2019E	2020E	2021E	2022E	2023E
IPL							
Regulatory ROE (Avg)	9.2%	9.8%	9.0%	9.0%	9.3%	9.5%	9.7%
GAAP ROE (AVG)	8.4%	8.9%	8.5%	9.4%	9.5%	9.4%	9.2%
WPL							
Regulatory ROE (Avg)	10.5%	10.1%	10.1%	9.7%	9.9%	9.9%	10.0%
GAAP ROE (AVG)	10.1%	10.3%	10.3%	9.8%	10.4%	11.0%	11.4%
ATC							
Earned ROE	10.5%	10.8%	10.5%	10.5%	10.5%	10.5%	10.5%

Source: BofA Global Research, Bloomberg

Valuation

We update the peer multiple to 17.1x for electric. We reiterate Buy with a $54.50/sh PO.

Table 7: LNT updated SOTP

2022E SotP Analysis - BofAe										
All figures in USD millions except per share										
Regulated Utilities	2022 Net Income	EPS	P/E Multiple					Equity Value		
			Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric			-	17.1x	-	-	-	-	-	-
Group EPS '18-'22 CAGR - Electric			-	5.00%	-	-	-	-	-	-
			-	-	-	-	-	-	-	-
Relative Utility Group P/E Multiple				18.0x						
IPL	$376	$1.50	19.0x	18.0x	2.0x	20.0x	21.0x	$7,135	$7,512	$7,888
WPL	$284	$1.13	20.0x	18.0x	3.0x	21.0x	22.0x	$5,669	$5,953	$6,237
ATC (LNT Share)	$37	$0.15	19.0x	18.0x	2.0x	20.0x	21.0x	$699	$736	$773
EPS (w/o Parent)	$697	$2.78						$13,504	$14,201	$14,898
Parent NI	-$7	-$0.03	18.0x	18.0x	1.0x	19.0x	20.0x	($132)	($140)	($147)
Add Back: Parent Interest Exp	$14	$0.05	18.0x	18.0x	1.0x	19.0x	20.0x	$245	$129	$272
Less: Parent Debt (Term Loan AEF)					*50% weighting*			($500)	($500)	($500)
								($388)	($511)	($375)
Total Implied			19.0x			19.8x	21.0x	$13,116	$13,690	$14,523
Shares Outstanding (2022E)								251	251	251
Total Equity Value Per Share								$52.00	$54.50	$58.00
Total Return Analysis										
Price Objective									$54.50	
Implied Return									7.60%	
Dividend Yield									2.80%	
Total Return									10.40%	

Source: BofA Global Research, Bloomberg

Ameren (AEE)

Among the positive drivers we see for Q2 is normalization of weather from 2019, partially offset by cooler weather as expressed by Heating Degree Days (HDDs), though this impact is tempered by fewer Cooling Degree Days (CDDs) both y/y and vs. normal. We estimate the positive impact from new rates in MO effective Apr 1 as 7 cents based on a pre-tax revenue net of fuel estimate of $83m, of which AEE is expected to realize ~80% during 2020 and which we assume is spread proportionally through the year. Normalization to account for a Callaway outage in 2019 would represent a further 8 cent uplift. We estimate 8 cents positive impact from O&M, which is roughly evenly split between Company Owned Life Insurance (COLI) benefit and additional non-fuel O&M savings included in the MO order (~5 cents each), offset partially by 2 cents of additional O&M inflation as per AEE's original guidance. On the negative side of the ledger we estimate 7 cents associated with COVID-19 impact relative to the company's expectation of 10 cents drag for the year given that MO began lifting its stay at home orders in early May. We also see 2 cents of interest expense as Ameren MO issued $465m at 2.95% in late Q1 and AEE issued $800m at 3.50% in early Q2, though only $435m of these issuances were allocated to refinancing with the remainder representing incremental interest expense. We also reflect proportional impact of an estimated 2 cent effect from higher bad debt expense, as well as a partial offset resulting from the Federal Energy Regulatory Commission (FERC) ROE ruling which effectively raised Ameren Transmission Company of Illinois's (ATXI) authorized ROE by 14 bps (~1 cent impact annualized). We estimate AEE EPS at $0.86/sh for Q2, slightly above $0.84/sh consensus estimates; we see upside risk to Street estimates as they are updated to fully reflect Q2 drivers, in particular the constructive MO rate ruling.

Q2 earnings walk

Table 8: AEE Q2 walk

Ameren 2Q20 Earnings Walk	Notes	EPS
2Q19 EPS		$0.72
Return to normal weather	Mild	$0.06
2Q20 weather impact	Cooler weather y/y	($0.04)
AEE Illinois		
IL Electric	2019 Average 30 YR UST was 2.75% vs. Current @ 1.431%	($0.02)
IL Gas		$0.01
IL Transmission/Dist./ATXI	Ratebase growth largely balanced by ROE change	$0.01
AEE Missouri		
New Rates	Effective 2Q20	$0.07
Callaway refueling		$0.08
PISA Benefit		$0.00
MEEIA Benefits	2020 impact weighted to 2H	$0.00
O&M, Other	Lower O&M over the year (a change for 2Q)	$0.08
Interest Refinancings	Two refis in Q2	($0.02)
Parent Company income tax exp		$0.00
Dilution	Dividend reinvestment plan and employees - $100Mn/yr	($0.00)
COVID-19	Reduced demand (2Q lift in May)	($0.07)
Other	Bad debt (2c for the year) & FERC (14bps adder)	($0.01)
2Q20E BofA Adjusted EPS		$0.86
2Q20E BofA Modeled EPS		$0.86
2Q20 Consensus		$0.84
BofA 2020E EPS		$3.45
2020 Consensus		$3.42
2Q19 Shares outstanding		247
2Q20 Shares outstanding		248

Source: BofA Global Research estimates, Bloomberg

Framing the latest debates and items to watch

We catch up on the latest moving parts across AEE's territory ahead of the Q2 call.

MO rate case a positive near term, appears underappreciated by investors

Among the key takeaways from the recent MO rate case settlement, in our view, are a reduction in revenues of -$32m, and a further reduction of fuel cost expenses (-$115m) and other costs by an additional -$50m. The net impact on an annualized basis is +$133m given AEE's ability to effectively manage these costs. With rates taking effect April 1st AEE should realize a partial year impact in 2020 - we calculate the annual impact of this result is $0.40/sh, or a 2020E impact of $0.30 (previously reflected in our estimates). Given the constructive nature of this rate case outcome, we think AEE is unlikely to seek to file another rate case in 2020. We believe the key considerations in terms of timing remain the impact of COVID-19-related shutdowns on lost sales and additional expenses as well as the placement of additional wind assets into service. The Street consensus estimates are anchored toward the low end of mgmt.'s guidance range following Q1 reporting and the outbreak of COVID-19 – though we believe a constructive rate case outcome could provide AEE with an O&M tailwind going into H2, with potential for an upside surprise to full-year results.

700 MW wind projects in service in late '20/early '21

AEE MO is adding 700 MW of wind generation to its fleet in two tranches: a 400 MW facility expected to be in service by year end 2020 and a second 300 MW facility which is largely expected to be in service in 2020 with approx. $100m of assets in Q1 2021. Prior to being added to AEE's rates as part of a rate case, the projects qualify for a partial return under the MO Plant in Service Accounting (PISA) framework and existing renewable rider. MO's PISA mechanism allows the wind assets that are placed into service to earn a partial return until a formal rate case: AEE plans to defer 85% of the depreciation on the newly installed project and earn a debt return on the non-equity portion of the assets placed in service, with the remaining 15% depreciation qualifying for cash recovery under the existing renewable rider. While the company would not receive full recovery until its wind projects are added to rates, we note the PISA mechanism allows for partial recovery – likewise the expected filing date for a new rate case in the first half of 2021 is not significantly later than prior indications from mgmt.

Next filing in MO – looking like '21

Given the announced in-service timing of the wind assets, the constructive rate order received earlier this year, COVID-19 uncertainty likely to persist through the balance of 2020, and ability to earn an interim return on newly-installed wind assets, we expect AEE to file its next case sometime in 1H21 at the earliest. We believe this is largely reflected in Street estimates as the company has continued to refrain from providing specifics as to its rate case filing strategy while highlighting the need to place its wind assets in service as well as account for COVID-19 uncertainty.

IL legislation – potentially post-Nov election

While the 2020 IL spring legislative session passed without action taken on the Downstate Clean Energy legislation, we note additional opportunities for action in the coming months. The state typically holds a veto session in October or November, with potential for this session to fall after state and national elections are held. The following opportunity if no action is taken during the veto session is a lame duck session held in January, prior to the seating of the new group of legislators. Our estimates reflect the current ROE base rate of 580 basis points with the potential of an additional 100 bps in the event of passed legislation representing upside risk.

30Y UST rate visibility is limited, we assume a more conservative stance

We tweak our forecast for the 30Y UST lower by 15-25 bps across 2021-25, with our updated forecast rates remaining below 2% until 2025 when they reach 2.20%. We perceive limited visibility of Street consensus estimates of long-term rates beyond 2021

and see little consensus among investors. Accordingly we adjust our forecast to reflect a "lower for longer" outlook, which we see as appropriate given the path of rates of late and Fed signaling long-term support for the economy in the wake of COVID-19.

IRP coming in Sep, will mgmt. deliver on further retirements?

AEE's next triannual MO IRP filing is due in Oct with the company expecting to file in Sep. Likely of particular interest among investors are prospects for the announcement of additional coal retirements other than Meramec, which is scheduled for retirement in 2022. The 2017 filing gave planned retirement dates for Sioux and Labadie as 2033 and 2036, respectively – though we see potential for one of these to be accelerated (note Sioux and Rush Island have the lowest levels of undepreciated rate base of AEE's fleet at $0.5B and $0.6B, respectively). AEE's decision on whether it accelerates retirements of unscrubbed coal is partially tied to the unresolved 8th Circuit Case (i.e. appealing the EPA Clean Air Act mandate) and partially tied to a lack of securitization legislation. Some coal experts have questioned whether the company would rush to accelerate the retirement of the fleet if the case were still pending. In the event that the company did pursue accelerated retirement in its IRP before case resolution, we could see Labadie as a more likely target since it faces just sulphur dioxide controls rather than Rush Island's bigger violation. On the other hand, if the 8th Circuit Case were resolved and AEE's plants were ordered to install scrubbers, this hundreds of million dollar requirements could make the plants uneconomic and more ripe for accelerated retirement. We believe additional potential hurdles could be in the form of lack of securitization legislation as well as sensitivity around potential job reductions, particularly in the wake of the COVID-19 outbreak.

EVRG process: clarity should drive re-rating in AEE

Our most recent accretion analysis as well as feedback from our conversations with stakeholders in both MO and Kansas (KS) suggest that while AEE has been linked to the Evergy (EVRG) strategic process in media reports, the company is likely not a front runner were it to secure a bid. In particular, we see potential for resistance from environmentally-aligned interveners in both KS and MO should AEE emerge as the winning bidder – given EVRG's coal-heavy fleet and AEE's own slow adoption of renewables and unscrubbed legacy generation, we think there could be less potential opposition to an EVRG bidder with a proven track record of accelerated coal retirements and renewable transition. Some investors appear to have largely focused on other names such as NextEra Energy (NEE) as potential bidders, and we could see a modest degree of drag in AEE shares associated with the possibility of its participation in a protracted bidding process. We attribute much of the recent pressure on AEE shares to these concerns – and clarity on EVRG strategic direction in 2H could potentially drive relative outperformance of AEE shares.

Evergy, Inc: AEE linked to strategic review in news; looking at dilution from possible AEE bid 17 June 2020

Updated estimates

We see a positive skew to Street consensus estimates for 2020, particularly driven by the positive MO rate order which went into effect on Apr 1. As COVID-related shutdowns and resulting load shifts continue to pressure utilities into Q3, we believe the O&M portion in particular of the MO order could provide a key near-term tailwind. We detail our tweaked assumptions below.

- **Raising MO ROE forecast in '20 to reflect O&M savings.** We raise our EPS estimate by 3 cents to $3.45 for 2020 driven by an earned ROE of 9.8% in MO (upper end of 9.4-9.8% authorized range). We remain confident in mgmt's ability to execute.

- **Assuming a more conservative 30Y UST forecast in IL.** We tweak our forecast for the 30Y UST, reducing our forecast for yields (and corresponding IL authorized ROE) by 20-25 bps across the 2021-25 timeframe – in line with our forecast for EXC's ComEd - such that our forecast yield remains below 2% until 2025.

- **Reflecting 10.02% base ROE for transmission.** We tweak the authorized ROE at the ATXI segment to reflect the latest FERC order, reflecting a base rate of 10.02% plus 50 bps adder through the forecast. This effectively increases our estimates by ~1 cent annually through the forecast period.

We make additional tweaks to our earned ROE forecast, assuming that MO remains near the high end of its authorized range through the forecast period. We believe our forecast embeds relatively conservative assumptions – in particular in IL where we apply a more punitive UST forecast and do not reflect potential upside from possible legislation resulting in a 100 bps adder to the base authorized electric ROE. With these assumptions in place our forecast has an EPS CAGR that declines to below the midpoint of the 6-8% guidance range through 2024, though we see upside risk to our estimates as detailed above.

Table 9: Updated estimates

Consolidated Projections	2019A	2020E	2021E	2022E	2023E	2024E	2025E	Segment CAGR ('20-'24E)	Segment CAGR ('19-'24E)
Ameren Missouri	$1.72	$1.86	$2.06	$2.18	$2.28	$2.38	$2.48	6.41%	6.68%
Ameren Illinois	$1.39	$1.34	$1.46	$1.63	$1.79	$1.99	$2.19	10.36%	7.43%
ATXI	$0.32	$0.32	$0.31	$0.30	$0.29	$0.29	$0.28	-2.92%	-2.43%
Other	-$0.09	-$0.07	-$0.07	-$0.07	-$0.07	-$0.07	-$0.06		
Total EPS	$3.35	$3.45	$3.76	$4.05	$4.30	$4.59	$4.88	7.01%	6.50%
Guidance		*$3.40-3.60*							8.70%
EPS CAGR off 2020 ($3.50)			7.47%	7.52%	7.11%	7.01%	6.87%		
YoY Growth	-0.53%	2.97%	9.02%	7.57%	6.30%	6.72%	6.31%		
Prior Estimates	*3.35*	*3.42*	*3.70*	*3.99*	*4.27*	*4.61*	*4.91*		
Consensus	$3.29	$3.42	$3.76	$4.05	$4.32	$4.47		6.31%	6.33%
Average Earned ROE (Auth in parenthesis)									
Missouri (Auth: electric 9.4-9.8%, gas 9.4-9.95%)	10.3%	9.8%	10.3%	9.8%	9.8%	9.8%	9.8%	9.8%	9.8%
Illinois (Auth: electric 580bps + 30yr T, gas 9.87%)	10.0%	8.8%	10.0%	8.8%	9.0%	9.2%	9.2%	9.3%	9.4%
BofA 30-yr Treasury assumption		*1.50%*		*1.50%*	*1.50%*	*1.60%*	*1.70%*	*1.95%*	*2.20%*
ATXI (10.02% plus 50bps adder)	10.82%	10.52%	10.82%	10.52%	10.52%	10.52%	10.52%	10.52%	10.52%
Consolidated FFO/Debt	20.9%	18.0%	18.4%	18.5%	18.6%	18.8%	19.2%		
Guidance (6-8% '20-'24 off of $3.50) --> *Midpoint*		$3.50	$3.75		$3.50	$3.75	$4.01	$4.29	$4.59
Low Implied		$3.50	$3.71	$3.93	$4.17	$4.42	$4.68		
High Implied		$3.50	$3.78	$4.08	$4.41	$4.76	$5.14		

Source: BofA Global Research estimates, Bloomberg

Valuation

We reiterate our Buy rating on AEE. We embed a more conservative set of assumptions around UST rates, and remain well within mgmt.'s guidance range while seeing potentially upside looking ahead. We believe shares of AEE could continue to outperform vs. the peer group driven by near-term catalysts including the expected IRP filing, IL legislation potential, and updated long term plan which the company historically provides with Q4 results. We raise our PO to $79 from $75 to reflect the updated Electric peer group multiple of 16.3x and our tweaked estimates. Reiterate Buy on solid +6-7% EPS growth through our forecast period as we believe AEE is one of the better-positioned names in our coverage universe.

Table 10: SOTP valuation

Ameren Sum of the Parts Valuation - 2022E									
All figures in $Mn except per share									
Regulated Utilities	2022E EPS	P/E Multiple					Equity Value		
		Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric		-	16.3x	-	-	-	-	-	-
Group EPS '18-'22E CAGR - Electric		-	5.00%	-	-	-	-	-	-
		-	-	-	-	-	-	-	-
		-	17.1x	-	-	-	-	-	-
Ameren Missouri	$2.18	18.1x		2.0x	19.1x	20.1x	$39.57	$41.75	$43.93
Ameren Illinois	$1.63	19.1x		3.0x	20.1x	21.1x	$31.10	$32.73	$34.36
Ameren Transmission (ATXI)	$0.30	16.1x		0.0x	17.1x	18.1x	$4.87	$5.17	$5.47
Parent/Unallocated Items	-$0.07	16.1x		0.0x	17.1x	18.1x	-$1.08	-$1.15	-$1.22
Total Implied Utilities	$4.05						$74.45	$78.50	$82.55
Shares outstanding	263								
Implied P/E		19.5x							
Valuation								$79.00	
BofAe Implied Multiple								19.5x	
PO								$79.00	
Upside/downside potential								7.7%	
NTM Dividend Yield								2.70%	
Total potential return								10.6%	

Source: BofA Global Research estimates, Bloomberg

American Electric Power (AEP)

We forecast a strong 2Q20 with EPS of $1.07 vs. $1.00 in 2Q19 and $1.02 consensus, driven primarily by previously announced 2020 O&M savings in addition to $100mn COVID-related cost savings (most of these, however, will likely be temporary in nature). Weather should also likely provide some uplift. A Transmission HoldCo true-up in 2Q should be effectively offset at the VIUs and T&D utilities (by rate changes, etc.). North Central should be on schedule with the latest PUCT decision; despite the TX rejection, AEP will reallocate MW to SWEPCO's LA and AR customers and will proceed with the full 1485 MW project. We highlight concerns of over-equitizing North Central, given guidance for 50-66% equity; we now assume he high end of this range. However, the possibility of Kentucky asset sales for further equity could provide upside; we accordingly adjust for a 2x premium in our SOTP to the Kentucky Power breakout. The one-year PTC extension should act as a safeguard if there are any delays for the final two wind farms, although no delays currently expected vs. the current YE-21 timeline). We watch progress on rate cases including Kentucky Power (filed June 29th, with procedural schedule starting in early Nov, 6-month timeline, new rates could go into effect YE-21), AEP Ohio (base rate case filed June 1st, expected one-year procedural schedule), and APCo Virginia (filed March 31st, still in initial stages, with intervenor testimony on July 30th). It would seem strategic action on utilities is still dependent on the outcome of its pending rate cases. While more equity from North-Central to be disclosed formally in its cash flow outlook could be cautious, much better clarity on where it stands on its 5-7% EPS CAGR could be the bigger (offsetting) positive. Maintain Neutral.

2Q20 Earnings Walk

We estimate EPS of $1.07 for 2Q20. This compares to $1.00 in 2Q19 and consensus of $1.02.

- **Drivers:** Aside from weather, we anticipate a strong 2Q will be driven by 2020 planned O&M savings in addition to $100mn COVID-related cost savings (the majority of which will likely be non-recurring). Expect a Transmission HoldCo true-up in 2Q to be effectively offset by rate changes at OH, TX, and by the VIUs (transmission revenues).
- **Other:** A number of 2020 full-year items are weighted heavier towards 2Q. This includes COVID-related wholesale load impact (mostly in 2-3Q), 2020 O&M savings (mostly after 1Q), Texas carrying charges (a 2Q item, reversal of 2Q19), and a Transmission HoldCo true-up (a 2Q item).
- **Wildcard:** Weather should likely prove a positive with a reversion to more normalized weather from weak 2Q19 weather, in addition to more favorable weather in 2Q20.

Table 11: AEP 2Q20 Earnings Walk: nice sized beat

American Electric Power 2Q20 Earnings Walk	EPS
2Q19 adjusted earnings	$1.00
Vertically Integrated Utilities	$0.11
Wholesale/Normal Load	($0.05)
Rate Changes	$0.03
Weather	
Return to Normal	$0.01
Current Quarter	$0.02
Transmission revenues	$0.06
O&M	$0.09
Depreciation and Other	($0.04)
Int/AFUDC	$0.00
Other	($0.01)
Trans./Dist. Utilities	$0.01
Rate Changes (AEP Ohio, TX DCRF)	$0.03
OH Legacy Riders	($0.01)
OH Reg Prov	$0.00
Weather	
Weather (Texas) Normalization	$0.00

Table 11: AEP 2Q20 Earnings Walk: nice sized beat

American Electric Power 2Q20 Earnings Walk	EPS
Weather (Texas) Impact	$0.00
AEP TX transmission revenues (T-cost filings pre-ratecase)	$0.00
O&M	$0.06
TX Carrying Chgs	($0.03)
Depreciation and Other	($0.02)
Other Taxes	($0.02)
Other/AFUDC	($0.00)
Transmission Holdco	($0.05)
Investment growth (ahead of schedule)	$0.04
O&M	$0.00
True-Up	($0.09)
Other	$0.01
Generation and Marketing	$0.01
Corporate/Other	($0.01)
Dilution	($0.00)
2Q20E Adjusted EPS	$1.07
2Q20 BAML EPS	$0.98
2Q20 Consensus	$1.02
2020 BAML EPS	$4.23
2020 Consensus	$4.28
2020 Guidance	4.25-4.45

Source: BofA Global Research Estimates

North Central: Moving forward despite TX rejection

AEP has received its final regulatory decision for its multi-state 1485 MW North Central wind project and can now move ahead with its construction plans. The Public Utility Commission of Texas (PUCT) rejected SWEPCO's request to acquire a 54.5% stake in Invenergy's three wind North Central Energy Facilities. AEP's subsidiary PSO (Public Service Company of Oklahoma) will be acquiring the remaining 45.5% equity interest in the wind farms. AEP reaffirmed its plans to develop close to 1,500 MW of wind capacity in OK despite the TX rejection. SWEPCO and PSO already have received approval from AR, LA, and OK regulators, as well as from FERC. The wind farms to be owned by AEP include Traverse Wind (999 MW), Maverick Wind (288 MW), and Sundance Wind (199 MW); all three are expected to complete construction within the next two years. With the TX rejection, capacity will be allocated with 464 MW to SWEPCO's Louisiana customers, 268 MW to SWEPCO's Arkansas customers, 78 MW to SWEPCO's wholesale customers, and 675 MW to PSO's customers. On balance, this is not a meaningful setback and was somewhat anticipated given the prior pushback from the PUCT.

Concerns of over-equitizing North Central Wind

We highlight recent concerns of AEP potentially over-equitizing the North Central Wind project, following prior mgmt commentary of expectations for 50-66% equity financing. While we had previously assumed 50% equity, we now assume 66% equity/34% debt for a more conservative approach. Timing of equity needs should align with wind farms going into service; the bulk of the needs will be in 2021 (~$1.7bn capex of the $2bn total). Note that we also update our projections to reflect a shift in MW allocation to SWEPCO – AR and SPEPCO – LA, following the PUCT rejection in Texas.

For 2Q, we expect to see updated guidance on equity and capex for North Central, following a 1Q decision to defer $500mn of capex out of 2020; this update (deferral year) should be made with 2Q results. We continue to assume $2bn capex for the project, with 66% equity financing (previously 50%). Expect AEP's next published capex forecast to include North Central Wind.

We see upside, however, from the possibility of Kentucky asset sales for further equity. We thus now include a 2x premium to the Kentucky Power breakout at the VIUs in our SOTP valuation (KY Power contributes $3.40/sh to valuation).

Estimating North Central's EPS Contribution

Below we include our latest earnings impact from the North Central Wind project. We assume the company earns a regulated return based on each subsidiary's equity ratio and ROE, indicating a $13mn Net Income impact in '21 (since just 200MW would be slated to come online by year-end) and $95mn in '22. Our equity need calculation now assumes 66% equity financing for the project, and we'd expect $0.17/sh of EPS impact when the full project is online (i.e. starting in '22).

The first wind farm to be constructed in '20 will receive the 100% PTC, while the other two wind farms to be constructed by YE-21 will receive the 80% PTC. The one-year PTC extension should act as a safeguard if there are any delays at the second two wind farms.

Exhibit 2: North Central EPS Impact

North Central EPS impact	2021	2022	2023	2024	2025
Wind Additions MW	199	1485	1485	1485	1485
PSO	*90*	*675*	*675*	*675*	*675*
SWEPCO - AR	*36*	*268*	*268*	*268*	*268*
SWEPCO - LA	*62*	*464*	*464*	*464*	*464*
SWEPCO - TX	*0*	*0*	*0*	*0*	*0*
SWEPCO - FERC	*10*	*78*	*78*	*78*	*78*
Assumed Capex $M	268	1997	1997	1997	1997
Ownership Interest	100%	100%	100%	100%	100%
Equity Ratio	50%	50%	50%	50%	50%
PSO	*49%*	*49%*	*49%*	*49%*	*49%*
SWEPCO - AR	*48%*	*48%*	*48%*	*48%*	*48%*
SWEPCO - LA	*52%*	*52%*	*52%*	*52%*	*52%*
SWEPCO - TX	*43%*	*43%*	*43%*	*43%*	*43%*
SWEPCO - FERC	*50%*	*50%*	*50%*	*50%*	*50%*
ROE	9.6%	9.6%	9.6%	9.6%	9.6%
PSO	*9.4%*	*9.4%*	*9.4%*	*9.4%*	*9.4%*
SWEPCO - AR	*9.5%*	*9.5%*	*9.5%*	*9.5%*	*9.5%*
SWEPCO - LA	*10.0%*	*10.0%*	*10.0%*	*10.0%*	*10.0%*
SWEPCO - TX	*9.4%*	*9.4%*	*9.4%*	*9.4%*	*9.4%*
SWEPCO - FERC	*10.0%*	*10.0%*	*10.0%*	*10.0%*	*10.0%*
NI $M	13	95	95	95	95
Shares outstanding	499	520	531	534	538
Total Equity Needed ($M)	177	1318	1318	1318	1318
Issuance Price (current price)	87.5	87.5	87.5	87.5	87.5
Incremental Shares outstanding (mn)	2.0	15.1	15.1	15.1	15.1
Dilution %	0.4%	2.9%	2.8%	2.8%	2.8%
New Shares outstanding	501	535	546	550	553
EPS	0.03	0.18	0.17	0.17	0.17

Source: BofA Global Research estimates

Rate cases: Kentucky Power, APCo Virginia, AEP Ohio

Kentucky Power filed a rate case on June 29th requesting a ~$70mn rate increase at a 10.0% ROE (43.25% equity ratio). AEP expects to receive a response in June, with a procedural schedule starting in early November and new rates likely going into effect by YE-21. The timing could line up with the $1.7bn investment needs for North Central.

APCo Virginia filed a rate case on March 31st, requesting ~$65mn rate increase at a 9.90% ROE (50.31% equity ratio). This filing is still in the initial stages of the procedural schedule, and is expected to kick off with intervenor testimony on July 30th.

AEP Ohio filed a base rate case on June 1st, requesting a ~$400mn rate increase at a 10.15% ROE (54.43% equity ratio). Expect the OH procedural schedule to be roughly a year in length (in line with historical trends).

Signs PPA for 400 MW IL wind project

AEP Energy recently signed a PPA with CIP (Copenhagen Infrastructure Partners) for production of the 400 MW Panther Grove Wind Energy Facility in IL. Construction of the wind farm will start in early 2021, with COD (commercial operation date) expected in late 2022. The PPA will be secured to serve C&I customers, such as Google, looking to source clean energy for retail supply.

ApCo issued RFPs to procure 50MW solar

AEP subsidiary Appalachian Power Co. recently issued RFPs for 50MW solar capacity in West Virginia with projects having a minimum bid capacity of 10MW and in-service date of 15 December 2022, besides the projects should be located in West Virginia and interconnected to Appalachian Power's West Virginia distribution system or to the PJM Interconnection market to qualify for the federal investment tax credit. The deadline for bid submission is Aug 6 2020. This was not unexpected. We also look for parallel efforts in WV by Mon Power/FE on its future generation resource needs as well.

EPS Estimates

We provide our latest EPS estimates for AEP below.

Exhibit 3: AEP EPS Estimates

EPS	2017A	2018A	2019E	2020E	2021E	2022E	2023E
APCo	$0.67	$0.73	$0.78	$0.79	$0.82	$0.83	$0.87
I&M	$0.38	$0.53	$0.51	$0.52	$0.55	$0.54	$0.55
SWEPCO	$0.25	$0.30	$0.37	$0.36	$0.38	$0.40	$0.43
PSO	$0.15	$0.17	$0.25	$0.24	$0.27	$0.30	$0.32
Other Utes (incl. KY)	$0.17	$0.27	$0.24	$0.24	$0.24	$0.24	$0.25
KY break out	$0.13	$0.14	$0.15	$0.16	$0.17	$0.17	$0.17
North Central Wind					$0.03	$0.18	$0.17
Vertically Integrated	$1.64	$2.00	$2.17	$1.91	$2.28	$2.32	$2.42
Guidance		$2.00	$2.17	$2.19			
Ohio	$0.66	$0.66	$0.67	$0.58	$0.63	$0.64	$0.67
Texas	$0.39	$0.41	$0.41	$0.43	$0.52	$0.59	$0.63
T&D	$1.01	$1.05	$1.00	$1.01	$1.15	$1.23	$1.30
Guidance		$1.05	$1.00	$1.03			
Transmission HoldCo	$0.72	$0.75	$1.05	$1.10	$1.17	$1.26	$1.34
Guidance		$0.75	$1.05	$1.08			
AEP Energy Supply	$0.30	$0.29	$0.30	$0.32	$0.21	$0.23	$0.24
Guidance		$0.29	$0.30	$0.35			
Corp & Eliminations	$0.01	($0.14)	($0.28)	($0.33)	($0.30)	($0.28)	($0.21)
Guidance		($0.14)	($0.28)	($0.30)			
Consolidated EPS without North Central	$3.68	$3.95	$4.24	$4.25	$4.51	$4.76	$5.09
CONSOLIDATED EPS with NORTH CENTRAL WIND	$3.68	$3.95	$4.24	$4.25	$4.53	$4.94	$5.26
EPS Growth (%)		*7.5%*	*7.3%*	*0.1%*	*6.8%*	*9.0%*	*6.5%*
Previous EPS (without North Central)	*$3.68*	*$3.95*	*$4.24*	*$4.25*	*$4.52*	*$4.83*	*$5.16*
Consensus		$3.93	$4.22	$4.28	$4.63	$4.99	$5.32
BAMLe CAGR without North Central (vs '18 mid)			10.2%	5.0%	5.4%	5.5%	5.7%
BAMLe CAGR with North Central (vs '18 mid)			10.2%	5.0%	5.6%	6.4%	6.5%
Annual Guidance	3.55-3.68	3.88-3.98	4.14-4.24	4.25-4.45			
Guidance: 5-7% EPS CAGR off of '18 (or '19 orig midpt)		$3.85	$4.19	$4.35	$4.59	$4.86	$5.15
Low			$4.14	$4.25	$4.46	$4.68	$4.91
High			$4.24	$4.45	$4.72	$5.05	$5.40
Share Count	492	493	494	496	499	520	531

Source: BofA Global Research Estimates

Valuation: Maintain Neutral, raise PO to $88

We maintain our Neutral rating and raise our Price Objective to $88 from $80. We update for the regulated peer ute multiple of 17.1x (previously 15.3x), which is the main driver of the PO change. We additionally now include a 2x premium for the Kentucky Power break out valuation. We tweak our estimates for North Central and also now reflect the associated equity issuance for the project (BofA ests at 66% equity financing up from prior 50%) for '21 and '22 (majority in '22, tied to construction needs). This implies <$1/sh accretion from the North-Central asset build now.

Exhibit 4: AEP SOTP Valuation

AEP SoTP	2022 EPS				P/E Multiple	Premium/ Discount	Value ($mn)	Value ($/Sh)
Group Peer Multiple - Electric					17.1x			
Group EPS '18-'22 CAGR - Electric					5.00%			
Vertically Integrated Utilities (SWEPCO, PSO, APCo) excl KY	$2.15				18.0x	0.0x	$20,073	$38.6
Kentucky Power break out	$0.17				18.0x	2.0x	$1,746	$3.4
T&D Utilities (Principally D) - TNC/TCC, Ohio Power	$1.23				18.0x	1.0x	$12,159	$23.4
Transmission-Only Utilities - Mostly FERC	$1.26				18.0x	1.0x	$12,374	$23.8
Parent & Other - Principally HoldCo Debt	($0.28)				18.0x	0.0x	($2,606)	($5.0)
Total Regulated & HoldCo Value	$4.53						$43,745	$84.2
Renewables								
Legacy Energy Supply + Marketing/ Increasingly Renewables	$0.23				18.0x	-3.0x	$1,789	$3.4
Total AEP Equity Value - Existing Assets								$87.6
Upside	2022E EPS (or discounted)	Capex	FFO	Earnings Impact (50% Equity)	P/E Multiple	Premium	Probability Weighted	
SWEPCO 1200MW RFP - in service '21 (mostly 80% PTC)	0.09	1,089	$75		18.0x	0.0x	100%	$1.7
PSO 1000MW RFP - in service '21 (mostly 80% PTC)	0.07	908	$55		18.0x	0.0x	100%	$1.3
Total	0.16	1,997						3.0
Probability-Weighted EPS	0.17							
Discount Factor by year	10%							
Total Capex (probability weighted)				1,997				
Total Equity Needed ($M) (assuming 50%)				1,318				
Issuance Price (current price)				87.51				
Shares Issued (mn)				15				
Dilution %				3%				
Value Dilution				($1,268)			($1,268)	($2.4)
Shares Outstanding								520
Total Equity Value Per Share								$88.0
							Price Appreciation	0.6%
							+2020 Dividend Yield	3.1%
							Total Return	3.7%

Source: BofA Global Research Estimates

American Water Works (AWK)

Amid the evolving COVID pandemic, we expect continued execution by AWK with their inaugural ten year capital forecast of $20-22Bn intact. We have less concerns on the margin around bad debt given ten of their fourteen states have already adopted accounting orders or other recovery mechanisms. We don't perceive any meaningful delays in spend or regulatory filings (albeit note the timing shift for new rates to take effect for NYAW) and remain confident in the management team following recent succession. Further acceleration in muni consolidation remains a critical tailwind out of recovery without any meaningful infrastructure bill materializing. While we appreciate the scarcity element and higher sustained investment trajectory for the subsector, we ultimately see the steep premium as unwarranted. We maintain our Underperform rating.

AWK 2Q20 Earnings Walk

We forecast 2Q20 adjusted EPS of $0.97, slightly above consensus and a $0.03 uptick y/y.

- **Key Drivers:** The primary positive drivers y/y are new rates implemented across a number of states in their footprint as well as various infrastructure surcharges. Weather tailwinds y/y and cost savings should help offset any COVID impacts and the reversal of gain on sale in the prior period, while MBB will have contribution from the new military bases.

Table 12: AWK 2Q20 Walk

AWK 2Q20 Earnings Walk		EPS
AWK 2Q19 EPS	$	0.94
Regulated		0.06
Infra Charges, Rate Cases & Step Increases		0.08
Depreciation		-0.02
COVID Challenges offset by Weather & O&M		0.00
MBB		0.02
Parent		-0.05
Interest/Other Impact		-0.02
Legacy Gain Last Year		-0.03
2Q20 BofAe Adjusted EPS	$	0.97
Consensus		$0.96
BofAe 2020 EPS	$	3.85
Guidance		3.79-3.89
2020 Consensus		$3.84

Source: BofA Global Research, Bloomberg

Reg., Leg., Muni & Military Prospects

We see AWK as particularly poised to execute on their LT plan despite the ongoing COVID pandemic. Earlier this year, the company announced a 10% dividend increase, in line with their targeted payout ratio of 50-60% and their targeted high end of the 7-10% outlined range. Along with continued regulatory filings – the company recently announced that Pennsylvania American Water filed a rate case request with the Pennsylvania Public Utility Commission for rates over a two-year period – we see the developments as affirmation by the company around their ability to manage through the crisis with its plan largely intact. With a largely resi customer base, bad debts have been our principal concern on the margin for water utilities. That said, we note accounting orders or mechanisms from the commission around recovery already in ten of the 14 states in which they operate, with discussions ongoing in all of their jurisdictions.

Following military business wins at San Antonio and West Point, both are now fully operational with contribution starting in 2Q and no delays despite the ongoing pandemic. Five other military bases remain potential candidates, with two to three expected to be awarded sometime during 3Q. Outside of the military business, we

expect some drag on new partnerships for Homeowners services – the other component of AWK's non-regulated business.

Meanwhile, municipal opportunities continue to arise despite the crisis, and we perceive particular acceleration of opportunities given the latest financial strain on munis from the pandemic shock – particularly if no infra bill or lifeline materializes.

We reiterate our Underperform rating on AWK shares given the steep premium vs. electric & gas peers.

EPS Estimates

The exhibit below reflects our latest EPS estimates with annuals remaining unchanged into upcoming results. We continue to expect sustained long term growth within their 7-10% LT EPS CAGR and 7% rate base growth longer term.

Table 13: EPS Estimates

AWK	2019A	2020E	2021E	2022E	2023E
Earnings Metrics					
Regulated Water EPS	3.60	3.84	4.19	4.43	4.66
Market Based EPS	0.45	0.47	0.51	0.53	0.57
Parent and Other EPS	-0.44	-0.46	-0.43	-0.40	-0.36
Adjusted EPS	3.61	3.85	4.27	4.56	4.87
Consensus	3.61	3.84	4.21	4.54	4.95
Guidance	3.56-3.64	3.79-3.89			
Previous BofA Adj. EPS	3.61	3.85	4.27	4.56	4.87

Source: BofA Global Research, Bloomberg

Valuation

The exhibit below reflects our latest valuation: We mark to market our valuation for the latest water utility multiple of 26.9x (vs. 26.3x), with our PO shifting to $135 (vs. $133). We maintain our Underperform rating given the large premium vs. electric & gas peers, which we see as unjustified given its only modest relative growth premium.

Table 14: SOTP

Water Utilities	2022 EPS	P/E Multiple					Equity Value		
		Peer	Prem/ Discount	Low	Base	High	Low	Base	High
AWK Earnings		26.9x							
Group EPS '18-'22 CAGR		8.30%							
Water Utilities		29.1x							
NJ	$1.12		3.0x	31.1x	32.1x	33.1x	$34.86	$35.98	$37.10
PA	$1.27		3.0x	31.1x	32.1x	33.1x	$39.64	$40.91	$42.18
IL	$0.35		3.0x	31.1x	32.1x	33.1x	$10.80	$11.14	$11.49
MO	$0.50		2.0x	30.1x	31.1x	32.1x	$14.96	$15.46	$15.96
IN	$0.29		1.0x	29.1x	30.1x	31.1x	$8.46	$8.75	$9.04
CA	$0.19		-1.0x	27.1x	28.1x	29.1x	$5.16	$5.35	$5.54
Other	$0.71		0.0x	28.1x	29.1x	30.1x	$19.96	$20.67	$21.38
Regulated Water EPS	$4.43						$133.83	$138.25	$142.68
Parent/Other Drag	-$0.40		0.0x	28.1x	29.1x	30.1x	-$11.29	-$11.69	-$12.10
Market Based Business									
Military (40%)	$0.21	26.9x	-3.0x	22.9x	23.9x	24.9x	$4.87	$5.08	$5.29
Non Military (60%)	$0.32			11.0x	12.0x	13.0x	$3.51	$3.83	$4.15
Total Market Based Business	$0.53						$8.38	$8.91	$9.44
Valuation	$4.56						$131.00	$135.00	$140.00
Current Price as of 07/17/20								*$138.32*	
Dividend Yield								1.4%	
Total Return							-3.86%	-0.97%	2.65%

Source: BofA Global Research, Bloomberg

CMS Energy (CMS)

Into 2Q, we perceive the critical update for CMS to be around FY20 guidance both around the extent of ongoing pandemic load impacts as well as the ability to drive cost savings. With a stronger-than-expected 2Q with favorable weather offsetting 1Q headwinds and the ability to materialize cost savings, we expect heightened confidence around FY20 EPS from mgmt and expect CMS to more firmly reaffirm its FY20 guidance range of $2.64-$2.68 (though likely contingent upon no escalation in shutdowns from a potential pandemic resurgence). In particular, we see a comfortable cushion for CMS to meet the mid-point of its guidance range relative to consensus expectations for the low-end of the range as we raise our forecast to the mid-point of the range. We expect CMS to provide an update around run-rate load impacts in June. Further with mgmt confidence emphasizing ability to drive cost savings beyond historically demonstrated 15c offset, we expect CMS to provide greater details around the extent of cost savings. With cost savings sustained, we express CMS as better positioned around a potential increase in corp tax rates under a Dem win in Nov '20 elections, with mgmt confidence around offsets to maintain customer affordability and headroom to support capex. Indeed, we expect improved confidence into the 2Q call to further support CMS shares in light of the latest re-rating across the group to defensive premium utilities focusing on reliable earnings. Maintain Buy.

2Q20 EPS Walk: Favorable weather, softer COVID impact

We forecast 2Q20 adjusted EPS of $0.45 vs. $0.33 in 1Q19 and $0.36 consensus.

- **COVID load impact, eased from peak:** Among most meaningful negative y/y drivers are load impacts from COVID-19 shifts with shelter-in-place orders implemented in Michigan, particularly around C&I load noting 3-4c negative impact monthly based on electric load impact through April. Load impact has since halved into May and again into June with businesses mostly reopen (though many such as restaurants and bars are at 50% capacity). As such, we estimate ~7c drag from COVID load impacts for 2Q20 as a key negative y/y driver. *Expect an update around run-rate impact based on Jun/Jul trends on the 3Q call.*

- **Very 2Q favorable weather, offsetting 1Q weather headwind:** We highlight substantially favorable weather trends (9% higher CDDs relative vs. normal), which we estimate at an 8c uplift y/y (in-line with 2Q18) with higher HDDs earlier in the quarter as well driving another 1c uplift y/y (shoulder month). Further, we highlight additional positive driver of normalization of 6c/sh favorable weather in 2Q19.

- **Key drivers:** Among additional drivers include ~6c contribution from new gas rates effective Oct '19, offset by ~6c negative impact from D&A and interest (closing of larger projects drive up depreciation costs). With mgmt having emphasized its ability to drive 15c O&M flex spend to offset COVID load impacts (not a cap but rather historically demonstrated), we estimate ~5c per quarter positive impact. We estimate 2c negative impact at Enterprises/DIG given 6c delivered in 1Q20 already relative to 8-9c embedded within FY20 guidance, with mgmt noting management of the business such as timing of plant outages.

Table 15: CMS 2Q Walk

CMS Energy 2Q20 Earnings Walk		EPS
Adjusted EPS 2Q19	$	0.33
Utility		
Weather/Load		
Return to normal		$0.06
Current quarter		$0.09
COVID Load Impact		($0.07)
Rate Changes		
New gas rates effective Oct 2019		$0.06
Other		
D&A, Interest, Other expenses		($0.06)
O&M Flex Spend		$0.05
Cost savings		$0.01
Pension benefit normalization		$0.01
Parent interest		($0.01)
Enerbank Variance		$0.00
Enterprise		
New DIG contracts 2H19		($0.02)
Dilution	$	(0.00)
2Q20 Adjusted EPS	$	0.45
2Q20 Consensus		0.36
2020 BAML EPS		$2.64
2020 Consensus		$2.64
2020 Guidance		*2.64-2.68*
Shares Outstanding 2Q19		284
Shares Outstanding 2Q20		285

Source: BofA Global Research estimates, company report

FY20 guidance confidence with solid 2Q, cost execution

With highly favorable weather in 2Q offsetting 1Q unfavorable weather headwinds (~18c hit), as well as eased COVID load impacts (on a run-rate basis into June), we perceive greater mgmt confidence around FY20 guidance range. *We expect CMS to more firmly reaffirm its FY20 guidance range, though contingent upon no escalation in shutdowns driven by a potential pandemic resurgence in the state*.

In particular with our 2Q20 EPS estimate, we see 1H20 EPS of $1.21 with $1.45 remaining for 2H20 to reach the mid-point of the FY20 guidance range. Accordingly, relative to 2H19 EPS of $1.41, assuming additional COVID load impact of 6c remaining (1c per quarter based on estimated run-rate in June), against remaining 10c O&M cost savings as an offset, ~32c new gas rates offset by ~8c non-recurring benefit opportunities (mainly around favorable 2H19 sales mix) and ~12c D&A, interest, and other expense (~6c quarterly drag), we see ~10c cushion to offset any negative weather or further COVID impacts and *still* reach the mid-point of the FY20 guidance range.

Accordingly, we raise our FY20 EPS estimate to the mid-point of guidance at $2.66 ($2.64 at the low-end prior). With improved FY20, we expect CMS to maintain *its long term EPS CAGR of 6-8%*, we slightly raise forward EPS estimates as well given that CMS typically rebases EPS based on year-end results. We expect the improved confidence in ability to maintain earnings through best-in-class execution to manage earnings, further reaffirming CMS as among the most reliable utilities from an earnings trajectory perspective to investors, even without full revenue decoupling, further supporting the latest re-rating across the group to defensive premium utilities in favor of CMS.

Table 16: CMS EPS Estimates: 7.0% CAGR through '24, back to mid-point for FY20 with improved confidence around costs against easing pandemic impacts

EPS	2017A	2018E	2019E	2020E	2021E	2022E	2023E	2024E	CAGR ('19-'24)
Electric	1.62	1.89	1.79	1.94	2.02	2.12	2.22	2.33	5.4%
Gas	0.62	0.60	0.82	0.91	0.99	1.09	1.20	1.31	9.8%
Utility	2.24	2.48	2.61	2.85	3.01	3.22	3.42	3.64	6.9%
Guidance				*2.84-2.88*					
IPPs	0.08	0.10	0.12	0.10	0.12	0.12	0.12	0.12	0.4%
Guidance				*0.08-0.10*					
Enerbank	0.11	0.13	0.15	0.18	0.20	0.21	0.22	0.23	9.6%
Guidance				*0.18-0.20*					
Parent	(0.28)	(0.38)	(0.38)	(0.47)	(0.48)	(0.48)	(0.48)	(0.49)	5.4%
Guidance				*(0.46)-(0.50)*					
Consolidated	2.17	2.33	2.49	2.66	2.86	3.07	3.28	3.50	7.0%
Guidance		2.30-2.34	2.47-2.51	2.64-2.68					
Consensus			2.50	2.64	2.85	3.07	3.28		

Source: BofA Global Research estimates, company report

Extent of cost savings, key 2Q call update to be provided

With the 2Q update, among most notable of updates, we expect mgmt to emphasize its cost savings strategy and provide greater details around the extent of cost savings it has been able to realize and expectations on a forward basis. Notably, mgmt has expressed that while it has highlighted historic ability to flex cost levers up to 15c of EPS offset, mgmt has been vocal in emphasizing that this *does not represent a cap on potential cost levers*.

In terms of cost levers, *mgmt emphasized sustainable cost reduction and management systems* rather than one-time cost cuts, with lower costs rolling into '21. In particular, mgmt emphasized leverage of its *lean operating system* implemented 4 years ago, focusing on waste elimination (both through process improvements and digital technology-enabled improvements) on an ongoing basis. Additionally, mgmt emphasized outperformance already on supply chain optimization, which has been underway for 12-18 months *already*. Additionally, mgmt highlighted O&M cost reductions including work at power plant units in economic reserve to lower costs and improve reliability into the summer peak, as well as shifting O&M employees to pre-approved capital work as well. Mgmt noted remote work by employees is expected to continue to an extent post-COVID as well. *We view confidence from mgmt around extent of cost savings against improving load trends as a positive data-point, and expect a detailed update with 2Q.*

Sustaining cost savings support rate headroom, critical with election dynamic

With sustained cost savings, mgmt emphasized initiatives continuing to provide long-term rate headroom into '21-'22 given carryover benefits, with incremental customer bill headroom for capital investments continuing to make for smooth regulatory approvals, with MPSC generally supportive of capex spend proposed in proceedings.

We emphasize ability to drive customer bill headroom as particularly important against the backdrop of Nov 2020 presidential elections. With Biden tax plan proposing an increase in the corporate tax rate to 28% (from 21%), we note that in contrast to 2017 tax reform, this would have a reverse impact to customer bill headroom. In particular the change in tax rate would drive ~$60mn impact to customer rates on raised rates, with the benefit of deferred income taxes (DFITs) halved as well (relative to prior 35%) reducing to $20mn annually (from $40mn prior with 21% tax rate). Recall, CMS currently already has a DFITs pass-through to customer approved for gas (and near-term for electric), with 21% tax rate driving a $1.6Bn reevaluation of DFITs passed back over a 40-year period (~$40mn a year), with a 28% lowering the reevaluation to ~$800mn over 40 years (reduced to ~$20mn customer benefit annually). Accordingly, CMS would need to support $80mn in savings to neutralize the impact for customers on a bill basis, critical to supporting capital spend on a forward basis.

Beyond cost savings, CMS emphasizes further customer bill headroom support and comfort to offset impacts from potential increase in the corporate tax rate, with ~$90mn reduction from roll-off of Palisades PPA and ~$$30mn O&M savings from retirements of Karn 1 and 2, among other opportunities. We view mgmt's best-in-class forward-planning around cost savings and confidence in maintaining customer affordability even with tax rate headwinds as further supportive of CMS' smooth and longer-dated capex outlook relative to peers.

MPSC ratecases on track, supportive of proposed spend

With prolonged ratecase schedules driven by pandemic delays across the utility group and subsequent ROE risks, CMS notes that all MPSC meetings have continued virtually and ongoing ratecase proceedings remain on schedule, *continuing to expect a final order in its pending Gas case in late October and a final order in its pending Electric case in Dec,* given respective 10 month statutory deadlines. With both ratecases, CMS emphasizes a constructive regulatory environment as well as alignment with MPSC commissioners and staff through both its IRP and long-term gas plan in place. Accordingly, CMS emphasizes MPSC support for proposed capital spend in proceedings, further supported by its customer bill affordability efforts.

Electric case remains on track of Dec 2020 order, staff supportive of capex

Indeed with the latest MPSC staff recommendation in CMS pending electric, MPSC staff filed testimony recommending a $90mn rate increase at a 9.75% ROE, 52.5% equity ratio and $11.71Bn rate base ('21 test-year). CMS had initially filed for a $244mn rate increase at a 10.5% ROE, 52.5% equity ratio, and $11.84Bn rate base. Critically, mgmt expresses alignment on capital spend, with main difference between Staff and request being around ROE as usual (with staff proposing 9.75% ROE in the prior ratecase as well before settling at 10%). Mgmt expresses proposed investment spend as in-line with its latest capital plan as well as its 5-Yr electric distribution infrastructure investment plan filed with the MPSC in Mar '18. With O&M spend requested, mgmt expresses approx. equal split between safety/reliability spend that it is currently earning upon, discretionary spend that CMS will not spend if not approved (including tree-trimming), and spend that it is not currently earning upon but still spending.

New gas rates remain on track for Oct 2020 order, staff supportive of capex

With its latest gas case filed at the MPSC in Dec 2019, CMS requested a $244.7mn rate increase at a 10.5% ROE, 52.5% equity ratio, and $7.38Bn rate base for test year ending Sept 30, 2021. Along with its ratecase, CMS filed its 10-year Natural Gas Delivery Plan (2021-2030), which aligns with its current 10-year capital plan, including upside (*$10Bn gas capex with $1.5-2.0Bn gas upside*). In its testimony filed, MPSC staff recommended a $139.1mn rate increase at a 9.6% ROE, 52.5% equity ratio, and $7.42Bn rate base. Notably, proposed spend was largely supported with lower ROE in staff testimony as typical of proceedings. In terms of procedural schedule, a target PFD is currently scheduled for Aug 12. *A final MPSC order is expected in Oct 2020 with a 10 month requirement in place.*

With its latest gas rate case approved in late Sept 2019, mgmt highlights ~2/3rd of rate step-up contribution for FY20 as already approved. Recall, the MPSC approved a $143.5mn rate increase (inclusive of $13mn deferred taxes) at a 9.9% ROE, 52.5% equity ratio, and $6.429Bn average ratebase in Consumers Gas ratecase (U-20322), relative to CMS' requested $204mn request at a 10.75% ROE, 52.5% equity ratio, and $6.54Bn average ratebase. *Mgmt. views the approval as supportive of gas capex, with 98% of requested capex spend approved* and PUC actually calling for main pipe replacement acceleration to ~$100mn/yr (from ~$75mn/yr). As such, we see the approval as in-line with the near-term plan, with mgmt. highlighting '19 and '20 capex plan covered with the order ($1.2Bn of gas infrastructure capex supported).

Duke Energy (DUK)

With the ACP overhang in the rearview, we see the story swiftly transitioning to a utility-centered story (albeit with ~$200mn per annum in renewables) where we still see rate case risk ahead with the DEC/DEP rate cases. Ability to garner a settlement on ROE/Cap structure would be clearly constructive for shares, although with a tight timeline ahead until hearings start we perceive downside risk to a 9.75% authorized ROE (inked with industrials). Meanwhile, we expect Duke's capex outlook to be reset higher with the upcoming September IRP that is likely broader than usual with the commission likely looking for a balance between the lowest cost plan and de-carbonization efforts. The IRP is likely to be an adjudicated process with multiple scenarios in which the commission will chose from, implying that a fully defined capex update is not likely to occur until the 4Q update. As such, we perceive a particularly weak '21 outlook given the loss of ACP earnings (30-35cents) and capex likely to be backfilled post-21, although with load trending slightly more favorable vs. expectations (-2-5% annualized) we could see some cost savings sustained into next year. Nevertheless, we expect mgmt. could rebase its 4-6% growth rate off a lower 2021 number, particularly cautious for shares. Longer-term improved regulatory mechanisms (multi-year rate plans, ROE banding, riders, etc.) stemming from the Clean Energy report recommendation to the legislature remain a possibility. Net-net, we maintain our Neutral rating seeing the ~15.2x P/E multiple (adjusted for renewables) as fairly capturing the growth outlook and risks ahead.

DUK 2Q20 EPS walk

We forecast 2Q20 EPS of $0.95 compared to 2Q19 results of $1.12 (-14% YoY) and consensus estimates of $1.01. Despite the loss of ACP (-13cent headwind YoY) and COVID related pressure, we see 2020 EPS at $5.07 near the bottom-end of mgmt.'s $5.05-$5.45 range.

- **Key drivers**: Positive YoY drivers include the implementation of rates and riders at the electric utilities (+$0.06), the wholesale contract moving to formula rates (+$0.01), new rates at Piedmont (+$0.001), still AFUDC on Atlantic Coast Pipeline (+$0.01), and the contribution from the Palmer commercial renewable projects and tax benefits from previously installed projects (+$0.03). Offsetting results are regulatory lag (-$0.04), impacts from COVID on load growth (-$0.10), higher interest expense (-$0.01), preferred coupon interest expense (-$0.04), share dilution (-$0.01), and reversal of weather benefits from 1Q19 (-$0.08).
- **Unknowns**: Weather is expected to be flattish to slightly favorable, although the exact magnitude is unclear. Another unknown impact is the decline in load growth from COVID19; while mgmt. provides sensitivity for the full-year impact of $0.25-$0.35, we expect a greater proportion of this to show up in 2Q given the timing of state re-openings. Further, it remains unclear if the company was able to bend the cost curve on O&M costs, which could be a potential offset as it experience 7cent favorable variance in 2Q19 and the majority of the 40cents offset are expected to show up in 2H; we could see a push to slightly favorable O&M variance.

Table 17: DUK 2Q EPS walk

DUK 2Q20 Earnings Walk	EPS
DUK 2Q19 EPS	1.12
Weather - normalize from 1Q19	-$0.08
Weather- 1Q20	$0.01
Electric	-$0.06
Rate implementation:	
DEC SC rates (full quarter)	$0.006
DEP SC rates (full quarter)	$0.004
Florida - multi-year plan	$0.01
SOBRA - FL	$0.00
Other Riders - IN and OH	$0.04
Regulatory lag	-$0.04
Load Growth - 1%	-$0.10
AFUDC equity	$0.01
Wholesale - fixed to formula rates	$0.01
Gas	$0.01
LDC Growth	$0.00
New Rates - PNY	$0.001
AFUDC for ACP	$0.01
Tax true-up reversal	$0.00
Renewables	$0.03
Palmer (60MW) and tax benefits	$0.03
Other	-$0.07
O&M	$0.00
Interest expense	-$0.01
Other - preferred	-$0.04
Dilution	-$0.01
DUK 2Q BofAe Adjusted EPS	$0.96
Consensus	$1.01
BofAe 2020 EPS	5.07
Guidance	5.05-5.45
2020 Consensus	5.11
DUK 2Q20 Shares Outstanding	736
DUK 2Q19 Shares Outstanding	728
Tax Rate	12%

Source: BofA Global Research estimates, company report, Bloomberg

Capex: look for details in 2Q but not defined until 4Q

Following the recent cancellation of ACP, we look ahead to the 2Q call where we expect mgmt. to articulate how it intends to backfill capex after reaffirming its 5yr $56bn capex plan. While Duke Energy Florida is proposing to spend ~$1bn on 750 MW of solar projects across Florida in the next three years with ~$500mn incremental, we perceive spending associated with the IRP and looping/laterals to source gas would occur in the *latter half* of the 5yr plan. The IRP is likely to be an adjudicated process with multiple scenarios in which the commission will chose from, implying that a fully defined capex update is not likely to occur until the 4Q update. As such, we expect capex will be delayed into 2021 with potential upside to capex stemming from the IRP and gas capex not likely defined until the 4Q call.

Upcoming IRP to potentially drive upside to capex and FFO

We expect Duke's capex outlook to be reset higher with the upcoming September IRP that is likely broader than usual with the commission likely looking for a balance between the lowest cost plan and de-carbonization efforts. We see the likelihood for meaningful clean energy capex opportunities underpinned by the IRP combined with the early retirement of coal plants in a similar fashion to Dominion's in Virgina. Critically, the IRP could also add to FFO via potential for the accelerated depreciation of coal plants driving further balance sheet improvement, and we even see an angle where Duke could utilize accelerated depreciation without the IRP (i.e. rate case).

NC rate cases remain key to watch: ROE and coal ash

We continue to expect DUK's rate case in the Carolinas to have a similar outcome to Dominion's coal ash order potentially further cautious for earned/recoverable ROEs where we already assume $0.10-$0.13/sh eventual drag. With upcoming hearings for the DEC/DEP rate case slated for July 27 and commentary suggesting the process could take 3-4weeks, it remains unclear if a settlement can be garnered with staff despite recently inked deals w/ industrials for a 9.75% ROE as we could still see downside to authorized levels. While we continue to account for coal ash impacts with 30-40bps of lag in the outer years, a less constructive outcome on ROEs could put further pressure our EPS CAGR. Rate cases remain cautious although see risks of the negative revisions priced-in/largely known.

FERC denied DEP's request to dismiss ROE complaint

We note FERC denied DUK subsidiary Duke Energy Progress' (DEP) request to reject the complaint filed by North Carolina Eastern Municipal Power Agency (MPA) in Oct 2019 against DEP on the matter of 11% ROE included in the Fifth Amended and Restated Full Requirements Power Supply Agreement executed between MPA and DEP. The agency found 11% ROE is excessive and also produced an affidavit from GDS Associates that comprised of a couple of approaches to determine the "zones of reasonableness" in favor of its argument. While the approaches yielded ROE zone of reasonableness of 7.66–12.02% with a median of 9.41%, and 7.26–10.55%, with a median of 8.17%, respectively, MPA forecasted a reduction of 1% in the ROE would reduce the charges by $5.8m per year. FERC dismissed DUK's argument of MPA's inability to establish the unreasonableness of the agreement, and ordered to appoint a settlement judge for a hearing with a refund effective date of Oct 11, 2019. *We note DEP has a wholesale ratebase of $3.2B including both South and North Carolina and as of 3Q19; unclear what portion of this* wholesale *ratebase* the *ROE update would have* been*. We see this as the latest (modest) negative impact from rate case activity to Duke. This is a small portion of overall earnings with likely in ~1c ($5.8M/yr) range but admittedly represents the latest pressure on generation – and highlights* the *latest FERC datapoint on where ROEs* (*even for generation*) *are deemed too high (as has been a focus for peers* like E*TR's SERI already). We expect this to prove as a premium to base ROEs for transmission and as such see a ~10% figure on MtM basis as a broad proxy for generation assets.*

Alternative rate mechanism legislation

We note continued progress, although still very early stages such that Duke is still pushing the Public Utilities Commission (PUC) for alternative rate mechanisms to move forward, such as Performance Based Rates (PBRs), Multi-year rate plans (MYRPs), ROE banding, securitization, riders and others. We believe there remains potential for Duke to have a recommendation back to the legislation that would include one of these alternative mechanisms. Management did make clear that is still early on in the process, but it seems like they are headed in the right direction especially with the upcoming report due from the Governor's committee on Clean Energy. The company is currently in the education phase and there are a number of different tools to look at. All of these tools would be positive for Duke, but there are a number of steps it will take to get there as past efforts stalled/failed. With that said, we see both increased confidence from the company and corresponding stakeholder commentary as supportive for DUK's legislative prospects in the 2021 long session, although wouldn't be implemented in a rate case until 2023.

EPS estimates

We tweak our EPS estimates lower to reflect expectations that 2021 capex will be delayed and now assume a 9.7% authorized ROE for the DEP/DEC rate cases (w/ potential for further downside if litigated). Given the difficulty in attaining its 4-6% EPS outlook, we wonder if DUK mgmt. will elect to re-base on the upcoming call or defer for a later period of time. At a minimum, we expect messaging to be somewhat squishy in regards to the 2021 outlook.

Table 18: DUK EPS Estimates

EPS Estimates	2019A	2020E	2021E	2022E	2023E	2024E
Electric						
Carolinas	1.95	1.90	1.89	1.96	2.02	2.09
Indiana	0.60	0.61	0.62	0.63	0.66	0.68
Ohio - Electric	0.22	0.25	0.25	0.27	0.30	0.35
Progress- Carolinas	1.12	1.15	1.17	1.21	1.24	1.26
Progress- Florida	0.96	0.97	1.01	1.03	1.05	1.06
Commercial Transmission	0.00	0.00	0.00	0.00	0.00	0.00
Eliminations	-0.04	0.00	0.00	0.00	0.00	0.00
Consolidated Earnings	4.81	4.88	4.94	5.10	5.26	5.45
Guidance	4.77	4.94				
Gas						
Ohio - Gas	0.12	0.14	0.16	0.19	0.20	0.21
Piedmont (PNY)	0.27	0.31	0.33	0.37	0.41	0.45
Midstream Pipelines	0.24	0.11	0.04	0.05	0.06	0.08
Eliminations	0.00	0.00	0.00	0.00	0.00	0.00
Consolidated Earnings	0.62	0.56	0.53	0.61	0.67	0.74
Guidance	0.51	0.72				
Commercial Renewables	0.27	0.32	0.33	0.30	0.28	0.29
Guidance	0.32	0.33				
Parent/Other	-0.64	-0.69	-0.58	-0.53	-0.46	-0.41
Guidance	-0.60	-0.73				
Adjustments						
BofAe EPS	5.07	5.07	5.23	5.48	5.75	6.06
Previous Estimates	*5.06*	*5.07*	*5.27*	*5.53*	*5.81*	*6.12*
Guidance	*4.95-5.15*	*5.05-5.45*				
Consensus	5.02	5.08	5.34	5.60	5.89	6.20
Mgmt EPS CAGR: 4-6% from 2019-2023E	5.00	5.25	5.51	5.79	6.08	6.39
Low End	4.80	5.05	5.41	5.62	5.85	6.08
High End	5.20	5.45	5.62	5.96	6.31	6.69
BofAe CAGR '19-'24e						3.9%

Source: BofA Global Research estimates, company report, Bloomberg

The open question remains how management could reposition its long-term EPS CAGR. While ACP should force some degree of guidance update by the time of its 2Q call in coming weeks, we anticipate a more meaningful roll-forward (and rebasing of its 4-6%) is likely only with 4Q. We anticipate a more comprehensive view of mitigating offsets to the outlook including initial expectations from its September IRP filing in the Carolinas and other mitigating capex (transmission, gas) to address ACP delays.

Valuation: PO of $87

We move our PO to $87 (from $84) based on mtm of peer utility multiples of 17.1x and 15.9x for gas and electric (from 16.4x and 15.6x), our lower EPS estimates. Net-net, we maintain our Neutral rating seeing the ~15.2x P/E multiple (adjusted for renewables) as fairly capturing the growth outlook and rate case risks ahead -> just what earned ROEs assumed in the Carolinas will be key.

Table 19: DUK SOPT Analysis

Duke Energy Sum of the Parts Valuation
2022E
All figures in $Mn except per share

	Metric	P/E Multiple					Equity Value		
	2022 EPS	Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric	-	-	17.1x	-	-	-	-	-	-
Group EPS '18-'22 CAGR - Electric	-	-	5.00%	-	-	-	-	-	-
	-	-	-	-	-	-	-	-	-
Electric Utilities			18.0x						
Duke Energy Carolinas	$1.96	17.0x		0.0x	18.0x	19.0x	$33.22	$35.18	$37.14
Duke Energy Progress/Carolinas	$1.20	17.0x		0.0x	18.0x	19.0x	$20.42	$21.63	$22.83
Duke Energy Florida	$1.02	18.0x		1.0x	19.0x	20.0x	$18.37	$19.39	$20.41
Duke Energy Indiana	$0.63	18.0x		1.0x	19.0x	20.0x	$11.40	$12.03	$12.67
Duke Energy Ohio/Kentucky	$0.27	17.0x		0.0x	18.0x	19.0x	$4.57	$4.84	$5.10
Total Electric Utility Value	$5.09						$87.97	$93.07	$98.16
Group Peer Multiple - Gas			15.9x						
Group EPS '18-'22 CAGR - Gas			5.10%						
Gas Utilities	2022 EPS		16.7x						
Duke Energy Piedmont	$0.37	15.7x		0.0x	16.7x	17.7x	$5.81	$6.18	$6.55
Duke Energy Ohio/Kentucky Gas	$0.19	15.7x		0.0x	16.7x	17.7x	$2.93	$3.12	$3.30
Total Gas Utility Value	$0.56						$8.74	$9.29	$9.85
Commercial Segment	2022 EBITDA								
Remaining Midstream assets	$107	8.0x	9.0x	0.0x	9.0x	10.0x	859	967	1,074
Transmission Segment	$6	8.0x	9.0x	0.0x	9.0x	10.0x	52	58	64
Segment Net Debt	-$3,623						-3,623	-3,623	-3,623
Add back Renewable Debt	$2,468						2,468	2,468	2,468
Renewables Segment NPV @ 8% Discount	$1,291						1,291	1,291	1,291
New Renewables NPV	$471						471	471	471
Net Infrastructure Equity							1,518	1,632	1,746
Net Infrastructure Equity Per Share							$2.08	$2.10	$2.39
Parent	2022 EPS								
NMC (Saudi Chemical JV)	$0.05	11.0x		-6.0x	12.0x	13.0x	$0.55	$0.60	$0.65
Parent Interest attributed to utility - 50%	-$0.53	19.1x		0.0x	18.1x	17.1x	-$5.03	-$4.77	-$4.50
Parent Debt- 50%	-$20,702						-$13.34	-$13.34	-$13.34
Total Equity Value							-$17.82	-$17.50	-$17.19
Shares Outstanding								776	
Total Equity Value							$81.00	$87.00	$93.00
Current Share Price							$82.40	$82.40	$82.40
NTM Dividend Yield								4.65%	
Total Return								10.23%	

Source: BofA Global Research estimates, company report, Bloomberg

DTE Energy

We forecast 2Q20 adjusted EPS of $1.27 vs. $0.99 in 2Q19 and $1.13 consensus. We expect that unlike Q1, Q2 will receive a boost from weather in particular with a higher incidence of CDDs in Q2 relative to last year and normal patterns – with Q2 typically a shoulder quarter we do expect some uplift from weather impact particularly as it appears that CDDs in June were 30%+ higher than normal. We estimate that Covid impact on electric sales will be felt most acutely in Q2 given the pace of phased reopening in DTE's MI territory, and we expect approximately half of DTE mgmt.'s forecast $40m decline in sales on an annualized basis to fall in the quarter.

- **Key Drivers:** Primary drivers include weather which is an 18 cent uplift at the electric utility reflecting normalization of 2019 (7 cents) and an estimated 9 cent boost from warmer-than-normal weather during Q2, weighted toward June. We also note that with at least partial stay-at-home orders in place for much of the quarter, the weather boost may be greater than in a 'normal' year. We continue to incorporate the impact of new electric rates which went into effect in May 2019, as well as a partial quarter impact of the new rate increase effective this year, along with correspondingly higher D&A and interest expense. While DTE mgmt. has flagged its previous expectation to utilize financial contingency to mitigate impacts of weather on its utility results, we expect a partial offset via O&M. In the non-reg business we see the biggest jump in the midstream GSP segment as we reflect our higher y/y operating earnings as the company incorporates the contribution of its acquired Haynesville assets.

- **Unknown:** Precise weather-related impacts are difficult to estimate – Q2 2020 CDDs reported *above normal by ~2x the amount below normal in 2019*, leading to our 13 cent estimate – though we highlight some upside to estimates as weather effects may be higher in the quarter due to Covid. We expect the majority of lost sales and additional expenses related to Covid to impact in Q2, with a total 16 cent drag at the electric utility. The Energy Trading business is difficult to forecast owing to the opaque nature of its operations – given significant volatility across most asset classes in the quarter there is potential for an above/below normal quarter, although we do not incorporate this into our estimates.

Table 20: DTE Q2 2020 earnings walk: upside vs. Street despite Covid

DTE Energy 2Q20 Earnings Walk	EPS
Adjusted EPS 2Q19	$0.99
Utility	$0.16
Electric	
Weather - return to normal	$0.07
Weather - 2Q20	$0.09
2019 GRC - $273mn effective 5/2/2019	$0.12
2020 GRC - $188mn effective 5/8/2020	$0.10
D&A, Interest, Other expenses	($0.13)
O&M savings vs. last year	$0.02
Sales impact - Covid	($0.08)
Additional costs - Covid	($0.03)
OID benefit	$0.02
Gas	
Weather - return to normal	($0.02)
Weather - 2Q20	$0.03
D&A, Interest, Other expenses	($0.04)
O&M	$0.02
Sales impact	($0.01)
Non-utility business	$0.16
GSP	0.10
P&IP	0.01
ET	0.04
Corp & Other	0.01
Dilution	($0.04)
2Q20E Adjusted EPS	$1.27
2Q20E Consensus	1.13
2020E BofAe EPS	$6.62
2020E Consensus	6.59
2020 Guidance Midpoint	6.47-6.75
Shares Outstanding 2Q19	184
Shares Outstanding 2Q20	192

Source: BofA Global Research Estimates, company report, Bloomberg

Covid impact on load – Q2 seen most affected

We expect mgmt. of DTE to provide an update on sales in its service territory on the Q2 call. Recall that mgmt. has mapped out two scenarios for returning from mandated shut down orders: May start scenario contemplates most C&I customers beginning a staggered reopening in May with a return to universities and K-12 schools under the regular fall schedule, and a Slow Start scenario with industrial customers remaining idle until late summer and schools and nonessential offices remaining closed until year-end. We note that the company has indicated that the pace of reopening in its service area so far has tracked with the May reopening scenario, though the reopening of schools and universities in the fall remains uncertain given Covid upticks across much of the country. Recall that Michigan reported one of the higher declines in Industrial activity with sales falling by 43% in April at the outset of shut down orders, though we note that based on company sensitivities Residential sales have 15x the earnings impact, making the reported 10.5% increase in sales in April 3x more meaningful from an earnings standpoint.

Table 21: Estimated earnings impact from April reported sales

April reported impact

Customer type	+1% annual impact	Impact (%)	Annual earnings impact ($m)
Residential	15	10.5%	39
Commercial	6	-17.0%	(26)
Industrial	1	-43.0%	(11)
Other	2	0.0%	-
Total			3
2020 guide midpoint		1,270	
Decline impact		0.2%	

Source: BofA Global Research Estimates, company report

Below we present illustrative earnings impact (annual) for a 1% drop in sales across all customer classes based on DTE sensitivities, along with the potential impact on Q2 from a +5%, -15%, -15% drop across the three major customer classes, respectively. We also highlight that our recent work on load trends across the US supports anecdotal reports of sales bottoming out in April and beginning a gradual and uneven recovery. Uncertainty around the reopening of schools and universities in the fall will continue to weigh on forecasts for electricity demand across customer classes.

Table 22: DTE electric demand impact

Flat 1% annual impact

Customer type	Sensitivity (%)	Annual earnings impact ($m)
Residential	-1.0%	15
Commercial	-1.0%	6
Industrial	-1.0%	1
Other	-1.0%	2
Total		24
2020 guide midpoint		1,270
Decline impact		-1.9%

Q2 demand shock illustrative

Customer type	Sensitivity (%)	Annual earnings impact ($m)
Residential	5.0%	19
Commercial	-15.0%	(23)
Industrial	-15.0%	(4)
Other	-15.0%	(8)
Total		(15)
2020 guide midpoint		1,270
Decline impact		-1.2%

Source: BofA Global Research Estimates, company report, Bloomberg

Electric rate case pushed, River Rouge acc. to '21

The Michigan Public Service Commission (MPSC) **approved** DTE Electric's petition to accelerate amortization the $108m portion of its $1.4B accumulated deferred income tax (ADIT) balance associated with the 2017 tax reform law, with the accelerated timeframe requiring DTE to fully amortize by the end of 2021 instead of the end of 2033. Critically, the change in amortization will allow DTE Electric to defer its next electric rate case filing from July 2020 to at least Mar 2021 which will in effect keep customer rates flat through 2022. Yet again, de-risking DTE's utility risk profile through 2020 as far as we're concerned and reiterating our confidence in the MI regulatory backdrop. DTE's application noted that its rate filing would have sought to recover Covid-related costs – recall that per an MPSC order, uncollectibles related to Covid are subject to deferral for future recovery, while a separate docket is pending at the MPSC that will determine whether direct expenses are recoverable as well. Note that DTE mgmt. intends to offset its lost sales and direct expenses via its financial contingency, which we estimate has improved over Q1 given strong weather tailwind at the utilities. We note this is a constructive order for DTE, as ADIT flowback is typically offset by a revenue reduction (since it is normally included in a rate case) though this interim order comes with no adjustment to revenues as it is between rate cases.

In the same order, the MPSC approved early retirement of the River Rouge 3 coal plant, accelerating retirement to May 2021 from previously-scheduled 2022. DTE is required to file a transition plan by Sep 30 that will address the plant retirement and solicit feedback from the community and other stakeholders – note the MPSC order states that the plan to be filed by DTE is not subject to commission approval. As part of the plant retirement, DTE will file for securitization of the undepreciated plant (estimated at

$70m based on filings) along with approximately $120m related to spending on tree trimming. Given the ADIT flowback is typically a cash-negative event we see the concurrent securitization as mitigating most of the cash impact.

The MPSC also approved DTE Electric's amended renewable energy plan, including approvals of new renewable generation to be added to rate base and sourced via PPAs. The commission approved DTE's Meridien Wind project including all engineering and construction – the project is expected to provide 225 MW of generation when it goes in service in late 2021. The MPSC also approved solar PPAs between DTE Electric and two generation stations operated by Ranger Power for 25 year terms, totaling 128 MW of energy. The aggregate additions will bring DTE's renewable generation to the 15% by 2021 requirement set by the state.

Gas rate case – decision expected by Sept

We continue to forecast an authorized ROE reduction of 9.9% for DTE Gas (from the current 10.0%) which is in line with the decision for DTE Electric from earlier this year. Based on PSC staff recommendation of 9.6% (which is in line with the ALJ) and company request for a 10.5%, we see 9.9% as a reasonable level which would be in keeping with the Michigan PSC's history of not making drastic reductions to ROEs and taking a more gradual approach, along with recognizing the lower rate environment. We expect DTE to continue to earn its authorized ROE through the forecast period and to hit the long-term mgmt. guidance CAGR of 9.0% over the 2020-24 period. Bottom line: we expect that DTE's utilities will under-earn their authorized ROEs somewhat in 2020 as a result of sales impacts but recover in 2021 with DTE Electric achieving its authorized 9.9%, while we expect DTE Gas to receive a ~9.9% in its pending rate case.

Table 23: ROE forecast

ROEs							
Authorized	2018A	2019A	2020E	2021E	2022E	2023E	2024E
DTE Electric	10.0%	10.0%	9.9%	9.9%	9.9%	9.9%	9.9%
DTE Gas	10.0%	10.0%	10.0%	9.9%	9.9%	9.9%	9.9%
Earned							
DTE Electric	9.8%	10.0%	9.8%	9.9%	9.9%	9.9%	9.9%
DTE Gas	9.5%	10.5%	9.8%	9.9%	9.9%	9.9%	9.9%

Source: BofA Global Research Estimates

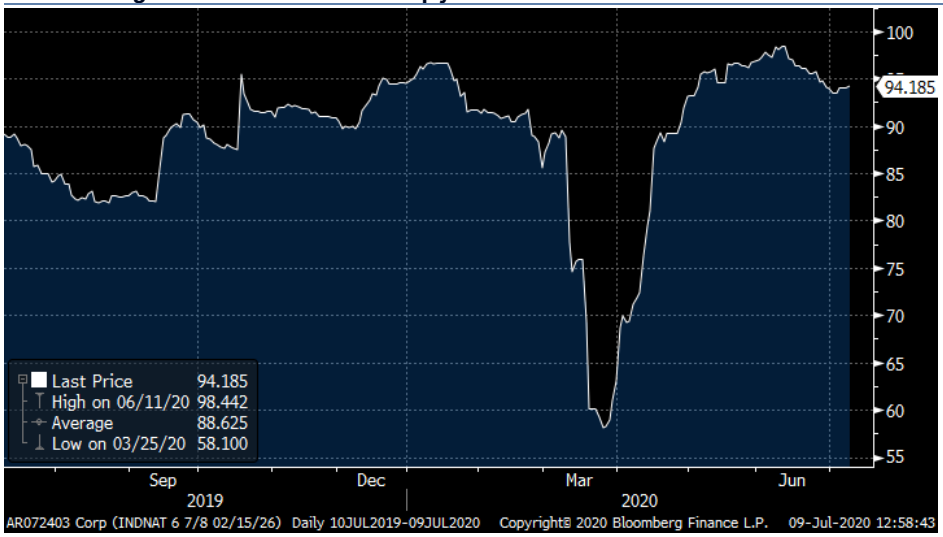
Midstream: read thru from D asset sale

We are forecasting a solid Q2 for DTE's Gas Storage & Pipeline (GSP) biz at approx. $70m operating income, a step-up from the same period last year. The major driver of improved midstream performance is the Haynesville Blue Union/Leap acquisition which is in its first year as part of DTE's midstream business, along with expansions at NEXUS and contributions from the Generation pipeline acquisition. While DTE's midstream business came sharply in focus during the late-March crude oil price collapse as investors ascertained the relative strength of its midstream counterparties, we sense investors have largely grown comfortable with DTE's position – especially in light of an improving natural gas supply/demand outlook given potential exit of producers of low-cost associated gas throughout US basins. Key Haynesville counterparty Indigo has seen its bonds recover substantially – and in fact trade higher than pre-crisis levels – see our recent Upgrade to Buy for more detail.

Following the D sale of its midstream assets to Berkshire *we sense a growing interest among investors in potential further M&A in the midstream space* – while DTE made its most recent acquisition less than 12 months ago, company mgmt. has stated that it continues to evaluate its portfolio on a regular basis and would be open to potentially monetizing assets in the right circumstance; were DTE to divest midstream assets we would expect it to be a fully-developed (with compression) pipeline or storage asset, rather than under-development projects such as LEAP or Generation. We continue to largely expect a status quo outlook for the company given its focus on growth; depending on the ultimate success in Dominion re-rating higher on a stand-alone strategy (or really CMS too), this could drive a further re-think strategically. Moreover,

given focus on growth at this segment only select assets would make sense to divest given need to maintain congruence of growth assets to maximize earned returns.

Exhibit 5: Indigo bonds have rebounded sharply from March lows



Source: Bloomberg

EPS Estimates

We raise our electric utility estimates on the expectation of warmer-than-normal weather enabling a rebuild of DTE's financial contingency. Our updated ests are now 1 cent above the midpoint of mgmt.'s 2020 range at $6.62 and 3 cents above Street consensus – we see upside to 2020 as well as Q2 estimates. We expect that warm weather should provide a tailwind to electric utility results following a warmer-than-normal Q2 and strong start to the key Q3: note that a higher incidence of customers remaining at home during Q3 may well contribute *more to weather impact than a normal year*, though the precise amount is difficult to estimate given uncertain path of state reopening measures. Bottom line: following DTE's reaffirmation of its 2020 guidance range on its Q1 call and commitment to re-establishing financial contingency, we expect company mgmt. will continue to project confidence on non-Covid financial mgmt. including O&M reductions intended to offset sales impacts, with a tailwind from weather in Q2 and early parts of Q3.

Table 24: DTE updated estimates: *getting above Street on '20 and '21*

Earnings Contribution	2018A	2019A	2020E	2021E	2022E	2023E	2024E
DTE Electric	3.70	3.87	3.98	4.27	4.52	4.56	4.83
DTE Gas	0.88	0.98	0.97	1.04	1.17	1.22	1.30
Total utility	4.57	4.85	4.94	5.31	5.69	5.79	6.13
Non-utility segment							
Gas Storage & Pipeline	1.29	1.15	1.49	1.59	1.91	1.91	1.97
Power & Ind. Products	0.90	0.72	0.72	0.79	0.45	0.53	0.63
Energy Trading	0.22	0.16	0.16	0.13	0.15	0.16	0.16
Corp & Eliminations	(0.67)	(0.58)	(0.62)	(0.69)	(0.72)	(0.65)	(0.65)
% of total	*-11%*	*-9%*	*-9%*	*-10%*	*-10%*	*-8%*	*-8%*
Total non-utility	1.73	1.45	1.74	1.82	1.79	1.95	2.11
DTE Consolidated	6.30	6.31	6.62	7.12	7.46	7.72	8.23
Guidance	*0.00*	*6.02-6.38*	*6.47-6.75*				
Prior Estimates		*6.31*	*6.56*	*7.18*	*7.34*	*7.63*	*8.19*
Consensus		6.24	6.59	7.08	7.47	7.78	
			5.0%				
DTE Guidance 6% CAGR ('20-24)			6.61	7.01	7.43	7.87	8.34
Low End				6.94	7.29	7.65	8.03
High End				7.07	7.57	8.10	8.66
BofAe CAGR '20-'24e		5.6%					
Shares outstanding	*181*	*185*	*192*	*194*	*197*	*208*	*209*

Source: BofA Global Research, Bloomberg

PO to $115; Reiterate Buy

We update our PO to $115 following mtm of electric and gas peer group multiples to 16.5x and 15.6x, respectively (17.2x and 17.4x prior). We continue to value midstream assets using a base EV/EBITDA multiple of 9.0x and adjust accordingly for in-progress Haynesville assets. We note that non-equity value of DTE's midstream and other non-reg assets has rebounded from March lows which implied minimal value (low single digits), principally as investor confidence in the outlook for the midstream sector has bounced back. We reiterate our Buy rating following the MPSC constructive decision on electric rate case timing and River Rouge securitization and resulting upward tweak in '20 ests.

Table 25: DTE SOTP

DTE Energy Segments	2022 EPS	Premium /(Discount)	Group Multiple	Applied Multiple	Value
Utility					
Group Peer Multiple - Electric			16.5x		
Group EPS '18-'22 CAGR - Electric			5.00%		
DTE Electric (Distribution)	$4.52	2.0x	17.3x	19.3x	$87.26
Group Peer Multiple - Gas			15.6x		
Group EPS '18-'22 CAGR - Gas			5.10%		
DTE Gas	$1.17	2.0x	16.4x	18.4x	$21.52
Utility Debt Adjustment (20% of non reg debt)	-				
50% interest expense	($0.15)		16.9x		($2.47)
Subtract 50% of holdco debt adjustment	($828)				($4.19)
Utility Equity Value per Share					$102.12

Non-Utility	2022 EBITDA	Premium /(Discount)	Group Multiple	Applied Multiple	
P&I					
Cogen + Legacy Coke Batteries	79	-2.0x	8.0x	6x	$477
NPV of RNG Development	$558		Implied Multiple ---->	6.8x	$558
REF Tax Credit Value (DCF), 2020-2023 @ 6%	198				$198
Energy Trading	44	0.0x	6.0x	6x	$263
Midstream (GSP)	904	-0.3x	9.0x	9x	$7,834
Allocated EBITDA	599	0.0x	9.0x	9x	$5,394
Momentum Midstream	$305	-1.0x	9.0x	8x	$2,440
Holding Company Borrowings					
Consolidated Projected B/S					20,119
(-) Unallocated GSP Project Debt					-
(-) DTE Gas / DTE Electric Debt					(11,839)
(-) Holdco debt adjustment (20%)					(1,656)
Net Non-Utility Net Debt					6,624
Non-Utility Equity Value					$2,705
Shares Outstanding					197
Non-Utility Equity Value per Share					$13.70

	2022 EPS	Premium /(Discount)	Group Multiple	Applied Multiple	
Corp & Other (ex-Interest Expense)	(0.05)	0.0x	19.1x	19.1x	($0.96)
Utility Equity Value per Share					($0.96)
12 Month Price Objective					$115
Implied Consolidated P/E					18.2x
Dividend Yield NTMe					3.8%
Estimated Total Potential Return					10.8%

Source: BofA Global Research, Bloomberg

Edison International (EIX)

With EIX's upcoming 2Q call we expect a miss on EPS, although comparability continues to remain outside of reach given still lack of recovery on O&M memo account items as we await an outcome with the 2021 GRC. Meanwhile, we continue to assume a 20% gross up to the low-end of $4.9bn liability range assumed by mgmt. as we expect an additional $670mn in equity issuance in the outer years (w/ the $1.95bn net imputed on the balance sheet). We note that the Bellwether trial for the Thomas fire is scheduled at the end of the year while there has been no date set for the Woolsey fire. That is not to say that mgmt. cannot reach a settlement with individual claimants prior to that date. While there are thousands of individual lawsuits, if mgmt. can garner meaningful settlements, we would expect the company to update its current charge of $4.9bn, although continue to perceive the bias is to the upside in terms of total liability assumed. With upcoming fire season and focus from the company on PSPS (although still needs permission from CAISO on transmission lines) and new technology deployed by the state (Blackhawks, fire retardants, etc.), execution will be critical to watch. We now move to a 4x discount (from 3x) to capture execution risk into this fire season (equivalent to ~50% prob. of triggering the liability cap with 46% earnings at risk). Still with shares trading at a ~30% discount vs. the broader utility group, we see an opportunity for a re-rating on fire execution and more clarity on the balance sheet.

EIX 2Q20 EPS walk

We forecast 2Q20 EPS of $0.95 compared to 1Q19 results of $1.58 and consensus estimates of $1.17.

- **Key drivers**: Positive YoY drivers include increase FERC and CPUC core contribution (+$0.16), and SCE financial and other benefit variances (+$0.08). Offsetting our estimates is the reversal of CPUC true-up from the GRC (-$0.20) negative variance from O&M expenses (-$0.30), higher D&A (-$0.04), wildfire mitigation costs (not earning ROE) and interest expense on contribution to fund (-$0.07), additional parent drag given HoldCo debt (-$0.07), and share dilution (-$0.20)
- **Unknowns**: We highlight uncertainty with O&M expenses as it continues to be somewhat challenging to handicap given the company will defer costs that are over and above the authorized limit; we expect a negative variance in 2Q20, similar to 1Q20.

Table 26: EIX 2Q20 EPS walk : mild results despite decoupling

Edison International 2Q20 Earnings Walk	EPS
Edison Electric 2Q19 Adjusted EPS	$1.58
SCE	($0.37)
FERC ROE & RB Growth	($0.00)
CPUC RB Growth and 52% Equity Cap	$0.16
CPUC Test year true-up reversal	($0.20)
O&M Effect	($0.30)
Depreciation	($0.04)
Property Taxes	$0.00
Energy Efficiency	$0.00
Wildfire Mitigation Costs	($0.04)
Interest expense for fund contribution	($0.03)
Financial and Other benefits	$0.08
EIX Parent and Other	($0.26)
HoldCo Drag	($0.07)
Dilution	($0.20)
2Q20E Adjusted EPS	$0.95
2Q20 Consensus	$1.17
2020 BAML EPS	$4.46
2020 Consensus	$4.42
2020 Guidance	4.32-4.62
2Q20 Shares Outstanding	373
2Q19 Shares Outstanding	327

Source: BofA Global Research estimates, company report, Bloomberg

Assumptions for remaining '17/18 wildfire exposure

We continue to assume a 20% gross up to the $4.9bn low-end of the '17/18 wildfire liability range, with the net remaining exposure of just $670mn after adjusting for the $1.9bn imputed from rating agencies on the balance sheet. We include this equity issuance in our 2021 share count to provide a fully-diluted EPS outlook. We note that the Bellwether trial for the Thomas fire is scheduled at the end of the year while there has been no date set for the Woolsey fire. That is not to say that mgmt. cannot reach a settlement with individual claimants prior to that dated. While there are thousands of individual lawsuits, if mgmt. can garner meaningful settlements, we would expect the company to update its current charge of $4.9bn that is assuming. We continue to perceive the bias is to the upside in terms of total liability assumed.

Table 27: EIX estimated remaining equity needs for '17/18 wildfires – 20% gross up of low-end

EIX Estimated Remaining Equity		
Current Charge: 2017 Thomas, Mudslides, Woolsey Fires: Low End of Range		-4,900
Gross Up Factor	20%	-5,880
Insurance Receivable		2,000
Wildfire Liability Incl Insurance Offset		-3,880
FERC Allocation ~5%	5%	194
Net Exposure		-3,686
Post Tax Net Exposure	28%	-2,654
Amount imputed from rating agencies ($1.9bn net flows through CFI)		1,984
Remaining Exposure		-670

Source: BofA Global Research estimates, company report

Managing the upcoming wildfire season will be critical

Communication with local authorities and the state is crucial given the need to focus on investments to harden the grid ahead of the upcoming wildfire season while at the same time procuring generators for its most critical customers. We see prioritization of wildfire mitigation and communication with the market as critical, especially ahead of the upcoming wildfire season. Public Safety Power Shutoffs (PSPS) efforts are likely to continue into the '20 season; and while weather conditions similar to last year would result in less shut-offs, mgmt. is going to continue covered conductors in the riskiest areas (1K circuit miles) and re-inspect structures in more than 50% of high-fire risk areas in order to raise the wind threshold and have an overall smaller impact on customers. Recent efforts by the state to deploy Blackhawk helicopters, new retardant technologies to drive more effective suppression, and focus on wildfire mitigation (increased state budget by $90mn), should help to some extent. While utilities continue to focus on PSPS, we remind investors that to shut-off transmission lines, the company will need permission from CAISO first. At the end of the day, fire risk into 2020 will be a binary event.

Just how much exposure is there?

We estimate the T&D cap for EIX is ~$3bn ($2.1bn net of tax) as the maximum amount over a 3year period (3yr rolling average); said another way just $720mn for EIX in 2020. We note that the company would first have to eat through the $1bn insurance deductible and then go through its cap; the company had $1.2bn of insurance through June 30, 2020 and is in the process of procuring the additional amount from July 1, 2020 – June 2021. The cap represents ~46% of EIX earnings that are exposed in addition to amounts of insurance less than $1bn in any given year (subject to a prudency review).

Table 28: EIX Max Liability Cap represents ~46% of earnings on an ongoing basis

Max Liability Cap	2019A	2020E	2021E	2022E	2023E	2024E	2025E
CPUC rate base	24,600	26,760	28,848	30,870	33,270	35,770	38,156
FERC Rate Base	6,200	6,600	6,773	7,033	7,082	7,104	7,099
Total Rate Base	30,800	33,360	35,620	37,903	40,352	42,874	45,255
Less: Generation	1,000	1,000	1,000	1,000	1,000	1,000	1,000
Total T&D Rate Base	29,800	32,360	34,620	36,903	39,352	41,874	44,255
Equity Cap	48%	52%	52%	52%	52%	52%	52%
AB1054 Cap	20%	20%	20%	20%	20%	20%	20%
Total T&D Rate Base	2,861	3,365	3,601	3,838	4,093	4,355	4,602
3 -Year Rolling Average		2,942	3,276	3,601	3,844	4,095	4,350
Tax Effective @ 27%		2,148	2,391	2,629	2,806	2,989	3,176
Amount per year over 3yr period		716	797	876	935	996	1,059
BofA Earnings Estimates		1,654	1,713	1,873	2,051	2,207	2,255
% of Earnings		43%	47%	47%	46%	45%	47%

Source: BofA Global Research estimates, company report

Tracking the memo recovery: critical to limit equity

Mgmt. filed its Fire Memorandum Account (FMA) update, which initiated track 2 of the 2021 General Rate Case (GRC) proceeding. The company is seeking recovery of $509mn of O&M related expenses and $302mn of capital spending. This is considered track 2 of its memo recovery request with a decision not expected until 1Q21 with the GRC. The other items pertain to a decision with Wildfire Memorandum Expense Account (WEMA) for higher insurance cost vs. those approved (requesting $505mn in recovery) with a decision expected in Aug. 2020 and the (Catastrophic Event Memorandum Account) CEMA with a decision in March 2021 (for $88mn request). We now include an estimate for 2020 costs that mgmt. will file at YE20 w/ a decision in '22 (potentially growing by $400-500mn).

Mgmt. will defer these cost (once it consumes amount as prescribed in the GRC), although it's not getting any cash recovery, hence the impacts to credit metrics. We continue to see uncertainty around these items and look for more clarity in the coming months to understand the totality of equity needs as mgmt. has its own internal planning assumptions around recovery. Bottom line, recovery clarity could still take some time and we continue to see some risks on recovery given agencies assume this will be recovered.

Table 29: EIX Wildfire Memorandum Accounts

Memorandum Account	Capital Expenditure	O&M Spent	Total Request	Timeline
Wildfire Mitigation Plan	302	304		PD 1Q21
Fire Hazard Prevention		198		PD 1Q21
Fire Risk Mitigation		8		PD 1Q21
Total 2018-2019 FMA	302	510	500	
Track 2: Wildfire Expense Memo Account	-	341	505	PD Aug 2020
Catastrophic Event Memo Account	57	79	88	PD March 2021
Track 3: 2020 wildfire O&M assumption		~400	400	File YE20; 2022
Total Other Wildfire-related Memo Accounts	57	820	993	
Grand Total	778	1482	1,493	

Source: BofA Global Research estimates, company report

EPS Estimates

We provide our latest EPS estimates for EIX below, moving slightly higher on assumed forward looking share price issuance. Our estimates below are based on a fully diluted assumption with $670mn of incremental equity in 2021and $100mn of ongoing equity needs thereafter. We also continue to assume a constructive outcome in the 2021 GRC in that the company will be able to accrue cost savings over-time (similar to SRE) where we see a 10cent benefit in 2022.

Table 30: EIX EPS estimates and Mini-model

EIX Mini-Model	2018A	2019A	2020E	2021E	2022E	2023E	2024E	2025E
Authorized Capital Structure								
Authorized Equity Capital %	48%	48%	52%	52%	52%	52%	52%	52%
Authorized CPUC ROE	10.30%	10.30%	10.30%	10.30%	10.30%	10.30%	10.30%	10.30%
FERC ROE Build								
FERC Base Rate	9.92%							
CAISO (RTO Participation Adder)	0.50%							
Avg Project Incentive Adder	0.78%							
Assumed Equity Capital %			47.5%	48%	48%	48%	48%	48%
Authorized FERC ROE Build	11.2%	11.2%	10.3%	10.3%	10.3%	10.3%	10.3%	10.3%
Ratebase Growth								
Ratebase - Including Adjustments Below (Avg)	28,601	30,913	33,360	35,620	37,903	40,352	42,874	45,255
Guidance Low ($Bn) (Ex. ~$1.6Bn of fire risk mitigation from AB 1054)			33,300	35,100	37,000	39,200		
Guidance Mid ($Bn) (Ex. ~$1.6Bn of fire risk mitigation from AB 1054)	28,500	30,800	33,350	35,500	37,600	40,100		
Guidance High ($Bn) (Ex. ~$1.6Bn of fire risk mitigation from AB 1054)			33,400	35,900	38,200	41,000		
Breakdown:								
CPUC Ratebase (Avg)	22,107	24,038	26,519	28,934	31,001	33,295	35,781	38,153
FERC Ratebase (Avg)	6,144	6,875	6,841	6,686	6,903	7,058	7,093	7,102
Ratebase Growth	9.4%	8.1%	7.9%	6.8%	6.4%	6.5%	6.2%	5.6%
% FERC	23%	22%	19%	18%	18%	17%	16%	19%
Shares (Basic)	326	342	378	392	393	395	397	397
Shares (Diluted)	326	340	370	387	394	396	398	400
Ratebase-Only EPS	4.37	4.59	4.74	4.85	5.06	5.37	5.69	5.98
Additions/Subtractions to Spend								
Storage Upside (included in base CaEx			0.00	0.00	0.00	0.00	0.00	0.00
Transmission project - pending potential rejection (~$100 Mn capex)			-0.01	-0.01	-0.01	-0.01	-0.01	-0.01
Wildfire mitigation spend (~$1.6bn excluded from earning ROE)			-0.10	-0.08				
Charge Ready II ($561Mn of Capital)			0.02	0.04	0.06	0.08	0.08	0.08
Changes to Capital Structure and ROE Adjustments				New Rate Case Cycle @ 4 years				*Restart*
Cost Savings (ex-Debt Cost Savings) -> Tied to Rate Case Cycle	0.00	0.02	0.20	0.05	0.10	0.20	0.25	0.05
Interest expense from Wildfire Contribution Debt (~$1.2bn) - Opco Non-recoverable		0.00	-0.11	-0.11	-0.10	-0.10	-0.10	-0.10
Energy Efficiency	0.03	0.05	0.04	0.04	0.04	0.04	0.04	0.04
AFUDC Benefits		0.24	0.25	0.25	0.25	0.25	0.25	0.25
Corp Donations and Executive Comp *(Offsets largely AFUDC)*			-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
Parent Drag & Edison Energy								
Edison Energy Group (EEG) --> Breakeven into '20 & Beyond?	-0.04	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Parent and Other	-0.23	-0.33	-0.31	-0.35	-0.39	-0.39	-0.39	-0.39
Toal Parent & Other Drag (Incl EEG)	-0.27	-0.33	-0.31	-0.35	-0.39	-0.39	-0.39	-0.39
Total EPS (Basic)	4.14	4.67	4.38	4.37	4.76	5.19	5.56	5.68
Total EPS (Diluted)	4.14	4.70	4.46	4.43	4.75	5.18	5.54	5.64
Previous estimate		4.70	4.45	4.42	4.73	5.16	5.52	5.62
Consensus		4.77	4.42	4.58	4.83	5.13		
Guidance		4.70-4.90	4.32-4.62					

Source: BofA Global Research estimates, company report

Valuation: $65

We move our PO to $65 based on peer multiples of 17.1x (from 17.6x) and now apply a 4x discount to our EPS assumptions (from 3x) to capture execution risk into this fire season (equivalent to ~50% prob. of triggering the liability cap with 46% earnings at risk). Still with shares trading at a ~30% discount vs. the broader utility group, we see an opportunity for a re-rating on fire execution and more clarity on the balance sheet.

Exhibit 6: EIX SOTP Analysis

EIX SOTP							
SCE Components	% SCE	Authorized ROE Reflected	2022 Earnings	2022 EPS	Peer Multiple	Premium/Discount	Value per Share
Group Peer Multiple - Electric					17.1x		
Group EPS '18-'22 CAGR - Electric					5.00%		
CPUC - Core	82%	10.30%	1,660	$4.21	18.0x	-4.0x	$58.74
CPUC/FERC - Further Capital	1%		30	$0.08	18.0x	-4.0x	$1.07
FERC	17%	10.30%	338	$0.86	18.0x	-4.0x	$11.95
Edison Energy			0	0.00	10.0x	0.0x	$0.00
Parent/Other			-155	-0.39	18.0x	-4.0x	($5.49)
Total EPS				$4.75			
Ongoing contribution to Wildfire Fund				$Mn	EPS	Multiple	
NPV of Ongoing Wildfire Contribution ($945mn over 10yrs)				($664)			($1.68)
Total Equity Value ($/sh)							$65
Price Appreciation							15.3%
NTM Yield							4.5%
Total Return							19.85%
Shares	*394*						

Source: BofA Global Research estimates, company report

Essential Utilities (WTRG)

With a largely resi customer composition and the shoulder season of gas, we see WTRG as well positioned to navigate the evolving COVID crisis. Execution on their capital plans remains largely intact despite modest setbacks ($30Mn) earlier this year, and we would anticipate some further tailwinds from acceleration in muni deals during a recovery period. Meanwhile, we further continue to await developments around the catch up component of repairs tax implementation as additional upside to the recently rolled out guidance with a filing expected imminently. We reiterate our Neutral rating on shares of WTRG, seeing risk/reward as fairly balanced at the current valuation.

WTRG 2Q20 Earnings Walk

We forecast 2Q20 adjusted EPS of $0.24 compared to 2Q19 adjusted results of $0.37 and consensus of $0.22.

- **Key Drivers:** The primary driver of the quarter is the dilution from the Peoples Gas acquisition. This should be somewhat offset by growth in the legacy water business: partial quarter benefit of new rates in PA along with favorable weather should help mitigate COVID related headwinds.

Table 31: WTRG 2Q20 Walk

WTRG 2Q20 Earnings Walk		EPS
WTRG 2Q19 EPS	$	0.37
Aqua		0.01
Peoples Gas		-0.03
Dilution		-0.11
1Q20 BofAe Adjusted EPS	$	0.24
Consensus		$0.22
WTRG Guidance		$1.53-$1.58
2020 Consensus		$1.53

Source: BofA Global Research, Bloomberg

Weather & Commission Help Should Mitigate COVID Impacts

WTRG has guided to 2020 earnings of $1.53-$1.58 and a 5-7% EPS CAGR through '22. The largely residential profile of the water biz provides some protection against load degradation while the gas biz remains in shoulder season, and we expect some benefit from favorable weather at least in 2Q. While early action was taken to maintain a more conservative amount of liquidity, bad debt has been our primary concern. That said, the May order in PA helps to de-risk this given their particularly large presence in the state: recall the PA PUC issued a letter directing utilities to track COVID expenses and authorized regulatory assets for uncollectible expenses incurred above those embedded in rates since the PUC's March 13, 2020 Emergency Order - any regulatory asset created under the authorization contained in the Secretary's Letter will ultimately be subject to review by the PUC in future proceedings. While this won't provide immediate help to cash flow, it should help limit degradation to P&L in the nearer term.

DELCORA Dilemna? Consolidation Prospects Remain Strong

The latest economic pressures are likely to further accelerate consolidation in the industry as muni budgets are further flex'd from the crisis - and any further resulting acquisitions would be upside to mgmt.'s latest reaffirmed targets. States we are watching in the near term include TX & OH following the passage of FMV legislation in the states early last year and VA passing the legislation more recently. While we perceive TX bids as likely more competitive, WTRG is currently the only large water utility in the state of OH - and we see particular opportunities as likely to emerge following the Campbell acquisition. We see NC as another state to watch given the new commission dynamic, albeit muni acquisitions there seem less clear cut relative to the more challenged munis in PA and IN.

Overall, we remain particularly bullish prospects for further consolidation for the water industry going forward shy of any infrastructure bill of magnitude materializing.

Meanwhile, watch developments around their pending DELCORA acquisition after the the independent authority filed an injunction to stop the county from dissolving the authority. That said, we don't see meaningful risk to the deal and it remains upside to estimates over time from the currently laid out plan.

Catch Up Filing Imminent

After closing on the Peoples Gas acquisition in Mid-March, the company elected the current component of repairs tax, reducing income tax by $5.9Bn for the quarter with expectations to drive $0.08-$0.12 worth of contribution for the year. This should limit any risk from rate cases in the state while further driving earnings upside. Meanwhile, the only rate case in North Carolina continues to progress with their request for $7Mn in additional revenue. So overall, we don't see strong reliance on rate cases to hit their targets, albeit watch timing of new rates for any acquisition upside.

Latest discussions suggested a filing for the catch up component imminently with the process taking six to nine months. We see this as the critical debate driving shares with another opportunity in the hundreds of millions over time.

Under implementation for the water biz, seven years of a ten year amortization went to the shareholder while three went to the ratepayer under a particularly constructive outcome. While it remains to be seen how the commission will rule this time around, a constructive outcome would give upside to their numbers.

We maintain our Neutral rating on shares, seeing risk/reward as balanced.

EPS Estimates

The exhibit below reflects our current EPS estimates ahead of the upcoming quarter. We see limited risk to NT numbers and continue to model to the high end of their LT CAGR guidance.

Table 32: EPS Estimates

EPS Estimates	2020E	2021E	2022E
PA	$0.73	$0.80	$0.86
OH	$0.07	$0.07	$0.08
IL	$0.07	$0.08	$0.08
TX	$0.06	$0.07	$0.07
NC	$0.04	$0.04	$0.05
Other States	$0.07	$0.07	$0.08
Water Utility	1.04	1.13	1.21
Peoples Gas	0.62	0.67	0.72
Parent & Other	*-0.10*	*-0.11*	*-0.14*
EPS	1.56	1.69	1.80
YoY Growth	*6%*	*9%*	*6%*
Guidance	1.53-1.58		
Fully Diluted Shares O/S	*254*	*254*	*254*
Previous EPS	*$1.56*	*$1.69*	*$1.80*
Consensus	1.53	1.66	1.79
DPS	0.99	1.06	1.13
Payout Ratio	*63%*	*62%*	*63%*
Guidance	*60-65%*		
Share Count	238	238	250

Source: BofA Global Research, Bloomberg

Valuation

The exhibit below reflects our latest SOTP after applying the current peer multiples to our valuation: 26.9x for water and 15.9x for gas (vs. 26.3x for water and 17.6x for gas previously). Our PO remains unchanged at $49 and we maintain our Neutral rating seeing risk/reward as balanced at the current valuation.

Table 33: SOTP

Water Utilities	2022 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*26.9x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		29.1x							
Water Utilities									
States	2022E EPS	ROE embedded							
PA	$0.86	10.0%	2.0x	30.1x	31.1x	32.1x	$26	$27	$28
OH	$0.08	9.4%	2.0x	30.1x	31.1x	32.1x	$2	$2	$2
IL	$0.08	9.1%	3.0x	31.1x	32.1x	33.1x	$3	$3	$3
TX	$0.07	10.0%	0.0x	28.1x	29.1x	30.1x	$2	$2	$2
NC	$0.05	9.2%	1.0x	29.1x	30.1x	31.1x	$1	$1	$1
Other (including acquisitions)	$0.08	9.2%	0.0x	28.1x	29.1x	30.1x	$2	$2	$2
Water utilities total (ex-Peoples)	$1.21			*29.9x*	*30.9x*	*31.9x*	$36	$38	$39
Gas Utilities									
Peer Gas P/E		*15.9x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		16.8x							
	2022E EPS	ROE embedded							
Peoples Gas	$0.72	12.1%	2.0x	17.8x	18.8x	19.8x	$13	$14	$14
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			-1165	50%			($582)	($582)	($582)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($531)	($492)	($576)
50/50 Weighted Drag from HoldCo Drag							($1,113)	($1,074)	($1,158)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							$45.00	$47.00	$48.00
Current Price								$43.88	
Dividend Yield								2.2%	
Total Return								9.36%	

Source: BofA Global Research, Bloomberg

Evergy Inc. (EVRG)

We forecast 2Q20 adjusted EPS of $0.70 vs. consensus of $0.68 and pro-forma 2Q19 results of $0.58. Our full-year forecast for EVRG of $3.06/sh reflects our expectation of drag resulting from Covid-related slowdowns – though we note EVRG remains one of the few companies in our coverage not to provide interim reporting during Q2, a decision related to the company's ongoing strategic process. We expect mgmt. will report a rebound in load across its service territory through Q2, largely in-line with utility peers, though we note EVRG remains exposed to key aerospace industrial customers in KS, with potential for a slower rebound across that sector.

- **Key Drivers:** Weather is expected to provide an uplift of $0.14/sh as we normalize for the negative effects of 2Q19 (4 cents) and account for milder weather in 2Q20 that increased the number of CDDs in EVRG's service area, particularly in KS. O&M savings including merger synergies are expected to provide an uplift of 6 cents as the company continues to look for ways to cut costs in order to realize full merger synergies, offset Sibley and Jeffery rulings from 2019 (1.5 cent drag in aggregate), and offset potential Covid-related drag on demand. We additionally see 4 cents of accretion from a lower share count in Q2 2020 following EVRG's share buyback program, but note that as this program has been suspended following the Elliott agreement this effect will abate in future quarters.

- **Unknowns:** Weather was warmer than normal in Q2 2020, particularly across EVRG's KS jurisdiction where June CDDs were well above normal. Given the greater importance of June CDDs in the shoulder Q2 quarter we expect a tailwind on results though we note the deviation from normal was more modest across MO. Weather impact on utility results is driven not just by the aggregate number of HDDs but also in the timing of deviations from norm (Jun CDDs worth more than April), and as such the precise weather impact is difficult to gauge. The Covid effect will likely be highest in Q2 as shut-in rules in EVRG's service territory were implemented in a staggered approach at the end of Q1 – we estimate a 7 cent drag.

Table 34: EVRG Q2 EPS walk

Earnings Walk	Notes	EPS
2Q19 EPS		0.58
Weather normal	Reverse favorable effect in Q2 2019	0.04
Weather 2Q20	CDD +19% vs norm; HDDs +13%	0.10
Other	Effect of COVID on load	(0.07)
2Q20 drivers:		
O&M	Cost savings, includes merger synergies	0.06
D&A expense		(0.01)
Interest expense	Incremental KCPL debt, holdco debt	(0.05)
COLI	Based on 2020 guidance	0.02
Jeffrey & Sibley	3 cent drag / annum for each, did not recognize in 2Q19	(0.02)
Accretion		0.04
2Q20E BofAe EPS		$0.70
2Q20 Consensus		$0.68
2020E BofAe EPS		$3.06
2020 Consensus		$3.05
2Q19 Share count		243
2Q20 Share count		227

Source: BofA Global Research Estimates, company report, Bloomberg

Stock trading dynamics

Shares of EVRG are back to trading near a relative high post-Covid, measured on a relative fwd 2Y PE compared to the IXU. Despite being a non-decoupled utility with exposure to two state jurisdictions, we sense investors are looking through near-term Covid impact and focusing on the potential for a constructive outcome from the ongoing strategic process. Recall that when we upgraded EVRG to Buy following the announcement of the formation of the Strategic Review and Operations Committee (SROC) on Mar 2, we applied a 2.0x premium to our electric utility peer multiple for valuation purposes after previously applying a discount to reflect EVRG's regulatory overhang and below-peer growth trajectory. With shares trading at a premium to the IXU of late we note investors remain focused on potential for a constructive SROC outcome, thought the company has not provided interim updates – we highlight the upcoming Jul 30 deadline for SROC recommendation to the board as the next key milestone, and remain Buy-rated.

Exhibit 7: EVRG relative chart

Source: Bloomberg

Covid: KS approves deferral, MO remains pending

In early July the KCC approved EVRG's petition for an Accounting Authority Order (AAO) to track and defer extraordinary costs (net of cost decreases) as well as lost revenues associated with the Covid pandemic. The AAO approval is not a finding that tracked costs and revenues will be recovered, rather that the items will be included in a future rate filing – recall that EVRG is under a rate stayout in KS until 2022 as part of its 2018 merger agreement. EVRG will be required to submit quarterly reports on the amounts tracked – including any federal or state assistance received. In its May filing, EVRG stated that several of its large industrial customers in KS – including Spirit AeroSystems, Textron Aviation, Hallmark Cards, and Goodyear – were forced to furlough employees or temporarily close facilities in its service territory. The AAO petition was supported by KCC staff in an earlier filing, nonetheless the KCC order is a constructive step for EVRG as it continues to deal with the pandemic and reflects a positive fact pattern toward eventual recovery of costs and lost revenues.

Separately, EVRG has filed testimony in its MO petition for an AAO all extraordinary costs and financial impacts that directly result from the Covid pandemic. The financial impacts include additional bad debt expense in excess of amounts recovered in rates and lost revenues, net of cost savings. As in its KS filing, EVRG disclosed that many of its large industrial customers - including a Ford plant – as well as commercial customers including casinos and the Kansas City Royals, were forced to curtail or suspend their

regular business activities, though the public filing does not detail lost sales resulting from the pandemic. The EVRG testimony proposes annual progress reports to track its Covid-related items for recovery, though given the KS ruling and evolving nature of the pandemic we expect the order to be for quarterly filings, should the AAO be approved.

Recapping a busy strategic quarter & looking ahead

Below we highlight some key takeaways from a series of developments during EVRG's strategic review that took place in Q2, and look ahead to the approaching milestones during the summer months which should bring clarity to the direction of the process – whether the company will contemplate M&A or an acceleration of rate base growth via a standalone plan.

KCC moves to get involved early in strategic process

The KCC approved a staff is petition for an order initiating an investigation into the ongoing EVRG strategic review. Staff's filing flagged a high degree of concern that Elliott's focus on increasing shareholder value will come at risk of ratepayers – forcing them to pay higher prices or have to suffer less reliable service in order to maximize shareholder value. Such a result is in direct opposition to EVRG obligations under a 2018 docket and the state's goal of making rates more competitive pursuant to SB 69 according to the filing. Staff did not ask the commission to take affirmative steps, referring to its inquiry as informational in nature. Staff will also petition for a new docket should EVRG elect for a standalone plan, given impact on potential core elements of the prior merger agreement under docket 18-095. Among the specific provisions of the 2018 merger agreement, staff calls out the items below as requiring particular scrutiny in the ongoing SROC review:

- 5-year Kansas rate moratorium following the 2018 rate cases.
- Earnings sharing plan to share merger synergies with shareholders/ratepayers.
- Upfront payments and bill credits.
- Recognition of $30m of merger savings in 2018 rate cases.
- Zero involuntary terminations in KS and maintain HQ in Topeka for 10 years.

New KCC appointment brings Industrials experience

On the same day as the KCC petition filing, Gov. Laura Kelley announced the appointment of Andrew French to the KCC seat being vacated by the expiration of Shari Feist Albrecht's term. French has most recently been employed as counsel at Smythyman & Zakoura, a Topeka-based law firm where he represented large industrial and commercial customers in utility-based litigation matters. With several years of experience litigating on behalf of large utility customers French brings highly relevant experience to the KCC's review of the SROC process and EVRG's retail rates.

Missouri: Focus on jobs, legislation path less clear

In contrast to the Kansas commission which just appointed Andrew French, an experienced litigator who has previously represented large industrial customers at the commission, the MPSC's five members are seen as more open to negotiation on individual issues, without a discernible ideological bent. Stakeholders see potential for progress on a number of issues including securitization and closure of aging coal plants – though this will require legislative action. The most recent appointed commissioner is seen as a proponent of renewable energy which may further accelerate the momentum for coal retirements. Commission staff are seen as key subject matter experts on issues such as authorized holdco equity layers, with commissioners largely relying on the analysis of staff to inform their decisions on such technical topics. The incumbent Missouri governor is largely expected to not seek an additional term if reelected this

November, having taken over from the predecessor halfway into the current term. In the event that the incumbent were to lose the election a new governor would take time to replace members of the MPSC, potentially slowing approval of any deal. With commissioners not ideologically opposed to a deal, a merger proposal that includes an additional rate stayout beyond the current one which runs through 2022 would be seen as most likely to garner support.

SROC milestones approaching in coming weeks

EVRG's Strategic Review & Operations Committee (SROC) created in EVRG's agreement with Elliott outlines specific dates by which proposals must be submitted, voted on, and presented publicly. Two of the four members of the SROC are the new directors selected by Elliott - industry vets Paul Keglevic and Kirk Andrews - giving the activist manager even representation with incumbent directors. Unsurprisingly, given intense focus by utility mgmt. teams and state utility regulators (not limited to EVRG) on maintaining ongoing service amid the Covid emergency, the SROC issued an updated time frame pushing back its most significant deliverables further into the year. We view the revised timeframe below as merely reflecting the practical realities of evaluating a complex transaction amid work-from-home restrictions and market volatility and remain constructive on the overall direction of the review.

- **SROC recommendation to Board due Jul 30.** The original timeline called for the committee to present to the Board its recommendation of a transaction or standalone strategy by May 30 - note that the specific recommendation will also determine the level of public disclosure, as we detailed previously.

- **Board announcement by August 17.** Previously June 17, giving the Board the same number of days to evaluate as under the previous timeframe. We note some nuance in the language of the agreement that allows members of the SROC to publicize both recommendations in the event of a tie vote and *both Elliott-appointed directors voting for the same recommendation*, in which case the external directors are permitted to discuss their vote publicly within 5 days of the earlier Jul 30 deadline.

- **Modified standalone plan by Oct 14 if selected.** Originally the deadline was Sep 4, so the time frame for a presentation of a potential standalone plan has been pushed back by six weeks. We continue to view this as the less likely option given specific wording of the SROC agreement and note that logistics around presenting such a plan may require rethinking in the wake of Covid. Note this deadline now also impacts EVRG's reporting to the KCC that is required pursuant to the commission's recent order, which is required to answer a set of questions about the committee's decision and process.

Updated estimates

We maintain our EVRG estimates at $3.06/sh for 2020 as we had previously reduced our forecast to account for Covid-related impacts and resulting company response via additional cost-cutting (mgmt. announced an additional 1% of cuts on the Q1 call). Our estimates are 1 penny above Street in 2020 after consensus forecasts were revised down to reflect the 2020 sales outlook. Looking ahead, we make tweaks and maintain our long-term EPS growth forecast which is based on rate base growth of 3-4% based on the most recent rolled-forward capex forecast presented by mgmt. on is Q4 call. While rate base and earnings growth is certainly below the peer group, we sense investors remain focused on the outcome of the strategic review principally, with organic growth considerations currently seen as less urgent by most investors.

Table 35: EVRG estimates

Evergy, Inc. Dashboard

EPS Estimates by Subsidiary	2018A	2019A	2020E	2021E	2022E	2023E	2024E
Evergy Metro	$0.76	$1.06	$1.07	$1.13	$1.17	$1.20	$1.23
Evergy Missouri West	$0.35	$0.37	$0.44	$0.47	$0.49	$0.51	$0.52
Kansas Central	$1.58	$1.43	$1.67	$1.78	$1.88	$1.92	$1.95
Parent/Other	($0.19)	($0.08)	($0.11)	($0.11)	($0.11)	($0.13)	($0.16)
GAAP EPS	$2.50	$2.79	$3.06	$3.28	$3.44	$3.50	$3.53
Y/Y EPS Growth %		*11.6%*	*9.7%*	*7.1%*	*4.7%*	*1.9%*	*1.0%*
Prior estimates	$2.50	$2.89	$3.06	$3.27	$3.40	$3.47	$3.50
Consensus (BBG)		$2.92	$3.05	$3.22	$3.38	$3.54	nm
DPS	$1.84	$1.95	$2.07	$2.19	$2.30	$2.42	$2.54
Dividend Payout (60-70%)	73.5%	69.8%	67.5%	66.8%	66.9%	69.0%	71.8%

Source: BofA Global Research, Bloomberg

Valuation

We update our PO to $68 reflecting an updated electric utility peer group multiple of 17.1x (17.6x previously). Our valuation is largely unaffected by the near-term drag on our estimates related to milder weather and Covid as both are expected to normalize by 2022. Shares have re-rated vs the peer group since our upgrade to Buy though we still perceive upside to the current share price amid ongoing strategic review.

Table 36: ERG SOTP

Evergy Sum-of-the-Parts Valuation	2022 EPS	P/E Multiple					Equity Value/Sh		
		Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric			17.1x						
Group EPS '18-'22 CAGR - Electric			5.00%						
			18.0x						
Evergy Metro	$1.17	19.0x		2.0x	20.0x	21.0x	$22.24	$23.42	$24.59
Evergy Missouri West	$0.49	19.0x		2.0x	20.0x	21.0x	$9.32	$9.82	$10.31
Evergy Kansas Central	$1.88	19.0x		2.0x	20.0x	21.0x	$35.58	$37.45	$39.33
Parent & Other	-$0.11	19.0x		2.0x	20.0x	21.0x	-$2.00	-$2.10	-$2.21
EVRG consolidated '22 EPS	$3.44				*20.1x*		$65.00	$69.00	$72.00

	After-tax amount $m	$/sh	Probability				
Deferral of Sibley return + D&A	23	-$0.10	50%			-$1.99	-$0.99	$0.00
Shares outstanding (Average 2022)	227							
Shares outstanding (Y/E 2022)	227							
EVRG Price Objective						$63.00	$68.00	$72.00
Implied Return							7.68%	
EVRG Standalone NTM Dividend Yield							3.47%	
Total Return							11.15%	

Source: BofA Global Research, Bloomberg

FirstEnergy (FE)

We anticipate a quiet second quarter call approaching. We again expect to see the Street focus on New Jersey given it's the only regulatory rate case the company is in right now. For FERC, interim rates already took effect with a ruling on its 10.8% ROE request outstanding, and for distribution, the schedule is still outstanding. The lack of regulatory activity outside of this until 2023 is a positive in our eyes. FE is somewhat shielded from COVID impacts as Ohio is decoupled, it has a low portion of revenue that is tied industrial sales (just 7%), just 10% of industrial revenue is volumetric-based, and FE recovers uncollectible expenses in OH / NJ through a rider and in PA / WV / MD through base rates. We look for commentary on the company's $3bn per year of capex trajectory – particularly as mgmt. has noted perhaps +$400mn of additional opps. We also look for hints towards the West Virginia IRP scheduled for later this year (given FE indicated it expects it will show need for capacity), and updates on credit rating agency discussions. We forecast a 2Q20 estimate of $0.54/sh – just 1c lower than Consensus.

2Q20 EPS Walk

We forecast a 2Q20 of $0.54/sh versus a Consensus of $0.55/sh and last year's 2Q19 estimate of $0.61/sh.

- **Drivers**: We anticipate 2c of riders and decoupling along with -6c of losing the OH DMR as key drivers for the quarter.
- **Other**: 2Q is generally not a large driver for the year given it is a shoulder month; as 2Q20 saw a hotter than normal June and colder than normal April, we factor in +1c. 2Q19 was slightly mild versus normal, we assume +1c in reversing last year's impact. We also factor in -2c of D&A, lower intr exp from refinancing maturities at lower interest rates that are balanced by higher distribution & transmission interest, and a flat parent with balancing tax implications.
- **Wildcard**: We only factor in -1c of Covid impact based on the four weeks of data provided on the last earnings call (i.e. -13% in C&I and +6% in resi). We anticipate O&M savings of +1c largely offset this.

Table 37: FE 2Q20 EPS Walk

FirstEnergy 2Q20 Earnings Walk	EPS
2Q19E Adjusted EPS	0.61
Regulated Distribution	-0.04
Weather Vs normal in 2Q19	0.01
Weather Vs normal in 2Q20	0.01
Distribution sales growth / Covid impact	-0.01
Riders: Including Ohio Grid Mod, Ohio decoupling, PA LTIIP, OH DCR	0.02
OH: DMR (stopped recognizing earnings benefit)	-0.06
FE Tomorrow	0.00
O&M: Pension & OPEB	0.01
D&A and taxes	-0.02
Debt maturities	0.00
Regulated Transmission	0.01
Revenues (net of D&A and taxes): higher ratebase	0.01
Parent and Other	-0.02
Tax rate benefit	-0.02
Timing of taxes	-0.02
2Q20E Adjusted EPS	0.54
2Q20E BofAe EPS	0.61
2Q20 Consensus	0.55
2Q Guidance	0.48-0.58
2020 BofAe EPS	2.46
2020 Consensus	2.48
2020 Guidance	2.40-2.60

Source: BofA Global Research estimates, company report, Bloomberg

Key topics for 2Q20

- **Capex**: Reiterated comments made around capex during fireside chat.

- succession planning and CEO turnover are likely a 2021 item- albeit as part of an entirely regulatory path. OH is likely to continue under PUCO leadership of Sam Randazzo and with ~2.5 years of the current admin left, there remains ample time for legislation or reg reform that establishes stability

FFO/debt, Balance sheet, credit rating

FE's Balance Sheet is improving with expectations of improving credit metrics translating at first with an upgrade from S&P and subsequently Moody's, albeit still largely in the 12% FFO/debt range for our reconciliation. We' expect a positive outlook from S&P first – as early as later this year. Mgmt. has acknowledged it is discussing its credit metrics with rating agencies, with potential positive news to come from S&P considering the agency lowered its FFO/debt threshold to 12%. Moody's upgrade threshold is 14% however, so the process may be a little more protracted - but there is potential opportunity for Moody's to bring down its upgrade threshold to 13% (note Fortis' is 11-13% and FE noted it sees its companies in line with theirs in terms of credit and risk). We could expect to see FE approach a 13% FFO/debt in the next few years, particularly as FE has plans for incremental equity starting in '22 and the years after (could be up to $600mn/yr). With its FES business disposition resolved, we perceive few angles to meaningfully shift its balance sheet outlook so look to '22-'23 when the potential Moody's upgrade could be.

Rate cases

FE is one of the least exposed amongst peers to lower authorized returns given the company re-affirmed limited regulatory activity thru the forecast outlook with capex largely recovered thru riders rather than litigated cases. We suspect this limited rate case risk profile will increasingly resonate with investors keen to pursue a less volatile & overall noisy profile. Outside its NJ cases, FE is not planning to file elsewhere for several years - specifically noting for at least three years without a case. The pandemic is not expected to have an impact on timing.

We are still awaiting outcomes in NJ. For distribution, FE awaits a rate case schedule from the ALJ. NJ is just 13% of our modeled '22 EPS and that the distribution case was never included in FE's 2020 guidance. FE noted previously it expects an opportunity to settle (at the earliest later this year), and updated timing for a full case to a result in '21. Recall NJ is already FE's lowest allowed ROE at 9.6%, and we model 9-9.5% earned in the next few years. This remains among the principle (small gyrations) in outlook still.

Sustainable capex

Mgmt. continued to reiterate that it has a strong ability to execute on its ~$3bn/yr capex plans (+/- ~$400mn/yr - more likely a +). Further, the company has flexibility in its size and geographic diversity that allows it to proactively shift where it deploys capex. Mgmt. again noted that it is leaning towards not pursuing a second round of IIP at JCP&L because it currently sees itself as having accomplished reliability projects in the state, while also having enough investments in other states. The West Virginia IRP this fall is likely to drive new generation needs, improving opportunities but unclear if this will see an aggregate uptick in capex levels; we would expect a generation outlook is more likely in 2H.

Succession

The company announced plans to search for a candidate internally, we would expect any succession to take place next year at the earliest (if not longer). We see a discussion of mgmt incentives around change in control as meriting some attention. We see governance and exec comp as having improved in recent years under its regulated strategy.

Estimates

We provide our latest EPS estimates below.

Table 38: FE EPS Estimates

EPS	2016A	2017A	2018A	2019E	2020E	2021E	2022E	2023E	2024E	2025E
Ohio Utilities	0.50	1.03	1.23	0.92	0.82	0.83	0.85	0.88	0.91	0.94
Ohio Edison (Inc PennPower)	0.35	0.59	0.64	0.50	0.48	0.49	0.51	0.53	0.55	0.57
CEI	0.09	0.27	0.39	0.26	0.20	0.20	0.20	0.21	0.21	0.22
TE	0.06	0.17	0.20	0.15	0.14	0.14	0.14	0.15	0.15	0.15
West Virginia										
MonPower	0.15	0.16	0.25	0.21	0.21	0.22	0.23	0.23	0.23	0.25
Maryland										
Potomac	0.14	0.10	0.10	0.10	0.12	0.14	0.16	0.18	0.20	0.22
New Jersey										
JCP&L	0.19	0.26	0.32	0.32	0.33	0.35	0.35	0.37	0.39	0.41
Pennsylvania	0.73	0.76	0.93	0.92	0.92	0.94	0.94	0.95	0.98	1.02
PennPower (already included in OE)	0.05	0.07	0.07	0.08	0.08	0.08	0.08	0.08	0.08	0.09
Penelec	0.21	0.22	0.32	0.29	0.29	0.30	0.30	0.31	0.32	0.33
WPP	0.27	0.25	0.23	0.24	0.24	0.23	0.23	0.24	0.25	0.26
MetEd	0.21	0.22	0.31	0.31	0.32	0.32	0.32	0.32	0.33	0.34
Regulated Utilities (Inc Transmission)	*1.66*	*2.23*	*2.75*	*2.40*	*2.33*	*2.40*	*2.45*	*2.53*	*2.63*	*2.75*
Regulated Distribution	-0.55	2.32	2.31	2.26	2.15	2.20	2.23	2.27	2.35	2.45
Guidance	2.60-2.70	2.27-2.31	2.34-2.40	2.20-2.26	2.13-2.27					
FET	0.45	0.62	0.58	0.66	0.69	0.75	0.82	0.89	0.95	1.02
Intrastate	0.28	0.13	0.21	0.16	0.18	0.20	0.22	0.25	0.27	0.30
Transmission	0.73	0.83	0.74	0.83	0.89	0.95	1.04	1.14	1.22	1.32
Guidance		.82-.84	.74-.76	.83-.84	.85-.89					
Competitive Energy Svcs.	0.60	0.46	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Guidance		0.42-0.46								
Corporate (reduced by pref)	-0.55	-0.53	-0.56	-0.51	-0.57	-0.55	-0.56	-0.55	-0.55	-0.55
Guidance		-0.51	(.58)-(.56)	(.53)-(.50)	(.58)-(.56)					
Eliminations		0.16	0.13	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Consolidated EPS	2.61	3.07	2.59	2.58	2.46	2.59	2.71	2.86	3.03	3.20
Guidance		3.00-3.10	2.50-2.60	2.50-2.60	2.40-2.60					
Previous EPS		3.07	2.59	2.58	2.46	2.59	2.71	2.86	3.03	3.20
Consensus EPS		3.05	2.54	2.53	2.48	2.63	2.76	2.89	3.02	
EPS CAGR off 2.15 (2018)					7.03%	6.47%	5.95%	5.85%	5.88%	5.83%
EPS CAGR off 2.43 ('19 2.55 Midpt less 0.12 DMR)					1.35%	3.34%	3.69%	4.13%	4.51%	4.68%
EPS CAGR off 2020						5.37%	4.89%	5.08%	5.31%	5.36%
EPS CAGR off 2021							4.40%	4.93%	5.29%	5.36%
Ex CES EPS	2.02	2.61	2.59	2.58	2.46	2.59	2.71	2.86	3.03	3.20
YoY Growth Rate Excl CEC EPS				0%	-4%	5%	4%	5%	6%	6%
Sum of the subs		3.24	2.49	2.58	2.48	2.59	2.71	2.86	3.03	3.22
Bottom - 5%			2.15	2.26	2.37	2.49	2.61	2.74	2.88	3.03
Top - 7%				2.30	2.46	2.63	2.82	3.02	3.23	3.45
Shares	429	444	538	539	543	543	549	561	572	583

Source: BofA Global Research estimates

Valuation

We provide our latest SOTP valuation below. We maintain our Buy rating and $45.50/sh SOTP valuation, tweaking our regulated peer ute multiple slightly higher to 17.1x (17.0x previously).

Exhibit 8: FE SOTP Valuation

FirstEnergy SOP Valuation									
	Metric	P/E Multiple					Equity Value ($/sh)		
	2022 EPS	Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric			17.1x						
Group EPS '18-'22 CAGR - Electric			5.00%						
Electric Utilities			18.0x						
FE Utilities: OH Utility (CEI, Ohio Edison, TE), Ex-DMR, Ex-PP	$0.78	16.0x		-1.0x	17.0x	18.0x	$12	$13	$14
FE Utilities: PA Utility (MetEd, WPP, PenElec, Penn Power) - WPP T Incl	$0.94	17.0x		0.0x	18.0x	19.0x	$16	$17	$18
FE Utilities: NJ Utility (JCP&L) - T&D	$0.35	17.0x		0.0x	18.0x	19.0x	$6	$6	$7
FE Utilities: Other Utility (MonPower, Potomac Ed) - T&D	$0.38	17.0x		0.0x	18.0x	19.0x	$7	$7	$7
Less: Intrastate Transmission embedded above	-$0.22	17.0x		0.0x	18.0x	19.0x	-$4	-$4	-$4
FE Utilities: Transmission (FET + Intrastate)	$1.04	17.0x		0.0x	18.0x	19.0x	$18	$19	$20
Total T & D 'Regulated' Utility EPS	$3.27				17.7x		$55	$58	$61
BAMLe Utility + Parent	$2.71								
Holding Company Liabilities & Earnings Drag									
FE: HoldCo Drag	-$0.56	16.7x		0.0x	17.7x	18.7x	-$9.4	-$10.0	-$10.6
Add Back: Interest Expense drag @ 50%	$0.22	16.7x		0.0x	17.7x	18.7x	$7.4	$3.9	$4.1
Holding Company Debt								$Mn	
Short Term Holdco Debt								$750	
Unsecured LT Debt								$6,100	
Total Debt								-$6,850	
Total Debt @ 50% Split								-$3,425	
$/Sh - Equity value in valuation								-$6.2	
Total Debt at Parent (per share)								*-$12.48*	
Other Liabilities	Liability	Probability					Low	Base	High
Shares Outstanding (2022e)								549	
Total Equity Value							$40.00	$45.50	$49.00
2020 Dividend								$1.57	
Current Yield								3.7%	
Price Return							-5%	8.0%	16%
Total Return							-1%	12%	20%

Source: BofA Global Research estimates

Pinnacle West (PNW)

We expect Q2 Operating EPS of $1.55/sh as compared to $1.34/sh Street estimates and $1.28/sh in 2019. Weather is expected to be the largest single driver as we normalize for the effects of a significantly below-normal 2019 and add further tailwind from 2020 CDDs. We further note that PNW had increased its bad debt expense target for 2020 given last year's disconnect moratorium, suggesting it may be better able to withstand an increase in delinquent accounts than peers. We see additional impact from COVID-19 on sales – though this impact appears to have largely abated as the quarter developed resulting in company-reported flat weather-normalized level of sales for a trailing 33-day period ending in June. However, given the uptick in cases of COVID-19 in the state of Arizona, we acknowledge that C&I sales may fluctuate through the coming quarter. Finally, PNW's most important earnings quarter is Q3, with potential upside to results from increased residential usage given that customer segment's higher margin contribution. While visibility around the near-term outlook appears to be improving (and for the better), we continue to see substantial risks around the pending rate case (and potential for ACC turnover), with upcoming staff testimony the next significant milestone to watch for – due Aug 3.

2Q20 Walk

We forecast 2Q20 adjusted EPS of $1.55 vs. $1.28 in 1Q19 and $1.34 Street consensus. We expect substantial upward revisions to Street estimates over the coming weeks.

- **Key Drivers:** Weather normalization will be a significant driver in Q2 as 2019 was a below-average weather quarter, with an uplift of 31 cents. In addition, we see 14 cents uplift from weather in 2020 as service territory CDDs were meaningfully above normal (14% above normal). We see COVID-19-related impacts on EPS of -15 cents, which is in-line with company provided disclosures during Q2. While PNW realized significant Q1 savings in O&M – near levels suggested by its full year 2020 guidance – we assume an additional one cent of savings in the quarter as mgmt. seeks additional offsets to drag resulting from lost sales. Finally, we see two cents of drag related to pension/OPEB given the six cent gains reported in Q1 relative to full-year company guidance.

- **Unknowns:** Weather and COVID-19 sales fluctuations are the two key wildcards in Q2, with both playing meaningful and opposite roles. Unlike Q1 where both weather and COVID-19 provided a drag on utility earnings, we see the two factors as largely offsetting in Q2. Our 14 cent weather uplift estimate is based on CDDs 14% above normal as reported by PNW, compared with 27% below normal in 2019. Our COVID-19 impact of 15 cents is based on an earlier intra quarter update by the company which disclosed an EPS impact of -$0.14/sh for the period of Mar 13 – May 26, and the expectation that drag from lost sales *abated slightly during June* given the state's reopening schedule, though we acknowledge some uncertainty here given: 1) relative weighting of warmer-month earnings, and 2) uptick in COVID-19 cases and resulting impacts on business and consumer behavior.

Table 39: PNW Q2 earnings walk

PNW 2Q20E Earnings Walk	EPS
2Q19 Adjusted EPS	$1.28
Weather return to normal	$0.31
Weather effect vs norm	$0.14
COVID-19 sales impact	($0.15)
Gross margin	$0.02
O&M	$0.01
D&A	($0.04)
Interest Expense	($0.01)
TEAM	$0.01
Other Opex - pension and OPEB	($0.02)
Dilution	($0.00)

Table 39: PNW Q2 earnings walk

PNW 2Q20E Earnings Walk	EPS
2Q20E Adjusted EPS	$1.55
2Q20E Consensus	$1.34
2020E Adjusted EPS	$4.80
2020E Consensus	$4.83
2020 Guidance	$4.75-4.95

2Q19 Shares Outstanding	113
2Q20 Shares Outstanding	113

Source: BofA Global Research estimates, Bloomberg

COVID-19 disclosures trending in the *right direction*

We estimate a 15 cent impact from COVID-19-related sales disruptions in Q2. PNW's early June update reported a 14 cent EPS drag from Mar 13 to May 26, which we assume is heavily weighted toward April-May when the full impact of state closures took effect. With sales impacts abating per the most recent disclosures which cover the period running through mid-June, we expect that the weather-normalized impact on sales in the month of June was not as intense as in the prior periods reported. Below we include the weather-normalized sales trends by customer class for several periods as reported by the company as well as trailing-period EPS impacts. While most of the figures below are reported by PNW in its interim updates, the $0.15/sh EPS drag for Q2 in the rightmost column is our estimate based on prior-reported figures.

Table 40: PNW COVID-19 sales and EPS impact

			Mar 13 - Apr 30		May 1 - May 26		May 13 - June 16	
Sensitivities	Sales	Annual EPS Impact	Sales	EPS impact 3/13 - 4/30	Sales	EPS Impact 3/13 - 5/26	Sales	EPS Impact Q2 (BofA estimate)
Residential	1%	$0.09	7%		4%		4%	
Commercial	1%	$0.05	-14%		-8%		-4%	
Industrial	1%	$0.01	-14%		-8%		-4%	
Total		$0.16-0.20	-7%	($0.10)	-4%	($0.14)	0%	($0.15)

Source: BofA Global Research estimates, company reports

Catching up with mgmt. on key topics

Below we review the key issues surrounding PNW after catching up with its management team on our recent fireside chat. We saw this as an opportune time to discuss the company's broader strategic vision and strategy for improving regulatory relationships. A recap of key topics follows.

- **Don't expect a settlement of the APS rate case.** Mgmt. sees little pathway to a settlement of the current APS rate case given the procedural and election schedules coming up in the second half of the year. Upcoming milestones in the rate case include filing of staff/intervener testimony on Aug 3 and the beginning of the Hearing on Sep 30. At this point in the calendar, PNW mgmt. expects that *even if a settlement agreement were reached with key counterparties, procedurally it would need to be approved by the next commission which will be seated in 2021.* Recall that 3 of 5 commissioner seats are up for election in Nov, with a minimum of 2 guaranteed to be replaced as Chair Bob Burns is termed out and Boyd Dunn is barred from running after forging signatures. Given these dynamics, mgmt. indicated the difficulty in reaching general consensus on key issues including revenue requirement, ROE, and equity layer with stakeholders and then seeking subsequent approval of a settlement agreement from a commission with 40% new members in 2021. Despite some earlier indications that a settlement may be possible (in order to give the current ACC an opportunity to decide APS' rates), all indications now point to a fully litigated outcome.

Table 41: APS case schedule

Event / Item Due	Original	Updated
Staff & Intervenor Testimony w/o Rate Schedules	5/20/2020	8/3/2020
Staff & Intervenor Testimony w/ Rate Schedules	5/27/2020	8/10/2020
APS Rebuttal Testimony	6/18/2020	9/1/2020
Prehearing Conference	7/13/2020	9/26/2020
Hearing Begins	7/17/2020	9/30/2020
Hearing Ends (30 day)	8/31/2020	11/11/2020
Transcripts Filed	9/11/2020	tbd
Briefs Due w/ Final Schedules	9/16/2020	tbd
Response Briefs Due	9/25/2020	tbd
Recommended Opinion and Order	11/25/2020	tbd
Exception Period Ends	12/16/2020	tbd
Open Meeting	12/17/2020	tbd
Deadline for Final Decision (AZ rule)	2/21/2021	tbd

Source: ACC docket #19-0236

Two other utilities (FTS and SWX) currently have rate cases pending before the ACC that are further advanced. FTS expects a fully litigated resolution to its case *prior to ACC turnover*, leaving APS in the unique position of having its case process straddle two ACC benches. *We perceive the protracted processes with these to suggest a case potentially delayed well into '21 with a new ACC composition.*

- **Pivot to clean generation is ongoing, expect mix of PPA and owned buildout.** Mgmt. expects to continue its pivot to a greater share of clean generation, as outlined in its decarbonization plan published earlier this year and recently-updated IRP filing. With 40% of its announced '21-22 capex plan allocated to clean generation, PNW is moving forward with a combination of owned and PPA renewable generation projects, and while the company intends to move forward with an ambitious Energy Storage buildout (750 MW through 2024 per the IRP), plans are currently on hold pending the outcome of the ongoing McMicken investigation. The company currently has two RFPs out for renewable generation including 150 MW of APS-owned solar and 250 MW of wind that may be owned or under a PPA structure. Critically, mgmt. sees future renewable solicitations as considering both owned and PPA structures given requirements to secure the most economic forms of supply. One potential form of additional PPA generation that was highlighted is a bolt-on addition to an existing renewable generation asset that is already contracted with APS, owing to the existence of already-built infrastructure that would reduce total costs to ratepayers.

- **Ratemaking and customer education are priorities – *but how to fix?*** *We see this as among the stickiest issues management has yet to resolve with its stakeholders.* Mgmt. highlighted its continuing efforts to rebuild relationships with regulators, as evidenced by frequent appearances at ACC open meetings to participate in direct dialogue with commissioners and the public – while efforts have yet to bear tangible outcomes, mgmt. indicated its intention to maintain the dialogue with stakeholders on the numerous issues in front of the ACC. We note the rate design question discussed in detail at a recent open meeting remains unanswered: given the requirement of the previous case settlement to encourage customers to opt-in to the "most economical plan", the company reported that a meaningful percentage of customers did not elect to do so, citing difficulty in getting customer engagement. Regarding future rate design, APS has proposed a flat bill option where the utility manages customers' thermostat settings though this proposal is opposed by some interveners for failing to send a price signal to customers.

- **No equity in '20, $300-400m coming *before* next case filing.** PNW does not expect to issue block equity until it is contemplating its next rate case filing. Company mgmt. has previously flagged some flexibility around APS' equity layer (rate case request of 54.7% has historically not been a negotiated term) with an

intention to true-up prior to its next filing. Consistent with prior statements, mgmt. does not expect to issue equity in order to preserve its credit rating. Our base case expectation is for a rate case filing in 2022, and we see an issuance of $350m, in line with the midpoint of mgmt. expectations, and a concurrent equity injection by PNW to APS in the same year. Additionally, while we forecast PNW's consolidated debt metrics to remain above the Moody's downgrade threshold through '22, we forecast the ratio dropping to ~18% by 2025 – consistent with mgmt. statements of some latitude on this front (not managing to a credit ratio).

Table 42: APS ROE and Equity forecast

Earned ROE - GAAP calculation	2018A	2019E	2020E	2021E	2022E	2023E	2024E
Average Equity Method - GAAP	10.45%	9.80%	9.51%	9.58%	9.19%	9.17%	9.65%
APS Earned ROE - GAAP	0.52%	9.80%	9.51%	9.58%	9.19%	9.17%	9.65%
Authorized Equity Layer	*55.80%*	*55.80%*	*55.80%*	*54.70%*			
Book equity (GAAP) %	*54.69%*	*53.13%*	*52.02%*	*52.07%*	*54.73%*	*53.19%*	*52.26%*
Equity Injection			5	260	625	10	10

Source: BofA Global Research estimates, company report

- **Renewable buildout is the path to greater cooperation with ACC.** PNW intends to shift its generation mix to 65% clean energy by 2030 (note this includes Palo Verde) by continuing its buildout of owned wind, solar, and storage and retiring Cholla in 2025. As part of its 2020-24 plan, the company intends to add 962 MW of renewable energy and 750 MW of storage, with the balance of the 2,900 MW in the plan consisting of Demand Side Mgmt, Demand Response, and Distributed Generation. *We look for whether management will be able to recover these in a rider treatment akin to its earlier AZ Sun program through the course of the pending rate case; we perceive this as increasingly key to rate case timeline and implicitly capex clarity too but don't perceive a need for pre-approval/CPCN for any of its renewables regardless. Meanwhile we anticipate a large chunk of its future renewable procurement to still be done on a PPA (rather than ownership) basis.*

- **Coal plans still key to de-risk in the rate case.** Given the uncertain treatment of the Four Corners scrubbers as part of the current rate case, mgmt. highlighted that previous dockets have laid out an evidentiary record for the need to invest in scrubbing technology and support for recovery in rates. While the rate case ask stands out for being one of the few among our coverage that actively seeks to *increase coal rate base,* PNW mgmt. stresses that Four Corners remains a key part of the company's generation mix today and expects to utilize the plant until its scheduled retirement in 2031 (itself pushed up from 2038 previously). We further note that the plant is a key employer in the Navajo Nation territory, making a potential early retirement thorny from a regulatory and political angle. PNW highlights that it sees its clean gen pivot as a key part of its strategy for enhanced cooperation with stakeholders and the ACC, noting significant support for renewables across the state.

Updated estimates

We update our PNW estimates as per below, as we increase our 2020 forecast from the low end of 2020 guidance to $4.80/sh, driven principally by the above-normal weather contribution in Q2. Our estimates are now three cents below Street consensus which itself is two cents below the midpoint of mgmt.'s guidance range. While PNW gave a relatively soft reaffirmation of 2020 guidance on its Q1 update, we see likelihood of a more confident tone on the upcoming call as a tailwind from warm Q2 weather and abating COVID-19 sales impacts has improved the near-term outlook of late, though we flag Q3 as critically important for the company's full year prospects given the importance of the peak cooling season. Looking ahead, we see an EPS CAGR of 3-4% through 2023 based on company-provided capex disclosures and assumptions around rate case filing

cadence and impacts on earned ROEs at APS. Upside to the current forecast is tempered somewhat by PNW mgmt. comments that the company intends to pursue PPA as well as utility-owned solutions for its future renewable procurement.

Capex updates

We perceive less confidence on long-dated further acceleration of current clean energy capex beyond '22, but rather more sustainable levels of investment. Meanwhile, we are critically focused on the 2Q call around the composition of just *what is reflected in its clean energy outlook.* As a reminder, the company has yet to clarify *what* specific projects are contemplated within its '21 guidance as far as clean energy investments go. We anticipate some level of details and/or risk of delay if not – but bias towards the former.

Table 43: PNW updated estimates

PNW EPS Estimates	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E	2025E
EPS From Continuing Operations	$4.55	$4.71	$4.95	$4.98	$5.30	$5.38	$5.76	$6.31	$6.34
Net Income (Loss) Attributable to Noncontrolling Interests	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17
Income From Discontinued Operations	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
Accounting Changes/Non Operating Adjustments	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
Linked to model - EPS	$4.37	$4.54	$4.77	$4.80	$5.12	$5.21	$5.60	$6.14	$6.18
APS - EPS From Continuing Operations	$4.66	$5.24	$5.19	$5.22	$5.55	$5.70	$6.13	$6.69	$6.72
Parent - EPS From Continuing Operations	($0.11)	($0.53)	($0.24)	($0.24)	($0.26)	($0.33)	($0.37)	($0.38)	($0.38)
Net Income (Loss) Attributable to Noncontrolling Interests	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)
EPS From Cont Ops Attributable to Common Shareholders	$4.37	$4.54	$4.77	$4.80	$5.12	$5.21	$5.60	$6.14	$6.18
Previous Estimates	*$4.37*	*$4.54*	*$4.77*	*$4.75*	*$5.12*	*$5.21*	*$5.60*	*$6.14*	*$6.18*
Guidance	4.15-4.30	4.35-4.55	4.75-4.95	4.75-4.95					
Consensus				$4.83	$5.07	$5.29			
Delta vs Consensus				($0.02)	$0.05	($0.07)			
EPS CAGR off 2019A				0.7%	3.6%	3.0%	4.1%	5.2%	4.4%
Street CAGR				3.1%	3.8%	3.9%			

Source: BofA Global Research estimates, Bloomberg

Valuation: PO to $78

We update our PO to $78 based on marking-to-market the electric utility peer multiple to 16.6x, from 15.6x previously. We continue to apply a -2.5x discount to PNW's consolidated '22 earnings, reflecting the unique set of regulatory risks facing the company in its sole AZ jurisdiction, notably timing of the current rate case whereby a settlement increasingly looks as if it is not an option and a *new* slate of commissioners will decide the pending proceeding – a decidedly uncertain prospect given Nov elections. Reiterate our Neutral rating as we see only modest return potential to shares at current levels.

Table 44: PNW updated SOTP

Price Objective $78	
PNW Valuation: P/E Based on 2022E EPS	
	Price Objective
2022 EPS	$5.21
Group Peer Multiple - Electric	16.6x
Group EPS '18-'22 CAGR - Electric	5.00%
P/E Multiple - Utility Average	17.4x
Premium	-2.5x
Price Objective	$78
2020 Dividend	$3.16
Dividend Yield	4.0%
Total Return (%)	1.6%

Source: BofA Global Research estimates, Bloomberg

PPL Corporation (PPL)

We remain Neutral rated on shares of PPL into the quarter. While shares have meaningfully underperformed this year, FX remains volatile with current forwards remaining at the low end of mgmt.'s assumptions (already lowered earlier this year) and we critically watch load impacts after mgmt. elected to keep guidance unchanged last quarter. While the UK is decoupled, volumes are only trued up on a two year basis and mitigating impacts in the jurisdiction could be critical to keeping guide intact. Meanwhile, we await any developments around a formal decision for a rate case in KY - which we continue to see as unlikely against the protracted pandemic and latest ROE backdrop – along with the RIIO-ED2 consultation from Ofgem expected later this month: LT ROEs in the UK remain a lingering uncertainty after latest pressure suggested by T&G drafts. Bottom line, we ultimately see risk/reward as balanced at the current valuation.

PPL 2Q20 Earnings Walk

We forecast 2Q20 adjusted EPS of $0.54 compared to $0.58 in 2Q19 & $0.56 consensus.

- **Key Drivers:** We expect COVID challenges in the UK and dilution to weigh on the quarter and offset currency tailwinds and O&M savings.

Table 45: PPL 2Q20 Walk

PPL 2Q20 Earnings Walk	EPS
2Q19 EPS	$0.58
WPD	
Rates & Loads	($0.05)
Pension Headwinds	($0.01)
FX Tailwinds	$0.05
Kentucky	
Reversal of Tax Benefit in 2Q19	($0.02)
New Base rates & Weather Against COVID Challenges	$0.00
PPL PA	
Growth & Covid Challenges	$0.01
Corp & Other	
Dilution	($0.03)
Depreciation	($0.02)
Interest	($0.01)
O&M Savings	$0.04
2Q20 BofAe Adjusted EPS	$0.54
2Q20 Consensus	$0.56
BofAe 2020E EPS	$2.45
2020 Consensus	$2.43
2020 Guidance	$2.40-2.60

Source: BofA Global Research, Bloomberg

Contemplating COVID Implications

After electing to keep guidance unchanged last quarter, we critically watch developments on load. Recall the company noted $0.03-$0.04 monthly impact in April primarily from lower electric sales in the UK and KY (2/3rds from the UK). Full disclosures noted specific early load observations and sensitivities in April: UK - +1-3% resi & (20-25%) C&I with a 1% change translating to a penny of EPS for each; PA - +6-8% resi & (15-20%) C&I with a 1% change translating to $0.005 for resi and no impact for C&I; KY - +5-7% resi and (15-20%). Given the extents of unknowns and a seemingly lack of conviction around full year guilde with 1Q results, we wouldn't be surprised for an expectation reset – albeit our estimates remain at the lower end but within their current guide.

FX Outlook: Forwards Remain Near Low End of Guide

After lowering embedded assumptions with an earlier update, FX rates and forecasts remain at the low end of the range. While the company is 86% hedged for the remainder of 2020 at an average rate of $1.55, it is only 8% hedged in 2021 at $1.32 and

completely exposed in outer years. On an open basis, every 1c in the exchange rate equates to about $0.01/sh of EPS for the company.

OFGEM Prospects: Contemplating Future UK Returns

Earlier this month, Offgem released its RIIO-2 draft proposals on price controls for the '21-26 period for transmission and gas distribution. The draft reflected a reduction of the base equity returns to 3.95% (post tax real, CPIH basis) for GT & GD, and 3.7% for ET vs. a previous 4.3% indication. The difference would appear principally driven by a change in lower interest rates reflected (and could yet change into the final decision).

While the draft proposals on Totex are 20-40% lower than business plans, the regulator indicated allowances to be considered on project by project basis instead of upfront considerations, and actual allowances could potentially be much higher than business plans. Ofgem's current base return proposal still includes a contentious -25bps adjustment justified by "information asymmetry" compared to -50bps adjustment previously included.

Shares of PPL underperformed on the news as we viewed the proposals more stringent than anticipated and as investors try to get a read-through to future returns for ED – a more protracted process that will shake out over the next couple of years. That said, the ED2 specific methodology expected later this month should provide some color around ED specific thoughts. We ultimately expect nuances between ED2 and the gas/transmission framework given different risk profiles. However, we see a desire from Ofgem to maintain incentives and give the best performing companies an ability to overearn, particularly as distribution networks will be a key enabler of the net-zero carbon target. Any developments out of the COVID crisis will also be critical in terms of nuances around their thought process for UK utilities longer term. *Our model assumes a base equity return of 3.95%, with up to 300bps of incentives.*

EPS Estimates

The table below reflects our latest EPS estimates after reflecting the latest currency forwards and on-going developments, and we see limited growth ahead given pension headwinds and questions around longer term UK returns, particularly without meaningful FX improvement.

Table 46: PPL EPS Estimates

PPL EPS Estimates	2020E	2021E	2022E	2023E
Regulated Utilities				
International Regulated	$1.39	$1.30	$1.29	$1.15
Pennsylvania Regulated	$0.62	$0.65	$0.68	$0.71
Kentucky Regulated	$0.55	$0.62	$0.68	$0.71
Domestic Utilities	*$1.18*	*$1.27*	*$1.36*	*$1.42*
Parent/Other	($0.13)	($0.12)	($0.12)	($0.10)
Consolidated EPS	$2.44	$2.44	$2.53	$2.47
Prior Estimates	*$2.45*	*$2.45*	*$2.52*	*$2.48*
Consolidated Growth CAGR off 2018 ($2.30 midpoint)	2.99%	2.04%	2.40%	1.41%
Consensus	$2.43	$2.45	$2.59	$2.76
Guidance	$2.40-2.60	$2.40-2.60		
DPS	1.66	1.68	1.69	1.71
DPS Growth (%)	*0.61%*	*1.00%*	*1.00%*	*1.00%*
DPS Payout	68.05%	68.61%	66.96%	69.33%
FFO (CFO pre-W/C) / Total Debt	15.02%	15.17%	15.51%	15.45%

Source: BofA Global Research, Bloomberg

Valuation: Risk/Reward Remains Balanced

The table below reflects our latest valuation based on a SOTP approach. On our latest estimates, we apply the current peer multiple of 17.1x (vs. 16.5x previously) for both PPL Electric and PPL Kentucky. Meanwhile, we ascribe a 25% premium to RAV for the UK biz.

Our PO ultimately remains unchanged at $27, and we continue to see risk/reward as balanced: Maintain Neutral.

Table 47: PPL SOTP

PPL Sum-of-the-Parts	EPS	Lower	Peer	Prem/ Disc.	Base	High	Equity Value Low	Base	High
RAV Approach	C2021 RAV								
WPD RAV	11,058	0.8x	1.0x	0.25x	1.3x	1.8x	$8,293	$13,822	$19,351
Less: WPD leverage (80% Gearing)							($8,846)	($8,846)	($8,846)
							($553)	$4,976	$10,505
UK Equity Value							($553)	$4,976	$10,505
Implied Valuation / Share							*-0.71*	*6.41*	*13.54*
Domestic: Regulated Utilities			2022 P/E Multiples						
Group Peer Multiple - Electric			17.1x						
Group EPS '18-'22 CAGR - Electric			5.00%						
		Base Multiple	18.0x						
PPL Electric Utilities	$0.68	17.0x		0.0x	18.0x	19.0x	$8,904	$9,429	$9,954
PPL Kentucky (KU/LG&A)	$0.68	17.0x		0.0x	18.0x	19.0x	$8,941	$9,469	$9,996
Parent/Int Expense	($0.12)	17.0x		0.0x	18.0x	19.0x	($1,526)	($1,616)	($1,706)
			50% Weighting						
PPL Cap Funding Debt	4,530		2,265				-2,265	-2,265	-2,265
Parent Interest Expense (Tax effected @ 21%)	142		71				1,204	1,276	1,347
--> Add back 50% of EPS drag above							-1,061	-989	-918
PPL Equity Value ($/Sh) Unrounded							$18.95	$27.41	$35.87
Shares Outstanding	2022 EPS						776	776	776
Total PPL Equity Value Per Share	$2.53						$19.00	$27.00	$36.00
Implied P/E							7.5x	10.7x	14.2x
Total Return Calculation									
Current Stock Price								$25.85	
Price Objective								$27.00	
Upside/Downside (%)								4.45%	
Dividend								$1.66	
Dividend Yield								6.42%	
Total Return								10.87%	

Source: BofA Global Research, Bloomberg

WEC Energy (WEC)

We expect WEC to hit the high end of its increased Q2 EPS guidance range of $0.67-0.69 for the quarter. WEC stood out as among the stronger 2020 guidance reaffirmations following Q1 reporting, with the company flagging ongoing O&M reductions above its original 2-3% forecast as an offset to an expected $70-80m gross margin drag due to sales lost resulting from Covid. The company provided an intra-quarter update where it flagged sales trending above its revised forecast, but it remains unclear whether the improving sales is due to faster-than-expected resumption of economic activity or to a higher incidence of Cooling Degree Days (CDDs) driven by unseasonably warm weather. Nonetheless, we perceive incrementally less pressure on mgmt. going into the Q2 print following the latest reaffirmation, and see the high end of 2020 guidance as well within reach.

WEC 2Q20 Earnings Walk

We forecast 2Q20 adjusted EPS of $0.69 compared to 2Q19 results of $0.74, consensus estimates of $0.67, and guidance of $0.67-0.69.

- **Key Drivers:** Weather is expected to be a key positive driver in Q2 with +3 cents from normalizing for below-normal temps in 2019 and an additional 5 cent uplift from warmer weather in 2019. While WEC has stated that Q2 sales have developed ahead of prior forecasts, we note it is unclear whether this is due to a faster reopening or to weather, accordingly we estimate an 8 cent quarterly drag from Covid lost sales based on company-provided sensitivities. American Transmission Co's (ATC) 3 cent uplift is driven by the Federal Energy Regulatory Commission's (FERC) Midcontinent Independent System Operator (MISO) order of 10.02% authorized ROE, recognizing benefits to 2015. Finally, in 2020 WEC realized the full benefits of its fuel cost recovery rider in Q1, resulting in a 2 cent drag in Q2 as compared to the prior year.

- **Unknowns**: Weather and Covid-linked shutdowns are both expected to have a disproportional impact on sales in Q2 and estimating the precise impact of both line items is difficult –warm weather along with a higher incidence of CDDs has coincided with the most acute period of lockdowns, largely mitigating the loss on our estimates. WEC maintains a Rabbi Trust to offset future legacy compensation obligations – while the trust tends to create Other Income in periods of strong market performance (as seen during Q2), the positive contribution tends to be offset in the O&M line, accordingly we do not estimate it in our walk below.

Table 48: WEC Q2 earnings walk

WEC 2Q20 Earnings Walk	EPS
2Q19 Adjusted EPS	$0.74
Weather - 2Q19 normalized	$0.03
Weather - 2Q20	$0.05
Covid impact	
Electric	($0.07)
Gas	($0.01)
Fuel cost recovery - all realized in Q1	($0.02)
Interest Expense - re-financing	($0.03)
D&A	($0.05)
O&M	$0.01
Storm expense	$0.00
ATC	$0.03
Infrastructure	$0.01
Dilution	($0.00)
Other income	$0.00
2Q20 Adjusted EPS	$0.69
2Q20 Consensus	$0.67
2Q20 Guidance	$0.67-0.69
2020 BofAe	$3.75
2020 Consensus	$3.73

Table 48: WEC Q2 earnings walk

WEC 2Q20 Earnings Walk	EPS
2020 Guidance	3.71-3.75
Share Count	
2Q19	317
2Q20	317

Source: BofA Global Research estimates, company report

Covid update and outlook

WEC last provided an update on Q2 sales expectations on its Q1 call, with the forecast below for the quarter and full-year results. An inter-quarter update from WEC disclosed that weather-normalized sales are trending above the current quarter outlook, which the full-year assumptions remain unchanged, following the lifting of state lockdown orders and resumption of business and commercial activity in a phased approach. Note that relative to 2019 normalized sales, mgmt.'s forecast calls for an annualized drop in total retail sales ex iron ore of 4.6%, with a modest 1.4% increase in residential sales offset by an 11.9% drop in C&I. While the WI Public Service Commission (WPSC) was one of the first commissions in the US to issue an order on deferral of Covid-related extraordinary items, we note the order includes bad debt and additional direct costs related to the pandemic and does not include lost revenues – we look to the Q2 update on cost cutting (where mgmt. flagged confidence) as well as weather contribution from higher than normal cooling days to provide the offset to lost revenues and allow mgmt. to hit the high end of its guidance range.

Table 49: WEC reported and forecast 2020 sales

	2020 Original	Q1 Actual	Q2 Forecast	2020 Revised
Residential	-0.2%	-4.6%	4.0%	1.4%
Small C&I	-0.3%	-2.6%	-8.0%	-4.6%
Large C&I	-1.0%	-3.1%	-18.0%	-10.5%
Total C&I	-1.2%	-2.5%		-11.9%
Total Retail	-0.6%	-3.2%		-5.3%
Total Retail ex iron ore	-0.5%	-3.4%		-4.6%

Source: Company report

Mgmt.'s Q1 announcement of an acceleration in cost cuts was predicated on offsetting an anticipated $70-80m in gross margin drag stemming from Covid. With additional Q2 data points now suggesting a meaningful weather tailwind, a key question remains whether mgmt. will continue to pursue aggressive cost reductions as originally planned, or whether an improving margin outlook will make less stringent cuts palatable. While some O&M reductions are a natural extension of telework and a reduced ability to travel, we perceive latitude to avoid certain discretionary cuts driven by better-than-expected contribution from weather during the quarter. Below we include our original estimate of O&M reductions aimed at offsetting the $70-80m of gross margin drag originally forecast from Covid-related shutdowns.

Table 50: Potential additional O&M savings; good historical success, but *where to now?*

	2016	2017	2018	2019	2020
Day to Day O&M	1,342	1,281	1,234	1,143	
y/y % chg		*-4.5%*	*-3.7%*	*-7.4%*	*-2-3%*
Addt'l O&M Cuts					
Pre-tax					75
Post-tax					63
PF Day-to-day O&M					1,052
y/y % chg					*-8.0%*

Source: BofA Global Research, company report

Infrastructure update: modest delay to Badger Hollow II

Though not particularly surprising following the announced delay of the Badger Hollow I solar facility, Badger Hollow II announced a project delay with an updated in-service date of year-end 2022 vs. year-end 2021 previously. WEC's contribution of $130m to the project is modest relative to its projected $1.8B spend during the forecast period. Given the delays are linked to Covid and staging of work crews in rural WI, we do not see the delays as indicative of further slippage or lack of execution on future projects.

Reflecting an NPV valuation across the infra segment

We update our valuation methodology for WEC. While we had previously continued to use a P/E based approach for valuing WEC's planned investment other than announced projects, we now update our approach to reflect this across the segment. We see a DCF approach as increasingly relevant given the reflection of asset lives of wind projects as well as varying risk profiles by asset type.

Table 51: Allocated and unallocated infra investment – NPV approach

Project Name	Investment	Unlevered NPV	Unlevered IRR	Capacity	In Service
Upstream Wind	307	115	8.8%	180	Jan-19
Bishop Hill III Wind	166	72	8.9%	119	May-18
Coyote Ridge Wind	145	63	8.7%	78	YE 2019
Thunderhead Wind	381	174	8.9%	270	YE 2020
Blooming Grove	389	192	8.9%	225	YE 2020
Total	1,388	616		871	
Shares		317			
Equity value per share		1.94			

Summary of unallocated CAPEX

Project Name	Investment	Unlevered NPV	Unlevered IRR	Capacity	In Service
2021 Capex	100	45	8.8%	67	YE 2021
2022 Capex	315	140	8.8%	210	YE 2022
2023 Capex	315	139	8.8%	210	YE 2023
2024 Capex	308	135	8.8%	205	YE 2024
Total	1,038	460		692	
Shares		317			
Equity value per share		1.45			

Source: BofA Global Research estimates,

Estimates: Moving to high end of '20 guidance

We update our consolidated WEC ests to reflect the high end of mgmt.'s $3.71-3.75/sh 2020 guidance range. Given the degree of confidence reflected by WEC mgmt. in the company's ability to meet its guidance following its Q1 reporting – indeed before the Q2 weather impact was fully known and before raising its quarterly guidance range – we feel comfortable at the high end of the range, even given the backdrop of continuing pressure on sales from Covid. We also tweak our ATC numbers slightly to reflect the updated FERC ROE of 10.02% plus 50 bps adder, though this has a modest impact on our numbers. Bottom line: we continue to see earnings growth near the high end of mgmt.'s 5-7% long-term guidance range through the forecast period.

Table 52: WEC updated SOTP

WEC EPS Estimates	2018A	2019A	2020E	2021E	2022E	2023E	2024E
WI Electric	$1.13	$1.15	$1.25	$1.26	$1.30	$1.34	$1.37
WPS	$0.55	$0.59	$0.56	$0.59	$0.64	$0.68	$0.71
WI Gas	$0.24	$0.26	$0.39	$0.48	$0.58	$0.67	$0.75
Peoples Gas	$0.42	$0.50	$0.44	$0.49	$0.55	$0.60	$0.65
North Shore Gas	$0.05	$0.05	$0.05	$0.05	$0.06	$0.06	$0.06
ATC	$0.36	$0.39	$0.42	$0.44	$0.47	$0.50	$0.51
We Power (PTF) + Non utility infrastructure	$0.70	$0.76	$0.77	$0.89	$0.91	$0.97	$1.03
MERC/MGU	$0.14	$0.15	$0.13	$0.14	$0.15	$0.16	$0.16
Parent & Int Expense	(0.23)	(0.24)	(0.26)	(0.38)	(0.41)	(0.43)	(0.43)
BofA Estimate	$3.34	$3.60	$3.75	$3.98	$4.25	$4.52	$4.81
Company Guidance			$3.71 -$3.75				
Prior Estimates			*$3.71*	*$3.96*	*$4.24*	*$4.51*	*$4.78*
BofA CAGR (off 2019 estimate of $3.50)			*7.24%*	*6.59%*	*6.70%*	*6.63%*	*6.56%*
Consensus			$3.73	$3.98	$4.26	$4.54	
Consensus CAGR			*6.5%*	*6.6%*	*6.7%*	*6.7%*	
Mgmt. Guidance 5-7% off $3.50 in 2019							
Low		$3.48	$3.71	$3.86	$4.05	$4.25	$4.47
Mid		$3.50	$3.73	$3.93	$4.17	$4.42	$4.69
High		$3.52	$3.75	$4.01	$4.29	$4.59	$4.91

Source: BofA Global Research, Bloomberg

Valuation

We update our valuation to reflect mark to market of electric and gas peer group multiples to 16.7x and 15.7x respectively. We additionally tweak our valuation premium applied to WI utilities to 4.0x to reflect the strong regulatory backdrop and long-term opportunity to invest in more rate base renewables. We also shift or Energy Infrastructure methodology to applying an NPV valuation to both announced as well as growth projects – recall that we had previously updated our valuation to reflect an NPV value for announced renewable projects. While execution by the mgmt remains strong and data points on sales remain constructive, we believe valuation is expensive with WEC shares trading at an implied P/E of 19.5x vs. electric/gas peer P/E of 17.5x/16.5x, respectively, reflecting 6-7% growth vs. mgmt.'s 5-7% guidance range even after the recent pullback that narrowed the premium between WEC and peers. We reiterate Underperform.

Table 53: WEC updated SOTP: raising our relative premium on WI to +4x and Bluewater to +2x; keeping renewables on DCF & IL at +1x. PTF also at +1x too.

Regulated Utilities	2022 EPS	2022 Net Income	P/E Multiple					Equity Value		
			Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric				16.7x						
Group EPS '18-'22 CAGR - Electric				5.00%						
Group Peer Multiple - Gas				15.7x						
Group EPS '18-'22 CAGR - Gas				5.10%						
Applied Multiple				Electric 17.5x Gas 16.5x						
WI Electric	$1.30	413	20.5x		4.0x	21.5x	22.5x	$8,487	$8,901	$9,314
WPS	$0.64	202	20.5x		4.0x	21.5x	22.5x	$4,152	$4,354	$4,556
WI Gas	$0.58	184	19.5x		4.0x	20.5x	21.5x	$3,582	$3,765	$3,949
Peoples Gas	$0.55	173	16.5x		1.0x	17.5x	18.5x	$2,860	$3,034	$3,207
North Shore Gas	$0.06	18	16.5x		1.0x	17.5x	18.5x	$291	$308	$326
ATC	$0.47	149	18.5x		2.0x	19.5x	20.5x	$2,768	$2,917	$3,066
We Power (PTF)	$0.61	193	17.5x		1.0x	18.5x	19.5x	$3,386	$3,579	$3,772
MERC/MGU	$0.15	48	16.5x		1.0x	17.5x	18.5x	$790	$838	$886
Parent & Int Expense	-$0.41	(129)	17.5x		1.0x	18.5x	19.5x	($2,268)	($2,397)	($2,527)
Total Implied Utilities	$4.25	1,251				20.2x		$24,048	$25,299	$26,550
Non Utility Energy Infrastructure								$1,292	$1,304	$1,315
Wind projects - announced	NPV value							$616	$616	$616
Wind projects - growth	NPV value							$460	$460	$460
Bluewater	$0.04	12	18.5x		2.0x	19.5x	20.5x	$217	$229	$240
Implied Valuation Multiple					19.5x				$4.12	
HoldCo Debt Adjustment										
Add Back: 50% of Interest Expense	$0.13	40	19.2x			20.2x	21.2x	$774	$815	$855
Subtract: HoldCo Debt (Net out 50%)	2,550	(1,275)						($1,275)	($1,275)	($1,275)
Total Equity Value								$24,839	$26,143	$27,446
Valuation								$78.00	$83.00	$87.00
Price Objective									$83.00	
Upside/Downside									-5.8%	
NTM Div Yield									3.0%	
Total Return									-2.8%	

Source: BofA Global Research, Bloomberg

Xcel Energy (XEL)

Below we find 2Q20 EPS of $0.43/sh, versus a $0.48/sh Consensus and a 2Q19 estimate of $0.46/sh.

- **Drivers**: We see Covid impacting sales about -5c, associated with a 6% sales drop; note our view that 2Q was impacted less than initially anticipated, but we expect the 'base case' for Covid to remain roughly around the same (or maybe just shy of the 'up to 17c EPS impact') as we think more impact could come later this year (e.g. if there is another shut-down or delay of openings). We expect this is balanced by +3c of O&M savings; while XEL communicated a 4-5% decrease YoY in O&M, we expect these to be more back-end loaded.

- **Others**: Rate changes in Minnesota (+4c), Colorado (+2c), and one month of NM (+0c) are not to be ignored. AFUDC was adjusted to $25-35mn annually (+1c) and capital rider revenue continues to add +2c. Interest expense (-2c) is in line with annual $50-60mn guidance, increase in D&A expense (-4c) is back end loaded, and property tax (-1c) is in line with annual $35-45mn guidance.

- **Unkown:**: Weather's return to normal was -1.4c and we expect another -1c of mild weather this quarter (which could be a wild card).

Table 54: XEL EPS Walk 2Q20

Xcel Energy 2Q20 Earnings Walk	EPS
Ongoing EPS 2Q19	$0.46
Weather	
Return to normal (1.4c of adverse impact)	($0.01)
Current quarter	($0.01)
Rate Changes	
NSPM Minnesota Electric Interim sales true up & Nuke decommissioning ($122mn, Jan 2020)	$0.04
PSCo Colorado - Electric rates ($35mn, Feb 25 2020)	$0.02
SPS New Mexico - Electric rates ($31mn, 1 month in 2Q20)	$0.00
SPS Texas - Electric rates (requested $136mn, 3Q20)	$0.00
Capital rider revenue	$0.02
AFUDC	$0.01
Other	
Interest Expense increase	($0.02)
Increase in D&A expense	($0.04)
O&M (we assume 4-5% decrease, but more back-end loaded)	$0.03
Property taxes	($0.01)
COVID 2Q impact (up to -17c '20 impact in base case)	($0.05)
Bad debt (would be considered in O&M)	*$0.00*
Dilution (settled)	($0.00)
2Q20E Adjusted EPS	$0.43
2Q20E BofA Securities Estimate	0.43
2Q20 Consensus	0.48
2020 BofA Securities EPS	$2.78
2020 Consensus	2.77
2020 Guidance	2.73-2.83
Shares Outstanding 2Q19	516
Shares Outstanding 2Q20	525
Tax rate	25%

Source: BofA Global Research estimates, company report, Bloomberg

Adj capex to incl. 50% Minnesota stimulus

Adjusting incremental capex into our numbers: 50% probability weighting

Of the $3bn capex proposed with XEL's MN stimulus filing, roughly half is intended to accelerate capex already planned in later years of the 5-year outlook (e.g. distribution and natural gas spend). The other half is for newly proposed projects (e.g. wind repowering presumably under latest PTC extension, solar, and electric vehicle spend).

Capex opportunities likely include $1-1.4bn of wind repowering ('21-23), $650mn of solar ('23-25), and $100-150mn of EV infrastructure ('anytime' but we would expect '21-'25). It is unclear to us how the accelerated capex for already planned distribution and nat gas spend would re-arrange existing capex plans.

We provide details on how we include in our numbers below. We factor in a 50% probability weighting that the incremental capex is added in full, and we take an average of the assumed capex ranges per item. For example, wind repowering's $1-1.4bn capex opportunity averages to $1.2bn; with a 50% probability, we factor in $600mn of additional capex to the years '21-'23 – or $200mn each year in '21-'23. The same applies for solar ($108mn each year in '23-25) and EV infra ($12.5mn in '21-'25).

Bottom line, we see this as a net positive datapoint to shares and highlighting an emerging angle to capex. Moreover, we see the capex step-up as among the only such increases thus far in the sector; expect financing update discussion with 2Q as well pending success of filing. This critically drives cumulative gross EPS of ~$0.10 by 2025, or net of equity, ~$0.07 upside on our probability weighted basis. Upside to our ests below do not *directly* tie to this given other model refinements.

Table 55: Incremental capex factored into our Minnesota capex

Incremental capex associated with Minnesota stimulus (keeping the remaining 'accelerated' as is)						Prob. weight:	50%
Type	Details	2021	2022	2023	2024	2025	Total
Wind repowering	$1-1.4bn in '21-23	200	200	200			600
Solar	$650mn '23-'35			108	108	108	325
EV infrastructure	$100-150mn anytime	12.5	12.5	12.5	12.5	12.5	63
Total	$1.75-$2.20bn	213	213	321	121	121	988

Source: BofA Global Research estimates, company report

Below, we reflect how our capex numbers have been adjusted in our model. We leave existing capex as is (i.e. don't pull forward Minnesota capex associated with accelerated distribution and natural gas proposed spend) and we add in the incremental capex associated with wind renewables above.

Table 56: BofA modeled capex for XEL

Subsidiary	2015A	2016A	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E	2025E
NSPM	1,855	1,205	1,017	1,150	1,417	2,025	1,793	1,883	2,121	1,966	1,966
SPS	600	513	560	1,021	844	1,025	530	700	750	800	800
PSCo	996	1,114	1,476	1,577	1,691	1,415	1,445	1,720	1,565	1,530	1,530
NSPW	252	204	219	227	212	250	320	345	350	425	425
Parent	(18)	220	48	(17)	61	(85)	(65)	10	10	10	10
Consolidated	3,683	3,256	3,319	3,957	4,225	4,630	4,023	4,658	8,726	4,731	10,368

Source: BofA Global Research estimates, company report

Recovery and commission procedures

We would anticipate the company looks to recover spend for wind repowering and solar incremental investments through its renewable rider, and spend for advanced grid through its transmission rider. Note the wind repowers would likely qualify for the 60% production tax credit (PTC) if equipment is safe-harbored this year in 2020. We expect the rest to fall under a sought after enhanced recovery mechanism that will be determined by the Commission. We also await developments on a wider effort to delay its rate case altogether and see the formal indication of such in this filing as a positive step.

More details on the capex positive: MN is first to stimulus program

As noted in our first take here, Xcel's Northern States Power Company Minnesota (MN) biz recently filed a proposal for $3bn accelerated and additional capex in the state. This will likely create new jobs in an effort to counter-balance 400,000 unemployment filings in MN from Covid and the economic shut-down. This is the first proposal of its kind nationally for a return to infrastructure 'stimulus' programs (akin to efforts in the 2008 GFC). Likely the first of several others – both in terms of peers following suit and XEL's other jurisdictions as well.

Fate of the docket: We see positively and giving rise to more

The filing seems likely to gain key support for two reasons. 1) It was made in response to the MN Public Utilities Commission (PUC) request from May to examine what utilities can do to spur jobs and economic development. 2) It will be in line with labor goals. We expect an update by later this year from the MN PUC as creating jobs amid a pandemic is a timely item, and we would also expect XEL to consider opportunities like this in other jurisdictions - particularly CO.

Next key datapoint: What happens with rate cases?

In its filing, the company expressed it would be open to staying out of a rate case in MN this year – in line with mgmt. commentary. Recall XEL was expected to file at the end of 2019 but was able to stay-out, meaning this would be the second stay-out. Whether this is possible will not be determined through this docket but rather was expressed by XEL as one way it could keep customer rates down. We expect to see discussion in the coming months of what XEL would need to file to pursue another stay-out. We would expect XEL to look similarly to CO as well – and that in both states it will expect to recover spend through existing trackers.

Estimates

We include our latest estimates below, highlighting capex changes made to the model as well as our assumption that 30% of this incremental capex (i.e. nearly $300mn) is funded with incremental equity. We include this additional equity need into our assumptions and find the EPS CAGR to be above midpoint of the 5-7% guide starting in '21 and beyond. Note that the our '20 estimates are the same as prior assumptions, given that while there was less Covid impact in 2Q than originally anticipated (just -5c we forecast associated with a 6% sales drop), there could be more impact on demand later this year given resurfacing concerns. XEL's base case includes 'up to 17c' of Covid impact for '20.

Table 57: XEL EPS Estimates

Subsidiary	2016A	2017A	2018A	2019E	2020E	2021E	2022E	2023E	2024E
Northern States Power Minnesota (NSPM)	0.96	1.01	0.96	1.05	1.11	1.28	1.39	1.46	1.53
Southwestern Public Service (SPS)	0.30	0.30	0.42	0.51	0.59	0.60	0.63	0.65	0.67
Public Service Colorado (PSCo)	0.91	0.94	1.08	1.11	1.07	1.11	1.17	1.24	1.32
Northern States Power Wisconsin (NSPW)	0.14	0.16	0.19	0.15	0.16	0.18	0.20	0.21	0.23
Parent (Excl Mankato)	(0.10)	(0.12)	(0.18)	(0.17)	(0.16)	(0.16)	(0.18)	(0.20)	(0.21)
Consolidated	2.21	2.29	2.47	2.64	2.78	3.00	3.20	3.36	3.55
EPS Growth (%)			*8%*	*7%*	*5%*	*8%*	*7%*	*5%*	*6%*
Prior Estimates			*2.47*	*2.64*	*2.76*	*2.94*	*3.14*	*3.33*	*3.51*
Guidance (Excl Mankato)	2.17-2.22	2.25-2.35	2.45-2.49	2.60-2.65	2.73-2.83				
Consensus			2.46	2.62	2.77	2.96	3.13	3.32	3.44
Mgmt EPS CAGR: 5-7% off 2018 base ($2.43)	2.21	2.29	2.47	2.60	2.78	2.95	3.12	3.31	3.51
		low	*2.43*	*2.55*	*2.73*	*2.87*	*3.01*	*3.16*	*3.32*
		high	*2.43*	*2.65*	*2.83*	*3.03*	*3.24*	*3.47*	*3.71*
BofAe CAGR '18-'23e (off $2.43)	6.7%								
BofAe CAGR '18-'24e (off $2.43)	6.5%								
Target FFO/Debt			17%	18%	17%	17%	17%		
BofAe FFO/Debt		22%	19%	19%	17%	18%	17%	17%	

Source: BofA Global Research estimates, company report, Bloomberg

Valuation

We MtM our peer multiple to 16.3x from 16.7x before. We maintain our PO of $62.50/sh (unch vs prior) and we reiterate our Neutral rating as we factor in our 50% probability weighted Minnesota capex opp'y to the model. We note this still needs regulatory approval.

Table 58: XEL SOTP

2022E SotP Analysis - BofA All figures in USD millions except per share										
Regulated Utilities	2022 Net Income	EPS	P/E Multiple					Equity Value		
			Bear	Peer	Prem/ Discount	Base	Bull	Bear	Base	Bull
Group Peer Multiple - Electric				16.3x						-
Group EPS '18-'22 CAGR - Electric				5.00%						-
										-
Relative Utility Group P/E Multiple				17.1x						
Northern States Power Minnesota (NSPM)	$748	$1.39	19.1x	17.1x	3.0x	20.1x	21.1x	$26.54	$27.93	$29.32
Southwestern Public Service (SPS)	$339	$0.63	19.1x	17.1x	3.0x	20.1x	21.1x	$12.04	$12.67	$13.30
Northern States Power Wisconsin (NSPW)	$106	$0.20	19.1x	17.1x	3.0x	20.1x	21.1x	$3.76	$3.95	$4.15
Public Service Colorado (PSCo)	$630	$1.17	19.1x	17.1x	3.0x	20.1x	23.1x	$22.35	$23.52	$27.03
Total/Average Utility Earnings (excl Mankato)	$1,824	$3.38			3.0x					
Parent/Unallocated (excl Mankato)	-$99	-$0.18	19.1x	17.1x	3.0x	20.1x	21.1x	-$3.50	-$3.69	-$3.87
Add back 50% of HoldCo interest	$70	$0.13	19.1x	17.1x	3.0x	20.1x	21.1x	$2.50	$2.63	$2.76
Less: 50% of HoldCo Debt	-$2,462							-$4.57	-$4.57	-$4.57
Total	$1,725	$3.20						$59.11	$62.44	$68.11
Shares Outstanding (2022e)									*539*	
Total Equity Value Per Share								$59.00	$62.50	$68.00
Dividend FY20									1.72	
Dividend Yield									2.7%	
Total Potential Return Projected								-5%	1.0%	10%

Source: BofA Global Research estimates, company report, Bloomberg

Table 59: Stocks Mentioned

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
LNT	LNT US	Alliant Energy Corp	US$ 49.99	A-1-7
AEE	AEE US	Ameren Corp	US$ 73.24	A-1-7
AEP	AEP US	American Elec Power	US$ 82.91	A-1-7
AWK	AWK US	American Water	US$ 126.46	A-3-7
ED	ED US	Consolidated Edison	US$ 85.47	A-2-7
DTE	DTE US	DTE Energy	US$ 100.76	A-2-7
DUK	DUK US	Duke Energy	US$ 86.65	A-2-7
EIX	EIX US	Edison Intl	US$ 60.01	B-2-8
ETR	ETR US	Entergy Corp.	US$ 96.45	A-1-7
WTRG	WTRG US	Essential Utilities	US$ 42.24	A-2-7
EVRG	EVRG US	Evergy	US$ 59.12	A-1-7
ES	ES US	Eversource Energy	US$ 87.77	A-3-7
FE	FE US	FirstEnergy	US$ 44.49	A-1-7
PNW	PNW US	Pinnacle West Capit	US$ 76.60	A-2-7
PPL	PPL US	PPL Corp.	US$ 25.25	B-2-8
WEC	WEC US	WEC Energy Group Inc	US$ 95.88	A-3-7
XEL	XEL US	Xcel Energy	US$ 64.35	A-2-7

Source: BofA Global Research, Bloomberg

Price objective basis & risk

Alliant Energy Corporation (LNT)
Our $54.5 PO is based on a sum of the parts analysis employing relative premium and discounts to the large cap regulated peer multiple of 17.1x 2022E P/E. While our PO is on a 1 year basis we note the 2022 P/E multiple reflects a discount back to 2019. We note that electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. We apply a 2.0x P/E premium on IPL as we see the ratecase overhang being resolved. We apply a 3.0x P/E premium on Eastern Wisconsin Electric Company reflecting 1) low risk investment nature of the state, 2) above average ROEs, 3) higher than average growth runway for investments, and 4) bad debt deferral. At ATC, we reflect a 2.0 x P/E premium on LNT's 16% share in the transmission company. Growth expectations for this segment are high, paired with above average ROEs that we believe face less downward pressure vs. regulated state distribution ROEs. We apply an in line multiple at the parent to account for the blend of numerous businesses some which benefit from long term stable PPAs via intercompany generation. Risks to our price objective are: 1) adverse rate case outcomes, 2) further equity dilution beyond our estimates, 3) interest rate risk, 4) natural disasters, and 5) lower allowed ROEs.

Ameren Corporation (AEE)
Our $79 price objective is predicated on a P/E based sum of the parts, valuing each business subsidiary relative to the 2022E ratebase weighted peer multiple of 16.3x for electric. We apply a 2.0x premium to peers at AEE Missouri to account for the improving prospects of capital spend, supplemented by a regulatory jurisdiction becoming more favorable - but lack of decoupling. We apply a 3.0x premium to peers at AEE Illinois to account for decoupling on the distribution business which aids in earnings predictability. The overall business is expected to grow at a more meaningful clip than that of peers - we see a 10% EPS CAGR at IL 2020-2024. At ATXI, we apply a 0x premium to peers to reflect the latest potential step down in FERC ROEs. At the Parent, we assume an in line multiple given the healthy debt metrics with FFO/Debt at 17%+. Electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector.

The upside (downside) risks to our price objective are the utilities earning their allowed returns or better (worse), a significant increase (decrease) in 30-year U.S. Treasury bond yields, and positive (adverse) regulatory outcomes that could impact mgmt's ability to earn its allowed return

American Electric Power (AEP)
Our price objective of $88 is based on SOTP analysis. We ascribe a peer forward P/E multiple (17.1x) with a 1.0x premium for its transmission-only Utilities segments, a 1.0x premium for its T&D utilities, and a 0x premium for regulated utilities as well as 2x for Kentucky Power. We note that electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. We assume 100% likelihood of the North Central wind project and assign it a 0x premium under the reg utes as well.

Downside risks to our price objective are 1) regulatory outcomes are less favorable than expected, which could result in reduced ROE, 2) large capital intensive are subject to delays or cost overruns, which can change the return profile, 3) natural disasters or catastrophic events can affect system reliability and are subject to regulatory cost recovery risk, 4) utilities are subject to interest rate risk to fund their business, which affects cost of capital, 5) commodity risk affects the generation business margins and indirectly affects the regulated business as a pass through cost, 6) consumer advocates are focused on bill inflation, which can affect regulatory outcomes, 7) non-regulated businesses are inherently more risky and subject to execution risk and commodity variation.

American Water Works (AWK)
Our PO for American Water Works is $135. We apply the sector average 26.9x (vs. 26.3x) to American Water's 2022E earnings based on the water peer multiple and a 8.1% group EPS CAGR for '18-'23E. We think this multiple is justified as in our view AWK largely drives the peer multiple as the largest publicly traded water utility. We ascribe a 3x premium for NJ, PA, and IL, and a -3x discount to the military biz. Meanwhile, we ascribe a 12x multiple to the non-regulated Retail biz. Also a -1x P/E for Cali utility. no prem/discount for 'Other' segment with smaller state exposures.

Risks to the downside are increase in market interest rates, potential impact of tax reform on utilities, operational errors, changes in valuation levels for water utilities. Risks to the upside are accelerating muni acquisitions, multiple expansion, and constructive legislation in regulatory jurisdictions

Consolidated Edison (ED)
Our $86 PO is based on a sum-of-the-parts analysis applying premiums and discounts to the regulated group multiples (16.8x/15.8x for electric/gas respectively) with a 1.0x premium to reflect defensive nature of the stock, and -1.0x discount on Steam to reflect lack of decoupling / weather risk. We note that both electric and gas peer P/E multiples are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We applied inline peer regulated multiple at CECONY despite its rate certainty for conservatism as our higher capex expectations are reflected in our EPS outlook. We apply a discounted PE for infrastructure projects given the lack of clarity around the capital structure. We further apply an EV/EBITDA approach on 2022E EBITDA to the CEB business using a 10.0x multiple for both the legacy portfolio and the renewables portfolio seeing it as having higher quality returns.

Downside risks: ED, like all utility stocks, is also sensitive to changes in the market level of interest rates. Utilities historically underperform if bond yields rise, and outperform when they fall. Further downside risks are the inability to recontract storage, adverse regulatory outcomes, a deteriorating regulatory environment, or unforeseen disasters such as the Harlem gas explosion, the SRE transaction not being completed. Customer inflation is also a downside risk. PCG related counterparty exposure is among the nearest exposures to watch.

DTE Energy (DTE)
We value DTE Energy at $115 using a SOTP approach.
We value the utility segment on a 2022E forward P/E multiple basis and the non-utility seg. on a 2022E forward EV/EBITDA multiple basis. For the utility segment we apply a 2x premium to our both reg. electric and gas utility peer multiple of (16.5x and 15.6x respectively). Both electric and gas peer P/E multiples are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We subtract out Corp & Other expense excl. interest rate.
For GSP we use a midstream peer group multiple of 9x, with a -1x discount for Momentum. P&I, we apply an 8x EV/EBITDA multiple, despite the lower equality of these earnings and opaque disclosures, as mgmt has been able to execute on new project origination. We value the reduced emissions fuel (REF) tax credits separately using a DCF methodology at 6% discount rate.

Upside risks to our PO are capex expansions, higher authorized ROEs, and strong performance in the ET segment. Downside risks are interest rate hikes, execution risk on organic growth initiatives at the nonregulated business, and less favorable regulatory environment.

Duke Energy (DUK)
Our $87 PO is derived from a sum-of-the-parts valuation. We value the Electric and Gas utilities using peer 2022E P/E multiples. We apply a 1.0x multiple premium to Duke's

operations in FL/IN to reflect more favorable regulatory environments. We apply an in-line multiple to the Carolinas given risk ahead. We value the other regulated electric utilities at 17.1x and the gas utilities at peer group multiples of 15.9x 2022E P/E, respectively. Both electric and gas peer P/E multiples are grossed up by 5% for the groups CAGR to reflect capital appreciation across the sector. The commercial midstream, and transmission are valued on a 2022E EV/EBITDA basis. We use a 9.0x multiple for midstream and transmission segment. We add the net present value of renewable segment using an 8% discount rate. We subtract out the impact of commercial debt, and add back for the renewable debt.

Upside risks: constructive rate case results, higher capital expenditure additions vs our assumptions, lower interest rates. Downside risks: poor rate case results, operating errors, and negative changes in the regulatory environment, Macro risks: Increases in interest rates and decreases in equity market valuations.

Edison International (EIX)
Our $65 PO is based on SOTP, applying a 4x disc to the FERC and CPUC jurisdictional subsidiaries, and the parent/other segment 17.1x on 2022E (grossed up by 5% to reflect capital appreciation across the sector). The disc reflects CA ongoing wildfire risk despite the improved construct through AB1054. We apply 10x 2022E P/E to the Edison Energy segment to reflect uncertainty in the nascent biz. We net out ongoing contribution to the fund on an NPV basis.

Downside risks: 1) Regulatory outcomes less favorable than expected. 2) Natural disasters or catastrophic events can affect system reliability and are subject to regulatory cost recovery risk. 3) Interest rate risk. 4) Non-reg businesses are inherently more risky and subject to both execution risk and commodity variation. 5) CA has specific risks given the differentiated regulatory regime. 6) CA wildfires.
Upside risks: rate case outcome above what's embedded in companies' guidance and BofA estimates, lower interest rates, more constructive regulatory / legislative outcomes to address wildfire risk

Essential Utilities (WTRG)
Our price objective is $47 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 2.0x premium to Peoples Gas given the organic growth opportunities.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Risks to the upside include upward revisions to street estimates and further accretion from implementation of the Repairs Tax Benefit.

Evergy, Inc (EVRG)
Our $68 price objective for EVRG shares is based on sum of the parts valuation, applying an in-line utility peer 2022E P/E of 17.1x. Electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We further apply a +2.0x turn discount across all jurisdictions based on our perception of improving regulatory relationships and possibility of further stakeholder engagement.

Downside risks to our price objective are adverse regulatory outcomes in rate cases, higher interest rate environments, adverse and unexpected risks associated with operating a nuclear facility, the possibility that the strategic review committee does not result in a transaction recommendation and that a modified standalone plan disappoints in rate base and earnings growth when presented later in 2020.

Upside risks to our price objective are favorable regulatory outcomes in rate cases, lower interest rate environments, higher than anticipated O&M benefits and merger synergies, ability to recover capital tied to retired coal plant.

FirstEnergy (FE)
Our PO of $45.5 is based on a SOTP: Multiples are driven by relative P/E premiums/discounts to the 2022 regulated peer multiple of 17x (previously 16.9x) . Electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. As for premiums/discounts, we view NJ as in-line given a generally constructive commission, PA as in-line as we view our more punitive ests already account for industrial load sensitivity incl O&G royalties, and others as in-line. In OH, we apply a -1x P/E discount multiple, We argue this accounts for overearning risk. Finally, we apply a 0x P/E premium to peers 2022E multiple to the Transmission business given some limited ability to invest and FERC ROE difficulties. We removed impact of DMR payments. We subtract out the holding co debt given the high parent lev. We net out potential liabilities from a potential FES bankruptcy by assuming all known 'extra' potential liabilities.

Downside risks: 1) Reg outcomes may improve/deteriorate, 2) legislative solutions may materialize for challenged parts of biz or FE could lose/fail to gain legislative support in key states, 3) int rates positively/negatively affect cost of cap, 4) reg staff or cons advocates may focus on issues beneficial/detrimental to ROEs, 5) exit from comp power biz may or may not have substantive liabilities accrued to equity holders.

Pinnacle West (PNW)
Our price objective of $78 is based on a peer utility 2022E P/E multiple of 16.6x with a -2.5x discount to account for PNW's risk around its pending rate case as well as headline risk related to disconnect policy review. Electric and gas peer P/E mult is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We ascribe an in-line premium despite clear renewable capex backdrop given ongoing regulatory risk associated with the company's upcoming rate filing and 2020 election risk.

Upside risks: 1) Regulatory relationships/outcomes could improve, including changes at the elected commission 2) load growth in territory above expectations 3) Riders and capital trackers could help achieve ROE 4) positive weather helps earnings 5) interest rate risk changes cost of capital - lower rates could improve 6) Consumer advocates or utility staff could become focused on issues that improve ROE

Downside risks: 1) Regulatory relationships/outcomes could decline, including changes at the elected commission 2) load growth in territory below expectations 3) Riders and capital trackers could hurt ROE 4) negative weather hurts earnings 5) interest rate risk changes cost of capital - higher rates could worsen 6) Consumer advocates or utility staff could become focused on issues that hurt ROE 7) Solar advocates in the state have engaged in public confrontations with the utility, which could change public relations in the future.

PPL Corporation (PPL)
Our $27 price objective is based on a sum of the parts methodology applying respective premium/discounts to the 2022E peer group multiple of 16.5x. Electric peer P/E multiple is grossed up by 5% to reflect capital appreciation across the sector. We apply a 1.25x RAV multiple in our base case for our Western Power Distribution (WPD) RAV approach, seeing the higher ROEs relative to other distribution networks commanding a premium valuation.

Downside risk to our price objective is exposure to FX rates. Since the UK segment represents a significant portion of PPL's earnings, a Federal Reserve decision to raise interest rates could produce a fall in the GBP/USD currency rate that would adversely

affect our estimates and valuation for PPL. Also, like all utility stocks, PPL has historically underperformed if bond yields rise. Upside risks are a rising $/pound (GBP) price, positive regulatory outcomes, and decreasing treasury yields.

WEC Energy Group Inc (WEC)
Our $83 PO is based on a 2022E SoTP analysis, based on the large cap electric group multiple of 16.7x and the gas regulated multiple of 15.7x. Both electric and gas peer P/E multiples are grossed up for a year to reflect capital appreciation across the sector.

We apply a 4.0x premium to WEC's WI electric & gas subs to compensate for surety in earnings growth for the next two years following the Commissions affirmation of the recent settlement on above average ROE's of 10%+. We apply a 1x premium to the gas utilities, incl IL's Peoples Gas and North Shore Gas with the Gas System Modernization Program (GSMP) and capex forecasts de-risked following the ICC order. We ascribe a 2x premium vs. the group at ATC to account for the steady nature of earnings growth as well as above average ROE's that are set at a federal level by FERC. We give Power the Future (PTF) a 1.0x premium multiple given the ROE is set indefinitely on historical and new investments. We ascribe an in line multiple for the parent accounting for the interest expense which finances overall utility operations. For the HoldCo adjustment to debt, we net out 50% of HoldCo debt from equity valuation and adjust to add back the parent drag on interest exp.

Upside risks are stronger than expected execution and accelerating capital oppt'y.

Downside risks are inability to achieve historical track record on cost cutting and ability to cont. to scale regulated investments given growing portion from contracted renewables.

Xcel Energy Inc (XEL)
Our PO is $62.5. We value Xcel Energy using a sum of the parts (SOTP) approach. Given the difference in geography, earnings strength, growth opportunity and risk profile, we divide the segments by subsidiary.

We use 2022E forward P/E multiples to derive a value for the different business segments, including the parent segment. We use a peer multiple of 16.3x . Electric peer P/E multiple is then grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We apply a 3x premium to subsidiaries. We see this multiple as appropriate as the company has growth opportunities, resolving regulatory drag and resolving uncertainty around rate cases. We stripped Mankato as a non-reg asset in our SOTP due to the sale. We also net back 50% of the parent interest expense and instead subtract out 50% of parent debt to more accurately reflect HoldCo leverage.

Downside risks are interest rate increases, regulatory risk such as lower authorized ROEs or less favorable riders/trackers for renewables and transmission, interest rate risk, execution delays, and weather anomalies.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AES	AES	AES US	Julien Dumoulin-Smith
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
NEUTRAL				
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Utilities Group (as of 30 Jun 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	76	51.01%	Buy	56	73.68%
Hold	33	22.15%	Hold	22	66.67%
Sell	40	26.85%	Sell	29	72.50%

Equity Investment Rating Distribution: Global Group (as of 30 Jun 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1632	52.21%	Buy	1031	63.17%
Hold	711	22.74%	Hold	444	62.45%
Sell	783	25.05%	Sell	407	51.98%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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Essential Utilities

All Aboard: Upgrading to Buy as WTRG Plan More than Just Holds Water

Rating Change: BUY | PO: 52.00 USD | Price: 47.27 USD

Execution Remains Strong Despite Pandemic Backdrop

Following a strong 2Q and mgmt. affirmation of guide, we are jumping back in to WTRG and upgrading from Neutral to Buy. We see shares as poised to outperform with consistent quarterly execution to drive EPS of $1.53-$1.58 this year and the 5-7% EPS CAGR through '22, and stress incremental upside opportunities as acquisitions continue to materialize across their water footprint (we stress sharp contrast vs. peer AWK who already reflects acquisitions in guide). With favorable transaction legislation now enacted in all eight of their Aqua jurisdictions, we expect water rate base to grow well in excess of the 6-7% outlined through '22: the further municipal budget strain from the ongoing pandemic will likely accelerate consolidation in the industry at an even faster pace - and we expect additional developments over the next several months (after closing two deals already in '20 with four add'l signed agreements translating to ~$300Mn of rate base & ~$15Mn of earnings). Meanwhile, the 2,700 miles of pipe replacement at the recently acquired Peoples Gas segment will help drive 8-10% organic rate base through '22 and beyond - while mgmt. benefits from repairs tax treatment at the sub in PA to drive returns without the need for a rate case (with the repairs tax catch up component filed with the commission last Thurs providing even more latitude). With a growing focus on ESG – and mgmt.'s proactive action around PFAs – we see this an underappreciated angle not reflected at the current valuation (particularly vs. peer AWK with an elevated premium). Bottom line, we see shares as poised to re-rate higher given consistent execution, elevated growth prospects, and increasing appreciation for clean quality stories.

Upgrading to Buy

While our estimates are largely unchanged, we have increasing conviction in mgmt.'s ability to consistently deliver and see the company as a prime beneficiary of further consolidation across the water industry - while the latest filing for the catch up component of Repairs Tax treatment in PA should provide further latitude to stay out of rate cases for the gas segment. After applying slightly higher premiums and marking to market for the latest water and gas multiples (28.1x and 16.3 vs. 26.9x and 15.9x previously), our PO ultimately shifts to $52 (from $47 previously). Upgrade to Buy.

Estimates (Dec)

(US$)	2018A	2019A	2020E	2021E	2022E
EPS	1.41	1.47	1.56	1.69	1.80
GAAP EPS	1.41	1.47	1.56	1.69	1.83
EPS Change (YoY)	3.7%	4.3%	6.1%	8.3%	6.5%
Consensus EPS (Bloomberg)			1.53	1.66	1.79
DPS	0.86	0.92	0.99	1.06	1.13

Valuation (Dec)

	2018A	2019A	2020E	2021E	2022E
P/E	33.5x	32.2x	30.3x	28.0x	26.3x
GAAP P/E	33.5x	32.2x	30.3x	28.0x	25.8x
Dividend Yield	1.8%	2.0%	2.1%	2.2%	2.4%
EV / EBITDA*	9.5x	36.6x	20.1x	18.5x	17.2x
Free Cash Flow Yield*	-1.1%	-1.8%	-3.7%	-2.6%	-2.1%

* For full definitions of *iQmethod℠* measures, see page 8.

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10 August 2020

Equity

Key Changes

(US$)	Previous	Current
Inv. Opinion	B-2-7	B-1-7
Inv. Rating	NEUTRAL	BUY
Price Obj.	47.00	52.00

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Stock Data

Price	47.27 USD
Price Objective	52.00 USD
Date Established	10-Aug-2020
Investment Opinion	B-1-7
52-Week Range	30.40 USD - 54.52 USD
Mrkt Val (mn) / Shares Out (mn)	11,588 USD / 245.2
Average Daily Value (mn)	42.81 USD
BofA Ticker / Exchange	WTRG / NAS
Bloomberg / Reuters	WTRG US / WTRG.N
ROE (2020E)	8.6%
Net Dbt to Eqty (Dec-2019A)	31.1%

ESG: Environmental Social Governance

PFA: Perfluoroalkoxy Polymer-Chemical Compound

iQprofile℠ Essential Utilities

*iQ*method℠ – Bus Performance*

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Return on Capital Employed	3.9%	3.5%	5.3%	5.0%	5.1%
Return on Equity	9.7%	8.9%	8.6%	8.2%	8.9%
Operating Margin	38.7%	38.4%	64.5%	66.5%	68.3%
Free Cash Flow	(127)	(212)	(428)	(304)	(246)

*iQ*method℠ – Quality of Earnings*

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Cash Realization Ratio	1.9x	1.3x	1.7x	1.8x	1.7x
Asset Replacement Ratio	3.4x	3.5x	3.1x	2.8x	2.5x
Tax Rate	NM	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	127.1%	31.1%	98.4%	106.0%	112.7%
Interest Cover	2.8x	3.1x	3.4x	3.4x	3.4x

Income Statement Data (Dec)

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Sales	835	886	955	1,005	1,053
% Change	3.7%	6.2%	7.7%	5.3%	4.8%
Gross Profit	838	890	1,551	1,656	1,752
% Change	3.5%	6.2%	74.3%	6.8%	5.8%
EBITDA	1,941	504	916	997	1,074
% Change	-86.4%	-74.1%	81.8%	8.8%	7.8%
Net Interest & Other Income	(99)	(100)	(181)	(195)	(215)
Net Income (Adjusted)	192	263	371	402	450
% Change	-19.9%	36.9%	41.2%	8.3%	12.0%

Free Cash Flow Data (Dec)

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Net Income from Cont Operations (GAAP)	192	225	397	431	457
Depreciation & Amortization	147	156	338	371	402
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	(15)	(10)	(75)	(75)	(75)
Other Adjustments, Net	45	(32)	(38)	(6)	(5)
Capital Expenditure	(496)	(550)	(1,050)	(1,025)	(1,025)
Free Cash Flow	-127	-212	-428	-304	-246
% Change	-31.5%	-66.5%	-102.1%	28.9%	19.2%

Balance Sheet Data (Dec)

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Cash & Equivalents	4	1,869	6	6	7
Trade Receivables	101	108	188	200	212
Other Current Assets	42	36	50	52	54
Property, Plant & Equipment	5,930	6,346	10,657	11,312	11,935
Other Non-Current Assets	887	1,003	1,003	1,003	1,003
Total Assets	6,964	9,362	11,904	12,574	13,211
Short-Term Debt	160	131	126	141	155
Other Current Liabilities	239	188	244	253	261
Long-Term Debt	2,398	2,943	4,597	5,138	5,653
Other Non-Current Liabilities	2,158	2,219	2,144	2,069	1,994
Total Liabilities	4,955	5,481	7,111	7,601	8,063
Total Equity	2,009	3,881	4,793	4,973	5,148
Total Equity & Liabilities	6,964	9,362	11,904	12,574	13,211

* For full definitions of *iQmethod*℠ measures, see page 8.

Company Sector

Water Utilities

Company Description

Essential Utilities is a regulated water/gas providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI - along with a natural gas presence through the recently acquired Peoples Gas providing distribution services to 740,000 customers in PA, WV, and KY.

Investment Rationale

We are Buy rated on shares of WTRG, seeing shares as poised to re-rate higher given consistent execution, acquisition upside, and increasing conviction around the premium story.

Stock Data

Average Daily Volume	905,604

Quarterly Earnings Estimates

	2019	2020
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NA

Why We're More Constructive Again

We are upgrading shares of WTRG following another consistent quarter of execution by management. Following a large 2Q beat, mgmt. reaffirmed their 2020 EPS of $1.53-$1.58 (while peer AWK revised down on COVID impact) and a 5-7% EPS CAGR through '22. We have increasing conviction around mgmt.'s ability to consistently deliver and see upside risk from further acceleration in muni acquisitions (excluded from guidance while already contemplated in the growth plan for AWK). In the near term, resi strength of their portfolio and constructive regulatory treatment (with the March order from the PA PUC boding particularly favorable given their large presence in the state) position the company to navigate pandemic challenges while the growing pipeline of municipal opportunities should provide a long term tailwind for the water biz; meanwhile after electing to implement Repairs Tax for the gas biz in PA (and a catch up filing to amortize capital already spent filed last week), we see a clear runway to drive earned returns for the next several years (Mgmt. noted expectations for the initial filing to drive $0.08-$0.12 worth of contribution for the year).

Following the adoption of Fair Market Value legislation in TX and VA, the company now has the constructive legislation in all eight states of their water footprint. We expect this to help further accelerate consolidation in the industry as muni budgets are further flex'd from the crisis - and any further resulting acquisitions would be upside to mgmt.'s latest reaffirmed targets. Despite the more recent adoption in the state, WTRG already announced their first acquisition in TX under the legislation and we perceive more and more acquisitions of muni's to materialize over the next several months across their footprint. Meanwhile, we are less concerned around recent media headlines around the DELCORA acquisition: we don't see meaningful risk to the deal and it remains upside to estimates over time from the currently laid out plan. With the PUC fully accepting the application last week, mgmt. noted expectations to close the transaction in early '21. Overall, we stress $300Mn+ in rate base opportunities from signed APAs expected to generate ~$15Mn in earnings that are all upside to the currently laid out plan.

Bottom line, we see upside to the plan given the more conservative approach to guide, and expect shares to rerate higher relative to AWK as investors continue to appreciate the premium story amid consistent management execution.

EPS Estimates

The exhibit below reflects our latest EPS Estimates. In addition to limited risk to NT numbers (despite some dilution from the expected equity offering) given the defensive nature of their portfolio and constructive regulatory treatment, we see the company as poised to deliver on their 5-7% EPS CAGR – with upside from a likely acceleration in industry consolidation. We continue to model towards the high end of their 5-7% EPS CAGR through '22. With consistency the metrics many in the industry continue to pursue as part of further re-rating opportunities, we see the relative *lack* of outperformance of late despite its track record and its relatively attractive ESG profile make it among the more compelling investments. With prospective EPS growth likely more consistent than earlier trajectory (which proved more 'lumpy' we perceive the outlook as ever more appealing for those seeking a de-risked outlook).

Table 1: EPS Estimates

EPS Estimates	2020E	2021E	2022E
PA	$0.73	$0.80	$0.86
OH	$0.07	$0.07	$0.08
IL	$0.07	$0.08	$0.08
TX	$0.06	$0.07	$0.07
NC	$0.04	$0.04	$0.05
Other States	$0.07	$0.07	$0.08
Water Utility	1.04	1.13	1.21
Peoples Gas	0.62	0.67	0.72
Parent & Other	*-0.10*	*-0.11*	*-0.14*
EPS	1.56	1.69	1.80
YoY Growth	*6%*	*9%*	*6%*
Guidance	1.53-1.58		
Fully Diluted Shares O/S	*254*	*254*	*254*
Previous EPS	*$1.56*	*$1.69*	*$1.80*
Consensus	1.53	1.66	1.79
DPS	0.99	1.06	1.13
Payout Ratio	*63%*	*62%*	*63%*

Source: BofA Global Research estimates

Valuation: Upgrading to Buy with $52 PO

The exhibit below reflects our latest SOTP after applying the current peer multiples to our valuation: 26.9x for water and 15.9x for gas (vs. 26.9x for water and 15.9x for gas previously). We raise our premiums across the board given particular confidence in management and their consistent ability to deliver, strong municipal acquisition prospects, and an underappreciated ESG angle. Our PO shifts to $52 (from $49 previously) and we are upgrading to Buy.

We note shares have notably lagged AWK, which has also consistently executed. We attribute some of this to WTRG's ownership of gas utility: ultimately we view this as quite value accretive and EPS accretive given sharp discrepancy in valuations. The question remains whether investors will value the consolidated entity for a clean(er) story with a carbon profile driven by a gas utility. We already substantially discount the gas utility: we perceive comps for the gas utility itself could well include the likes of ATO among other higher quality avenues.

We perceive management to be exceptionally consistent and focused on executing across a range of opportunities. Numerous acquisition avenues yet to be discovered.

Table 2: SOTP

Water Utilities	2022 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*28.1x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		30.4x							
Water Utilities									
States	2022E EPS	ROE embedded							
PA	$0.86	10.0%	4.0x	33.4x	34.4x	35.4x	$29	$29	$30
OH	$0.08	9.4%	2.0x	31.4x	32.4x	33.4x	$2	$3	$3
IL	$0.08	9.1%	3.0x	32.4x	33.4x	34.4x	$3	$3	$3
TX	$0.07	10.0%	2.0x	31.4x	32.4x	33.4x	$2	$2	$2
NC	$0.05	9.2%	2.0x	31.4x	32.4x	33.4x	$1	$2	$2
Other (including acquisitions)	$0.08	9.2%	0.0x	29.4x	30.4x	31.4x	$2	$2	$2
Water utilities total (ex-Peoples)	$1.21			*32.8x*	*33.8x*	*34.8x*	$40	$41	$42
Gas Utilities									
Peer Gas P/E		*16.3x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		17.2x							
	2022E EPS	ROE embedded							
Peoples Gas	$0.72	12.1%	3.0x	19.2x	20.2x	21.2x	$14	$15	$15
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			-1165	50%			($582)	($582)	($582)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($553)	($511)	($598)
50/50 Weighted Drag from HoldCo Drag							($1,135)	($1,094)	($1,180)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							$49.00	$52.00	$53.00
Current Price								$47.27	
Dividend Yield								2.1%	
Total Potential Return								12.09%	

Source: BofA Global Research, Bloomberg

Price objective basis & risk

Essential Utilities (WTRG)
Our price objective is $52 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. These peer multiples are 28.1x and 16.3 vs. 26.9x and 15.9x, respectively, previously. We apply a 3.0x premium to Peoples Gas given the organic growth opportunities, while applying a variety of premiums to its water (2x previously) subsidiaries: +4x to PA, +3x to IL, +2x to OH, +2x for TX, +2x for OH, and no premium for balance of biz.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AES	AES	AES US	Julien Dumoulin-Smith
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
NEUTRAL				
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith

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Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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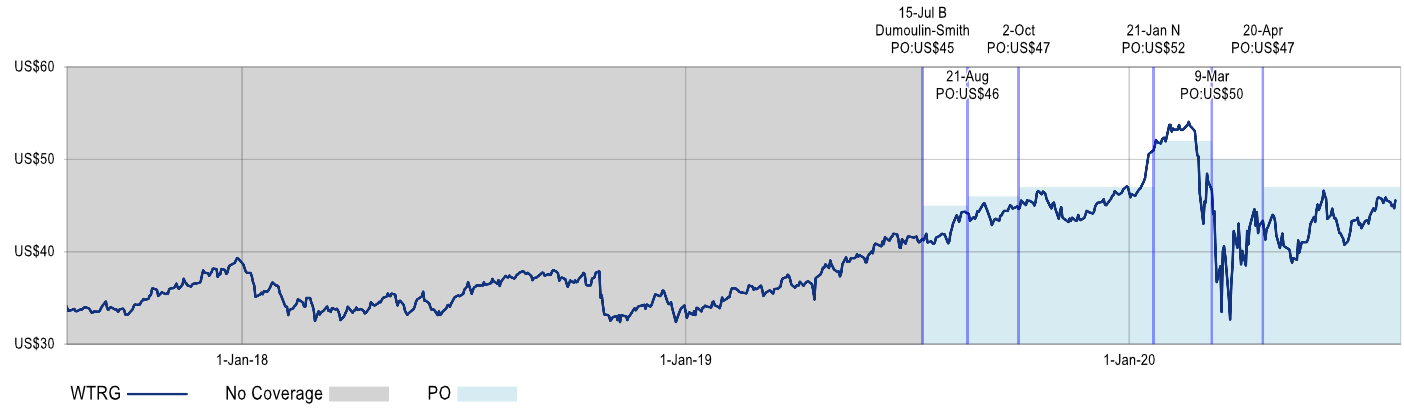
Essential Utilities (WTRG) Price Chart



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Equity Investment Rating Distribution: Utilities Group (as of 30 Jun 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	76	51.01%	Buy	56	73.68%
Hold	33	22.15%	Hold	22	66.67%
Sell	40	26.85%	Sell	29	72.50%

Equity Investment Rating Distribution: Global Group (as of 30 Jun 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1632	52.21%	Buy	1031	63.17%
Hold	711	22.74%	Hold	444	62.45%
Sell	783	25.05%	Sell	407	51.98%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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North American Electric Utilities

EEI: The Final Day of our Virtual Exploration Tour

Price Objective Change

12 November 2020

Equity
North America
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So big surprises? No; but datapoints, plenty.

As we close out this year's EEI we appreciate that few companies provided material updates. That said numerous companies provided substantive incremental datapoints on their trajectories – and overall large-cap companies did well in de-risking their outlooks including D, DUK, SO, and NEE. While large-caps have done relatively well already this year, we perceive support for each of these discrete stories to bolster sector prospects. By contrast, among the lone more cautious updates was AEP's '21 EPS guidance release & 5-yr view, which painted a slowing view vs earlier elevated expectations. Among other companies offering more cautious updates on their prospects included FE and EVRG albeit both are already at substantial discounts. We perceive persistent confidence in CNP on its subsequent roll forward (with details on both ENBL and LDC strategy), and a positive clear read-thru to NI. We suspect both will continue to trend well. With LDCs in focus, we perceive BKH as warranting greater attention given initiation of an EPS CAGR & yet further positive capex revisions. Other smids such as IDA and POR offered confidence inducing updates on their prospects – with expectations still relatively lower for POR, we flag this as particularly compelling. Finally, with DTE among the most controversial equities into the EEI conference we see mgmt's ability to add cnofidenc to reaching the high end of '21 affirmed that lingering doubts on spin could drive yet a further pos re-rating. Meanwhile on rate case developments, PNW offered among the single updates for a constructive new rider to limit renewable lag but ACC acceptance is still key. See earlier write-ups from Day 1, Day 2 and Day 3 here.

So who were our latest meetings? Wednesdays Slate

We met with AY, ED, ES, HE, LNT, MGEE & WTRG yesterday to close out the conference. AY appears poised to provide substantial 4Q updates, likely slowing its DPS growth to a mid-single digit (see table below), from 8-10%. That said, buyout opportunities of partners and expansions at existing sites provide a rare opportunity for higher return opportunities for YieldCo. We stress its focus on smaller acquisitions too also lend themselves to sustained higher returns too. ED's new CEO was indeed impressive & thoughtful on expanding ED increasingly into renewables; its challenges in NY remain real with pressures on '21 EPS. ES was indeed positive – and whether it raises its outlook for a 6-8% EPS CAGR (or not), we see a clear bias to argue this company will achieve a 7% EPS CAGR through '25 when disclosed on 4Q call (formally rolling in transmission, CMA accretion, and smaller South Fork offshore wind project). With expectations higher, these developments appear largely appreciated by the market. Rather, more importantly, we perceive near-term confidence around draft net metering decision and forthcoming affirmation on BOEM permitting process as all boding relatively well for shares. As for LNT, we perceive confidence on substantial cost reductions & emphasize this aspect as a key point to enable yet further T&D spending (that was otherwise displaced with its 3Q updates with renewables taking its 'place' in its 5-year capex budget). On balance, our favorite defensive utility still. MGEE was indeed constructive on just how further coal retirements could meaningfully shift its outlook from cost structure – enabling yet larger capex program and potentially protracted rate case stayouts. Our ES PO shifts to $95 (vs. $90) on group multiples.

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Alliant Energy (LNT)

Alliant mgmt. highlighted the meaningful rate of change ahead in the composition of its generation portfolio, with an estimated 14% of its 2020 rate base allocated to coal generation forecast to shift to 7% by 2030 following the retirement of Lansing, conversion to gas of Burlington, and in-servicing of currently planned renewables (1000 MW WI solar, 400 MW IA solar). Among the operational improvements driven by the evolving generation portfolio are meaningful reductions in O&M, with mgmt. targeting cuts of 3-5%/yr, among the more impressive cost cutting targets across our coverage. Maintain Buy on LNT as remains our favorite defensive utility idea.

Driving 3-5% O&M reduction through renewables build

With 1400 MW of solar scheduled to come on line in coming years along with pending retirements of Edgewater (414 MW in 2022), Lansing (275 MW in 2022), and conversion of Burlington (2021), LNT mgmt. flagged an impressive outlook for O&M reductions of 3-5% per annum through 2024 as high fixed cost generation is swapped for renewables. The majority of savings are expected to come from lower overhead associated with no longer operating coal generation (including lower headcount) as well as additional investments in technology and automation across the enterprise. We note that the overall trajectory of O&M reduction implies ~15% aggregate savings over the course of the forecast period, one of the more impressive cost reduction trajectories across our coverage. Following the latest announcements of coal retirements and conversions in Iowa, mgmt. continues to evaluate the rest of its coal burning fleet to determine if and when an accelerated retirement is appropriate (coal rate base expected to fall from 14% to 7% of total through the decade). We note that MGEE mgmt. has been discussing potentially accelerating the retirement of Columbia generating (which is co-owned by LNT, MGEE, and WEC) though LNT mgmt. has stressed that it continues to evaluate plant productivity with needed future investments in deciding whether or not to accelerate a retirement.

Cash tax runway until 2024, steady balance sheet improvement seen

LNT mgmt. sees itself as not paying cash taxes based on its current appetite and tax credit profile until 2024. Mgmt. is not currently making any assumptions about potential monetization of investment tax credits in the event that such a provision were passed as part of a stimulus bill – the expectation remains that the federal government is reluctant to pick winners in terms of fuel type when crafting tax policy as it pertains to renewable generation. In terms of the balance sheet, LNT sees its FFO metrics improving over the course of the forecast period with current levels in the 'mid teens' (our forecast sees a range from 16-18% through 2024).

Clear path to 5-7% through 2024

While we attribute some of LNT shares' underperformance in the week following the Q3 announcement to lingering expectations of a capex increase at the roll-forward, we now sense that investors have largely come to appreciate that the composition of spending is weighted toward renewables in the near part of the forecast period, with a corresponding shift toward more distribution spend in later years. With no block equity in the current forecast and robust O&M reductions targeted, we continue to see LNT as one of the best-positioned Midwest utilities looking ahead.

Atlantica Sustainable Infrastructure (AY)

We continue to question the yieldco ESG re-rating trend, given the level of growth prospects that has been priced into shares across the sector. With AY expected to announce '21 guidance and a LT growth CAGR next quarter, we remain skeptical around ability to maintain 8-10% DPS growth. That said, mgmt expects AY's valuation to be supported by $200-$300mn of annual investment, at high-single-digit to low-double-digit returns, and an 80% payout; if achievable, this could admittedly help support div growth. The critical question will be whether the opportunities exist. In European markets, we note several administrations pushing for infrastructure programs with renewable components. The U.S., similarly, may provide a supportive environment for renewable development. The other question will be the level of support received from AY's sponsor AQN, given their own current issues. We would expect less support from AQN near-term, although in the longer term this may change. Maintain Neutral.

How to justify the yieldco re-rating trend?

Our meeting focused firstly on the latest yieldco re-rating trend, with questions on being able to justify current valuations in the sector. Mgmt expects AY's valuation to be supported by growth, with $200-$300mn of investments annually, including in 2020 thus far. Finding opportunities with an adequate return profile will be the key challenge, given declining returns across the renewables space. Mgmt did note that while returns have seen compression over the last couple of years, the recent declines in interest rates have helped to make returns somewhat more justifiable. A higher share price should further help to reduce dilutive impact of dropdowns partially funded with equity issuance. Assuming a high-single-digits levered return on equity investment and an 80% payout on ~$250mn annual investment and employing 3.3x CAFD/Debt, we perceive AY could potentially stand to grow at **~4% annual DPS**; suspect a substantially moderated growth rate from 8-10% given reduced usage of HoldCo debt. We note the $200-300 Mn is a placeholder but mgmt. appears abundantly confidence it can execute at this scale with its current employee base. However, the critical question will be whether sufficient opportunities exist today to generate this level of investment at adequate returns.

Exhibit 1: Placeholder drop down math

Drop Down Math			
		HoldCo Debt	74.25
Share Price	30	Debt/CAFD	3.3x
Midpoint of CAFD	250	Shares Issued (ex-Debt)	5.86
CAFD	22.5	Dilution (% Shares)	5.74%
CAFD Yield	9%	DPS Dilution =>	0.10
80% DPS Payout	18	Interest Expense	0.03
DPS Upside	0.176471	Debt Coupon	5%
Current Div	1.68	Financing Costs (EPS Terms)	*0.12*
Div % Inc (Pre-Financing)	0.105042	DPS Upside	0.05
		DPS Accretion @ 80%	3%
		DPS Accretion @ 100% payou	6%

Source: BofA Global Research, Bloomberg

Growth prospects and return expectations across geographies: watch for expansions & buyouts of partners *to continue*

In the U.S., Atlantica targets high single digit returns, while in international markets, the target is in the low double digits in certain geographies. In European markets, we see several administrations pushing infrastructure programs with renewable components which could drive growth for AY (given strong Spanish base with solar asset portfolio). In the U.S., as well, a potential Biden administration could boost growth prospects through improved returns and opportunities. We note AY's continued expansion in North American markets with its first investment in Canada, a $20mn district heating

investment. Separately, we highlight room for several more "niche opportunities" akin to the recent Solana tax equity investor buyout (we note peers including CWEN have also entered this area with re-powerings of existing projects).

Growth: Dropdowns vs. third-party partnerships vs. M&A

Atlantica noted several avenues through which to pursue growth, including investments to develop existing assets, partnerships with developers and construction companies (e.g. Algonquin, etc.), and third-party M&A through competitive deals. While AY expects that partnerships may comprise a smaller portion of growth in the short term (as partners are still developing their portfolios), longer term they are expected to make up a greater portion of the overall development pipeline.

Consolidated Edison (ED)

Con Ed's incoming CEO presented his vision for the company that largely builds on the strategic direction of the utility and non-reg business to date. At the regulated utilities the near term challenge remains managing the financial and operational impacts of Covid which are expected to persist into 2021 (and led to the recent '20 guidance cut). At the Clean Energy Business, the company continues to target investments of $400m/yr with an expectation to pivot to greater reliance on tax equity given its $800m backlog of accumulated tax credits as well as pursuing develop-build-flip projects that are less capital intensive. Incremental renewable investment opportunities were laid out for the regulated business as well, though the EV 'make ready' initiative had been previously known and battery storage potential remains in early days. Maintain Neutral on ED; we were impressed by the incoming CEO's eloquent description of future strategy – and efforts to expand renewable mandate but perceive pressures as likely to persist into 2021. We see question as still pending around future gas strategy, pressures from lost fees persisting into '21, and a regulatory backdrop that remains at an elevated risk (into 1Q21 O&R rate case filing). On balance, we perceive challenges ahead prior already reflected in its discount to peers.

2021 drivers: deferring bad debt, uncertain on foregone fees

We expect that per its usual schedule ED will provide forward guidance for 2021 with its Q4 update next Feb. Company mgmt. Among the key updates in the company's Q3 results is the deferral of Covid-linked bad debt expense – the uptick in expense reached $46m at the Con Ed Co of NY (CECONY), surpassing the materiality threshold of $20m that is part of ED's rate plans and allowing full deferral of the expense item to be considered in the next rate case filing (2022). Mgmt. indicated that it expects to defer these expenses in '21 as well, not surprising given the q/q uptick of $30m in bad debt expense as of Q3. Less obvious is whether foregone fees will be deferred in 2021 given the uncertain duration of the prohibition on charging fees to residential customers affected by Covid – recall this was the change in law (Cuomo exec orders) that drove the deferral of bad debt expense. ED estimates that it is losing $6.4m in fees *per month* during the pandemic, with an estimated half of that attributed to residential customers (though not clear how many of those are directly attributable to Covid). As we previously indicated in our updated estimates, we expect 6 months' of lost fee revenue and direct Covid expenses to impact ED by -7c, with an additional -7c due to lower Steam demand (TTM earned ROE at the Steam business is 5.6% as of Q3).

Table 1: EPS forecast

ED 2021 EPS Walk	EPS	Note
Start: 8.8% earned ROE	4.54	Based on CECONY earning full authorized
Less: foregone fees 6 months	(0.04)	6 months' impact, $6.4m revenue per month
Less: direct Covid expenses	(0.03)	Q2 impact was ($0.06)
Less: higher bad debt expense	-	Now deferred
Less: Steam lower demand	(0.07)	
BofA 2021 EPS estimate	4.40	

Source: BofA Global Research estimates

Renewable opportunities: EV station build out, still early on utility-scale storage

Incoming management flagged the opportunity to add to rate base meaningfully over the coming years via a number of renewable energy initiatives that are not fully captured in the current rate base forecast. We previously incorporated the EV 'Make Ready' charging station program into our forecasts, with an estimated EPS impact ranging from $0.02-0.04/yr based on ED's $314m of capex allocated to the program.

Table 2: Make-Ready Spend Detail

	State total	CECONY	O&R	ED Total	Central Hudson	NYSEG	Niagara Mohawk	RG&E
Level 2 Plugs	95	42	16	58	18	51	87	23
DC Fast Charger	386	192	4	195	3	13	25	8
Incentive	480	234	19	253	21	64	112	31
Futureproofing	38	19	2	20	2	5	9	2
Implementation	72	35	3	38	3	10	17	5
Transit Authority	10	3		3			5	2
Total	601	290	24	314	26	78	143	40

Source: BofA Global Research estimates

Near-term upside from spending opportunities on utility-scale storage is less obvious though mgmt. reports high-level discussions with state regulators including the New York State Energy Research and Development Authority (NYSERDA). Among the structures under consideration is a partnership with private developers whereby battery storage is developed and utility-owned for a period of 7-10 years after which ownership would revert to the developer, with initial procurement estimated in the 300 MW range in ED's service territory. We note that conversations around this remain in early stages without a formal proposal, though we do expect acceleration of renewable and storage solicitations (ED estimates ~2.5 GW of renewables needed annually to reach state interim decarb goals by 2030).

Essential Utilities (WTRG)

Management Successfully Navigating COVID & Peoples Integration

Following their positive 3Q report last week in which management reaffirmed full year guidance of $1.53-$1.58 - noting expectations to be at the top end of the range and affirmation of their 5-7% EPS growth through '22 - latest discussions with management stressed confidence around execution of their strategy with the company successfully navigating the pandemic while integrating their Peoples Gas acquisition. Recall the company has elected to use Repairs Tax accounting treatment and has effectively implemented the last several months – with guidance of $0.08-$0.12 benefit annually. We await developments around the regulatory process of the catch up component after the earlier filing, with resolution expected early in April of 2021. Rather than drive incremental upside to their 5-7% EPS CAGR, the filing seeks to extend the growth without a need for a rate case. As opposed to going in for new rates in 2023 to take effect in 2024, a constructive outcome from the catch up filing would benefit '23, with incremental benefits in '24, and '25 to help drive earned returns for the segment in outer years without any rate relief until 2026. Bottom line, the repairs tax debate boils down to Peoples Gas ROE lag in '23, likely to a modest degree. Focus on EPS growth roll-forward to '23 (presumably with 4Q) will be of importance. Given the uncertainties in the outlook mgmt. intends to limit its roll forward to a 3-year outlook in spite of peers having a 5-year outlook. On balance we feel comfortable in mgmt's ability to manage lag around its ROEs at core water utilities including PA into a potential water filing next year.

Muni Pipeline Remains Strong amid pending DELCORA developments

With FMV legislation now in all eight water & wastewater states in WTRG's footprint following the passage in Virginia earlier this year, the company continues to execute on tuck in acquisitions and discussions continue to highlight a robust pipeline of opportunities. The company has already closed on Campbell, East Norriton, and Rockwell Utilities this year, with another ~353Mn of rate base opportunities from signed APAs expected to generate an additional ~$18Mn of earnings potential. Meanwhile, the company is actively pursuing acquisition opportunities across all of their water geographies, with ~360K customers identified, the majority being wastewater. We expect more firm announcements in coming weeks.

We see the latest pressures put on munis from the ongoing pandemic as likely to only further accelerate consolidation in the industry. Meanwhile, a further environmental push under a Biden administration could provide additional capital opportunities as compliance costs with PFAs and water quality concerns have already started contributing to the push away from muni owned water systems.

Management remains confident on the DELCORA process, with a regulatory approval expected in mid-March. This would put the company on track to potentially close the transaction in April or May after the 30 day appeal window. Meanwhile, a hearing is scheduled for early December regarding the litigation around the trust with a ruling expected from the judge within 60 days. Recall the company has until August to pull on the ~$300Mn equity forward to be used for DELCORA and other acquisitions.

We reiterate our Buy rating, seeing upside risk in the event of better than expected execution on their long-term growth rate.

Eversource Energy (ES)

Poised to Extend with Upcoming Roll Forward: Q'n is Just How Much Upside?

Following their 3Q report last week in which ES management reaffirmed full year guidance of $3.60-$3.70 (excluding full year costs related to the recently completed acquisition of Columbia Gas of Massachusetts) and its long-term EPS growth rate from its core regulated business of 5-7%, latest discussions with management continued to stress confidence around the trajectory of the company. While still unclear if it will formally raise to 6-8% trajectory, it is clear mgmt. will pivot to high end of its EPS growth rate by 4Q with inclusion of both smaller offshore (South Fork) likely alongside inclusion of CMA and potentially modest capex. We see a positive near-term tailwind between offshore wind trends and otherwise constructive updates. Management plans to roll forward their five year outlook through 2025 with full year results, with inclusion of Columbia Gas and some added capex from annual updates across their businesses including some transmission projects incremental to the plan. We perceive another ~$50Mn in transmission spend vs. what was previously contemplated; meanwhile, new MA legislation allowing the expansion of utility-owned solar generation is awaiting conference committee after being enacted in the House: this would allow utilities to own up to 10% of solar amount on its system, suggesting 230MW permitted for NSTAR Electric that would be incremental to the plan. We don't necessarily anticipate offshore wind or AMI to be firmly included with the update given a lack of clarity around approvals and timing, but nonetheless could see management point to a higher range from just the CMA accretion given the low acquisition price of 1x rate base. Expectations are for CMA alone to be accretive this quarter with further incremental accretion each year. It remains unclear if management would formally shift up guidance as opposed to pointing to the higher end given additional opportunities not yet formally included.

Offshore Protracted, but Upside Here too Quite Possible

After early commentary from Orsted around offshore delays, ES indicated changes in expectations around most recent in service dates of end of 2023 for South Fork wind (vs. End of 2022 previously), that it is unlikely to achieve end of '23 in-service date previously alluded to for Revolution Wind, and that it is unlikely to achieve the end of '24 in-service date for Sunrise Wind. Following the BOEM review schedule for South Fork Wind, the COP decision is due in January 2022 while the BOEM review schedule for Revolution Wind is now expected in early '21 (vs. late this year previously). After filing the COP application for Sunrise wind, the BOEM review schedule is expected in 2021. We see 2026 as entirely possible – and therefore outside of the 5-year window for the 2021-2025 CAGR roll forward. Management expects news from BOEM around Vineyard Wind shortly to help provide further clarity on their projects.

That said, a growing consideration is improvements to the economics of the projects: commentary from management highlighted that delays have provided latitude for better tech and we see improving O&M as another interesting nuance. It remains to be seen how prospects can further improve under a Biden administration given his support for offshore wind. We could yet see extensions for tax credits & inclusions for offshore wind and we perceive potential appetite for ITCs through 2025.

While current projects face delays on the margin, the company has capacity to build 4GW (with the JV representing 1.7GW) as they look to optimize their local expertise, and Orsted and ES announced their joint proposal to develop Sunrise Wind 2 (a new offshore wind farm for New York State). We perceive there may have only been three bidders for the project and quite possible multiple bids are awarded.

We see near-term resolution around low income rates in CT and storm response as key to enabling re-rating of shares higher. While we could yet see penalties accrue around Isaias, we stress the watered down Take Back our Grid Act in Connecticut was ultimately much less punitive than initially feared. We raise the PO from $90 to $95 on higher

group electric/gas multiples (17.3x/15.3x) vs. prior (16.5x/13.8x) Maintain Neutral given we see balanced risk/reward.

That said, we look for resolution around potential latest proposed decision in net metering tariff adjustment that would reduce rates in CT. Management remained confident in its ability to recover lost revenues from NEM in final order. Watch this in coming weeks to drive shares given $16Mn+ impact.

Hawaiian Electric Industries (HE)

Sustained cost reductions remains a key focus area ahead

With discussions, mgmt focused on sustaining cost reductions into '21+. Mgmt expressed a focus on sustained cost savings with the PUC mgmt audit. Among key cost levers expressed include strategic sourcing (renegotiating supply agreements with vendors, etc), work force reduction strategy (reduced overtime and improved scheduling coordination), process improvements, and other cost efficiency to lower cost of services.

That being said, in terms of O&M reductions to date, mgmt acknowledges meaningful portion (half of 3Q) associated with delayed but needed generation overhauls and station maintenance work, effectively timing shifts into 4Q and 1Q21 with FY20 utility guidance remaining at the bottom half of the range despite YTD performance. On a forward basis, mgmt express ability to keep O&M at or below inflation as key to forward performance beyond commitments of $25mn in annual cost reductions.

On balance a constructive meeting when considering both O&M tailwinds discussed from latest cost cuts pursued as well as potentially bottoming out on ASB. That said, clear pressures exist into '21 to drive EPS pressures vs Street. We maintain our Underperform pending clarity on critical PBR reforms ahead in coming weeks – this will be the single most important datapoint for shares in years.

PBR key focus on potential to reduce structural lag towards 9.0%

Among notable commentary, mgmt expressed potential opportunity to improve earned ROEs towards 9.0% (relative to authorized ROE of 9.5%) following the conclusion of PBR through the reduction of structural lag. While LTM ROE stands at 8.4% (with structural lag comprising ~120bps), mgmt expressed near-term O&M levels as an exception given push-out benefit with negative impact to 4Q/1Q21 ahead. As such, mgmt expects PBR resolution of structural lag potentially supporting towards a 9.0% earned ROE relative to a lower than 3Q normalized baseline ROE.

In terms of PBR discussions, mgmt expressed positives as support for earning sharing mechanisms (ESM) including both positive and negative, potentially with sharing in under-earning as well. Additionally, mgmt expressed focus on incentive PIMs with a range being established. Accelerating the annual accrual date for RAM to Jan 1 annually from June 1 also helps with structural lag. That said, 'day-1 savings' will likely be a focus as well, with Consumer Advocate proposing 4x cumulative value of accelerated RAM accrual relative to HE proposing the already committed $25mn by 2022 reduction.

Mgmt continues to expect a final PUC decision for PBR Phase II in Dec. That said, mgmt emphasizes specific rate tariffs will be established to implement new and gauged mechanisms after the order, as a new step by the PUC. As such, the timeline to reduce structural lag remains unclear. With potentially multi-year targets, mgmt expressed the extent of which under-earning can be mitigated in 2021 remains contingent on PBR results. Nonetheless, we perceive potential upside relative to earned ROE reflected in the low 8% range in our forecast but emphasize need for execution.

ASB remains cautious with yet further NIM compression likely ahead

On the other hand, ASB discussions remained cautious. With continued NIM compression into 3Q already at 3.12% (vs. 2Q/1Q NIM of 3.21%/3.72%), mgmt expressed further pressure ahead relative to already below-expectation 3Q levels. This is primarily driven

by the spread between higher rate existing loans rolling off and being replaced by new customer loan agreements at lower rates, with mgmt expressing a slow but gradual continued decline in NIMs likely as long as interest rates are lower relative to a year prior. With rates expected to remain low through the near-term, we expect continued pressure at the ASB segment. While, mgmt did not explicitly guide expectations for lower NIM relative to 3.12% in 3Q into 2021, noting variables including potential for higher margin mix as well, downward pressure on existing vs. new pricing remains.

For loan loss provision, mgmt continues to express uncertainty, though noting it exercises conservatism in projecting potential loan losses. If actual net charge offs are ultimately less than what is provisioned for ASB could see some provision come back. Mgmt expresses YTD provision largely in-line with its expectations. However, mgmt notes this could worsen if additional lockdown and economic pressures worsen (with economic impact with sustained tourism reopening uncertain).

MGE Energy (MGEE)

MGEE mgmt. expressed confidence in its near-term regulatory outlook with the pending decision of its WI rate case settlement expected before the end of the year. While capex shifted incrementally during the 2020-22 period it still remains elevated as MGEE works to complete its utility scale solar build at Badger Hollow and Two Creeks. Ahead of the roll-forward of its 3-year capex plan to be rolled out with the Q4 results, we look ahead to potential updates on further generation spend (particularly given WEC's confirmation of the exercise of its West Riverside option) though see these as mid-2020s items. Maintain Underperform on MGEE.

Generation investment needed by mid-decade

MGEE is in the process of completing 170 MW of utility scale solar at its Badger Hollow, Two Creeks, and O'Brien facilities with all targeted for completion by 2022. Unlike WEC, which confirmed its intention to exercise the option it holds to purchase an incremental 200 MW of generation capacity at LNT's recently opened West Riverside facility for total capex of $180m, MGEE did not confirm its plans with the option it holds for 50 MW (with option good until 2025). While the *specific* generation addition plans remain to be determined, MGEE mgmt. reiterated that it does see investment opportunities in new generation by the mid-2020s with expected upcoming retirements of gas combustion turbines (75 MW), Blount Generating (94 MW), and expiring PPAs (50 MW). We perceive that MGEE mgmt. is holding off on making fuel type decisions for its future generation fleet until necessary investments are required, rather than committing to a specific fuel now (such as gas as a bridge to renewables). While we do see a step-down in capex in the 2023+ timeframe following the placement in service of the current crop of renewables, we note there is mid-decade upside from the next tranche of generation spend, as well as incremental opportunities such as deployment of advanced meters.

Looking constructive on WI rate settlement

The Wisconsin electric 2021 rate settlement remains pending with the commission, though mgmt. indicates confidence in achieving a final order before year-end. Under the proposal rates would remain flat at the electric utility along with a 4% increase in gas rates, with a tightening of the fuel cost bandwidth to 1% from 2%, with an expected continuation of the ROE and authorized equity layer. With the majority of stakeholders in the proceeding signing off on the proposed settlement, we see a constructive outcome as more likely than not.

Storage co-investment opportunities with WEC, others

Following fellow WI utility WEC's update which is targeting 600 MW of rate base storage rollout through its forecast period, MGEE sees opportunities for co-investment, in particular in storage attached to co-owned projects (Badger Hollow, Two Creeks). Intriguingly, the opportunity extends beyond pairing storage with generation assets to the distribution system as well, though specific projects and investment sizes were not included in MGEE's update. As with additional generation investment, we see storage co-investment as a potential area to watch though likely in the 2022+ timeframe (beyond the current capex forecast).

Stocks mentioned

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
LNT	LNT US	Alliant Energy Corp	US$ 57.42	B-1-7
AY	AY US	Atlantica Sustain	US$ 33.87	B-2-7
ED	ED US	Consolidated Edison	US$ 81.72	A-2-7
WTRG	WTRG US	Essential Utilities	US$ 46.37	B-1-7
ES	ES US	Eversource Energy	US$ 94.42	C-2-8
HE	HE US	Hawaiian Electric	US$ 37.05	A-3-7
MGEE	MGEE US	MGE Energy	US$ 72.16	A-3-7

Source: BofA Global Research

Price objective basis & risk

Alliant Energy Corporation (LNT)
Our $61 PO is based on a sum of the parts analysis employing relative premium and discounts to the large cap regulated peer multiple of 16.8x 2023E P/E. We note that electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. We apply a 3.0x P/E premium on IPL as we see the rate case overhang being resolved. We apply a 4.0x P/E premium on Eastern Wisconsin Electric Company reflecting 1) low risk investment nature of the state, 2) above average ROEs, 3) higher than average growth runway for investments, and 4) bad debt deferral. At ATC, we reflect a 2.0 x P/E premium on LNT's 16% share in the transmission company. Growth expectations for this segment are high, paired with above average ROEs that we believe face less downward pressure vs. regulated state distribution ROEs. We apply an in line multiple at the parent to account for the blend of numerous businesses some which benefit from long term stable PPAs via intercompany generation. Risks to our price objective are: 1) adverse rate case outcomes, 2) further equity dilution beyond our estimates, 3) interest rate risk, 4) natural disasters, and 5) lower allowed ROEs.

Atlantica Sustainable Infrastructure (AY)
Our $33/sh PO is based 50% on a DCF valuation and 50% on our Growth approach. Our Growth value is $36 (weighted 50%). Our DCF value is $29.00 (weighted 50%).

Assumptions in our DCF valuation are:
- A 7.0% discount rate based on a CAPM methodology assuming a 0.6% risk free rate and a 5.5% equity risk premium
- 2% annual escalator in corporate expenses

Main assumptions in our Growth valuation are:
- Run-rate CAFD generated by the current portfolio of $213 Mn
- 750 MW of future drop downs
- A target payout ratio of 80%

Downside risks are 1) the company may not be able to access capital markets at favorable terms, 2) the company may not be able to make accretive acquisition opportunities to fuel growth, 3) the company may not be able to grow DPS at the targeted growth rate, 4) the company may not be able to sustain its current dividend levels, and dividend yield could increase.5) PCG related counterparty exposure is among the nearest exposures to watch.

Consolidated Edison (ED)
Our $82 PO is based on a sum-of-the-parts analysis applying premiums and discounts to the regulated group multiples (16.6x/14.0x for electric/gas respectively) with a -1.0x discount on both Steam & Electric to reflect Covid recovery overhang. Steam for lack of decoupling. Both electric and gas peer P/E multiples are grossed up for a year to 2021 by 5% to reflect capital appreciation across the sector. We applied inline peer regulated multiple at CECONY despite its rate certainty for conservatism as our higher capex expectations are reflected in our EPS outlook. We apply a discounted PE for infrastructure projects given the lack of clarity around the capital structure. We further apply an EV/EBITDA approach on 2023E EBITDA to the CEB business using a 10.0x multiple for both the legacy portfolio and the renewables portfolio seeing it as having higher quality returns.

Downside risks: ED, like all utility stocks, is also sensitive to changes in the market level of interest rates. Utilities historically underperform if bond yields rise, and outperform when they fall. Further downside risks are the inability to recontract storage, adverse regulatory outcomes, a deteriorating regulatory environment, or unforeseen disasters such as the Harlem gas explosion, the SRE transaction not being completed. Customer

inflation is also a downside risk. PCG related counterparty exposure is among the nearest exposures to watch.

Essential Utilities (WTRG)
Our price objective is $51 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. These peer multiples are 25.5x and 13.9x. We apply a 3.0x premium to Peoples Gas given the organic growth opportunities, while applying a variety of premiums to its water (2x previously) subsidiaries: +4x to PA, +3x to IL, +2x to OH, +2x for TX, +2x for OH, and no premium for balance of biz. We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Eversource Energy (ES)
Our sum of the parts based price objective of $95 uses P/E multiples on 2023E earnings. For electric utilities, we attribute a 4x premium NSTAR, and 3x premium to PSNH and CL&P to peer 17.3x multiple, reflecting future potential positive revisions to capex and earnings. For gas, we apply a 3x premium to the peer 15.3x multiple, given capex upside particularly in MA and a 2x for Columbia Gas. Both electric and gas peer P/E multiples are grossed up by 5% to reflect capital appreciation across the sector. We value Aquarion at a 1x premium to the 27.5x water multiple. We reflect ES's 50% ownership in Revolution and South Fork offshore wind sites on an NPV basis. We take out 50% of parent debt, and 50% of interest to accurately reflect parent leverage.

Upside risks to our price objective are additional capex announcements on the T&D side, as well as success in offshore wind RFPs.

Downside risks are reduction in authorized ROEs, inability to meet earned ROE expectations, as well as failure to receive permitting on incremental capex opportunities

Hawaiian Electric Industries (HE)
Our PO of $34 for Hawaiian Electric Industries is based on a sum of the parts approach. We apply: 1) a 2023E forward P/E multiple in line with electric utility peer multiple of 16.9x. We see this as justified given ongoing issues in the regulatory environment need to be resolved and the earnings gap vs what is required to achieve authorized ROEs across all three of the jurisdictions. Electric utility peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector, 2) a 2021E forward price to tangible book value of 1.50x to the banking subsidiary, a 0.5x premium to smid cap regional peers (0.96x), in-line with Hawaiian banks peers due to outperformance. We then take into account parent overhead by applying the same multiple here as to the utility segment to 50% of parent interest and subtracting the per share value of the remaining 50% of the debt. Downside risks are delays on capital expenditures, weakening regulatory environment, PUC denial of new capital investments or lower authorized ROEs. Upside risks are expansion of capital expenditure plan, significant improvements in earned and/or authorized ROEs

MGE Energy (MGEE)
Our $62 PO is based on a sum-of-the-parts analysis applying premiums and discounts to the regulated group multiples (16.5x/13.9x for electric/gas respectively) with a 4.0x premium on WI regulated gas and electric to reflect the constructive regulatory mechanism, and a 2.0x premium on Transmission assets. We note that both electric and gas peer P/E multiples are grossed up for a year to 2021 by 5% to reflect capital appreciation across the sector. We apply utility premiums to the non-regulated Elm Road and West Campus assets as these are leased under long-term contractual arrangements. Downside risks: MGEE, like all utility stocks, is sensitive to changes in the market level of

interest rates. Utilities historically underperform if bond yields rise, and outperform when they fall. Further downside risks are the inability to secure further renewable rate base investments, adverse regulatory outcomes, a deteriorating regulatory environment, or adverse weather leading to less consumption of electricity and gas. Upside risks are acceleration of renewable gen investment, legacy coal asset early retirement, and enactment of further pro-renewable state policies.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AES	AES	AES US	Julien Dumoulin-Smith
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Enphase Energy	ENPH	ENPH US	Aric Li
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
NEUTRAL				
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Atlantica Sustainable Infrastructure	AY	AY US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Southwest Gas Holdings	SWX	SWX US	Richard Ciciarelli, CFA
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	TransAlta Renewables Inc.	YRNW	RNW CN	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Utilities Group (as of 30 Sep 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	79	51.63%	Buy	59	74.68%
Hold	36	23.53%	Hold	24	66.67%
Sell	38	24.84%	Sell	25	65.79%

Equity Investment Rating Distribution: Global Group (as of 30 Sep 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1749	54.79%	Buy	1114	63.69%
Hold	677	21.21%	Hold	415	61.30%
Sell	766	24.00%	Sell	386	50.39%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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January 11, 2021

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	Outperform/Moderate
Price:	$48.72
Target Price ($US):	$54.00
Market Cap ($US millions):	$11,950
ADTV (US$ millions):	$61.0

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2018A	$1.08	-	$838.1	-	45.1x
2019A	$1.00	-	$889.7	-	48.7x
2020E*	$1.15	$1.59	$1,396	$1,639	42.5x
2021E	$1.68	$1.67	$1,625	$1,819	29.0x

FYE 12/30; Revenue in USD millions.

All historical EPS and B&S EPS estimates GAAP.

*Guidance: $1.53-$1.58 ("adjusted") reflects full year of Peoples.

Source: Capital IQ, B&S Estimates

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2021 guidance in-line, muni acquisition program remains on-track with key DELCORA court win.

Essential Utilities issued initial 2021 EPS guidance of $1.64-$1.69, bracketing incoming consensus of $1.67 (2020E: $1.59), highlighting the steady growth story of the regulated utility business. At the mid-point, the 2021 guidance represents year/year EPS growth of 5%, a solid figure in what remains a highly uncertain macro environment. We reiterate our Outperform rating for shares of WTRG, which are among our current top ideas in the water/environmental sector.

Key Guidance/Outlook Highlights:

- Diluted EPS: $1.64-$1.69 (midpoint $1.665)
- 3-year EPS CAGR: 5% to 7% (through 2023)
- 3-year Capex Target: $3 billion (Water + Gas)
- 3-year Rate Base CAGR – Water: 6% to 7%
- 3-year Rate Base CAGR – Gas: 8% to 10%
- Water Customer Growth: 2% to 3% (organic + acquisitions)

Discussing the municipal acquisition pipeline, Essential says that it currently has purchase agreements in place representing 225,000 customer connections and $420 million in rate base. This is up from 212,000 connections at the end of 3Q despite the tabling (for now) of the Norristown (PA) opportunity, reflecting in part the recent addition of Bourbonnais (IL) and underscoring the depth and cadence of the municipal M&A market in the fair market value era.

The $276 million purchase of DELCORA is the biggest deal pending, and we believe recent developments bode well for the transaction. A legal challenge brought by Delaware County politicians received a major setback when the Delaware Court of Common Pleas ruled in Essential's/Aqua's favor. Attention now turns to the PUC, where the deal must be approved before moving on to closing. We see the DelCo ruling as a key win for Aqua and would be very surprised if the PUC does not approve the deal. We anticipate a 2Q21 close.

WTRG and its regulated utility peers have performed respectably of late on a risk-adjusted basis (WTRG +5% TTM), but have lagged the broader bull market (S&P 500 +17% TTM) and in particular the huge gains in the water industrial sector (peer group average +33% TTM). We believe WTRG shares offer a compelling reward/risk equation, and reiterate our Outperform rating. Our price target of $54 reflects a P/E of 32times, in-line with the water utility peer group.

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Disclosure Appendix

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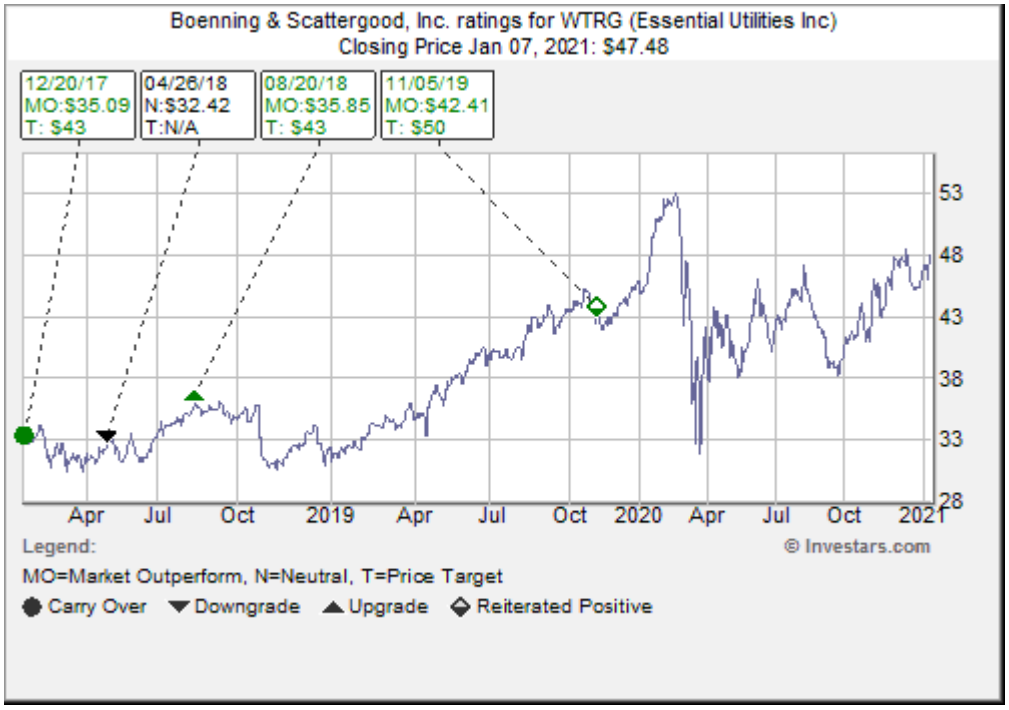

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- ***Neutral (Hold):*** The security's total return over the next year or longer is expected to be roughly equivalent to the total return of the S&P 500™ over the identical period.
- ***Underperform (Sell):*** The security's total return over the next year or longer is expected to be less than the total return of the S&P 500™ over the identical period.

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- ***High:*** The security has lower-than-average fundamental predictability and/or higher-than-average price volatility.
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Coverage Universe (a)	% of Universe
Outperform (Buy)	32%
Neutral (Hold)	46%
Underperform (Sell)	1%
Not Rated	20%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	21%
Neutral (Hold)	9%
Underperform (Sell)	100%
Not Rated	7%

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August 14th, 2019

Coker Palmer Institutional

Equity Research
Water & Sustainable Infrastructure

Aqua America, Inc.

WTR - NYSE

Recent Px: $43.65

Company Update:

Company Delivers Favorable Q2 Results & Outlook; Advise Buying Dips

Investment Summary: *Aqua reported solid Q2 results as the company beat our non-GAAP diluted EPS estimate. Many developments transpired during the quarter that are imperative to our model, including a timing discrepancy in the P&L recognition of the Pennsylvania rate case, a delay in the close of the Peoples acquisition, and approval of the large Peoples rate case. As a result, WTR was short of our Q2 top-line estimate, and we were forced to meaningfully modify our model. However, the revision positively affects the model by swinging our 2019 diluted EPS estimate to the top-end of the guidance range from the bottom, and for 2020 and 2021, diluted EPS estimates are essentially the same. On top of these factors, the long U.S. Government bond yield fell over the course of Q2, as well as the five-year WTR beta (according to FactSet). In turn, the stronger 2019 estimated Aqua fundamentals, together with the lower long yield and beta, drive up the valuation multiple, and with our 2020 diluted EPS estimate unchanged, our fair value rises due to the valuation multiple increase. Accordingly, we view the Q2 report and resultant outlook favorably. Still, the stock run-up (along with top water utility peers) the past two weeks on trade tensions, and a falling risk-free rate, is pressing shares against our revised fair value that is at Street-high. Plus, we see the emergence of chatter around Fed rate cutting, and/or a trade truce, contracting the valuation multiple. As such, we see strong potential for a lid to be placed on shares, and for pullback and volatility. That said, our desire to recommend accumulating shares on the solid Q2 report and attractive outlook is offset by valuation. With this in mind, we encourage investors to take a year-end 2020 investment horizon with Aqua and buy dips, because once valuation rolls to 2021 estimates, it becomes compelling once again, and WTR is armed with many catalysts to power the stock to the next year fair value that currently stands at $51/sh according to our model.*

- **Aqua delivers Q2 bottom-line beat.** Q2 non-GAAP diluted EPS of $0.37 was $0.03 higher than our estimate. Revenue of $218.9m was $7.8m beneath our $226.7m estimate. The sales difference was a function of timing discrepancy in the model around incorporating the Pennsylvania rate case versus when the rate case went into effect. For simplicity, we plugged an April 1st rate case impact start into the model, yet the rate relief began May 24th. Had we forecasted a one-month recognition of the rate case in the model for Q2, our sales estimate would have matched the Q2 report. On that note, bottom-line outperformance stemmed from better-than-expected other income lines below the line.
- **Flow-through on model revision strengthens 2019 to 2021 earnings estimates and the financial condition.** During Q219, Aqua announced it anticipates closing the Peoples acquisition this fall instead of this summer. Moreover, WTR announced a Peoples rate case outcome of $59.5m. Going into Q2, we modeled Aqua and Peoples to begin operating as one company in Q319, and we estimated a $54.1m positive top-line impact, starting in Q419, from the Peoples rate case. Owed to the Peoples developments, we push out the close of the Peoples deal, in our model, by one quarter to Q419, which cuts our Q319 estimates, and we bump up our Q419-start Peoples rate case estimate to $59.5m to mirror the outcome. We also adjust the Aqua Pennsylvania rate case inclusion in the model to more accurately reflect timing. The model flow-through from these changes, and the update for actual Q2 figures, causes our 2019 non-GAAP diluted EPS estimate to climb by $0.06 to $1.50 (top of the $1.45 to $1.50 2019 guidance range), strengthening cash generation to a degree that reduces net debt estimates while lifting dividend estimates. Due to the greater 2019 non-GAAP diluted EPS estimate, lower net debt forecast, and higher dividend projection, our target P/E valuation multiple swells. For 2020 and 2021, the model flow-through leads to non-GAAP diluted EPS estimates for each year staying the same. This translates into YoY non-GAAP diluted EPS growth of ~6.5% for each year over the 2019 to 2021 period, implying to us our earnings estimates are on track when considering the Aqua rate base, and consolidated company breakdown, guidance for the Peoples and WTR combined entity.
- **We see stock pullbacks creating investment opportunity.** With our 2019 dividend and non-GAAP diluted EPS estimates rising to $0.91/sh from $0.90/sh, and $1.50 from $1.44, respectively, combined with the drop in the year-end 2019 consensus 30-year U.S. Government bond yield estimate to 2.5% from 3.0%, and the WTR five-year beta fall to 0.63 from 0.65 (FactSet), our target P/E valuation multiple amplifies to 28.2x from 26.4x. As a result, our fair value increases by $3 to $45. We support our valuation with the justified P/B multiple and justified dividend yield approaches that point to fair values of $45 and $47, respectively, based on a multiple and yield of 3.2x and 1.95%, respectively. Peeking into next year, our model suggests P/E multiple expansion to 29.9x, and when applied to our 2021 non-GAAP diluted EPS estimate of $1.70, the 29.9x multiple implies 2021 year-end fair value is $51/sh. Bearing this in mind, upside to the $51 mark from the present trading level stands at 16.8%, yet, accumulating shares at the current price sets up for the risk of pullback on current year (2020-based) valuation. Furthermore, we see potential for pullback on the back of easing trade tensions and discussion of Fed rate cuts. To these points, we advise investors to accumulate shares on dips with an investment horizon through 2020 year-end, and as Aqua catalysts come to fruition, we see value in the stock being unleased to ultimately drive it to the $51 fair value by end of next year.

Ticker	WTR
Last Price	$43.65

Valuation Parameters	
Risk-Reward	0.9x
Upside	$49
Fair Value	$45
Downside	$38

Market Capitalization	
Market Cap ($m)	9,419
Cash ($m) (2018A)	4
Debt ($m) (2018A)	2,398
Enterprise Value ($m)	11,814

Financial Estimates

	2018	2019E	2020E	2021E
Rate Base ($m)	4,500	7,073	7,657	8,246
EBITDA ($m)	470	576	881	940
EPS	$1.41	$1.50	$1.59	$1.70
DPS	$0.84	$0.91	$0.98	$1.06

Valuation

	2018	2019E	2020E	2021E
P/E	31.0x	29.1x	27.4x	25.7x
Dividend Yield	1.9%	2.1%	2.2%	2.4%
EV/EBITDA	25.1x	20.5x	13.4x	12.6x

Market Stats	
Shares, FD (2018A)	178m
Short Interest, % Float	530%
Beta	0.63
52 Wk High	$44
52 Wk Low	$32
Average Daily Volume (90-Day)	1,051k

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Please see full disclosures in the Appendix of this report.

Exhibit 1: Base Case P&L

Aqua America, Inc.
Income Statement
(in millions except per share data)

Coker Palmer Institutional
Richard Verdi; 646.827.9586

December Fiscal Year	FY 2016	FY 2017	FY 2018					FY 2019E					FY 2020E	FY 2021E
Non-GAAP	Year	Year	1Q18	2Q18	3Q18	4Q18	Year	1Q19	2Q19	3Q19E	4Q19E	Year	Year	Year
Revenue	**$819.9**	**$809.5**	**$194.3**	**$211.9**	**$226.1**	**$205.7**	**$838.1**	**$201.1**	**$218.9**	**$244.7**	**$473.4**	**$1,138.2**	**$1,944.9**	**$2,015.9**
Operating & Maintenance	304.9	287.2	73.9	73.5	68.6	92.4	308.5	79.3	86.4	92.3	239.2	497.2	985.4	995.2
Depreciation	131.0	136.3	36.0	36.6	37.5	36.0	146.0	39.1	39.6	40.1	61.8	180.5	253.7	262.9
Amortization	2.0	0.4	0.1	0.1	0.2	0.2	0.6	0.3	(2.9)	0.2	0.2	(2.2)	0.9	0.9
Non-Income Taxes	56.4	56.6	15.0	14.8	15.6	14.4	59.8	15.0	14.9	16.0	18.8	64.7	78.6	80.6
Operating Income	**325.6**	**329.0**	**69.3**	**86.8**	**104.3**	**62.8**	**323.2**	**67.4**	**80.9**	**96.1**	**153.4**	**397.9**	**626.4**	**676.3**
Interest Expense, Net	(80.6)	(88.3)	(23.5)	(23.7)	(25.4)	(26.3)	(98.9)	(27.9)	(28.9)	(29.8)	(48.6)	(135.2)	(213.5)	(234.2)
Allow. for Funds for Construction	8.8	15.2	2.9	2.6	3.1	4.5	13.0	4.1	3.6	3.9	5.6	17.1	25.1	24.5
Gain on Sale of Other Assets & Other	0.4	0.5	0.2	0.1	0.3	14.3	14.9	6.0	10.9	8.4	8.4	33.7	20.0	20.0
Equity Earnings in JV	1.0	0.3	(0.2)	0.5	(0.1)	(0.1)	0.1	0.5	1.2	0.6	0.3	2.7	1.9	1.5
Income Before Taxes	255.2	256.7	48.7	66.2	82.2	55.2	252.3	50.2	67.8	79.2	119.1	316.3	459.9	488.1
Income Taxes	21.0	16.9	(2.1)	(0.4)	3.9	0.0	1.5	0.5	0.9	1.7	13.2	16.3	51.1	54.2
Net Income (Continuing Operations)	**234.2**	**239.7**	**50.8**	**66.6**	**78.2**	**55.2**	**250.8**	**49.7**	**66.8**	**77.5**	**105.9**	**299.9**	**408.8**	**433.9**
Diluted EPS	**$1.32**	**$1.35**	**$0.29**	**$0.37**	**$0.44**	**$0.31**	**$1.41**	**$0.28**	**$0.37**	**$0.43**	**$0.42**	**$1.50**	**$1.59**	**$1.70**
Diluted Shares Outstanding	177.8	177.2	178.2	178.3	178.4	178.4	178.4	178.6	178.7	178.8	254.3	197.6	254.9	255.9
Margin Analysis														
Operating & Maintenance	37.2%	35.5%	38.0%	34.7%	30.3%	44.9%	36.8%	39.4%	39.5%	37.7%	50.5%	43.7%	50.7%	49.4%
Depreciation	16.0%	16.8%	18.5%	17.3%	16.6%	17.5%	17.4%	19.4%	18.1%	16.4%	13.1%	15.9%	13.0%	13.0%
Amortization	0.2%	0.1%	0.1%	0.1%	0.1%	0.1%	0.1%	0.2%	-1.3%	0.1%	0.0%	-0.2%	0.0%	0.0%
Non-Income Taxes	6.9%	7.0%	7.7%	7.0%	6.9%	7.0%	7.1%	7.4%	6.8%	6.6%	4.0%	5.7%	4.0%	4.0%
Operating Income	39.7%	40.6%	35.7%	40.9%	46.1%	30.5%	38.6%	33.5%	37.0%	39.3%	32.4%	35.0%	32.2%	33.5%
Income Before Taxes	31.1%	31.7%	25.1%	31.3%	36.3%	26.8%	30.1%	24.9%	31.0%	32.4%	25.2%	27.8%	23.6%	24.2%
Income Taxes	8.2%	6.6%	-4.4%	-0.6%	4.8%	0.0%	0.6%	0.9%	1.4%	2.1%	11.1%	5.2%	11.1%	11.1%
Net Income	28.6%	29.6%	26.2%	31.4%	34.6%	26.8%	29.9%	24.7%	30.5%	31.7%	22.4%	26.4%	21.0%	21.5%
Growth Rates yr/yr														
Revenue	0.7%	-1.3%	3.5%	4.2%	5.2%	1.2%	3.5%	3.5%	3.3%	8.2%	130.1%	35.8%	70.9%	3.7%
Operating Income	1.4%	1.0%	-0.8%	2.5%	7.0%	-18.4%	-1.8%	-2.7%	-6.7%	-7.8%	144.3%	23.1%	57.4%	8.0%
Income Before Taxes	7.1%	0.6%	-6.3%	-0.5%	3.2%	-5.6%	-1.7%	3.0%	2.3%	-3.6%	115.8%	25.4%	45.4%	6.1%
Net Income	4.9%	2.4%	3.6%	9.2%	2.6%	3.2%	4.6%	-2.2%	0.3%	-0.9%	91.9%	19.6%	36.3%	6.1%
Diluted EPS	4.5%	2.3%	3.4%	9.1%	2.5%	3.1%	4.5%	-2.4%	0.1%	-1.1%	34.6%	6.5%	6.4%	6.4%

Source: Aqua America, Coker Palmer Institutional Equity Research Estimates

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Energy | Power & Utilities

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AGA Meeting Takeaways

In this note, we briefly summarize takeaways from each of our AGA meetings over the past two days.

Ameren Corp. (AEE), Outperform rating, $84 price target

- **IL Downstate Clean Energy Act:** AEE feels good about bill passage this year given bipartisan support / job creation potential. Whether it is addressed during the current legislative session ending 5/31, in a special session or the veto session remains to be seen. Recall that the Act would increase the adder on the ROE formula from 580 to 680 bps above the 30-YR treasury. It would also create the opportunity for solar/storage/EV investment in a state where AEE is purely T&D.
- **MISO ROE decision possible this Thursday:** AEE is hopeful that FERC will revise the methodology/raise the base ROE given consensus that it is based on a flawed methodology and the fact that transmission investment is more risky than distribution.
- **Next rate case in MO**: The primary factors determining timing of the next rate case are the wind projects slated to go into service late this year and early next year, and COVID-related issues. The only restriction on filing in MO is a 60-day notice. AEE expects to earn its allowed ROE in MO (recently increased from 9.2-9.7% to 9.4-9.8%) with help from PISA accounting and RESRAM riders.
- **O&M savings**: As AEE stated on the Q1 call, it expects to deliver within its 2020 EPS guidance by offsetting COVID-related impacts with reduced O&M. The reductions fall into several buckets, including reduced hiring, travel, consultants, etc.

See inside for our takeaways on 11 more companies.

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Avangrid (AGR), In Line Rating, $46 price target

- **Vineyard Wind:** AGR still expect BOEM to release draft cumulative impact statement on June 12 and for final EIS to come in November in line with BOEM's most recent schedule. AGR noted they have been in constant contact with BOEM, giving us more confidence that this schedule will hold. As a reminder, the cumulative impact statement will have impacts on other projects in the area, such as ES and Orsted's Revolution Wind.
- **NECEC**: The ME Department of Environment Protection issued a permit last week, so they now have all state permits. They are still waiting for Army Core of Engineers and a Presidential permit. YE'22 in-service still targeted but could see delay of a few months depending on remaining permits.
- **Analyst Day**: AGR expects to hold this event in coordination with Iberdrola in 4Q and will likely include disclosures on par with prior years (LT growth rate through 2024, rate base and capex, capacity factor forecasts for the renewables business, etc.)
- **CEO Succession plan:** The board is considering both internal and external candidates we would expect a successor to be name prior to current CEO Jim Torgerson's departure in June.

CenterPoint Energy (CNP), In Line rating, $18 price target

- **COVID update:** All of the states in CNP's service territory are in the process of reopening, giving confidence in the expected U-shaped recovery by September. Notably, the Toyota plant in Indiana is reopening.
- **2020 and long-term EPS guidance**: assumes earnings at or near allowed returns across the utilities and a continuation of 2% customer growth at Houston Electric. CNP does not expect ROEs in rate cases to be pushed much lower than current levels.
- **CEO search**: as CNP highlighted on the Q1 call, it is currently in the back end of the process.
- **Business Review and Evaluation Committee will pick up soon**. CNP said its Board always considers both corporate and asset-specific M&A, including as it relates to ENBL, though the tax basis still an issue with that. The company will publicly share any updates that it has after the Committee's recommendation to the Board in October and potentially before the Analyst Day in 1Q21.
- **Credit metrics**: as CNP stated on the Q1 call, it expects higher than 14.5% FFO to debt this year, providing some cushion for COVID with respect to company's 14% target long term. CenterPoint anticipates that rating agencies will revisit outlooks after the CES divestitures closes in Q2. Recall that CNP is currently on negative outlook at both Moody's and S&P, which were last updated prior to the $1.4Bn equity investment.

CMS Energy (CMS), In Line Rating, $63 price target

- **Covid sales impacts:** CMS indicated they see the $0.03-$0.04/sh per month hit to EPS quoted on the 1Q call as likely being the trough in terms of impacts. With reopening's starting in Michigan, they are already seeing signs that ultimate monthly impacts will be less.
- **Seeking approval to defer certain Covid costs:** Michigan has already authorized utilities to defer bad debt expense and has opened the door for consideration of other cost deferrals. In April, CMS also sought approval to defer other Covid-19 costs related to sequestering labor for 14 days at power plants and compression stations, keeping certain labor at home in home reserve status, incremental cleaning, and new technology for employees to work from home. All together these costs could total $2.2M to $15.3M per month.
- **Covid mitigation plans:** On the 1Q call, CMS noted that they have reduced expenses by $0.10-$0.15 in a given year in response to weak load or other unexpected negatives. At AGA, they reminded us that this was just to show what they have done in the past and was not meant to be considered a ceiling.
- **Enerbank:** CMS sounded relatively upbeat on Enerbank's positioning noting that while originations slowed in March they did see a nice recovery in April.
- **M&A Strategy**: CMS is focused on its organic growth plan and executing their capex backlog, while like any other prudent management team they consider M&A but view such transactions as having a high hurdle rate.

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Consolidated Edison (ED), In Line rating, $85 price target

- **Long-term EPS growth rate**: Items causing the reduction to 2020 EPS guidance is not expected to be carried forward into 2021 and beyond. Con Ed's 3-5% EPS CAGR through 2024 off of the original (higher) 2020 guidance remains intact.
- **COVID impacts:** Con Ed does not expect to recover lost revenue from suspension of late fees and connect / disconnect fees. Some incentives in the CECONY rate plan are harder to achieve in the COVID environment; these include work that is customer-facing, such as selling energy efficiency, connecting distributed energy resources, etc. While the incentives are not based on cumulative results, a ramp-up in 2021 could be required to recover lost ground.
- **O&M**: expected to be lower in 2020 than original plan due to acceleration of cuts that were originally planned for 2021 and 2022, as per the CECONY rate agreement. The bulk of the cuts are expected to be sustainable.
- **Equity issuance plans:** ED entered a bank loan agreement at the parent on April 6th that gave it the ability to borrow $750mm on a 364-day basis. It is designed to provide liquidity that the equity offering would have provided, so it gives ED flexibility to find a more opportune time to issue equity but still expected this year. Recall that the company has guided to up to $600mm this year and $1.1Bn in 2021/22. Con Ed typically issues equity to target a regulatory cap structure rather than an FFO to debt credit metric.
- **Pipeline update**: Sponsors still see a narrow path for a Mountain Valley Pipeline in-service date by YE'20. It is thought possible that the project will be delayed again given a federal judge's (in Montana) ruling in a case involving Keystone crude pipeline that the US Army Corps of Engineers did not comply with the Endangered Species Act. Last week, the judge refused to limit his decision to Keystone, prompting the US Justice Department to ask the 9th Circuit Court of Appeals to stay the lower court's ruling. Separately, Stagecoach does not fit into ED's long term plans in a decarbonized world, but the company is not in a hurry to reduce its ownership.

DTE Energy (DTE), In Line rating, $120 price target

- **Covid sales impacts**: Due to AMI, DTE is seeing real time impacts of reopening's in MI and is seeing load improve a little bit more than their assumptions discussed on the 1Q call.
- **Michigan regulatory environment**: Continue to be pleased with relationship in MI noting that the recent electric rate order was constructive.
- **Power & Industrials segment**: DTE noted that their industrial energy services business benefits from long-term contracts and is well insulated during Covid 19. The RNG business is also holding up well as pricing for RNG in California remains strong and there is still demand for new RNG projects.
- **Gas Storage and Pipelines segment**. The business (both in Appalachian and Haynesville basins) continues to deliver ahead of plan into 2Q in part driven by higher gas futures due to reduced associated gas supply.

Duke Energy (DUK), In Line rating, $90 price target

- **Covid sales impacts**: Load trajectories appear to be relatively consistent with what DUK had expected at the time of the 1Q call.
- **Rate cases:** No material updates in either the NC cases or in IN. They are awaiting a response in NC to the motion to consolidate hearings in the DEP and DEC cases and expect a rate order in IN around mid-year.
- **ACP:** The court order on Nationwide Permit 12 could be impactful on ACP. The Army Corp has already filed an appeal in the 9th Circuit Court and we could see a decision this month on their request for a stay of the application of the court order on the use of the nationwide permitting process. The appeal itself will likely play out through the rest of this year. They also await a decision on the Appalachian Trail crossing from the Supreme Court and a revised Biological Opinion from the US Fish and Wildlife Service. Michigan regulatory environment:
- **Credit Metrics**: An announced cost reduction puts them in targeted 15% FFO/Debt range for this year. No change to 2020 financing plan.

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Sempra Energy (SRE), Outperform rating, $138 price target

- **Chile:** SRE still expect to close the sale of its Chilean business by the end of the month. The last step before closing is getting workers from State Grid International, a Chinese company, into the country, which has of course been complicated by Covid-19. As we understand it, the workers might also need to be quarantined for 14 days before closing.
- **LNG:** Announced production at Cameron 3 during conference. They continue to expect to make a final investment decision on the ECA project in Mexico this quarter. The project still needs an export permit from Mexico –also complicated by Covid- before a decision can be made.
- **2020 EPS Guidance**: SRE continued to sound optimistic on their positioning in 2020 despite Covid, reiterating plans to deliver in the upper end of their current guidance as discussed on the 1Q call.
- **Covid exposure**: SRE's utilities are well positioned for Covid given decoupling and tracking mechanisms in California and still strong demand in Texas.
- **Credit Ratings**: We believe SRE's comments suggest they will be more likely to accept a credit rating downgrade (they are rated Baa1 by Moody's, so a credit downgrade is still high rated IG) at Moody's, which placed them on an outlook for downgrade earlier this year, than to issue incremental equity

Southern Company (SO), In Line rating, $59 price target

- **Covid sales impacts:** SO indicated that load in April was pretty consistent with what they expected at the time of the 1Q call and with their guidance for Covid to negatively impact revenues in the $250m-$400m range.
- **Mitigation plans:** SO is hopeful they might get some help from weather this summer but also noted that they still feel well positioned to offset Covid-related sales impacts with cuts to O&M. They will also benefit from the ability to defer Covid-related costs, like bad debt expense, in GA and MS now**.**
- **Doing more with less at Vogtle:** SO continues to adjust the Vogtle construction site in the wake of the labor force reduction last month. They have seen Cost performance Index (CPI) improve and are now focused on getting earned hours back to where they were. While they expect monthly completion in May at Unit 3 to hover around 1-1.5%, in line with what they delivered in April, they are hopeful that they will ramp back up to 2% in June even with around 2,000 fewer laborers on site.

WEC Energy (WEC), In Line rating, $93 price target

- **Covid sales impacts:** Recent sales trends have been consistent with the revised forecasts issued on the 1Q call.
- **Customer arrears/bad debt expense:** WEC has been pleasantly surprised by trends so far in terms of customer arrears but they will have a better idea of impacts as time goes on.
- **M&A:** WEC's message was relatively consistent in terms of how they think about M&A. They were willing to comment specifically on EVRG, however, noting that they were not interested in participating in any formal auction and also highlighted concerns with the Sibley coal plant disallowance in particular**.**

Essential Utilities (WTRG), In Line rating, $42 price target

- **PA Commission order on uncollectible expense:** In a letter dated 05/13/20 the PA commission directed state utilities to create a regulatory asset for any incremental uncollectible expenses incurred above those embedded in rates since the issuance of the Emergency Order.
- **M&A:** COVID has impacted the pace of discussions on M&A/tuck in opportunities but WTRG is in discussions with several municipalities and has line of sight to sizable water/wastewater acquisitions.
- **Delcora:** Still expected to close by year end but may get pushed into early next year. $300MM in equity issuance still anticipated late this year or early next.

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- **Peoples Gas repairs catch up:** There could be further potential earnings upside if the commission allows favorable treatment of the legacy tax balance ($0.05 - $0.10 annual EPS uplift not in our forecast). WTRG is expected to file with the PA commission in summer this year, timing on a final decision is unknown.

Xcel Energy (XEL), In Line rating, $65 price target

- **XEL is very comfortable in delivering 2020 EPS guidance**. The company believes there is opportunity to cut O&M more than 4-5% if the COVID impact is worse than their base case assumptions. So far, it has been better.
- **COVID expenses**: Minnesota is the latest state where XEL received a COVID expense deferral order, with a decision last week. Xcel has had some discussions in various states about tracking savings as well, but nothing has been finalized.
- **Long-term capex opportunities**: incremental capex could be driven by electric vehicle infrastructure, Minnesota renewables (could be highlighted in upcoming IRP) and PPA buyouts. These can be thought of as extending the five-year 5-7% growth rate rather than increasing it.
- **Rate case update**: Xcel is pleased with the recent modifications (resulting in an $11mm revenue increase) that came out of the reconsideration of the Colorado electric rate case. The company is generally pleased with the recent testimony in the Colorado gas rate case, especially as it pertains to the strong cap structure recommended by Staff and the Office of Consumer Council.. XEL is also having discussions in rate cases about how it can help the economy (i.e. workforce) by putting private capital back to work. This could also benefit them by allowing for more capex and/or acceleration of capex and also remove political pressure associated with a rate case.

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Historical Ratings Definitions

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Buy- the total forecasted return is expected to be greater than 10%
Hold- the total forecasted return is expected to be greater than or equal to 0% and less than or equal to 10%

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Sell -the total forecasted return is expected to be less than 0%

On October 31, 2014, Evercore acquired International Strategy & Investment Group LLC ("ISI Group") and ISI UK (the "Acquisition") and transferred Evercore Group's research, sales and trading businesses to ISI Group. On December 31, 2015, the combined research, sales and trading businesses were transferred back to Evercore Group in an internal reorganization. Since the Acquisition, the combined research, sales and trading businesses have operated under the global marketing brand name Evercore ISI.

ISI Group and ISI UK:

Prior to October 10, 2014, the ratings system of ISI Group and ISI UK which was based on a 12-month risk adjusted total return:

Strong Buy- Return > 20%
Buy- Return 10% to 20%
Neutral - Return 0% to 10%
Cautious- Return -10% to 0%
Sell- Return< -10%

For disclosure purposes, ISI Group and ISI UK ratings were viewed as follows: Strong Buy and Buy equate to Buy, Neutral equates to Hold, and Cautious and Sell equate to Sell.

Evercore Group:

Prior to October 10, 2014, the rating system of Evercore Group was based on a stock's expected total return relative to the analyst's coverage universe over the following 12 months. Stocks under coverage were divided into three categories:

Overweight- the stock is expected to outperform the average total return of the analyst's coverage universe over the next 12 months.
Equal-Weight- the stock is expected to perform in line with the average total return of the analyst's coverage universe over the next 12 months.
Underweight -the stock is expected to underperform the average total return of the analyst's coverage universe over the next 12 months.
Suspended- the company rating, target price and earnings estimates have been temporarily suspended.

For disclosure purposes, Evercore Group's prior "Overweight," "Equal-Weight" and "Underweight" ratings were viewed as "Buy," "Hold" and "Sell," respectively.

Ratings Definitions for Portfolio-Based Coverage

Evercore ISI utilizes an alternate rating system for companies covered by analysts who use a model portfolio-based approach to determine a company's investment recommendation. Covered companies are included or not included as holdings in the analyst's Model Portfolio, and have the following ratings:

Long- the stock is a positive holding in the model portfolio; the total forecasted return is expected to be greater than 0%.
Short- the stock is a negative holding in the model portfolio; the total forecasted return is expected to be less than 0%.
No Position- the stock is not included in the model portfolio.
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Stocks included in the model portfolio will be weighted from 0 to 100% for Long and 0 to -100% for Short. A stock's weight in the portfolio reflects the analyst's degree of conviction in the stock's rating relative to other stocks in the portfolio. The model portfolio may also include a cash component. At any given time the aggregate weight of the stocks included in the portfolio and the cash component must equal100%.

Stocks assigned ratings under the alternative model portfolio-based coverage system cannot also be rated by Evercore ISI's Current Ratings definitions of Outperform, In Line and Underperform.

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Evercore ISI rating (as of 05/19/2020)

Coverage Universe			**Investment Banking Services I Past 12 Months**		
Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	368	48	Buy	98	27
Hold	305	40	Hold	48	16
Sell	53	7	Sell	4	8
Coverage Suspended	32	4	Coverage Suspended	10	31
Rating Suspended	12	2	Rating Suspended	2	17

Issuer-Specific Disclosures (as of May 19, 2020)

Price Charts

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August 08, 2019

Aqua America

WTR | $42.06

In Line | TARGET PRICE: $37.00

Commentary

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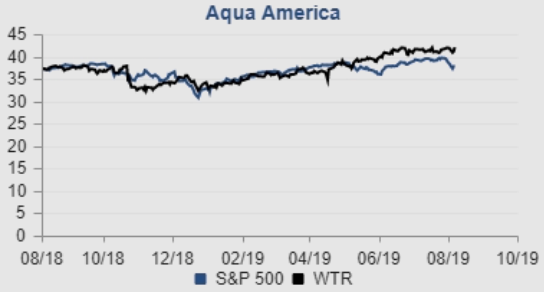
Company Statistics

Market Capitalization (M)	$9,074
Shares Outstanding (M)	216
Dividend	0.91
Dividend Yield	2.2%
Payout Ratio	61.2%
Expected Total Return	(9.9)%
Fiscal Year End	Dec

Earnings Summary

	2019E	2020E	2021E
EPS	**$1.48**	**$1.56**	**$1.64**
P/E	**28.4**	**26.9**	**25.7**
EPS vs Consensus	**6.9%**	**(0.6)%**	**(1.9)%**
Consensus EPS	**$1.38**	**$1.57**	**$1.67**
Consensus P/E	**30.4**	**26.7**	**25.2**

1 Year Price History



Source: FactSet

In Line Quarter; Eyes On The Prize

WTR reported a largely in line 2Q19. FOUR key items worth highlighting are: 1) The Peoples Gas acquisition is still expected to close in fall of this year; 2) Potential acquisition of a PA-based wastewater operator DELCORA (~$300mm rate base and ~$0.03 EPS uplift by our estimate); 3) Repair tax pass-through may be pursued next year; and 4) Long-term guidance is expected to be issued in December. We use a sum-of-the-parts approach to value WTR using a blend of water and gas multiples. At this current juncture, we think the stock trades above our bull-base valuation and we see limited near-term upside; **our rating remains In Line.**

Earnings notes. 2Q19 adjusted EPS of $0.37 was flat to prior year. EPS growth from rate cases and customer growth (acquisitions/ organic) was offset by higher depreciation, lower consumption, and impact of repairs tax. 2019 capex is still expected to be ~$550mm and the company reaffirmed its $1.4bn capex plan through '21, which supports 7% rate base growth in their legacy water business. The Y/Y customer growth rate is still expected to be between 2-3% for '19 (from both organic growth and acquisitions).

Peoples Gas update. Aqua still targets to close the Peoples Gas acquisition in fall of this year. A settlement agreement has been filed with the administrative law judge with a recommended decision expected later this month, and a final PA commission order is expected in the fall. On the rate case front, a settlement agreement seeking $59.5mm in rate increase is awaiting commission approval. New rates are expected to go into effect in October 2019.

Repairs tax election at Peoples could be up to $0.10 EPS accretive ($2/sh or 5% valuation uplift). In 2012, Aqua changed its tax method of accounting for qualifying utility asset repairs in PA. The tax accounting method was changed to permit the expensing of certain utility asset repairs/maintenance costs that were previously being capitalized and depreciated for tax purposes. The company used flow-through accounting for the tax benefits of the repair tax accounting change per the Pennsylvania rate order from June 2012. The flow-through accounting implementation resulted in a reduction in the company's effective income tax rate, which in turn lowered income tax expense and increased net income. WTR's effective tax rate was materially lower than the statuary tax rate at (7.7%) / 6.6% / 8.2% for the years '18 / '17 / '16 respectively. Higher earnings power supported higher returns on equity, which allowed Aqua to invest over $2bn of capital on system improvements over the past seven years without having to go in for rate cases in PA. If regulators approve a similar tax treatment at Peoples, it could be up to $0.10 accretive to EPS and $2/sh accretive to value by our math. We will look for additional color at the Analyst Day in December this year.

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DELCORA opportunity. On the call management announced that the Delaware County Regional Water Authority (DELCORA) had signed a letter of intent with the company committing to exclusive discussions, which could result in a potential combination. DELCORA is a wastewater conveyance and treatment authority that serves approximately 500,000 people in 42 municipalities in Delaware and Chester Counties in southeastern Pennsylvania. We estimate that this could be a potential ~$300mm rate base ($0.03 EPS) uplift, assuming 50%/50% debt/equity financing if they were to move forward.

We are maintaining our $37 price target for WTR; our rating remains In Line. Our $37 target price is based on a sum-of-the-parts valuation where we assign 23.0x '21 P/E to the earnings contribution from the legacy water business and ~21.0x to earnings from the gas segment. The 23.0x water P/E is in line with our water regulated peer average target multiple. The gas multiple of ~21x is also in line with current gas LDC trading valuation multiples. Our bull case valuation of $39 assumes that both the water and gas segment trade at 5% premium to our base case scenario. Our bear case valuation of $33 assumes a 10% discount multiple to our base case scenario for both segments. Please see Exhibit 1 for additional details.

Exhibit 1
WTR Post-Merger Valuation Framework

SOTP Valuation (Base Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.16	23.0x	$27.00
Gas EPS	$0.48	21.5x	$10.00
	$1.65		$37.00

SOTP Valuation (Bull Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.16	24.1x	$28.00
Gas EPS	$0.48	22.6x	$11.00
	$1.65		$39.00

SOTP Valuation (Bear Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.16	20.7x	$24.00
Gas EPS	$0.48	19.4x	$9.00
	$1.65		$33.00

Source: Evercore ISI Research

VALUATION METHODOLOGY

Our $37 target price is based on a SOTP where we assign 23.0x P/E to the earnings contribution from the legacy water business and ~21.0x to earnings from the gas segment. The 23.0x water P/E is in line with our water regulated peer average target multiple. The gas multiple of ~21.0x is also in line with current gas LDC trading valuation multiples.

RISKS

Risks to our thesis include an unfavorable regulatory outcome leading to lower rate base growth and/or lower allowed or earned ROEs in ongoing and future rate cases. Other risks include exposure to unusual weather, impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer, cyber security and water contamination.

COMPANIES UNDER COVERAGE BY AUTHOR

Symbol	Company	Rating	Price (2019-08-08)	Evercore ISI Target
AWK	American Water Works Company, Inc.	Outperform	$118.45	$108.00
AWR	American States Water Company	Underperform	$80.41	$54.00
CTWS	Connecticut Water Service, Inc.	In Line	$69.73	$67.00
CWT	California Water Service Group	In Line	$52.40	$44.00
DCP	DCP Midstream, LP	In Line	$24.66	$34.00
ET	Energy Transfer Partners, L.P.	Outperform	$13.33	$18.00
KMI	Kinder Morgan, Inc.	Outperform	$19.97	$23.00
MPLX	MPLX LP	Outperform	$27.12	$39.00
SJW	SJW Group	In Line	$64.19	$62.00
TRP	TC Energy Corp.	In Line	CAD63.62	CAD60.00
WMB	The Williams Companies Inc.	Outperform	$23.62	$31.00
WTR	Aqua America	In Line	$42.06	$37.00

TIMESTAMP

(Article 3(1)e and Article 7 of MAR)

Time of dissemination: August 08 2019 09:11

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In Line- the total forecasted return is expected to be in line with the expected total return of the analyst's universe
Underperform- the total forecasted return is expected to be less than the expected total return of the analyst's universe
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Strong Buy- Return > 20%
Buy- Return 10% to 20%
Neutral - Return 0% to 10%
Cautious- Return -10% to 0%
Sell- Return< -10%

For disclosure purposes, ISI Group and ISI UK ratings were viewed as follows: Strong Buy and Buy equate to Buy, Neutral equates to Hold, and Cautious and Sell equate to Sell.

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Underweight -the stock is expected to underperform the average total return of the analyst's coverage universe over the next 12 months.
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Evercore ISI rating (as of 08/08/2019)

Coverage Universe			**Investment Banking Services I Past 12 Months**		
Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	396	51	Buy	268	68
Hold	315	41	Hold	170	54
Sell	39	5	Sell	16	41
Coverage Suspended	18	2	Coverage Suspended	14	78
Rating Suspended	10	1	Rating Suspended	4	40

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Price Charts

Ratings Key

B	Buy	OP	Outperform	L	Long	CS	Coverage Suspended
H	Hold	IL	In Line	NP	No Position	RS	Rating Suspended
S	Sell	UP	Underperform	S	Short		

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Water Utilities Q2 2019 Earnings Recap

The sector continues to look expensive to us on both an absolute and relative basis. Water utilities in our coverage universe are currently trading at a 30x P/E multiple on '21E EPS versus our fair value estimate for the space at 23x (58% / 75% premium to the electric utilities / S&P 500, respectively, versus the 10-year average of ~35% / ~50% based on a one-year forward P/E). 2Q19 earnings results were a mixed bag for the water utilities; see our key takeaways by company below.

AWK ($108PT, Outperform). 2Q19 EPS of $0.94 was a penny higher than consensus.

- The quarter benefitted from ~$0.10 EPS uplift from one-time items (land sales etc) offset by wet weather impact of $0.05.
- FY '19 adjusted EPS guidance range of $3.54-$3.64 was reaffirmed. The long-term EPS CAGR is still projected to be in the top half of the 7-10% range anchored off '17 adjusted EPS of $3.03, with dividends expected to grow at the high end.
- Capex guidance for the year was raised $100mm to $1.9bn, primarily driven by regulated acquisitions.
- We continue to struggle with the valuation for water utilities in our coverage universe. Despite a NTM total return proposition of -9% under our base case scenario (group average is around -11%), we think AWK offers the most attractive risk / reward proposition among our coverage universe over the long term, remain **Outperform**.

AWR ($60PT, Underperform). AWR reported 2Q19 adjusted EPS of $0.64 vs consensus of $0.56.

- Quarterly dividend was increased 10.9% and long term they are now targeting more than 7% compounded annual dividend growth (vs more than 6% previously)
- Company's proposed water rate case settlement was approved by the commission; gross margin is expected to increase by $7mm / $10mm / $12mm in '19 / '20 / '21, respectively.
- The commission issued a proposed decision in the ongoing electric rate case approving the settlement reached between the company and various parties. If approved, the rate increase would be retroactive, beginning 1/1/18.
- Reaffirmed ASUS 2019 EPS guidance range of $0.43 to $0.47, consolidated capex this year is still expected to be in the $115mm to $125mm range.
- We are raising our '19 / '20 / '21 EPS forecast to $2.00 / $2.10 / $2.25, driven by better than expected results YTD.
- Raising target price from $57 to $60, remain **Underperform.**

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CTWS ($70PT, In Line). CTWS reported 2Q19 EPS of $0.48 vs prior year EPS of $0.39.

- The company filed an updated settlement agreement related to the SJW / CTWS merger application in CT. The one key addition to the previous application filed on 4/3/19 was that of rate credits totaling $300k/yr for a period of ten years, starting with the next general rate case (~$0.01 annual EPS impact before offsets). The agreement provides the companies with the opportunity to offset these credits with merger-related cost savings.
- SJW and CTWS expect the transaction to close in the third quarter of 2019, be neutral to slightly dilutive in the first full year, and be high-single-digit EPS accretive in the second full year post-closing.
- We are maintaining our $70 target price and **In Line** rating.

CWT ($46PT, In Line). CWT reported 2Q19 EPS of $0.35 vs consensus of $0.38.

- They are in settlement discussions in their ongoing rate case in CA. Recall they had filed their GRC in CA on 7/2/18, requesting $828.5mm in capital spend from '19-'21. The rate increase application requests $50.7mm / $31.5mm / $33.0mm revenue increases for years '20-'22, respectively. The company expects a final decision by YE '19 with rates effective 1/1/20.
- The company is dealing with a new variable: Public Safety Power Shutoffs (PSPS). Electric companies have been authorized to shut off the grid in addressing wildfire risk. They have redirected staff resources towards internal operational / wildfire readiness training, as well as hardening of their system for wildfires. They expect $2-3mm in equipment leases costs in 2H19 (59 generators for wildfire response)
- CWT's cost of capital filing is due in March next year. Currently they are approved for an equity / debt layer of 53% / 46%, and an ROE / cost of debt of 9.2% / 5.5%, respectively.
- We are maintaining our $46 target price and **In Line** rating.

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SJW ($62PT, In Line). SJW reported 2Q19 EPS of $0.47 vs consensus of $0.56. Excluding one-time items, second quarter adjusted EPS came in at $0.58 versus $0.72 in the prior year.

- The company filed updated settlement agreement related to SJW/CTWS merger application in CT. The one key addition to the previous application filed on 04/03/19 was that of rate credits totaling $300k/yr for a period of ten years, starting with the next general rate case (~$0.01 annual EPS impact before offsets). The agreement provides for the companies' opportunity to offset these credits with merger-related cost savings.
- SJW expects the transaction to close in the third quarter of 2019, be neutral to slightly dilutive in the first full year, and be high-single-digit EPS accretive in the second full year post-closing.
- They settled with the California Public Utilities Commission (CPUC) over past customer billing practices. If approved by the Commission, the company would pay ~$2.1mm in one-time customer credits ($0.06 EPS hit booked in Q2) and invest $5.0mm in utility plant without seeking an investment return or rate recovery (<$0.01 EPS hit).
- In Texas (which represents ~5% of total EPS) legislations SB-700 and HB-3542 will take effect 09/01/19: the former will allow water utilities to recover and earn a return on capex in-between rate cases (similar to DSIC/infrastructure surcharges mechanisms in other states); HB-3542 allows a utility in Texas to value acquired assets at fair market value for ratemaking purposes.
- We are maintaining our $62 target price and **In Line** rating.

WTR ($37PT, In Line). 2Q19 adjusted EPS of $0.37 was largely in line with expectations and flat to prior year.

- The Peoples Gas acquisition is still expected to close in fall of this year. A settlement agreement has been filed with the administrative law judge with a recommended decision expected later this month, and a final PA commission order is expected in the fall. On the rate case front, a settlement agreement seeking $59.5mm in gas rate increase is awaiting commission approval. New rates are expected to go into effect in October 2019.
- Potential acquisition of a PA-based wastewater operator DELCORA may be in the cards (~$300mm rate base and ~$0.03 EPS uplift, by our estimate).
- Repair tax pass-through could be pursued next year, and could be up to $0.10 EPS accretive ($2/sh or 5% valuation uplift).
- Long-term guidance is expected to be issued in December '19; we are maintaining our $37 price target for WTR and **In Line** rating.

Exhibit 1
AWK Valuation Framework

Scenario	EPS CAGR*	'21EPS	'20 P/E	Valuation	Tot. Return
Base Case	7.9%	$4.10	26.5x	$108	-9%
Bull Case	9.3%	$4.32	27.8x	$120	1%
Bear Case	7.0%	$3.97	25.1x	$100	-15%

**17 through '21*

Valuation: Our $108 price target is 26.5x our FY '21 EPS estimate of $4.10/share. That is a ~15% premium to our water utility average target multiple of 23x, due to the company's best-in-class earnings and dividend growth, as well as geographical / regulatory diversity. The latter not only minimizes regulatory risks, but also offers a competitive advantage to capitalize on industry consolidation opportunities, given AWK's presence in 16 states. Our bull case valuation of $120 for AWK assumes growth in the upper half of their targeted 7-10% EPS growth guidance range and a 5% premium to a '21 P/E multiple of 26.5x. Our bear case valuation of $100 assumes AWK can grow earnings at the low end of the targeted 7-10% growth range and we apply a 10% discount to a '21 P/E multiple of 26.5x.

Source: Evercore ISI Research

Exhibit 2
AWR Valuation Framework

Scenario	EPS CAGR*	'21EPS	'20 P/E	Valuation	Tot. Return
Base Case	9.2%	$2.25	26.5x	$60	-27%
Bull Case	10.0%	$2.30	27.8x	$64	-23%
Bear Case	8.2%	$2.19	25.1x	$55	-33%

**18 through '21*

Valuation: Our $60 price target is 26.5x our FY '21 EPS estimate of $2.25/share. That is a ~15% M&A premium to our water regulated target multiple of 23x. Our bull case valuation of $64 for AWR assumes they can grow EPS at 10% through '21 and trade at a 5% premium to our base case '21 P/E multiple of 26.5x. Our bear case valuation of $55 assumes that they grow earnings at 6.5%, 100 bps lower than our base case and trade at 5% discount to our '21 base case P/E multiple of 26.5x.

Source: Evercore ISI Research

Exhibit 3
CTWS Valuation Framework

Scenario	EPS CAGR*	'21EPS	'21 P/E	Valuation	Tot. Return
Base Case	7.1%	$2.75	25.3x	$70	2%
Bull Case	8.1%	$2.83	26.6x	$75	9%
Bear Case	6.1%	$2.67	24.0x	$64	-6%

**18 through '21*

Valuation: Our $70 price target is 25.3x our FY '21 EPS estimate of $2.75/share. That is a ~10% M&A premium to our water regulated target multiple of 23x. Our bull case valuation of $75 for CTWS assumes they can grow EPS at 8.1% 100 bps higher than our base case forecast and trade at a 5% premium to our base case '21 P/E multiple of 25.3x. Our bear case valuation of $64 assumes that they grow earnings at 6.1%, 100 bps lower than our base case and trade at 5% discount to our '21 base case P/E multiple of 25.3x.

Source: Evercore ISI Research

Exhibit 4
CWT Valuation Framework

Scenario	EPS CAGR*	'21EPS	'21 P/E	Valuation	Tot. Return
Base Case	8.7%	$1.75	26.5x	$46	-14%
Bull Case	9.7%	$1.80	27.8x	$50	-6%
Bear Case	7.7%	$1.70	25.1x	$43	-19%

**18 through '21*

Valuation: Our $46 price target is 26.5x our FY '21 EPS estimate of $1.75/share. That is a ~15% M&A premium to our water regulated target multiple of 23x. Our bull case valuation of $50 for CWT assumes they can grow EPS at 9.7% 100 bps higher than our base case forecast and trade at a 5% premium to our base case '21 P/E multiple of 26.5x. Our bear case valuation of $43 assumes that they grow earnings at 7.7%, 100 bps lower than our base case and trade at 5% discount to our '21 base case P/E multiple of 26.5x.

Source: Evercore ISI Research

Exhibit 5
SJW Valuation Framework

Valuation	Post Merger	No Merger	Base Case (a)	Valuation	Bull Case	Bear Case
Consolidated 2021 EPS	**$2.55**	**$2.30**		**Consolidated 2021 EPS**	**$2.55**	**$2.30**
Forward P/E Multiple	25.5x	25.5x		Forward P/E Multiple	26.5x	24.5x
Implied Valuation	**$65.0**	**$59.0**	**$62.0**	**Implied Valuation**	**$68.0**	**$56.0**
Current Stock Price (07/25/19)	$64.3	$64.3	$64.3	Current Stock Price (07/25/19)	$64.3	$64.3
Price Appreciation	**1.1%**	**-8.2%**	**-3.6%**	**Price Appreciation**	**5.8%**	**-12.9%**
Dividend Yield	**1.9%**	**1.9%**	**1.9%**	**Dividend Yield**	**1.9%**	**1.9%**
Total Shareholder Return	**3.0%**	**-6.4%**	**-1.7%**	**Total Shareholder Return**	**7.6%**	**-11.0%**

Valuation: Our base case valuation of $62 is an average of our post-merger and no-merger valuations. Firstly, our $65 post-merger valuation is based on a pro-forma FY '21 EPS estimate of $2.55 and a 25.5x P/E multiple, which represents a ~10% M&A premium to our regulated water target multiple of 23.0x. Secondly, our no-merger valuation of $59 is based on a standalone FY '21 EPS estimate of $2.30 and a 25.5x P/E multiple. In our bull case of $68, we assume that the merger goes through and assign a 1.0x higher P/E multiple vs. the base case. In our bear case valuation of SJW, we assume the merger is not consummated and assign a 1.0x lower P/E multiple vs. the base case.

Source: Evercore ISI Research

Exhibit 6
WTR Valuation Framework

SOTP Valuation (Base Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.16	23.0x	$27.00
Gas EPS	$0.48	21.2x	$10.00
	$1.65		$37.00

SOTP Valuation (Bull Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.16	24.1x	$28.00
Gas EPS	$0.48	22.3x	$11.00
	$1.65		$39.00

SOTP Valuation (Bear Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.16	20.7x	$24.00
Gas EPS	$0.48	19.1x	$9.00
	$1.65		$33.00

Valuation: Our $37 target price is based on a SOTP valuation where we assign 23x P/E to earnings contribution from the legacy water business and ~21x to earnings from the gas segment. The 23x water P/E is in line with our water regulated peer average target multiple .The gas multiple of ~21x is also in line with current gas LDC trading valuation multiples. Our bull case valuation of $39 assumes that both the water and gas segment trade at 5% premium to our base case scenario. Our bear case valuation of $33 assumes 10% discount multiple to our base case scenario for both segments.

Source: Evercore ISI Research

Risks. Risks to our thesis include an unfavorable regulatory outcome leading to lower rate base growth and/or lower allowed or earned ROEs in ongoing and future rate cases. Other risks include exposure to unusual weather, impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer, cyber security and water contamination.

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Buy- Return 10% to 20%
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Cautious- Return -10% to 0%
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Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	384	51	Buy	253	66
Hold	295	40	Hold	154	52
Sell	40	5	Sell	15	38
Coverage Suspended	21	3	Coverage Suspended	16	76
Rating Suspended	7	1	Rating Suspended	2	29

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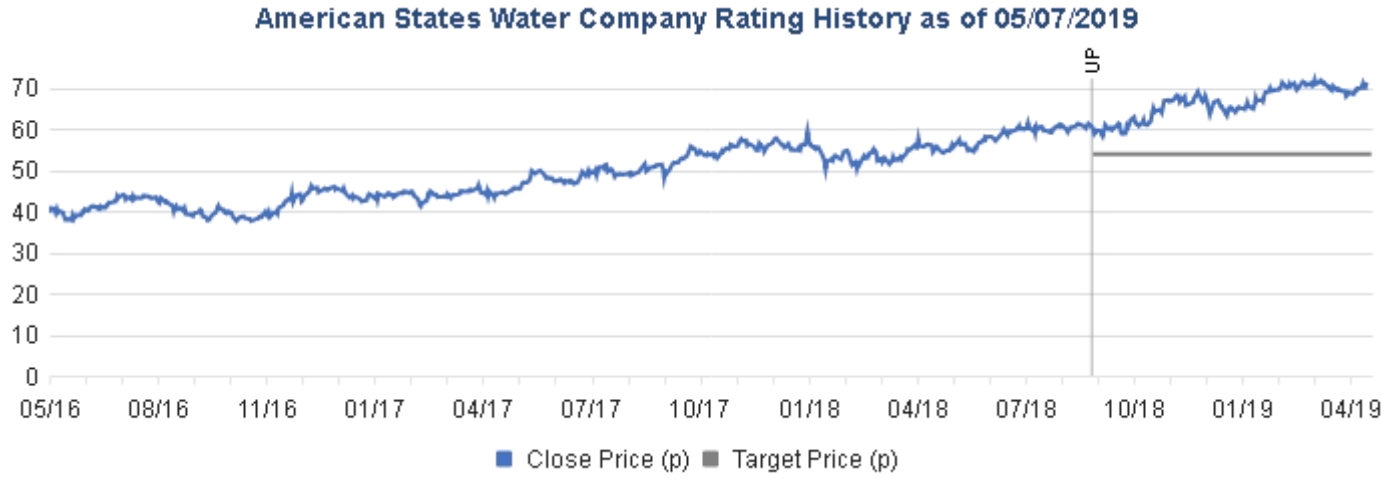

Ratings Key

B	Buy	OP	Outperform	L	Long	CS	Coverage Suspended
H	Hold	IL	In Line	NP	No Position	RS	Rating Suspended
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EVERCORE ISI

Energy | Power & Utilities

January 11, 2021

Essential Utilities Inc.

WTRG | $48.31

In Line | TARGET PRICE: $49.00 (from $42.00)

Company Update

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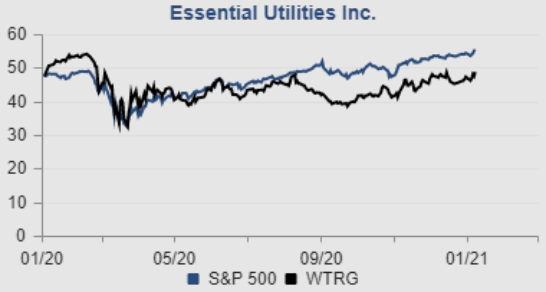
Company Statistics

Market Capitalization (M)	$11,817
Shares Outstanding (M)	245
Dividend	1.03
Dividend Yield	2.1%
Payout Ratio	61.7%
Expected Total Return	3.8%
Fiscal Year End	Dec

Earnings Summary

	2021E	2022E
EPS	**$1.67**	**$1.79**
P/E	**28.9**	**27.0**
EPS vs Consensus	**(0.2)%**	**0.1%**
Consensus EPS	**$1.67**	**$1.79**
Consensus P/E	**28.9**	**27.0**

1 Year Price History



Source: FactSet

Announces '21 EPS Guidance Range, Extends Long-Term Growth Rate Target Through '23

Essential Utilities initiates' 2021 EPS guidance range of $1.64-$1.69, extends 5-7% EPS growth target through 2023. Essential hosted a guidance call earlier today to discuss company's 2021 expected EPS projection and three year outlook. The company initiated 2021 EPS guidance range of $1.64-$1.69 which at the mid-pt of $1.66 is in line with consensus/our estimate of $1.67 and points to year over year growth rate of 7% towards the high end of management targeted 5-7% long term growth rate. WTRG also extended its capex and rate base growth forecast by one year through 2023 and still anticipates water rate base growing by 6-7% (excluding acquisitions) and gas rate base 8-10% on average through that period. Fueling this growth is $3B in expected combined investments from 2020 through 2023. They expect to issue some equity to fund base capex (we model $100MM through 2023), municipal system acquisitions and dividends which are expected to grow in line with earnings. The company also extended its 5-7% EPS growth target through 2023 and introduced 60% emission reduction target by 2035. WTRG anticipates closing the DELCORA acquisition in the second quarter this year and plans on filing a general rate case application in PA later in the year for rate effective in late '21/early '22.

We are introducing '23E of $1.90, raising target price to $49. We are also modestly adjusting our '21/'22 eps estimates to $1.67/$1.79 respectively. Our 23E of $1.90 drives a CAGR of 7% (using 2020 guidance mid-pt of $1.56) which is at the high end of company's targeted 5-7% earnings growth rate. We further note that our EPS forecast could be conservative if WTRG announces more private and municipal water/waste water system acquisitions above their current forecast. Our $49 target price is based on a SOTP where we assign 29.5x P/E to the '23 earnings contribution from the legacy water business and ~ 17.5x to earnings from the gas segment. The 29.5x water P/E is a ~30% premium to our water utility average target multiple of 23x which we think is warranted in this environment given above average residential customer mix which positions them well against COVID related demand headwinds. Majority of their water EPS is derived from PA which is also a relative advantage versus peers. The gas multiple of ~17.5x is also in line with our target Electric/gas utility multiple. We see bull/bear case valuation of $56/$43 respectively, and given the potential upside from municipal water/waste water deals and other complementary growth projects we assign low probability to our bear case scenario, see page 2 of the report.

Q3 2020 Earnings Recap. WTRG reported Q3 '20 Adjusted EPS of $1.01 versus consensus of $1.02. Management Reaffirmed 2020 EPS guidance range of $1.53-$1.58, but expected to be at the top end. WTRG still projects EPS to grow in the range of 5-7% on average from 2019 through 2022. In Q3, company announced offering of 6.7MM shares via an equity forward agreement (~$300MM in proceeds). Proceeds which are expected to be used to fund general corporate purposes, including the acquisition of the Delaware County Regional Water. Quality Control Authority (DELCORA) and other water and wastewater acquisitions in its pipeline.

See inside for detail on the DELCORA opportunity, Repairs Tax Election Uplift, and our price target.

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DELCORA opportunity. In September '19, management had announced a signed purchase agreement with Delaware County Regional Water Authority (DELCORA), following the latter's signing of a letter of intent with Aqua committing to exclusive discussions in August '19. DELCORA is a wastewater conveyance and treatment authority that serves approximately 500,000 people in 42 municipalities in Delaware and Chester Counties in southeastern Pennsylvania. We estimate that this could be a potential ~$300mm rate base / $0.03 EPS annual uplift (included in our forecast), assuming 50%/50% debt/equity financing. WTRG expects to close the transaction in second quarter this year.

Repairs Tax Election Uplift, 8-12c/yr. Essential's 2020 and forward looking EPS guidance includes 8-12c/share annual earnings uplift which is more/less in line with our estimate of ~10c. There may be additional accretion from historical balances pending commission review and final decision. For context, in 2012, Aqua (water utility) changed its tax method of accounting for qualifying utility asset repairs in PA. The tax accounting method was changed to permit the expensing of certain utility asset repairs/maintenance costs that were previously being capitalized and depreciated for tax purposes. The company used flow-through accounting for the tax benefits of the repair tax accounting change per the Pennsylvania rate order from June '12. The flow-through accounting implementation resulted in a reduction in the company's effective income tax rate, which in turn lowered income tax expense and increased net income. WTR's effective tax rate was materially lower than the statuary tax rate at (7.7%) / 6.6% / 8.2% for the years '18 / '17 / '16 respectively. Higher earnings power supported higher returns on equity, which allowed Aqua to invest over $2bn of capital on system improvements over the past seven years without having to go in for rate cases in PA. There could be further earnings upside (~$0.05 annual EPS uplift by our estimate) if the commission allows favorable treatment of the legacy tax balance. WTRG is asking the commission to apply the earnings upside to years 2023 and beyond such that the company can delay its 2023 rate filing by a year.

We are raising our target price to $49; our rating remains In Line. Our $49 target price is based on a SOTP where we now assign 29.5x P/E to the '23 earnings contribution from the legacy water business and ~ 17.5x to earnings from the gas segment. The 29.5x water P/E is a ~30% premium to our water utility average target multiple of 23x which we think is warranted in this environment given above average residential customer mix which positions them well against COVID related demand headwinds. Majority of their water EPS is derived from PA which is also a relative advantage versus peers. The gas multiple of ~17.5x is also in line with our target electric/gas multiple. Our bull case valuation of $56 assumes that they are able to achieve ~$0.06 combined upside from tax repairs, and both the water and gas segment trade at 10% premium to our base case scenario. Our bear case valuation of $43 assumes a 5% discount multiple to our base case scenario for the water segment, current trading multiple of comparable gas LDC's and low end of targeted LT EPS growth. Please see Exhibit 1 for additional details.

Exhibit 1

WTR Valuation Framework

SOTP Valuation (Base Case)	'23E	'23 P/E	Valuation
Legacy WTR EPS	$1.33	29.5x	$39.00
Gas EPS	$0.57	17.5x	$10.00
	$1.90		$49.00

SOTP Valuation (Bull Case)	'23E	'23 P/E	Valuation
Legacy WTR EPS	$1.37	32.5x	$45.00
Gas EPS	$0.59	19.3x	$11.00
	$1.96		$56.00

SOTP Valuation (Bear Case)	'23E	'23 P/E	Valuation
Legacy WTR EPS	$1.26	28.1x	$35.00
Gas EPS	$0.54	14.7x	$8.00
	$1.80		$43.00

Source: Evercore ISI Research

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VALUATION METHODOLOGY

Our $49 target price is based on a SOTP where we now assign 29.5x P/E to the '23 earnings contribution from the legacy water business and ~ 17.5x to earnings from the gas segment. The 29.5x water P/E is a ~30% premium to our water utility average target multiple of 23x which we think is warranted in this environment given above average residential customer mix which positions them well against COVID related demand headwinds. Majority of their water EPS is derived from PA which is also a relative advantage versus peers. The gas multiple of ~17.5x is also in line with our target electric/gas multiple

RISKS

Risks to our thesis include an unfavorable regulatory outcome leading to lower rate base growth and/or lower allowed or earned ROEs in ongoing and future rate cases. Other risks include exposure to unusual weather, impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer, cyber security and water contamination.

COMPANIES UNDER COVERAGE BY AUTHOR

Symbol	Company	Rating	Price (2021-11-01)	Evercore ISI Target
AEE	Ameren Corp.	Outperform	$75.06	$84.00
AEP	American Electric Power	Outperform	$78.78	$95.00
AES	The AES Corporation	Outperform	$25.50	$23.00
AWK	American Water Works Company, Inc.	Outperform	$156.84	$129.00
AWR	American States Water Company	Underperform	$80.61	$60.00
CMS	CMS Energy Corp.	In Line	$57.16	$63.00
CNP	CenterPoint Energy, Inc.	In Line	$20.78	$23.00
CWEN	Clearway Energy	In Line	$34.89	$22.00
CWT	California Water Service Group	In Line	$55.29	$40.00
D	Dominion Energy, Inc	In Line	$72.63	$77.00
DTE	DTE Energy Co.	In Line	$117.73	$121.00
DUK	Duke Energy Corp.	In Line	$89.28	$89.00
ED	Consolidated Edison Inc.	In Line	$68.59	$80.00
EIX	Edison International	In Line	$61.50	$72.00
ES	Eversource Energy	In Line	$89.23	$91.00
ETR	Entergy Corp.	In Line	$94.44	$106.00
EVRG	Evergy	Outperform	$52.55	$62.00
EXC	Exelon Corp.	Outperform	$41.95	$45.00
FE	FirstEnergy Corp.	In Line	$30.36	$41.00
HE	Hawaiian Electric Industries Inc.	Underperform	$34.06	$34.00
NEE	NextEra Energy Inc	In Line	$79.71	$75.00
NI	NiSource Inc	Outperform	$21.82	$26.00
NRG	NRG Energy Inc.	Outperform	$39.69	$40.00
OGE	OGE Energy Corp	Outperform	$31.61	$35.00
PCG	PG&E Corp.	Rating Suspended	$12.17	
PEG	Public Service Enterprise Group	In Line	$56.90	$53.00
PNW	Pinnacle West Capital Corp.	In Line	$76.77	$85.00
PPL	PPL Corp.	In Line	$27.77	$31.00
SJW	SJW Group	In Line	$69.28	$60.00
SO	Southern Co.	In Line	$61.24	$59.00
SRE	Sempra Energy	Outperform	$118.25	$138.00
VST	Vistra Energy Corp	Outperform	$21.27	$27.00
WEC	WEC Energy Group, Inc.	In Line	$86.88	$93.00
WTRG	Essential Utilities Inc.	In Line	$48.31	$49.00
XEL	Xcel Energy Inc.	In Line	$64.37	$65.00

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(Article 3(1)e and Article 7 of MAR)

Time of dissemination: January 11 2021 06:49 PM ET

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In Line- the total forecasted return is expected to be in line with the expected total return of the analyst's universe
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Sell -the total forecasted return is expected to be less than 0%

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Buy- Return 10% to 20%
Neutral - Return 0% to 10%
Cautious- Return -10% to 0%
Sell- Return< -10%

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Short- the stock is a negative holding in the model portfolio; the total forecasted return is expected to be less than 0%.
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Stocks included in the model portfolio will be weighted from 0 to 100% for Long and 0 to -100% for Short. A stock's weight in the portfolio reflects the analyst's degree of conviction in the stock's rating relative to other stocks in the portfolio. The model portfolio may also include a cash component. At any given time the aggregate weight of the stocks included in the portfolio and the cash component must equal100%.

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Evercore ISI rating (as of 01/11/2021)

Coverage Universe			**Investment Banking Services I Past 12 Months**		
Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	438	55	Buy	98	22
Hold	301	38	Hold	29	10
Sell	28	4	Sell	3	11
Coverage Suspended	13	2	Coverage Suspended	5	38
Rating Suspended	12	2	Rating Suspended	3	25

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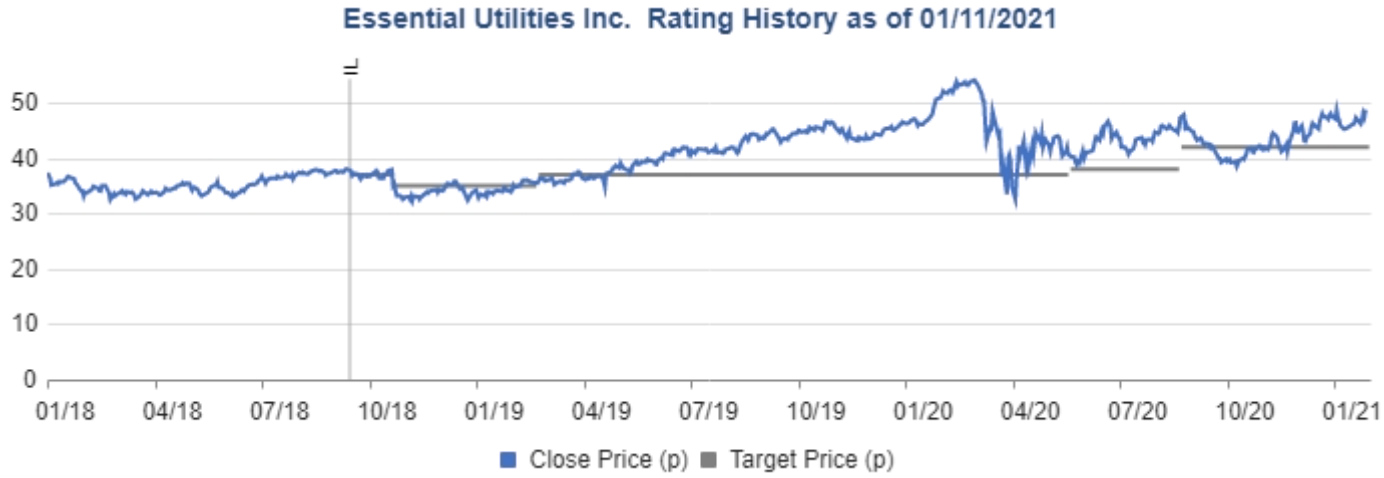

Ratings Key

B	Buy	OP	Outperform	L	Long	CS	Coverage Suspended
H	Hold	IL	In Line	NP	No Position	RS	Rating Suspended
S	Sell	UP	Underperform	S	Short		

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EVERCORE ISI

Energy | Power & Utilities

February 27, 2020

Essential Utilities Inc.

WTRG | $46.96

In Line | TARGET PRICE: $37.00

Company Update

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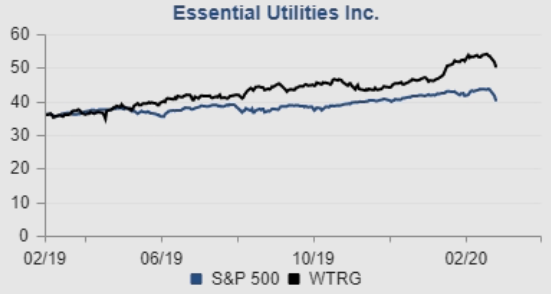
Company Statistics

Market Capitalization (M)	$9,559
Shares Outstanding (M)	216
Dividend	0.91
Dividend Yield	2.0%
Payout Ratio	61.2%
Expected Total Return	(14.4)%
Fiscal Year End	Dec

Earnings Summary

	2019E	2020E	2021E
EPS	**$1.48**	**$1.56**	**$1.64**
P/E	**29.9**	**28.3**	**27.0**
EPS vs Consensus	**1.9%**	**(1.8)%**	**(2.4)%**
Consensus EPS	**$1.45**	**$1.59**	**$1.68**
Consensus P/E	**30.5**	**27.8**	**26.4**

1 Year Price History



Source: FactSet

LT Growth Outlook Below Expectations

WTRG lagged peers today (-8% vs water uts/UTY -6%/-5%) amid a broad market sell off on a weaker than expected LT EPS growth outlook. The company initiated 2020 EPS guidance range of $1.53 - $1.58 and projects earnings to grow in the range of 5-7% on average from 2019 through 2022. Starting with 2019 adjusted EPS of $1.47, 6% EPS growth rate mid-pt would translate into 2021 EPS of $1.65 (includes ~10c repair tax uplift) materially below our bull case scenario of $1.78 which assumes repair election + Delcora accretion, see our last note here. Peoples Gas acquisition is expected to close in March 2020, combined water and gas, Essential expects to invest $2.8B from 2019 through 2022. The abovementioned capex investment (including ~$25MM towards reducing PFOS/PFOA levels) is projected to generate rate base growth of 6-7% in the water business and 8-10% in gas through the forecast period. We will be back with a model update and our '22 EPS projection, see additional details within.

2020 Guidance & LT EPS Growth. As we stated earlier, Essential initiated 2020 EPS guidance range of $1.53-$1.58 and projects EPS to grow in the range of 5-7% on average from 2019 through 2022. Both the guidance and LT earnings growth rate include 8-12c/year EPS uplift from repair tax flow through at Peoples gas. $2.8B in planned investments through 2022 is driving projected 6-7%/8-10% rate base growth at water/gas during that period. Included in the capex plan is $25MM in investment towards reducing PFOS/PFOA (potentially harmful chemicals in the water stream) levels to 13 parts per trillion across their service territory significantly below federal governments health advisory level of 70 parts per trillion. The company pointed to lower future earned ROE's (2019 returns were higher due to repairs flow through in the water business), regulatory lag on municipal acquisitions, and dilution from additional equity units as primary drivers of the lower expected EPS CAGR versus rate base growth.

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Repairs Tax Election Uplift, 8-12c/yr. Essential's 2020 and forward looking EPS guidance includes 8-12c/share annual earnings uplift which is more/less in line with our estimate of ~10c. There may be additional accretion from historical balances pending commission review and final decision. For context, in 2012, Aqua (water utility) changed its tax method of accounting for qualifying utility asset repairs in PA. The tax accounting method was changed to permit the expensing of certain utility asset repairs/maintenance costs that were previously being capitalized and depreciated for tax purposes. The company used flow-through accounting for the tax benefits of the repair tax accounting change per the Pennsylvania rate order from June '12. The flow-through accounting implementation resulted in a reduction in the company's effective income tax rate, which in turn lowered income tax expense and increased net income. WTR's effective tax rate was materially lower than the statuary tax rate at (7.7%) / 6.6% / 8.2% for the years '18 / '17 / '16 respectively. Higher earnings power supported higher returns on equity, which allowed Aqua to invest over $2bn of capital on system improvements over the past seven years without having to go in for rate cases in PA.

DELCORA Acquisition. In September '19, management had announced a signed purchase agreement with Delaware County Regional Water Authority (DELCORA), following DELCORA signing of a letter of intent with Aqua committing to exclusive discussions in August '19. DELCORA is a wastewater conveyance and treatment authority that serves approximately 500,000 people in 42 municipalities in Delaware and Chester Counties in southeastern Pennsylvania. We estimate that this could be a potential ~$300mm rate base / $0.03 EPS uplift in '21 (company expects to close in late '20/early '21), assuming 50%/50% debt/equity financing.

Peoples Gas Update. In March 2019, Essential received regulatory approval for the Peoples transaction from the Kentucky Public Service Commission, followed by approval in Kentucky next month. On 10/28/19 the PA Administrative Law Judge assigned to the case issued a proposed decision approving the Peoples Gas acquisition which was subsequently approved by the Commission in January this year. The company expects to complete the acquisition in March 2020.

2019 EPS. Essential reported FY 2019 adjusted EPS of $1.47 which was more/less in line with our forecast of $1.48. Compare to prior year EPS was $ 0.06 or 4.3% higher driven by rate/surcharges supporting capex +$0.16, customer growth +$0.03, higher expenses -$0.06, and lower usage/other -$0.07.

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VALUATION METHODOLOGY

Our $37 target price is based on a SOTP where we assign 23.0x P/E to the earnings contribution from the legacy water business and ~21.0x to earnings from the gas segment. The 23.0x water P/E is in line with our water regulated peer average target multiple. The gas multiple of ~21.0x is also in line with current gas LDC trading valuation multiples.

RISKS

Risks to our thesis include an unfavorable regulatory outcome leading to lower rate base growth and/or lower allowed or earned ROEs in ongoing and future rate cases. Other risks include exposure to unusual weather, impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer, cyber security and water contamination.

COMPANIES UNDER COVERAGE BY AUTHOR

Symbol	Company	Rating	Price (2020-27-02)	Evercore ISI Target
AWK	American Water Works Company, Inc.	Outperform	$128.81	$118.00
AWR	American States Water Company	Underperform	$82.80	$60.00
CWT	California Water Service Group	In Line	$50.69	$46.00
DCP	DCP Midstream, LP	In Line	$15.52	$29.00
ENB	Enbridge Inc.	In Line	$37.89	$48.00
EPD	Enterprise Products Partners LP	Outperform	$23.00	$32.00
ET	Energy Transfer Partners, L.P.	Outperform	$10.78	$18.00
KMI	Kinder Morgan, Inc.	Outperform	$19.62	$22.00
MMP	Magellan Midstream Partners, L.P.	Outperform	$55.47	$67.00
MPLX	MPLX LP	In Line	$19.15	$34.00
OKE	ONEOK Inc.	In Line	$67.78	$65.00
PAA	Plains All American Pipeline, L.P.	In Line	$13.69	$20.00
PAGP	Plains GP Holdings, L.P.	In Line	$13.83	$25.00
SJW	SJW Group	In Line	$65.23	$65.00
TRGP	Targa Resources Corp	In Line	$32.54	$39.00
TRP	TC Energy Corp.	In Line	CAD71.83	CAD60.00
WMB	The Williams Companies Inc.	Outperform	$19.04	$28.00
WTRG	Essential Utilities Inc.	In Line	$46.96	$37.00

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TIMESTAMP

(Article 3(1)e and Article 7 of MAR)

Time of dissemination: February 27 2020 09:58

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Outperform- the total forecasted return is expected to be greater than the expected total return of the analyst's coverage universe
In Line- the total forecasted return is expected to be in line with the expected total return of the analyst's universe
Underperform- the total forecasted return is expected to be less than the expected total return of the analyst's universe
Coverage Suspended- the rating and target price have been removed pursuant to Evercore ISI policy when Evercore is acting in an advisory capacity in a merger or strategic transaction involving this company and in certain other circumstances.*
Rating Suspended- Evercore ISI has suspended the rating and target price for this stock because there is not sufficient fundamental basis for determining, or there are legal, regulatory or policy constraints around publishing, a rating or target price. The previous rating and target price, if any, are no longer in effect for this company and should not be relied upon.*

*Prior to October 10, 2015, the "Coverage Suspended" and "Rating Suspended" categories were included in the category "Suspended."

FINRA requires that members who use a ratings system with terms other than "Buy," "Hold/Neutral" and "Sell" to equate their own ratings to these categories. For this purpose, and in the Evercore ISI ratings distribution below, our Outperform, In Line, and Underperform ratings can be equated to Buy, Hold and Sell, respectively.

Historical Ratings Definitions

Prior to March 2, 2017, Evercore ISI's recommendations were based on a stock's total forecasted return over the next 12 months:

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Buy- the total forecasted return is expected to be greater than 10%
Hold- the total forecasted return is expected to be greater than or equal to 0% and less than or equal to 10%
Sell -the total forecasted return is expected to be less than 0%

On October 31, 2014, Evercore Partners acquired International Strategy & Investment Group LLC ("ISI Group") and ISI UK (the "Acquisition") and transferred Evercore Group's research, sales and trading businesses to ISI Group. On December 31, 2015, the combined research, sales and trading businesses were transferred back to Evercore Group in an internal reorganization. Since the Acquisition, the combined research, sales and trading businesses have operated under the global marketing brand name Evercore ISI.

ISI Group and ISI UK:

Prior to October 10, 2014, the ratings system of ISI Group LLC and ISI UK which was based on a 12-month risk adjusted total return:

Strong Buy- Return > 20%
Buy- Return 10% to 20%
Neutral - Return 0% to 10%
Cautious- Return -10% to 0%
Sell- Return< -10%

For disclosure purposes, ISI Group and ISI UK ratings were viewed as follows: Strong Buy and Buy equate to Buy, Neutral equates to Hold, and Cautious and Sell equate to Sell.

Evercore Group:

Prior to October 10, 2014, the rating system of Evercore Group was based on a stock's expected total return relative to the analyst's coverage universe over the following 12 months. Stocks under coverage were divided into three categories:

Overweight- the stock is expected to outperform the average total return of the analyst's coverage universe over the next 12 months.
Equal-Weight- the stock is expected to perform in line with the average total return of the analyst's coverage universe over the next 12 months.
Underweight -the stock is expected to underperform the average total return of the analyst's coverage universe over the next 12 months.
Suspended- the company rating, target price and earnings estimates have been temporarily suspended.

For disclosure purposes, Evercore Group's prior "Overweight," "Equal-Weight" and "Underweight" ratings were viewed as "Buy," "Hold" and "Sell," respectively.

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Long- the stock is a positive holding in the model portfolio; the total forecasted return is expected to be greater than 0%.
Short- the stock is a negative holding in the model portfolio; the total forecasted return is expected to be less than 0%.
No Position- the stock is not included in the model portfolio.
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Stocks included in the model portfolio will be weighted from 0 to 100% for Long and 0 to -100% for Short. A stock's weight in the portfolio reflects the analyst's degree of conviction in the stock's rating relative to other stocks in the portfolio. The model portfolio may also include a cash component. At any given time the aggregate weight of the stocks included in the portfolio and the cash component must equal100%.

Stocks assigned ratings under the alternative model portfolio-based coverage system cannot also be rated by Evercore ISI's Current Ratings definitions of Outperform, In Line and Underperform.

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Evercore ISI rating (as of 02/27/2020)

Coverage Universe			**Investment Banking Services I Past 12 Months**		
Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	411	54	Buy	99	24
Hold	276	36	Hold	37	13
Sell	43	6	Sell	6	14
Coverage Suspended	23	3	Coverage Suspended	8	35
Rating Suspended	14	2	Rating Suspended	2	14

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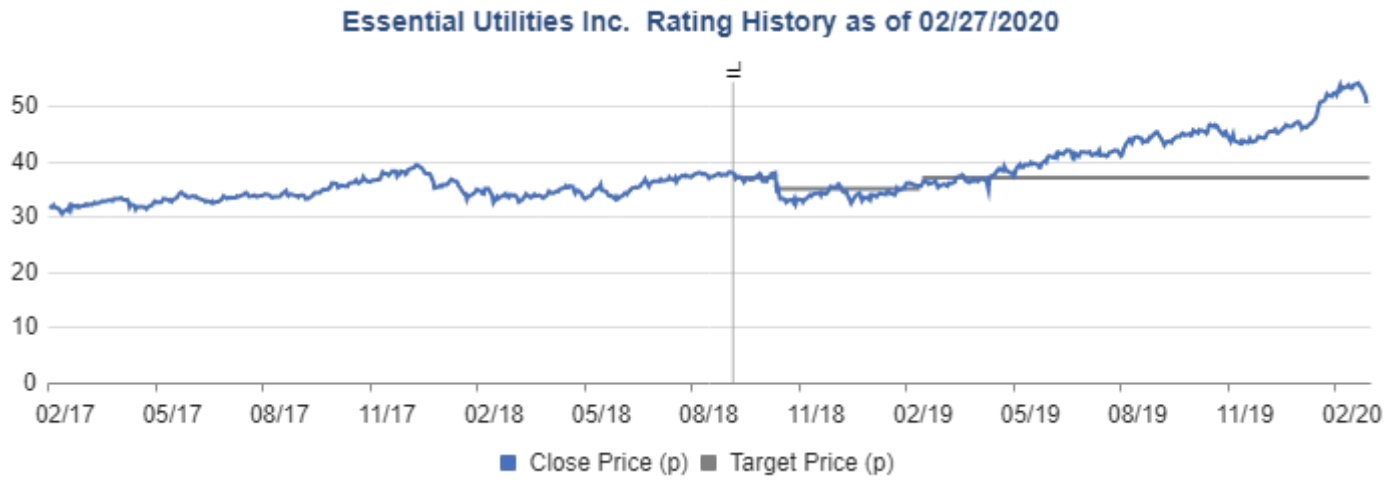
Price Charts



Ratings Key

B	Buy	OP	Outperform	L	Long	CS	Coverage Suspended
H	Hold	IL	In Line	NP	No Position	RS	Rating Suspended
S	Sell	UP	Underperform	S	Short		

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EVERCORE ISI

Energy | Power & Utilities

May 07, 2020

Essential Utilities Inc.

WTRG | $40.59

In Line | TARGET PRICE: $38.00 (from $37.00)

Earnings Report

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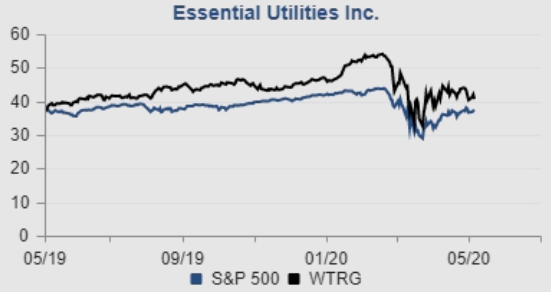
Company Statistics

Market Capitalization (M)	$8,597
Shares Outstanding (M)	223
Dividend	0.95
Dividend Yield	2.5%
Payout Ratio	61.2%
Expected Total Return	1.2%
Fiscal Year End	Dec

Earnings Summary

	2020E	2021E	2022E
EPS	**$1.55**	**$1.65**	**$1.80**
P/E	**24.8**	**23.3**	**21.3**
EPS vs Consensus	**(0.8)%**	**0.2%**	**1.9%**
Consensus EPS	**$1.57**	**$1.65**	**$1.77**
Consensus P/E	**24.6**	**23.3**	**21.8**

1 Year Price History



Source: FactSet

Good quarter, 2020 & LT EPS Targets Reaffirmed

WTRG reported Q1 '20 Adjusted EPS of $0.60 versus consensus of $0.58. The company booked $0.02 EPS uplift from repairs pass-through in the quarter in line with original guidance of $0.08 - $0.12 EPS benefit for the year. There could be further potential earnings upside if the commission allows favorable treatment of the legacy tax balance (not in our forecast). Essential also reaffirmed its 2020 EPS guidance range of $1.53-$1.58 and still projects EPS to grow in the range of 5-7% on average from 2019 through 2022. The company filed for Delcora waste water acquisition approval with the commission in the first quarter and still expects to issue $300MM in equity later this year to finance the deal ($0.03 EPS contribution included in our forecast). They are closely monitoring COVID-related implications on consumption, collections and capital expenditures and based on current available information don't expect a material financial impact to 2020 EPS.

Target Price $38, rating still In Line. We are maintaining our EPS estimates which incorporate company guidance issued at analyst day earlier in the year. Our '20/'21/'22 EPS forecast of $1.55/$1.65/$1.80 drives a '19 through '22 CAGR of ~7% towards the high end of company's targeted EPS growth rate of 5-7%. Our $38 target price is based on a SOTP where we assign 23.0x P/E to the earnings contribution from the legacy water business and ~17x to earnings from the gas segment. The 23.0x water P/E is in line with our water regulated peer average target multiple. The gas multiple of ~17x is also in line with current gas LDC trading valuation multiples. Rating remains In Line

Repairs Tax Election Uplift, 8-12c/yr. Essential's 2020 and forward looking EPS guidance includes 8-12c/share annual earnings uplift which is more/less in line with our estimate of ~10c. There may be additional accretion from historical balances pending commission review and final decision. For context, in 2012, Aqua (water utility) changed its tax method of accounting for qualifying utility asset repairs in PA. The tax accounting method was changed to permit the expensing of certain utility asset repairs/maintenance costs that were previously being capitalized and depreciated for tax purposes. The company used flow-through accounting for the tax benefits of the repair tax accounting change per the Pennsylvania rate order from June '12. The flow-through accounting implementation resulted in a reduction in the company's effective income tax rate, which in turn lowered income tax expense and increased net income. WTR's effective tax rate was materially lower than the statuary tax rate at (7.7%) / 6.6% / 8.2% for the years '18 / '17 / '16 respectively. Higher earnings power supported higher returns on equity, which allowed Aqua to invest over $2bn of capital on system improvements over the past seven years without having to go in for rate cases in PA. There could be further earnings upside (~$0.05 annual EPS uplift by our estimate) if the commission allows favorable treatment of the legacy tax balance.

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RISKS

Risks to our thesis include an unfavorable regulatory outcome leading to lower rate base growth and/or lower allowed or earned ROEs in ongoing and future rate cases. Other risks include exposure to unusual weather, impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer, cyber security and water contamination.

COMPANIES UNDER COVERAGE BY AUTHOR

Symbol	Company	Rating	Price (2020-07-05)	Evercore ISI Target
AEE	Ameren Corp.	Outperform	$69.95	$84.00
AEP	American Electric Power	Outperform	$78.79	$95.00
AES	The AES Corporation	Outperform	$12.14	$20.00
AGR	Avangrid Inc	In Line	$41.88	$46.00
AWK	American Water Works Company, Inc.	Outperform	$119.25	$118.00
AWR	American States Water Company	Underperform	$74.17	$60.00
CMS	CMS Energy Corp.	In Line	$54.52	$63.00
CNP	CenterPoint Energy, Inc.	In Line	$17.75	$17.00
CWEN	Clearway Energy	In Line	$20.48	$20.00
CWT	California Water Service Group	In Line	$45.10	$46.00
D	Dominion Energy, Inc	In Line	$78.22	$82.00
DTE	DTE Energy Co.	In Line	$99.18	$120.00
DUK	Duke Energy Corp.	In Line	$80.51	$90.00
ED	Consolidated Edison Inc.	In Line	$74.53	$86.00
EIX	Edison International	In Line	$54.78	$80.00
ES	Eversource Energy	In Line	$77.90	$91.00
ETR	Entergy Corp.	In Line	$93.08	$106.00
EVRG	Evergy	In Line	$56.15	$64.00
EXC	Exelon Corp.	Outperform	$35.07	$49.00
FCFE18-MX	CFE Capital S. de R.L. de C.V.	Outperform	MXN19.30	MXN19.00
FE	FirstEnergy Corp.	Outperform	$40.26	$50.00
HE	Hawaiian Electric Industries Inc.	Underperform	$36.72	$36.00
NEE	NextEra Energy Inc	In Line	$226.04	$249.00
NI	NiSource Inc	Outperform	$22.97	$28.00
NRG	NRG Energy Inc.	Outperform	$32.13	$47.00
OGE	OGE Energy Corp	Outperform	$29.30	$35.00
PCG	PG&E Corp.	Rating Suspended	$11.15	
PEG	Public Service Enterprise Group	In Line	$47.94	$53.00
PNM	PNM Resources, Inc	In Line	$38.39	$44.00
PNW	Pinnacle West Capital Corp.	In Line	$72.05	$85.00
PPL	PPL Corp.	In Line	$24.36	$31.00
SJW	SJW Group	In Line	$58.61	$65.00
SO	Southern Co.	In Line	$54.33	$59.00
SRE	Sempra Energy	Outperform	$123.91	$138.00
VST	Vistra Energy Corp	Outperform	$17.95	$32.00
WEC	WEC Energy Group, Inc.	In Line	$85.36	$93.00
WTRG	Essential Utilities Inc.	In Line	$40.59	$38.00
XEL	Xcel Energy Inc.	In Line	$60.06	$65.00

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Time of dissemination: May 07 2020 08:34 PM ET

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Outperform- the total forecasted return is expected to be greater than the expected total return of the analyst's coverage universe
In Line- the total forecasted return is expected to be in line with the expected total return of the analyst's universe
Underperform- the total forecasted return is expected to be less than the expected total return of the analyst's universe
Coverage Suspended- the rating and target price have been removed pursuant to Evercore ISI policy when Evercore is acting in an advisory capacity in a merger or strategic transaction involving this company and in certain other circumstances.*
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*Prior to October 10, 2015, the "Coverage Suspended" and "Rating Suspended" categories were included in the category "Suspended."

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Sell -the total forecasted return is expected to be less than 0%

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Prior to October 10, 2014, the ratings system of ISI Group LLC and ISI UK which was based on a 12-month risk adjusted total return:

Strong Buy- Return > 20%
Buy- Return 10% to 20%
Neutral - Return 0% to 10%
Cautious- Return -10% to 0%
Sell- Return< -10%

For disclosure purposes, ISI Group and ISI UK ratings were viewed as follows: Strong Buy and Buy equate to Buy, Neutral equates to Hold, and Cautious and Sell equate to Sell.

Evercore Group:

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Overweight- the stock is expected to outperform the average total return of the analyst's coverage universe over the next 12 months.
Equal-Weight- the stock is expected to perform in line with the average total return of the analyst's coverage universe over the next 12 months.
Underweight -the stock is expected to underperform the average total return of the analyst's coverage universe over the next 12 months.
Suspended- the company rating, target price and earnings estimates have been temporarily suspended.

For disclosure purposes, Evercore Group's prior "Overweight," "Equal-Weight" and "Underweight" ratings were viewed as "Buy," "Hold" and "Sell," respectively.

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Short- the stock is a negative holding in the model portfolio; the total forecasted return is expected to be less than 0%.
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Stocks included in the model portfolio will be weighted from 0 to 100% for Long and 0 to -100% for Short. A stock's weight in the portfolio reflects the analyst's degree of conviction in the stock's rating relative to other stocks in the portfolio. The model portfolio may also include a cash component. At any given time the aggregate weight of the stocks included in the portfolio and the cash component must equal100%.

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Evercore ISI rating (as of 05/07/2020)

Coverage Universe			**Investment Banking Services I Past 12 Months**		
Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	366	48	Buy	97	27
Hold	304	39	Hold	49	16
Sell	54	7	Sell	4	7
Coverage Suspended	33	4	Coverage Suspended	11	33
Rating Suspended	13	2	Rating Suspended	2	15

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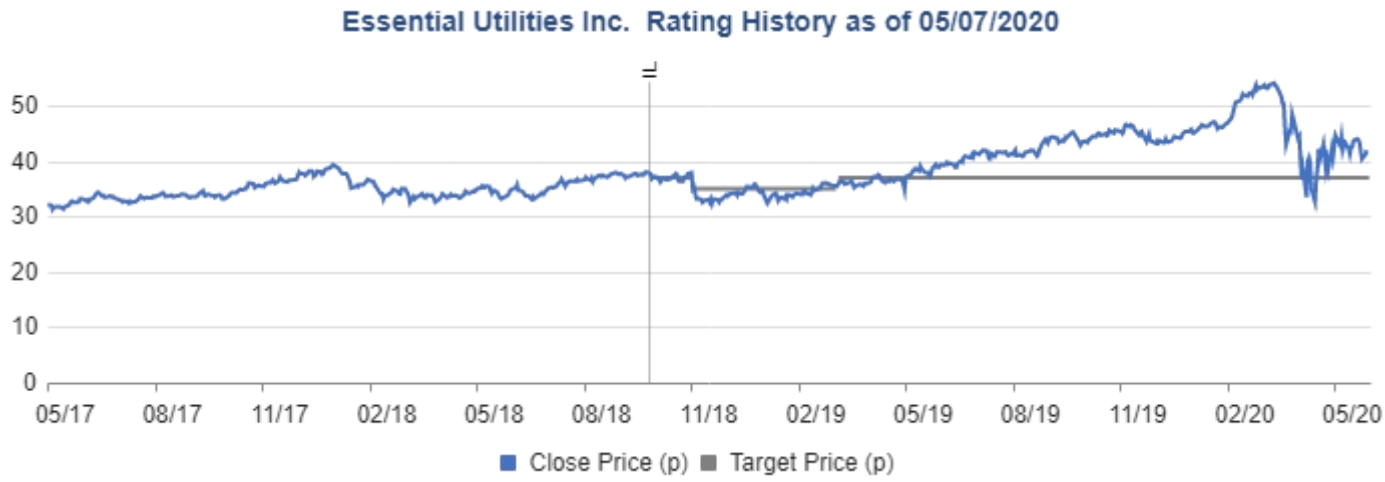
Price Charts



Ratings Key

B	Buy	OP	Outperform	L	Long	CS	Coverage Suspended
H	Hold	IL	In Line	NP	No Position	RS	Rating Suspended
S	Sell	UP	Underperform	S	Short		

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EVERCORE ISI

Energy | Power & Utilities

August 07, 2020

Essential Utilities Inc.

WTRG | $45.56

In Line | TARGET PRICE: $42.00 (from $38.00)

Earnings Report

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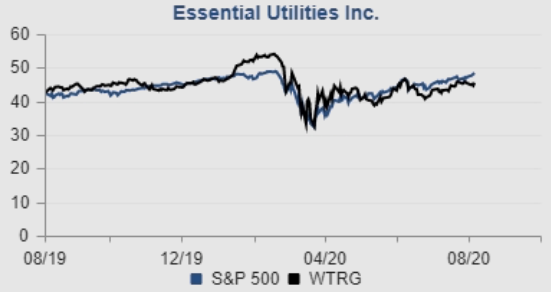
Company Statistics

Market Capitalization (M)	$8,597
Shares Outstanding (M)	223
Dividend	1.03
Dividend Yield	2.7%
Payout Ratio	66.1%
Expected Total Return	11.8%
Fiscal Year End	Dec

Earnings Summary

	2020E	2021E	2022E
EPS	**$1.55**	**$1.65**	**$1.80**
P/E	**24.8**	**23.3**	**21.3**
EPS vs Consensus	**(0.8)%**	**0.2%**	**1.9%**
Consensus EPS	**$1.57**	**$1.65**	**$1.77**
Consensus P/E	**24.6**	**23.3**	**21.8**

1 Year Price History



Source: FactSet

Solid Quarter, LT Outlook Reaffirmed

Essential posted a solid beat in the second quarter reporting EPS of $0.29 versus consensus of $0.23. Helped in part by favorable weather, residential load more the offset decline in Commercial/Industrial usage resulting in no meaningful COVID impact during the quarter. The company filed for repair tax catch-up with the PA Commission (~$0.05 annual EPS uplift if approved our estimate) and advanced Delcora transaction process expected to close early next year. They still expect to issue $300MM in equity later this year to finance the deal ($0.03 EPS contribution included in our forecast). WTRG also reaffirmed its 2020 EPS guidance range of $1.53-$1.58 and still projects EPS to grow in the range of 5-7% on average from 2019 through 2022.

Target Price $42, rating In Line. Our $42 target price is based on a SOTP where we now assign 26.5x P/E to the '22 earnings contribution from the legacy water business and ~ 16.5x to earnings from the gas segment. The 26.5x water P/E is a ~15% premium to our water utility average target multiple of 23x which we think is warranted in this environment given above average residential customer mix which positions them well against COVID related demand headwinds. Majority of their water EPS is derived from PA which is also a relative advantage versus peers. The gas multiple of ~16.5x is also in line with current gas LDC. We see bull/bear case valuation of $48/$38 respectively, and given the potential upside opportunity from tax catch up, municipal water/waste water deals and other complementary growth projects we assign low probability to our bear case scenario, see page 2 of the report.

Repairs Tax Election Uplift, 8-12c/yr. Essential's 2020 and forward looking EPS guidance includes 8-12c/share annual earnings uplift which is more/less in line with our estimate of ~10c. There may be additional accretion from historical balances pending commission review and final decision. For context, in 2012, Aqua (water utility) changed its tax method of accounting for qualifying utility asset repairs in PA. The tax accounting method was changed to permit the expensing of certain utility asset repairs/maintenance costs that were previously being capitalized and depreciated for tax purposes. The company used flow-through accounting for the tax benefits of the repair tax accounting change per the Pennsylvania rate order from June '12. The flow-through accounting implementation resulted in a reduction in the company's effective income tax rate, which in turn lowered income tax expense and increased net income. WTR's effective tax rate was materially lower than the statuary tax rate at (7.7%) / 6.6% / 8.2% for the years '18 / '17 / '16 respectively. Higher earnings power supported higher returns on equity, which allowed Aqua to invest over $2bn of capital on system improvements over the past seven years without having to go in for rate cases in PA. There could be further earnings upside (~$0.05 annual EPS uplift by our estimate) if the commission allows favorable treatment of the legacy tax balance.

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DELCORA opportunity. In September '19, management had announced a signed purchase agreement with Delaware County Regional Water Authority (DELCORA), following the latter's signing of a letter of intent with Aqua committing to exclusive discussions in August '19. DELCORA is a wastewater conveyance and treatment authority that serves approximately 500,000 people in 42 municipalities in Delaware and Chester Counties in southeastern Pennsylvania. We estimate that this could be a potential ~$300mm rate base / $0.03 EPS uplift in '21 (included in our forecast), assuming 50%/50% debt/equity financing.

We are changing our PT to $42 for WTR; our rating remains In Line. Our $42 target price is based on a SOTP where we now assign 26.5x P/E to the '22 earnings contribution from the legacy water business and ~ 16.5x to earnings from the gas segment. The 26.5x water P/E is a ~15% premium to our water utility average target multiple of 23x which we think is warranted in this environment given above average residential customer mix which positions them well against COVID related demand headwinds. Majority of their water EPS is derived from PA which is also a relative advantage versus peers. The gas multiple of ~16.5x is also in line with current gas LDC. Our bull case valuation of $48 assumes that they are able to achieve ~$0.05 combined upside from tax repairs, and both the water and gas segment trade at 10% premium to our base case scenario. Our bear case valuation of $38 assumes a 5% discount multiple to our base case scenario for both segments and low end of targeted LT EPS growth. Please see Exhibit 1 for additional details.

Exhibit 1
WTR Valuation Framework

SOTP Valuation (Base Case)	'22E	'21 P/E	Valuation
Legacy WTR EPS	$1.26	26.4x	$33.00
Gas EPS	$0.54	16.5x	$9.00
	$1.80		$42.00

SOTP Valuation (Bull Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.29	29.0x	$38.00
Gas EPS	$0.55	18.1x	$10.00
	$1.85		$48.00

SOTP Valuation (Bear Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.19	25.1x	$30.00
Gas EPS	$0.51	15.7x	$8.00
	$1.70		$38.00

Source: Evercore ISI Research

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VALUATION METHODOLOGY

Our $42 target price is based on a SOTP where we now assign 26.5x P/E to the '22 earnings contribution from the legacy water business and ~ 16.5x to earnings from the gas segment. The 26.5x water P/E is a ~15% premium to our water utility average target multiple of 23x which we think is warranted in this environment given above average residential customer mix which positions them well against COVID related demand headwinds.

RISKS

Risks to our thesis include an unfavorable regulatory outcome leading to lower rate base growth and/or lower allowed or earned ROEs in ongoing and future rate cases. Other risks include exposure to unusual weather, impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer, cyber security and water contamination.

COMPANIES UNDER COVERAGE BY AUTHOR

Symbol	Company	Rating	Price (2020-07-08)	Evercore ISI Target
AEE	Ameren Corp.	Outperform	$81.06	$84.00
AEP	American Electric Power	Outperform	$85.37	$95.00
AES	The AES Corporation	Outperform	$16.55	$20.00
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AWR	American States Water Company	Underperform	$76.65	$60.00
CMS	CMS Energy Corp.	In Line	$61.75	$63.00
CNP	CenterPoint Energy, Inc.	In Line	$20.27	$18.00
CWEN	Clearway Energy	In Line	$25.77	$22.00
CWT	California Water Service Group	In Line	$46.96	$40.00
D	Dominion Energy, Inc	In Line	$79.63	$77.00
DTE	DTE Energy Co.	In Line	$116.94	$120.00
DUK	Duke Energy Corp.	In Line	$84.21	$87.00
ED	Consolidated Edison Inc.	In Line	$73.92	$85.00
EIX	Edison International	In Line	$53.87	$72.00
ES	Eversource Energy	In Line	$88.10	$91.00
ETR	Entergy Corp.	In Line	$102.29	$106.00
EVRG	Evergy	Outperform	$54.75	$62.00
EXC	Exelon Corp.	Outperform	$37.90	$45.00
FCFE18-MX	CFE Capital S. de R.L. de C.V.	Outperform	MXN25.28	MXN19.00
FE	FirstEnergy Corp.	In Line	$29.18	$41.00
HE	Hawaiian Electric Industries Inc.	Underperform	$35.04	$34.00
NEE	NextEra Energy Inc	In Line	$282.81	$277.00
NI	NiSource Inc	Outperform	$24.34	$26.00
NRG	NRG Energy Inc.	Outperform	$33.98	$40.00
OGE	OGE Energy Corp	Outperform	$32.94	$35.00
PCG	PG&E Corp.	Rating Suspended	$9.10	
PEG	Public Service Enterprise Group	In Line	$54.63	$53.00
PNM	PNM Resources, Inc	In Line	$42.84	$44.00
PNW	Pinnacle West Capital Corp.	In Line	$80.79	$85.00
PPL	PPL Corp.	In Line	$26.50	$31.00
SJW	SJW Group	In Line	$64.76	$60.00
SO	Southern Co.	In Line	$53.89	$59.00
SRE	Sempra Energy	Outperform	$128.20	$138.00
VST	Vistra Energy Corp	Outperform	$18.83	$27.00
WEC	WEC Energy Group, Inc.	In Line	$92.99	$93.00
WTRG	Essential Utilities Inc.	In Line	$45.56	$42.00
XEL	Xcel Energy Inc.	In Line	$70.10	$65.00

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Buy- Return 10% to 20%
Neutral - Return 0% to 10%
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Sell- Return< -10%

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Evercore ISI rating (as of 08/07/2020)

Coverage Universe			**Investment Banking Services I Past 12 Months**		
Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	377	49	Buy	110	29
Hold	307	40	Hold	49	16
Sell	46	6	Sell	4	9
Coverage Suspended	21	3	Coverage Suspended	6	29
Rating Suspended	15	2	Rating Suspended	3	20

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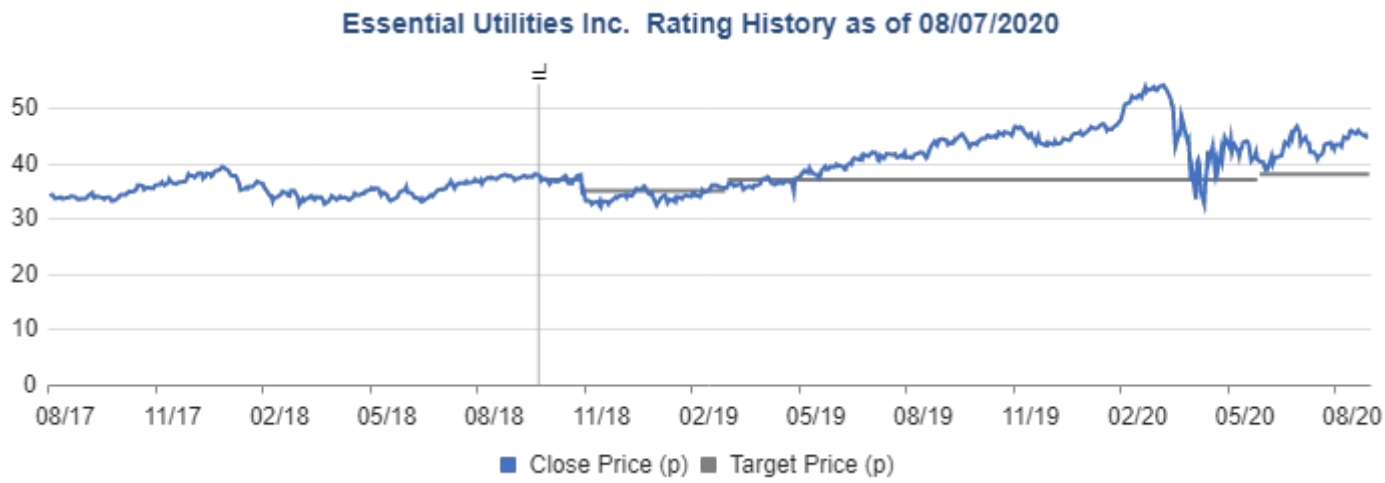

Ratings Key

B	Buy	OP	Outperform	L	Long	CS	Coverage Suspended
H	Hold	IL	In Line	NP	No Position	RS	Rating Suspended
S	Sell	UP	Underperform	S	Short		

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Americas Utilities

Analyzing water utility premiums - Upgrade AWK to Buy, Initiate WTRG at Neutral

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We initiate coverage on Essential Utilities Inc. (WTRG) and transfer primary coverage on American Water (AWK) from Michael Lapides to Insoo Kim with the following updated views:

Analyzing the water utility premium valuation: fundamentals + ESG. While we recognize the current 10-11x relative P/E premium versus electric/gas utilities, we view this as justified given two quantifiable advantages: 1) our analysis shows every $1 invested in water assets is worth more given a longer depreciable life vs electric, and 2) long visibility of above-average growth due to significant water pipe investment needs. In addition, we see continued ESG momentum sustaining additional relative premium for water utilities. With this in mind:

- **We upgrade AWK to Buy with a $146 price target (16% total return)** as we see 1) best-in-class 8.3% EPS CAGR, 2) one of the highest beta-adjusted returns among Regulated Utilities (Exhibit 3), and 3) its ESG-favorable position as the only large-cap, pure-play water utility in the U.S. We view this defensive utility offering investors an attractive investment opportunity with double-digit upside potential.
- **We initiate coverage of WTRG at Neutral with a $45 price target (7% total return)** given 1) robust 6.6% EPS CAGR post Peoples Gas acquisition, but 2) current multiples that largely reflect the water/gas sum-of-the-parts valuation.
- **AWK/WTRG both remain relatively defensive in the current COVID-19 environment,** outperforming the XLU by 7%/3% since March 1. Also, we favorably view their heavy residential revenue mix which could help offset potential near-term demand impact from commercial/industrial customers.

As highlighted in our recent note, we remain positive on the Utilities sector, both on an absolute and relative basis, given 10-year treasury yields below 1% and the regulated utilities' more resilient earnings power relative to that for the broader market, especially in the current COVID-19 environment. We see 15%/25% total return for Regulated Utilities and Diversified Utilities, respectively.

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PM Summary: Premium water utility multiples are justified; buy AWK

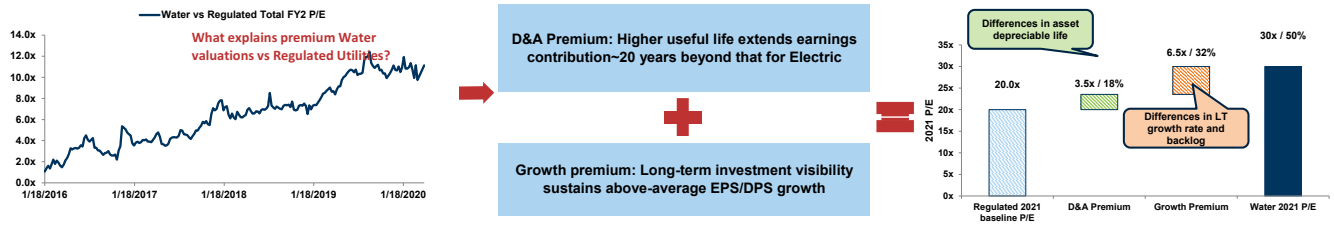
Despite the large relative P/E premiums for water utilities currently, we see two quantifiable advantages versus electric utilities that provide justification: 1) every $1 invested in water assets is worth more given a longer depreciable life, and 2) material organic/inorganic growth visibility that should sustain above-average earnings growth longer-term. Combined with a favorable ESG screen, we believe water utilities could see further relative multiple expansion from current levels.

To this end, we transfer primary coverage of AWK from Michael Lapides to Insoo Kim and upgrade from Neutral to Buy given best-in-class growth, more robust credit metrics, and its ESG-friendly status as a large-cap pure-play water utility, while we initiate on WTRG with a Neutral rating as we believe valuations fairly reflect the water/gas business mix.

Do water utilities deserve the current premium? We believe so. Based on our new and detailed analysis (please refer to the following section), we see certain fundamental advantages that justify the current 11.3x premium versus electric utilities. The primary drivers include:

1. **D&A premium (3.5x):** Every $1 invested to longer useful-life water assets (50 years vs. 30 years for electric) extends their value - translating into roughly 2% higher earnings growth.
2. **Growth premium (6.5x):** We see water utilities sustaining their above-average earnings/dividend growth over electric utilities over at least the next 15 years, given significant water investment needs in the U.S.
3. **Other qualitative factors:** 1) scarcity of water investor-owned utilities (IOUs), 2) ESG-related premium for pure-play water utilities (which we believe may impact WTRG given its new exposure to gas utilities).

Exhibit 1: Longer useful life and long-term investment visibility largely justify premium water valuations vs. electric/gas



Source: Goldman Sachs Global Investment Research

Following our analysis, we revise our regulated baseline water multiple from 25.5x to 30.0x, which incorporates the 10x D&A/growth premium to our 20x base P/E for electric/gas utilities on 2021E EPS.

With this revised base, we make the following recommendations:

- **Upgrade AWK to Buy**: **best-in-class growth and a pure-play large-cap water utility.** We expect AWK to continue to achieve above-average EPS growth, with our

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estimates (1% above consensus) implying an 8.3% EPS CAGR from 2019-2022 - at the middle of the company's 7-10% guidance - driven by a combination of core regulated investments, continued municipal utility acquisitions, and contributions from its contracted segments. Despite the 16% total return screening as comparable to 15% for Regulated Utilities, we believe AWK's below-average beta and ESG-friendly profile could drive further relative multiple expansion for this secular growth story.

- **Initiate on WTRG at Neutral**: **water/gas mix fully reflected in valuations.** We see WTRG's recent acquisition of Peoples Gas, a private gas utility business boosting consolidated rate base growth to 9.7% from 2019-2022 versus 9% prior as a stand-alone water utility, along with benefits from acquisition synergies. Our estimates - largely in-line with consensus - reflect a 6.6% EPS CAGR from 2019-2022, although we expect long-run growth to trend closer to rate base growth. We see the current 4.3x valuation discount versus water peers as largely appropriate given our view that gas utilities warrant a lower multiple. Our $45 target incorporates a 27.3x blended P/E multiple, resulting in a 7% total return versus the sector average at 15%.

Balance sheet/credit metrics favor AWK. While both AWK and WTRG maintain an A issuer rating by S&P, we see AWK's 15-17% FFO/debt, versus WTRG's 12%, through 2022 more favorably in the current economic environment. Parent debt levels - sub-20% for AWK verus 25-30% for WTRG - also screen better for AWK, as WTRG's recently completed Peoples Gas acquisition contributing to a more levered balance sheet.

How much near-term demand impact do AWK/WTRG face from COVID-19? Could be modest. We note that both AWK and WTRG derive less than 10% of revenues from industrial customers, while more than 60% from residential customers. GIven our view (see recent note) that residential volumes should see an increase in demand, we estimate that a +3%/-5%/-10% change in residential/commercial/industrial demand could actually result in a relatively neutral net income impact, while acknowledging the difficulty in estimating the net outcome.

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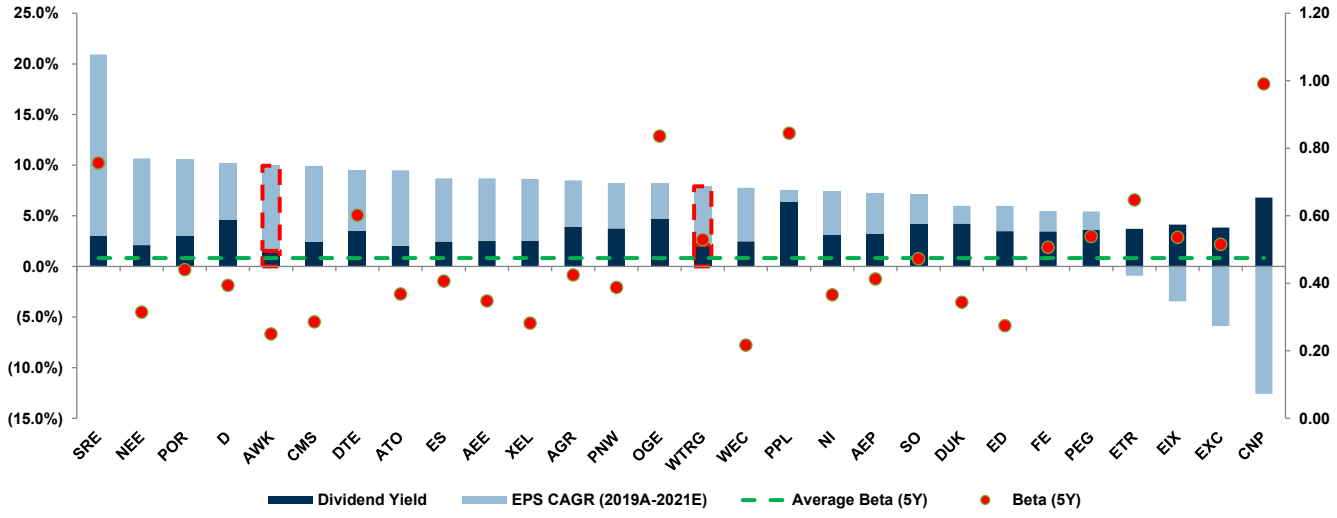
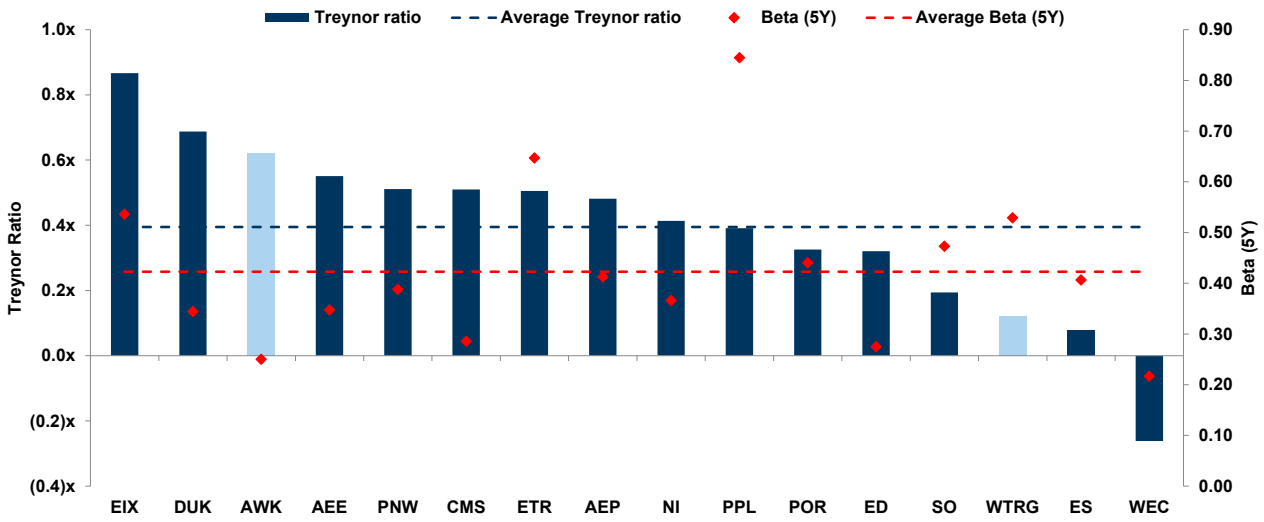
Exhibit 2: We see AWK providing one of the best EPS growth and dividend yield in our coverage universe, all at a below-average beta...
Utilities coverage Dividend yield, EPS CAGR (2019A-2021E) & 5Y Beta



Source: FactSet, Company data, Goldman Sachs Global Investment Research

Exhibit 3: ...with one of the best beta-adjusted total return potential among Regulated Utilities.
AWK/WTRG Risk-adjusted total return (Treynor ratio) vs Regulated Utilities coverage



Source: FactSet, Goldman Sachs Global Investment Research

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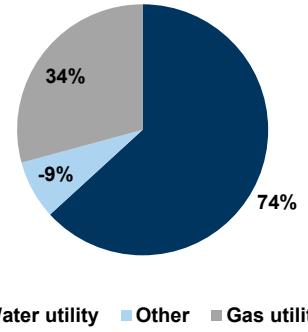
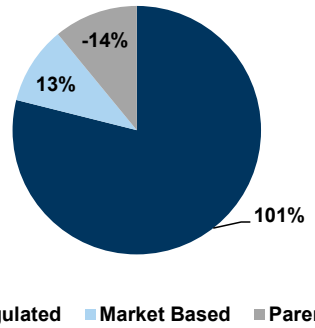
Exhibit 4: We favor AWK for its best-in-class EPS growth and ESG-friendly pure-play water profile
Company Summary

	WTRG	AWK
Rating	**Neutral (Initiating)**	**Buy (from Neutral)**
Total Return	**7%**	**16%**
Market Cap	**$9.6bn**	**$23.0bn**
EPS Mix (2020E)		
Utility States	**Water:** PA, TX, IL, IN, OH, NC, VA, NJ **Gas:** PA. WV, KY	**Water (regulated):** NJ, PA, MO, IL, CA, IN, WV, GA, HI, IA, KY, MD, MI, NY, TN, VA
Customer Growth/ Customer count (2018A)	**Water utility -** 2.3% (Growth through acquisition - 1.4%, Organic growth - 0.9%) **Customer count** - 10.1 mn	**Water utility -** 0.7% **(**Growth through acquisition - 0.3%, organic growth - 0.4%**)** **Customer count -** 31.8 mn
Reg. Utility Earnings Growth ('19-'22E)	6.6%	8.3%
Investment Thesis	(+) Peoples Gas acquisition boosts rate base growth to 9-10% and 6-7% EPS growth through 2022 (+) Synergy from Peoples Gas acquisition (-) Water/gas mix a potential headwind to further multiple expansion from an ESG perspective	(+) Above-average 8.3% EPS CAGR from 2019-2022E and 10% DPS CAGR (+) Size benefits to take advantage of accretive municipal acquisition (+) Status as the only large-cap, pure-play water utility - favorable from a scarcity/ESG perspective
Near-term Risk	* Lower than expected synergy benefits from the acquisition of Peoples gas * Water/gas utility growth impacted by current COVID-19 pandemic	* Regulated/non-regulated segment growth impacted by current COVID-19 pandemic
Company Overview	*Water utility business in 8 states (PA being the largest one) *Recent acquisition of Peoples Gas adds PA, WV and KY gas jurisdictions * 2nd largest publicly traded water/gas utility company	* Largest publicly traded utility company in the US *Owns water and waste water utility services to residential, commercial and industrial customers *Operates in 46 states in the US and Ontario, Canada
Credit Rating (Issuer Credit) (Moody's/S&P)	--/A	Baa1/A
Sub-Sector (% earnings)	Water utility (70%) Gas utility (30%)	Water utility (87%) Non-regulated businesses (13%)

Source: Company data, Goldman Sachs Global Investment Research

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Exhibit 5: AWK has largely maintained its ESG fund overweight status, while WTRG has dropped more meaningfully since prior to Peoples Gas acquisition completion

Top 10 ESG Relative overweight companies in US as of Sept 2019 and Apr 2020

Top 10 ESG Relative overweight companies in US (April 2020)

	Company	GICS 1
1	NASDAQ INC ORD	Financials
2	XYLEM INC ORD	Industrials
3	IDEX CORP ORD	Industrials
4	EPAM SYSTEMS INC ORD	Information Technology
5	TRIMBLE INC ORD	Information Technology
6	UBER TECHNOLOGIES INC ORD	Industrials
7	GUIDEWIRE SOFTWARE INC ORD	Information Technology
8	PTC INC ORD	Information Technology
9	DENTSPLY SIRONA INC ORD	Health Care
10	VERISK ANALYTICS INC ORD	Industrials
14	**AMERICAN WATER WORKS COMPANY IN**	**Utilities**
21	**ESSENTIAL UTILITIES INC ORD**	**Utilities**

Top 10 ESG Relative overweight companies in US (Sept 2019)

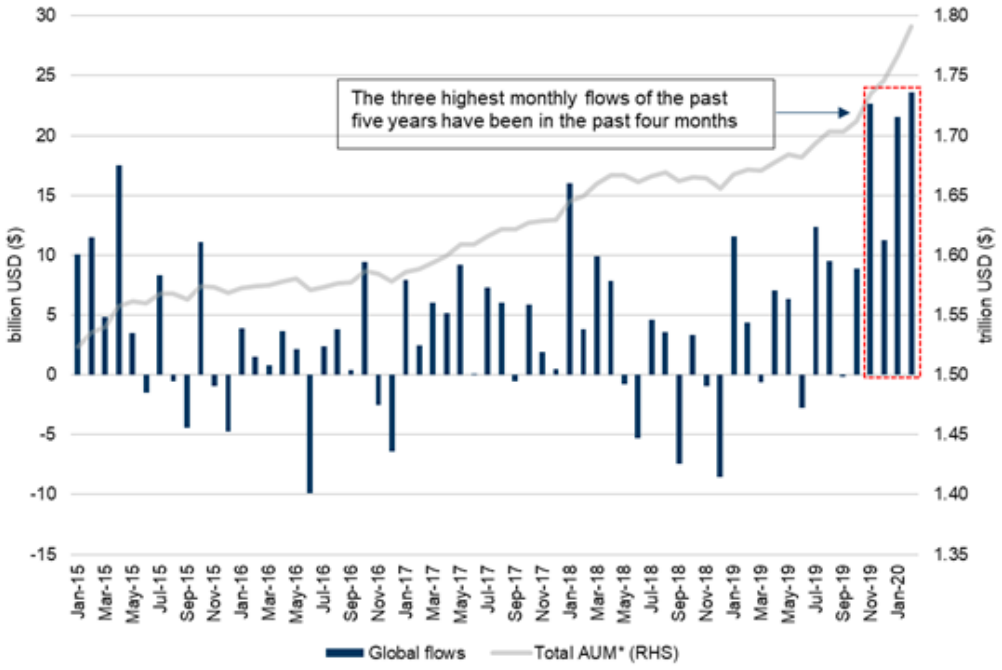
	Company	GICS 1
1	Xylem Inc	Industrials
2	Trimble Inc	Information Technology
3	**Aqua America Inc**	**Utilities**
4	First Solar Inc	Information Technology
5	A.O. Smith Corp	Industrials
6	Hologic Inc	Health Care
7	**American Water Works Company Inc**	**Utilities**
8	Gap Inc	Consumer Discretionary
9	Toro Co	Industrials
10	First American Financial Corp	Financials

Companies with market caps > $5B and domiciled in US; *ESG Relative overweights are calculated by dividing a company's ESG fund universe ACWI constituent weighting over its ACWI weighting; ACWI= MSCI All Country Weight Index

Source: Bloomberg, Morningstar, Goldman Sachs Global Investment Research

Exhibit 6: GS SUSTAIN: Positive ESG flows have persisted remaining robust through the early phases of the COVID-19 crisis

Monthly ESG fund flows (January 2015 through February 2020)



*AUM values are derived from historical flows and agnostic of market effect

Source: Morningstar

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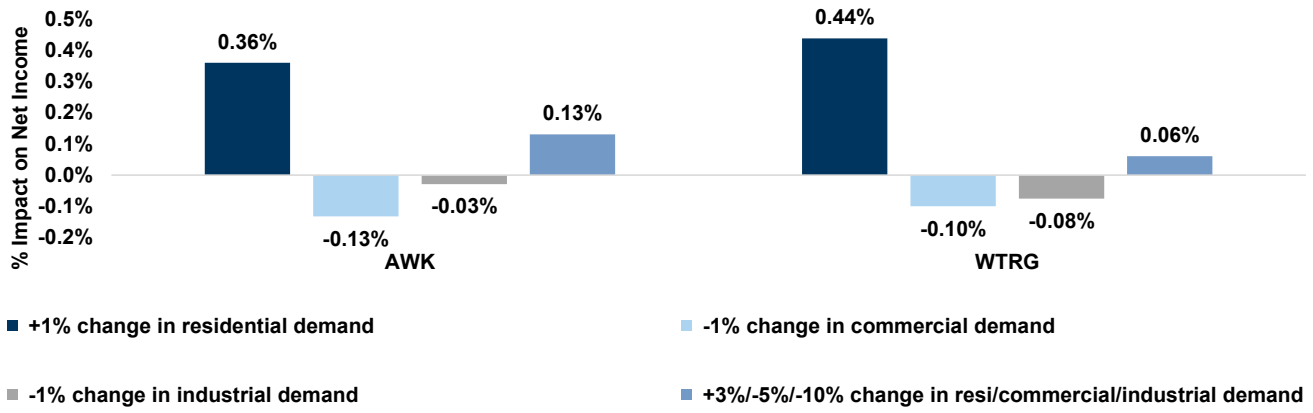
Exhibit 7: We see a moderate earnings impact for every 1% change in water demand, with higher residential demand that could potentially offset commercial/industrial declines
% Impact on Net Income from change in residential/commercial/industrial demand



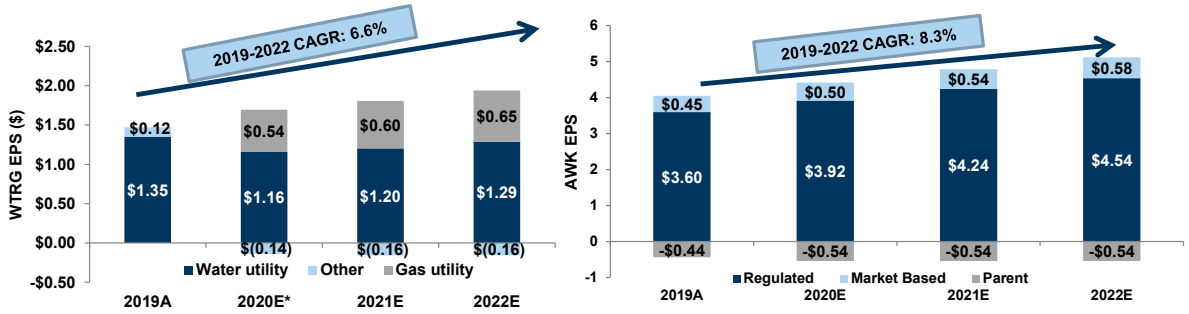
Source: Company data, Goldman Sachs Global Investment Research

Exhibit 8: We favor AWK's balance sheet and credit metrics versus WTRG, although both screen relatively stable in our view
AWK/WTRG GSe Credit metrics

Credit metrics (Gse)	AWK			WTRG		
	2020	2021	2022	2020	2021	2022
Net Debt/cap	61%	60%	58%	49%	51%	52%
Net Debt/EBITDA	5.2x	5.0x	4.7x	7.3x	6.4x	6.4x
FFO/Debt	15%	16%	17%	11%	12%	12%
Holdco debt (% of total debt)	19%	18%	18%	34%	29%	27%
Credit rating (Parent)	A/Baa1 (S&P/Moody's)			A/NR (S&P/Moody's)		

Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 9: We see robust EPS growth at AWK, with a more modest growth at WTRG through 2022 given timing of rate recovery and transitions in tax-advantaged mechanisms...
EPS 2019A-2022E



* 2020 incorporates full-year of Peoples Gas earnings ; 2021 summation for WTRG off by $0.01 due to rounding issue

Source: Company data, Goldman Sachs Global Investment Research

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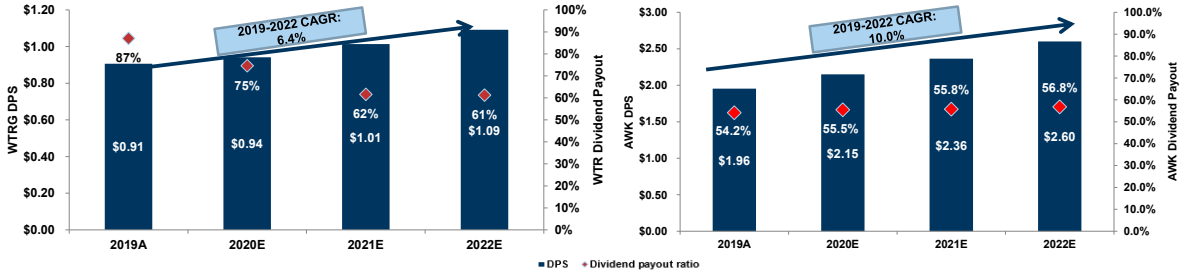
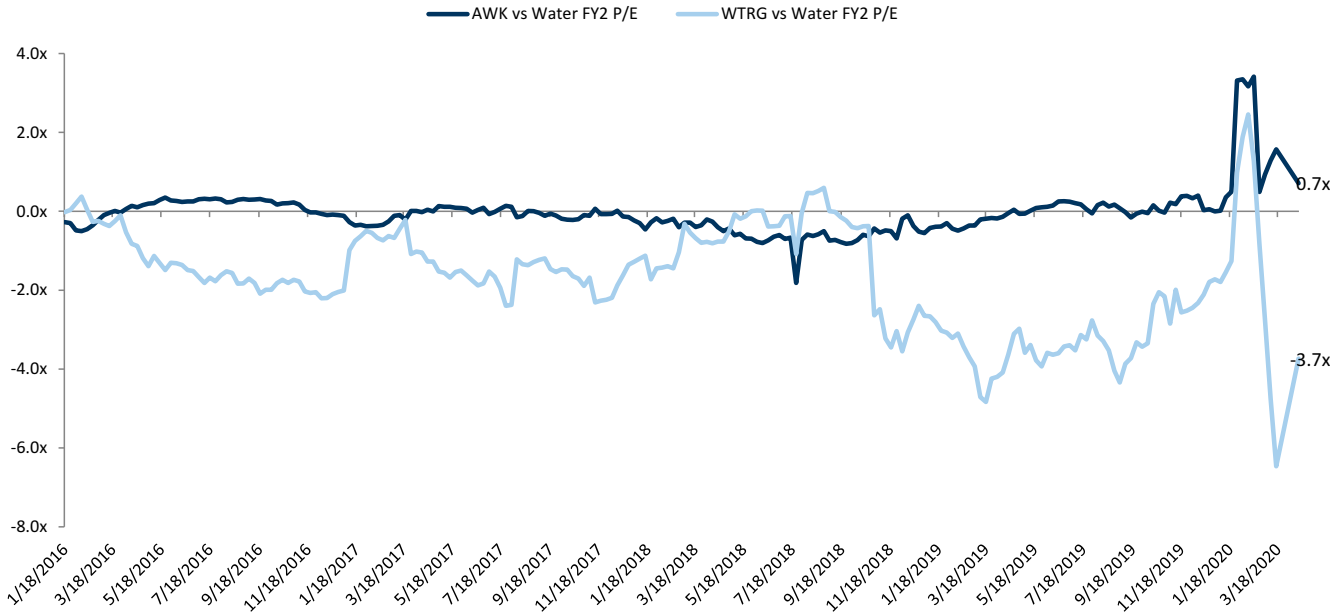
Exhibit 10: ...with a more robust dividend growth for AWK
DPS and payout as % of consolidated EPS



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 11: We view AWK's premium valuation as sustainable given its best-in-class growth and ESG-friendly profile, while WTRG's relative discount screens appropriate given its gas utility exposure
AWK & WTRG vs Water FY2 P/E



Source: Goldman Sachs Global Investment Research, FactSet

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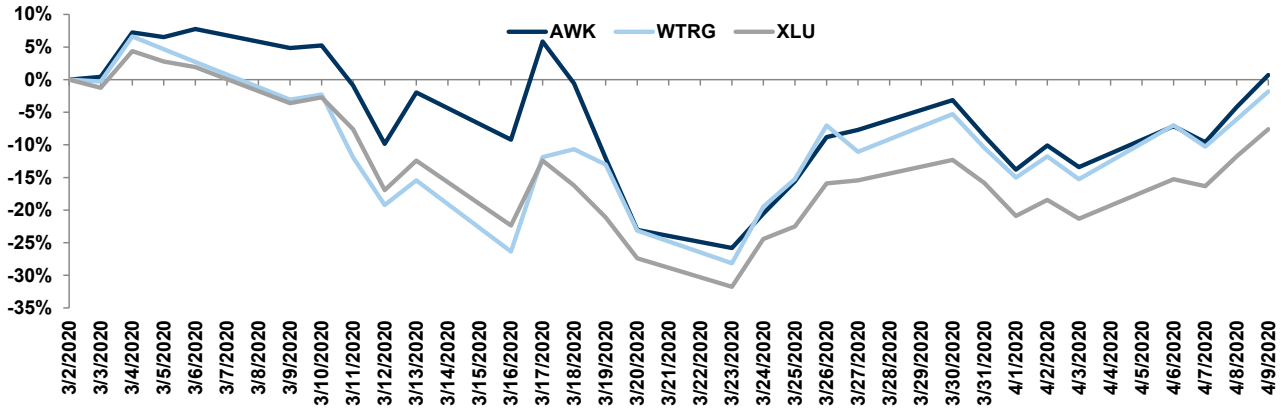
Exhibit 12: Both AWK and WTRG continue to remain relatively defensive in the current COVID-19 environment, outperforming the XLU since March 1

AWK/WTRG/XLU Performance since March 2020



Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 13: We expect further multiple expansion for AWK given best-in-class growth, low beta, and favorable ESG profile

Water Comparable Valuation

Water Utilities Comparable Analysis													
			Close	12-Mo	Tot Ret	EPS			P/E			Dividend	EPS CAGR
	Ticker	Rating	4/13/20	Px. Tgt	to Target	2019A	2020E	2021E	2019E	2020E	2021E	Yield	2019A-21E
American Water	**AWK**	**Buy**	**$127.24**	**$146**	**16%**	**$3.61**	**$3.88**	**$4.24**	**35.3x**	**32.8x**	**30.0x**	**1.5%**	**8.4%**
American States Water	AWR	NC	$86.42	--	--	$2.24	$2.21	$2.34	38.6x	39.0x	36.9x	1.3%	2.2%
Essential Utilities	**WTRG**	**Neutral**	**$42.80**	**$45**	**7%**	**$1.47**	**$1.56**	**$1.65**	**29.1x**	**27.5x**	**26.0x**	**2.1%**	**5.8%**
California Water Service	CWT	NC	$52.87	--	--	$1.31	$1.53	$1.70	40.4x	34.6x	31.1x	1.5%	14.0%
Middlesex Water Company	MSEX	NC	$62.37	--	--	$2.01	$2.04	$2.19	31.0x	30.6x	28.5x		4.3%
SJW Corp.	SJW	NC	$62.66	--	--	$0.82	$2.31	$2.50	76.4x	27.1x	25.1x	1.9%	74.5%
York Water Company	YORW	NC	$42.39	--	--	$1.11	$1.21	$1.25	38.2x	35.2x	33.9x		6.1%
Water Utilities Mean					**12%**				**41.3x**	**32.4x**	**30.2x**	**1.7%**	**16.5%**
Water Utilities Median					**12%**				**38.2x**	**32.8x**	**30.0x**	**1.5%**	**6.1%**
Regulated Utilities Mean					**15%**				**20.8x**	**20.1x**	**18.9x**	**3.2%**	**5.4%**
Regulated Utilities Median					**16%**				**19.6x**	**19.4x**	**18.4x**	**3.2%**	**5.6%**

Estimates for Non-Covered Companies represent Factset Consensus

Source: Goldman Sachs Global Investment Research, FactSet

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Water Utilities – abundant growth opportunities in fragmented market

Water utilities are responsible for the operation and maintenance of water treatment plants and distribution networks, crucial for ensuring reliability and quality of supply. Water and wastewater services are primarily the two sources of revenue for a water utility.

- **Water services involve: (1) sourcing, (2) treatment and (3) distribution of water.** We outline the three steps in further detail below:
  - **Pumping Station:** A pumping station abstracts water from aquifers, rivers, reservoirs and lakes, using pumps, pipes and electricity.
  - **Treatment Facility:** After drawing the water, it is sent to a treatment facility, where chemicals and filtration systems minimize impurities and meet federal, state and local quality standards. Chemical and electric costs stand out as the two largest O&M expenses at a treatment facility.
  - **Distribution System:** The US water pipe network stretches across 70,000 miles, distributing water to the ultimate customers. Key periods of water pipe installations include: (1) late 1800s, (2) the 1920s and (3) the 1940s/1950s. Given the age of the current distribution system, pipe replacement spending represents the largest share of investor owned utilities' capital spending budget for the foreseeable future.
- **Wastewater services** involve the collection of wastewater from customers' premises through sewer lines. The wastewater is then transported through a sewer network to a treatment facility, where it is treated to meet required regulatory standards for wastewater before being returned to the environment. The solid waste by-product of the treatment process is disposed of or recycled in accordance with applicable standards and regulations.

Aging infrastructure and increased regulation in the sector are primary drivers for the need to modernize the country's water and wastewater infrastructure related to water quality and the management of water and wastewater residual discharges. Because pipe assets last a long time, water systems that were built in the latter part of the 19th century and throughout much of the 20th century have not, for the most part, experienced the need for pipe replacement on a large scale. To put this aging infrastructure into context, the American Water Works Association (AWWA) estimates that the cost of restoring underground pipes will total at least $1 trillion through 2035, without including the cost of constructing new infrastructure or repairing treatment plants. The estimate assumes pipes are replaced at the end of their useful lives. Over a 40-year period, through 2050, AWWA estimates the needs will exceed $1.7 trillion. Replacement needs account for about 54% of the national total, with the balance attributable to population changes over that period.

The key regulations that govern the distribution of water include the Safe Drinking Water Act and the Clean Water Act:

- **Federal Safe Drinking Water Act (1974):** The Federal Safe Drinking Water Act

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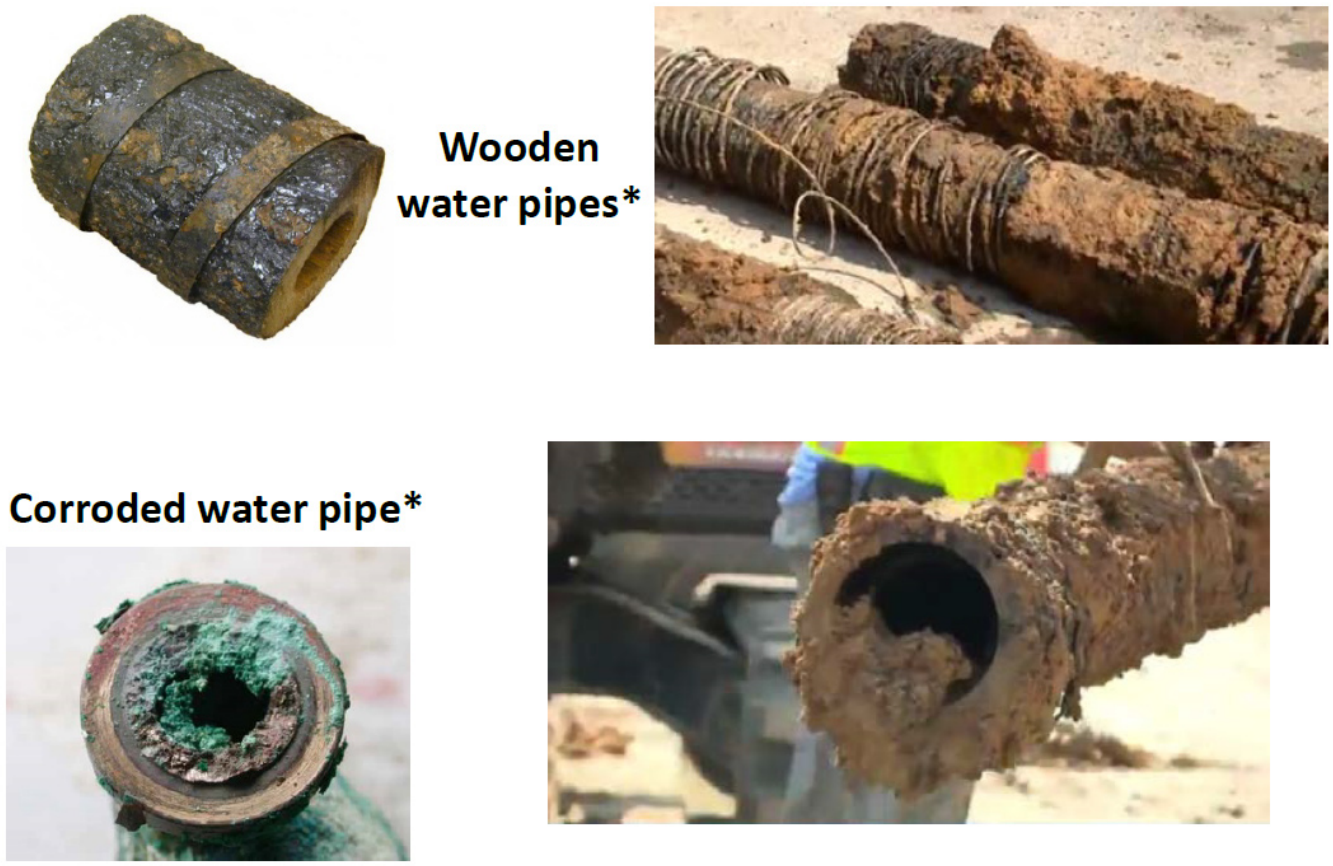
established national quality standards for drinking water. Under the SDWA, the EPA prescribes the legal limits of contaminants and sets water-testing schedules.

- **Clean Water Act (1972):** The Federal Clean Water Act regulates discharges from drinking water and wastewater treatment facilities into lakes, rivers, streams and groundwater.

Exhibit 14: The aging water and wastewater infrastructure in the United States require replacement and modernization, with at least $1 trillion investment potential through 2035
Aging US Pipe Infrastructure



*Not American Water Pipes

Source: AWK Dec 2017 Investor Presentation

The water utility sector is highly fragmented — more than 50,000 water utility systems exist nationwide — with investor-owned and privately held water utilities operating less than 15% of these systems. According to the U.S. Environmental Protection Agency (EPA), based on the 2015 U.S. Census American Housing Survey, approximately 89% of the U.S. population obtains its water from community water systems, and 11% of the U.S. population obtains its water from private wells. Of the approximately 50,000 community water systems in the U.S., 81% serve less than 3,300 customers, making the water industry the most fragmented of the major utility industries (natural gas, electric, water/wastewater). The majority of these community water systems are government-owned, and the balance of the systems are regulated utilities.

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Although not as fragmented as the water industry, the wastewater industry in the U.S. also presents opportunities for consolidation. According to the EPA's most recent survey of wastewater treatment facilities (which includes both government-owned facilities and regulated utility systems) in 2012, there were approximately 15,000 such facilities in the nation serving approximately 76% of the U.S. population. The remaining population represents individual homeowners with their own treatment facilities; for example, community on-lot disposal systems and septic tank systems. A majority of wastewater facilities are government-owned rather than regulated utilities.

Fair Market Value (FMV) legislation will continue to motivate consolidation of the water and wastewater industry, providing municipalities with an option for exiting the business if they are dealing with challenges associated with their aging, deteriorating water and wastewater assets, do not have the expertise or technical capabilities to continue to comply with ever-increasing environmental regulations or simply want to focus on other community priorities. The sector has been ripe for consolidation for decades and the largest water utilities have recently altered their strategic growth efforts to focus on buying mid-sized municipal water and wastewater systems fueled by fair market value (or FMV); legislation allows the water utilities to include into rate base the fair market value of the acquired municipal water assets instead of the depreciated original cost of water/wastewater assets. The legislation includes a process for engaging two independent utility valuation experts to perform appraisals that are filed with the public utility commission and then averaged and compared to the purchase price. The rate-making rate base is the lower of the average of the appraisals or the purchase price and is subject to regulatory approval. FMV is on the books in 10 states, including several of AWK/WTRG operating jurisdictions, and is pending before state legislatures in three more states.

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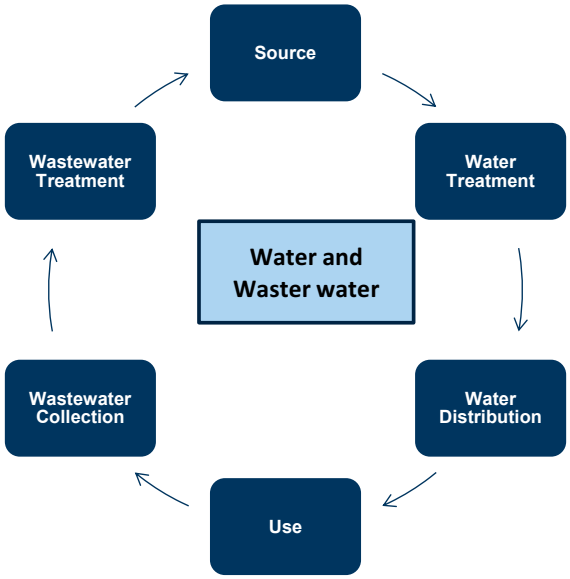
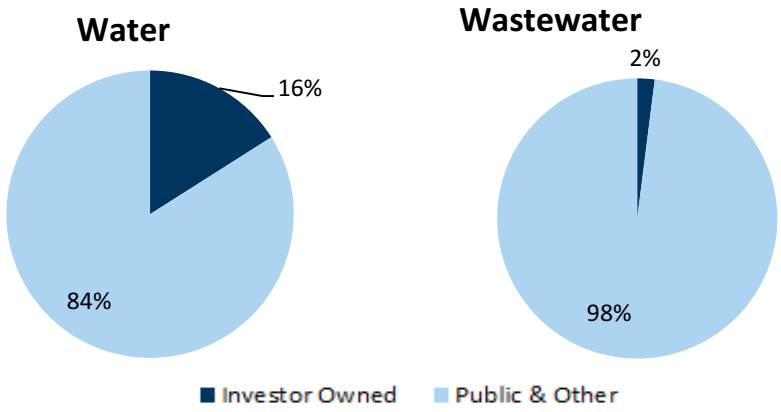
Exhibit 15: Water utilities are responsible for the operation and maintenance of water treatment plants and distribution networks, crucial for ensuring reliability and quality of supply
Water and Wastewater Cycle



Source: Goldman Sachs Global Investment Research

Exhibit 16: The sector remains ripe for consolidation given that investor-owned and privately held water utilities operate just 16% of these systems...
Water Industry- Investor Owned vs Public & Other market share



Source: Company data, Goldman Sachs Global Investment Research

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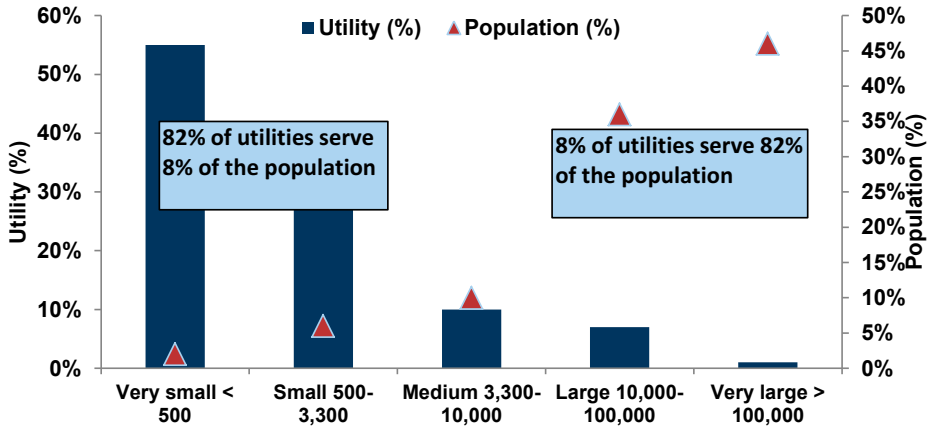
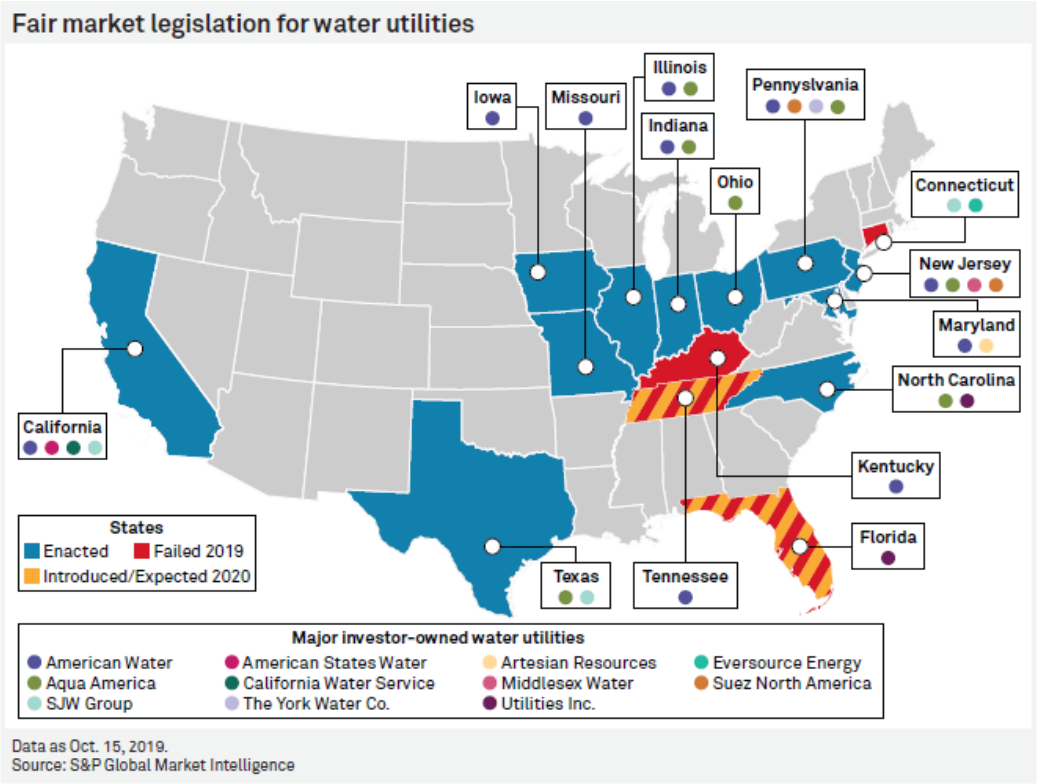
Exhibit 17: ... within a highly fragmented industry where of the 51,000 community water systems (CWS) only 4,221 or 8%, serve more than 246 million or 82%, of the total population.
State of the Water Industry - System size by population served



Source: Company data, Goldman Sachs Global Investment Research, AWWA, Environmental Protection Agency (EPA)

Exhibit 18: FMV legislation provides further impetus for consolidation in the sector and allows an accretive approach to valuing the acquired system's assets; currently in the books in 11 states and pending in 2 more states.
Fair Market Legislation for Water Utilities



Data as of Oct 25, 2019

Source: SNL

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What factors explain premium water valuations vs other regulated utilities?

Water utilities currently trade at a 30.2x FY2 P/E multiple, at a 11.3x premium to regulated electric/gas utilities trading at a 18.9x blended FY2 P/E multiple. Over the past few years, many investors had difficulty validating the valuation gap, questioning what level is justified. Fundamentally, we believe higher EPS/DPS growth trajectory, both historically and pro-forma, serves as the primary driver, with water utilities having grown EPS at a ~3%/2% CAGR above electric/gas utilities, respectively, over the past 10 years. The next task is determining how long water utilities can sustain this earnings gap, which we quantify in the following section. Below, we note a few factors (both quantitative and qualitative) that account for premium water valuations vs regulated electric detailed below:

Quantitative factors:

- **Longer asset life (D&A premium)** — Our analysis shows that every dollar invested in water assets yields a better return vs that for electric assets, driven by higher useful life (~20 years) extending the earnings potential. This D&A advantage translates into 2% in incremental EPS growth.
- **Continued robust capital program (Growth premium)** — As mentioned in the previous section, water IOUs have significant long-term investment opportunities (pipe replacement, treatment facilities, storage facilities, dams, wells and pumps), supported by favorable regulatory mechanisms to reduce lag in rate recovery. In addition, municipal acquisitions by IOUs continually add additional rate base backlog.

Qualitative factors:

- **Scarcity** — There are only a handful of investable water utilities for public investors. AWK, the largest water utility, has a market capitalization of more than $24 billion, and the remaining 11 investor-owned utilities have a combined market capitalization of just $22 billion. Trading volumes for the smallest water utilities average below 20,000 shares daily, which we believe could be beneficial for larger water IOUs like AWK and WTRG.
- **Take-out potential** — While initially slow, consolidation within the industry has accelerated during the past 30 years. Acquisitions by domestic and international utilities and by private equity has shrunk the group to just 12 investor-owned water utilities, while a handful of other large water utilities are owned by private equity investors. We attribute some of the relative premium of small-cap water utilities to take-out potential.
- **ESG focus** —Investor focus on ESG (environmental, social, governance) factors have increased meaningfully in recent years. While social and governance factors apply to many IOUs, pure-play water utilities satisfy the environmental factor, which could continue to support valuations. We note that AWK is a pure-play water utility, while WTRG now derives ~30% of its earnings from the recently acquired Peoples Gas business.

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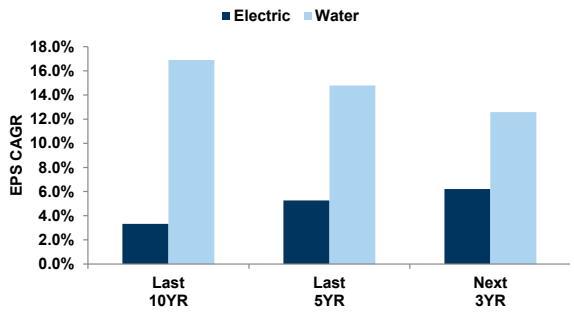
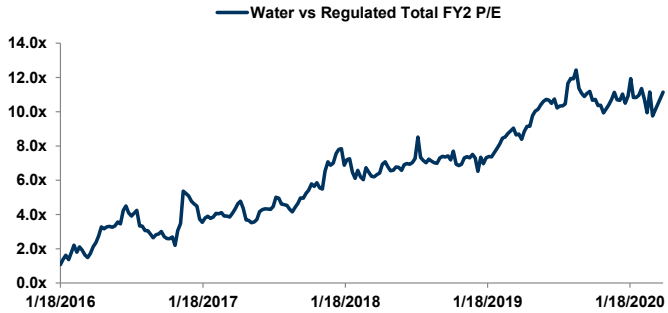
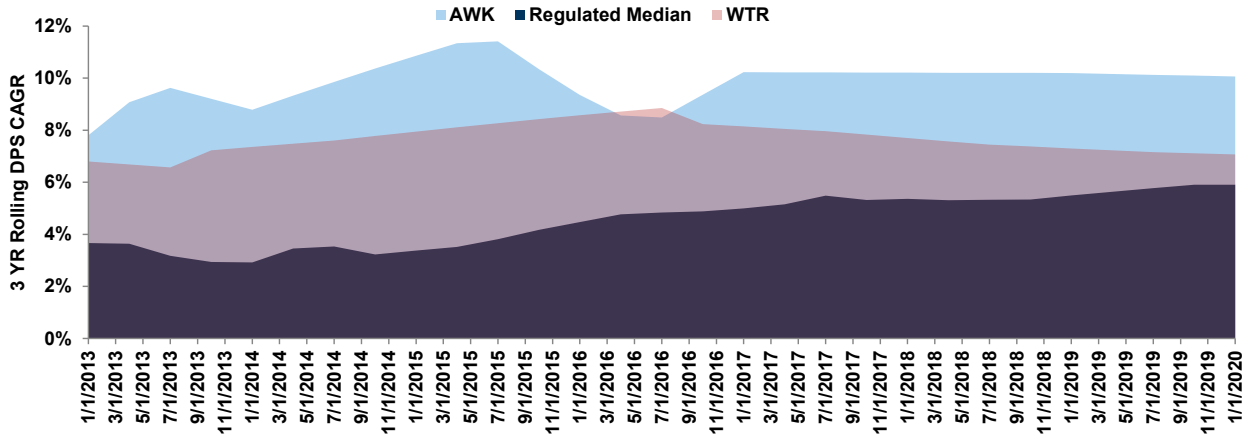
Exhibit 19: We note higher weighted average EPS growth CAGR for Water utilities vs Electric/Gas over the past 10 years have contributed to increasing relative premiums vs. Regulated Utilities...
Market cap weighted EPS Growth CAGRs - Water vs Electric; Water vs Regulated FY2 P/E





Source: Company data, Goldman Sachs Global Investment Research, FactSet

Exhibit 20: ... with AWK and WTRG consistently recording a DPS CAGR above regulated peers...
3 yr Rolling DPS CAGR



Source: Goldman Sachs Global Investment Research, FactSet

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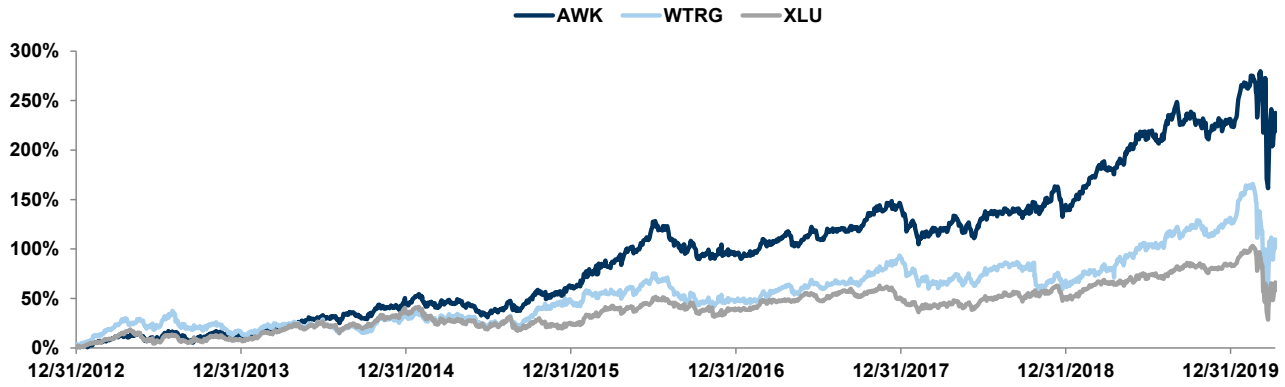
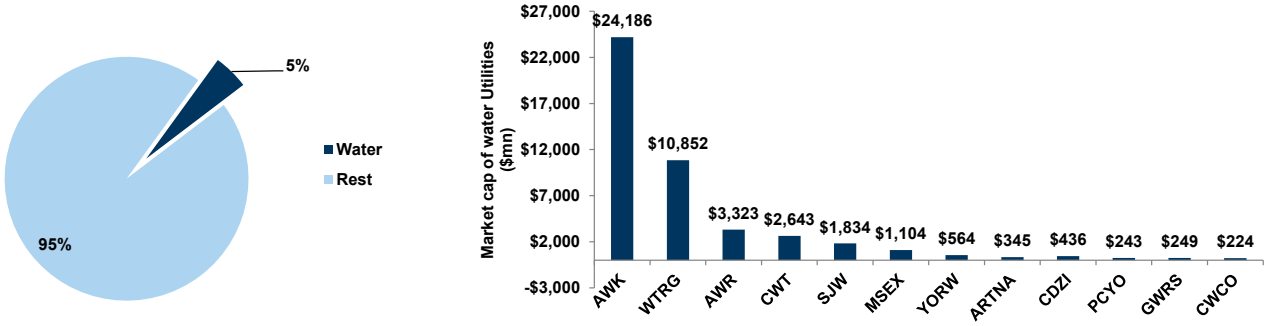
Exhibit 21: ... and rewarding investors with superior returns over the past 7 years vs the XLU
AWK/WTRG/XLU Performance since 2013



Source: Goldman Sachs Global Investment Research, FactSet

Exhibit 22: We note that the comparable group for Water companies remains limited, with 12 publicly traded water utilities in the US, including AWK and WTRG, and only 6 companies with a market capitalization in excess of $1 billion.
Water utilities market cap as % of total utilities market cap; Water utilities market cap ($mn)



Source: Goldman Sachs Global Investment Research, FactSet

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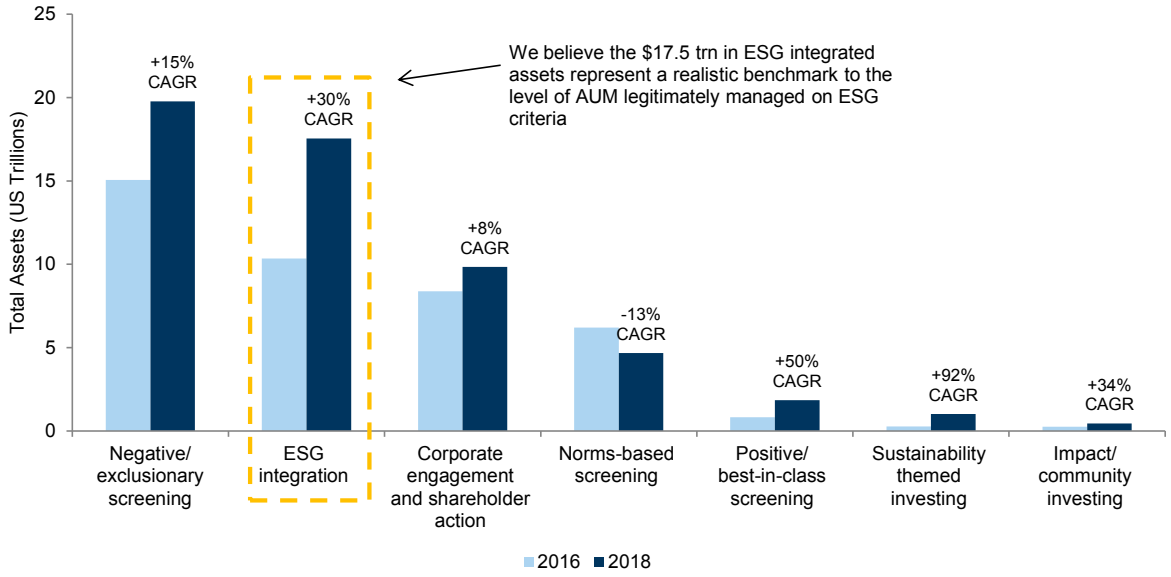
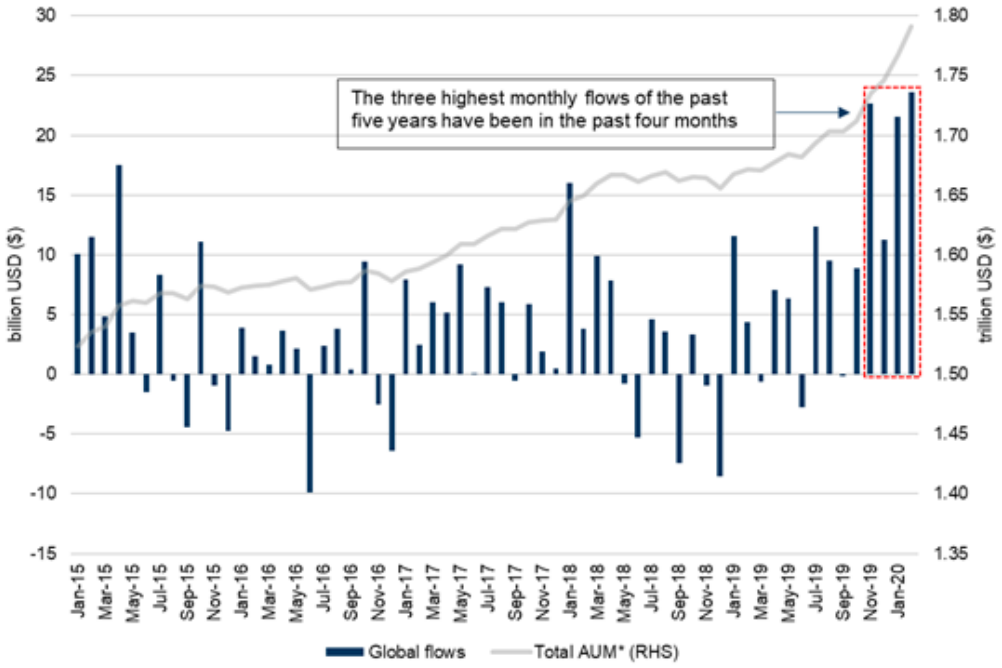
Exhibit 23: GS SUSTAIN: With ESG an increasingly important criteria for investors and fund flows...
Growth of investment assets incorporating ESG by type, including double counting (2016-2018)



Source: Global Sustainable Investment Alliance

Exhibit 24: ... that have remained robust through the early phases of the COVID-19 crisis (GS SUSTAIN)...
Monthly ESG fund flows (January 2015 through February 2020)



*AUM values are derived from historical flows and agnostic of market effects

Source: Morningstar

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Exhibit 25: ...we expect AWK's large-cap, pure-play water utility profile to benefit from ESG fund positioning.
AWK/WTRG Ranking based on ESG Relative overweight*

Top 10 ESG Relative overweight companies in US (April 2020)

	Company	GICS 1
1	NASDAQ INC ORD	Financials
2	XYLEM INC ORD	Industrials
3	IDEX CORP ORD	Industrials
4	EPAM SYSTEMS INC ORD	Information Technology
5	TRIMBLE INC ORD	Information Technology
6	UBER TECHNOLOGIES INC ORD	Industrials
7	GUIDEWIRE SOFTWARE INC ORD	Information Technology
8	PTC INC ORD	Information Technology
9	DENTSPLY SIRONA INC ORD	Health Care
10	VERISK ANALYTICS INC ORD	Industrials
14	**AMERICAN WATER WORKS COMPANY IN**	**Utilities**
21	**ESSENTIAL UTILITIES INC ORD**	**Utilities**

Top 10 ESG Relative overweight companies in US (Sept 2019)

	Company	GICS 1
1	Xylem Inc	Industrials
2	Trimble Inc	Information Technology
3	**Aqua America Inc**	**Utilities**
4	First Solar Inc	Information Technology
5	A.O. Smith Corp	Industrials
6	Hologic Inc	Health Care
7	**American Water Works Company Inc**	**Utilities**
8	Gap Inc	Consumer Discretionary
9	Toro Co	Industrials
10	First American Financial Corp	Financials

Companies with market caps > $5B and domiciled in US; *ESG Relative overweights are calculated by dividing a company's ESG fund universe ACWI constituent weighting over its ACWI weighting; ACWI= MSCI All Country Weight Index

Source: Bloomberg, Goldman Sachs Global Investment Research, Morningstar

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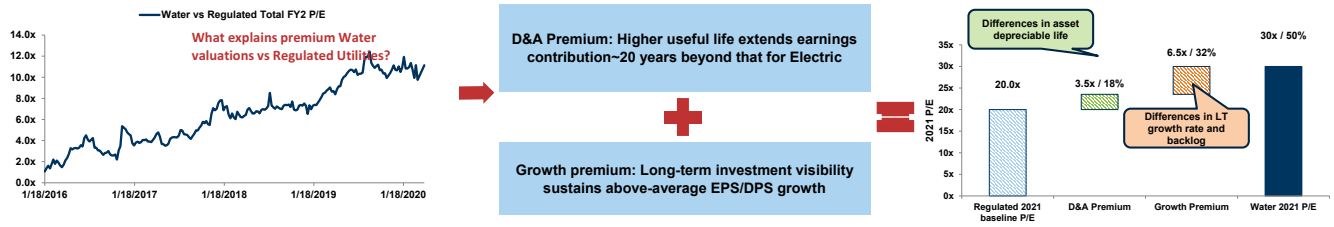
What premium do water utilities warrant?

Our analysis shows that water utilities deserve a meaningful P/E premium above electric utilities, with the current 11.3x premium largely justified.

We believe two quantifiable factors - D&A and investment growth - largely justify the current relative premium. We detail these calculations below.

Exhibit 26: We introduce our analysis on the earnings growth differential between water, electric and gas utilities, which we break into two components to arrive at our 30.0x baseline water multiple vs 20.0x baseline for our regulated coverage



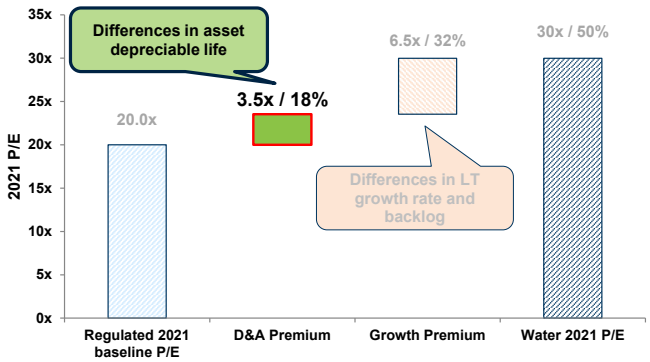
Source: Goldman Sachs Global Investment Research

1. D&A premium:

A higher useful life for water assets (50 years vs 30 years for electric) extends the earnings potential ~20 yrs beyond what that realized for electric assets, with earnings differential increasing steadily over time, warranting for a 17%/3.5x premium for each dollar invested in rate base.

Exhibit 27: We attribute around 18% (3.5x) of water utilities' current 57% (11.3x) premium vs Regulated Utilities to longer depreciable asset life for water assets

GS 2020 Water baseline multiple



Source: Goldman Sachs Global Investment Research

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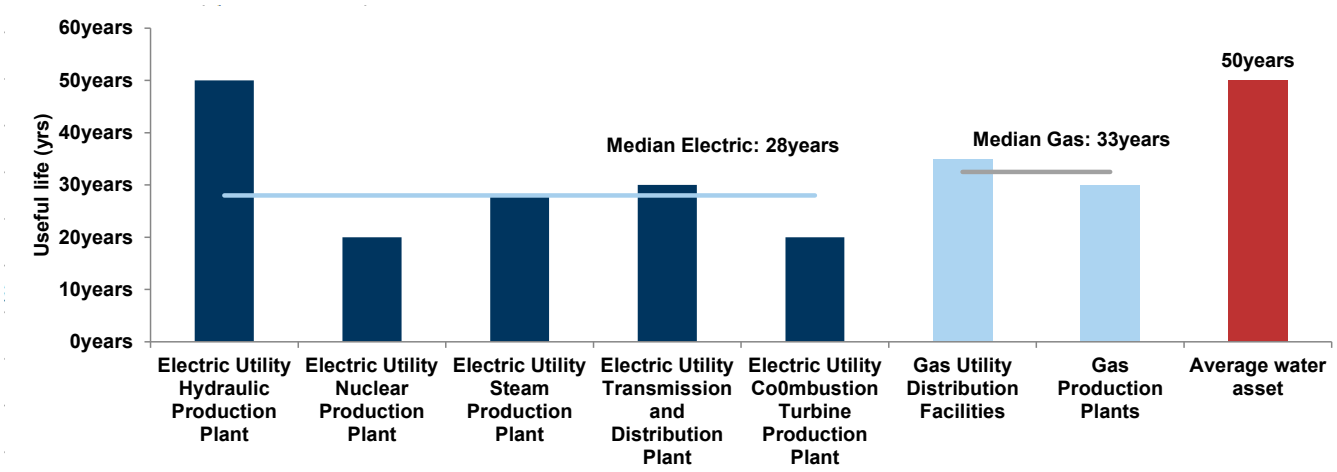
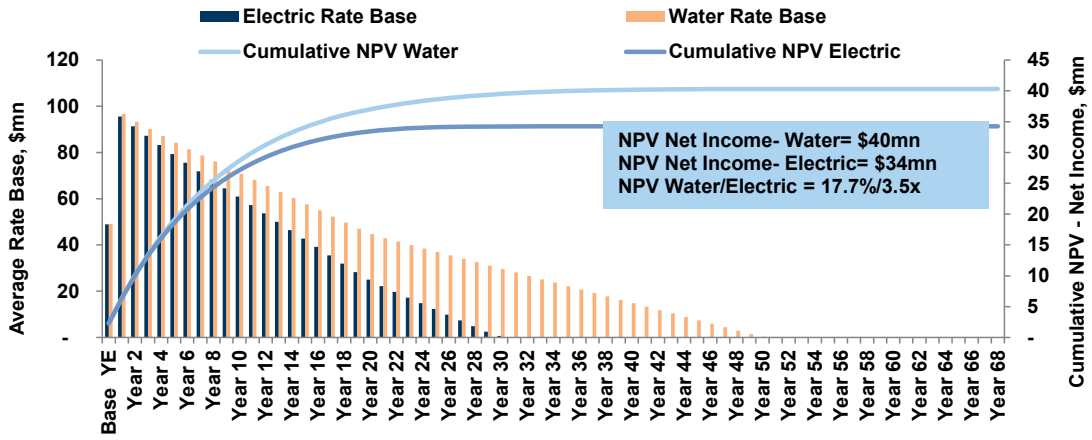
Exhibit 28: We note the useful life for the average water asset is ~20 years higher than that for electric/gas assets...
Asset Useful life by Subsector



Source: Thomson Reuters

Exhibit 29: ...which extends the asset's earnings potential for every $1 invested into regulated rate base...
Hypothetical average Rate Base/ Net Income ($mn) assuming an initial investment of $100mn and 30/50 yrs of useful life for an Electric/Water Utility



$100mn initial investment used for illustrative purposes

Source: Goldman Sachs Global Investment Research

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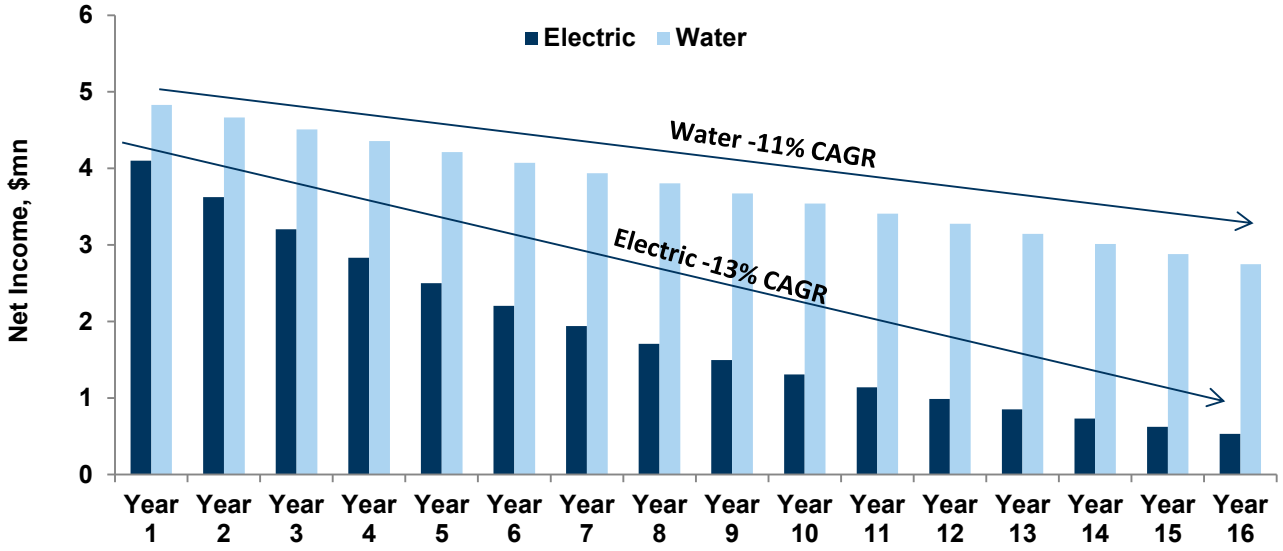
Exhibit 30: ...accounting for ~2% of incremental earnings CAGR for water vs electric...
Hypothetical average Rate Base/ Net Income ($mn) assuming an initial investment of $100mn and 30/50 yrs of useful life for an Electric/Water Utility

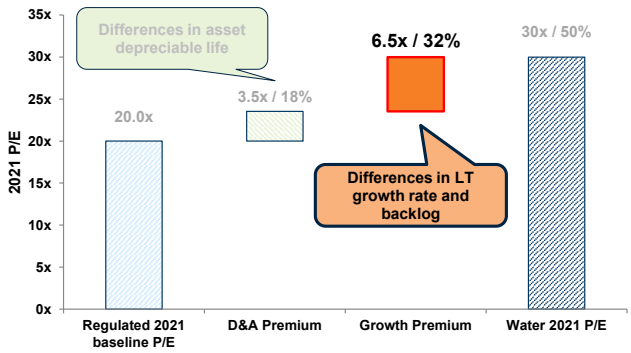


Source: Goldman Sachs Global Investment Research

2. Growth premium:

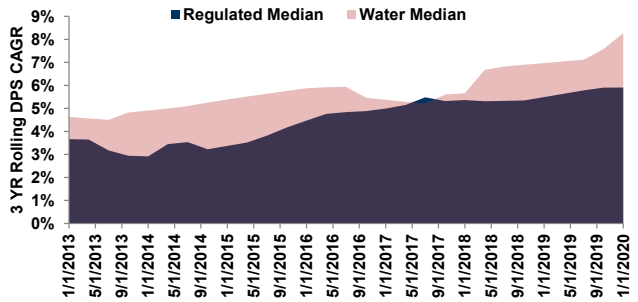
Even excluding the EPS advantage from D&A, we expect the water utility industry's significant investment backlog supporting continued above-average EPS growth (7% for water vs. 5% for electric) longer-term. We arrive at our 32%/6.5x premium based on a 15-year relative dividend-discount model (DDM), which we believe could prove conservative given AWWA's estimated $1 trillion in water pipe replacement needs through 2035.

Exhibit 31: We justify the remaining 32% (6.5x) premium based on significant water pipe investment needs that should sustain water utilities' higher EPS growth profile versus electric utilities
GS 2020 Water baseline multiple



Source: Goldman Sachs Global Investment Research

Exhibit 32: Given water utilities' ~3% higher DPS CAGR versus other regulated utility peers...
3 yr Rolling DPS CAGR



Source: Company data, Goldman Sachs Global Investment Research, FactSet

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Exhibit 33: ...we expect water utilities to continue growing EPS/DPS above other regulated utilities longer-term, even after excluding the D&A advantage

Growth premium for an average Water Utility based on DDM assuming a starting investment of $10,000mn, ke=8%, LT growth rate =4% and tax rate=26%

Year	Average Water Utility Dividend Growth rate (YR1-15 CAGR)	Water Dividend (mn)	Electric Dividend Growth rate (YR1-15 CAGR)	Electric Dividend (mn)
1	7.0%	$255	5.0%	$243
2	7.0%	$273	5.0%	$256
3	7.0%	$291	5.0%	$269
4	7.0%	$310	5.0%	$282
5	7.0%	$331	5.0%	$296
6	7.0%	$352	5.0%	$309
7	7.0%	$375	5.0%	$324
8	7.0%	$400	5.0%	$338
9	7.0%	$427	5.0%	$352
10	7.0%	$459	5.0%	$367
11	7.0%	$493	5.0%	$383
12	7.0%	$530	5.0%	$402
13	7.0%	$570	5.0%	$422
14	7.0%	$612	5.0%	$442
15	7.0%	$657	5.0%	$464
15+	4.0%	$17,087	4.0%	$12,058
NPV @ ke 8%		$8,671		$6,556

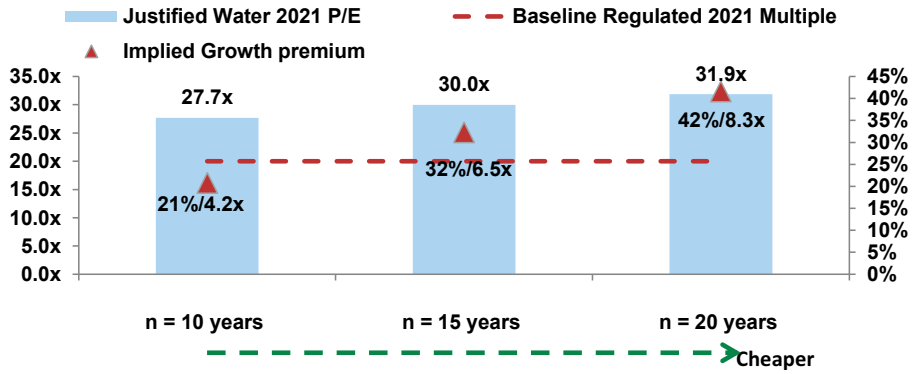
Implied Water Growth premium (post adjusting for D&A premium) =$8,671/$6,556 ~32%/6.5x

$10,000mn starting amount selected for illustrative purposes; ke, LT growth rate, and tax rate figures reflect normalized industry averages

Source: Company data, Goldman Sachs Global Investment Research

Exhibit 34: We note that our base case of 15 years growth at 7% growth could prove conservative given long-term visibility of water investment needs

Justified Growth Premium for Water vs Regulated Electric assuming High Growth stage of 10/15/20 years



n= High growth years, LT growth rate =4%

Source: Goldman Sachs Global Investment Research

Our revised 30.0x 2021 baseline multiple for water accounts for 3.5x/6.5x D&A/growth premium over the regulated baseline multiple of 20.0x.

We note that our analysis solely focuses on the longer useful life of water assets and higher growth opportunities to explain the premium water valuations; however, we note that qualitative drivers mentioned in the prior section - scarcity, take-out potential, ESG focus - could apply an additional layer of premium.

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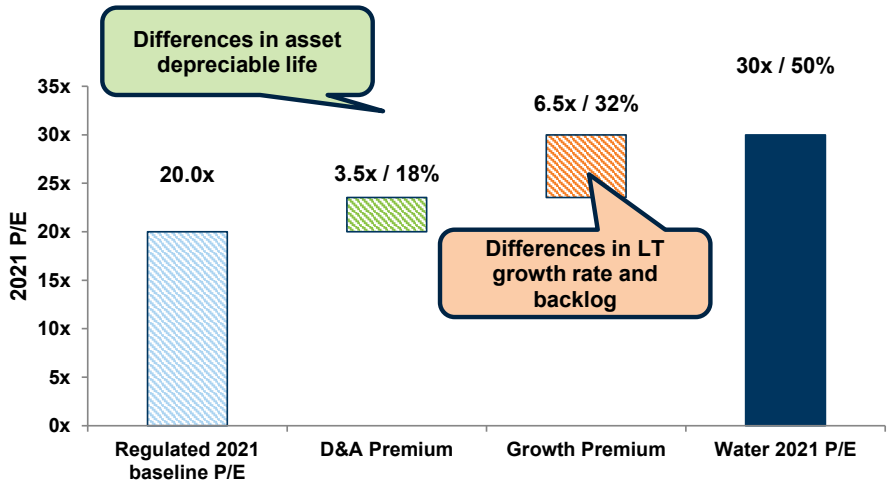
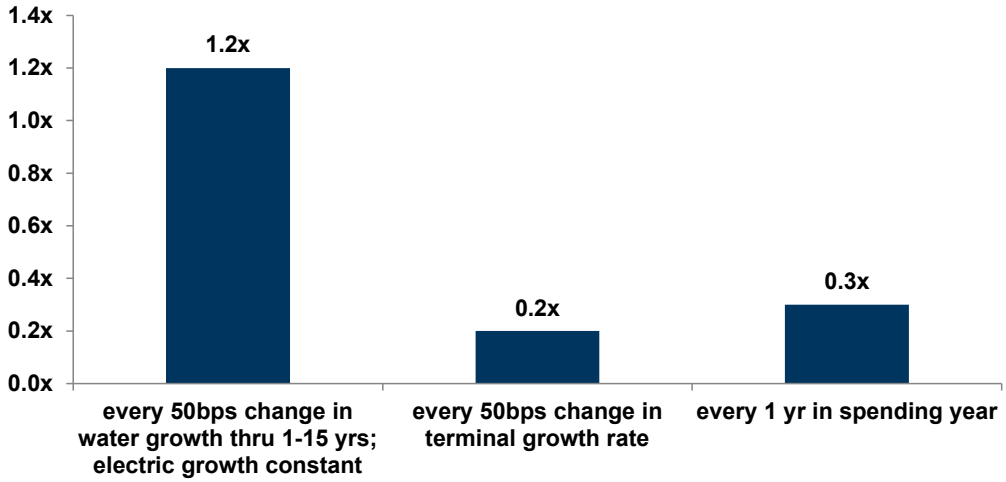
Exhibit 35: Accordingly, our revised 30.0x 2021 baseline multiple for water accounts for 3.5x/6.5x D&A/growth premium over the regulated baseline multiple of 20.0x...
Water 2021 baseline P/E vs Regulated



Source: Goldman Sachs Global Investment Research

Exhibit 36: ...while noting our analysis remains sensitive to changes in various assumptions
Premium sensitivity to change in growth rate (yr 1-15), terminal growth rate and spending years



AWK/WTRG both stand to benefit from robust investment backlog

We see both AWK and WTRG able to sustain their robust water rate base growth outlook for at least the next 15 years. The AWWA's estimated $1 trillion in water pipe replacement needs in the U.S. - through 2035 - could imply around $40bn/$10bn of investment backlog for AWK/WTRG based on their respective market share (by customer connections). Given $13.7bn/$5.0bn YE2019 rate base for AWK/WTRG, respectively, we believe the these investments could support 3x/2x in rate base by 2035, or a 6.5%/4.9% rate base CAGR. While this growth rate alone could signal a slowing of earnings growth power, we note this does not account for additional rate base opportunities from ongoing municipal acquisitions or investments in new

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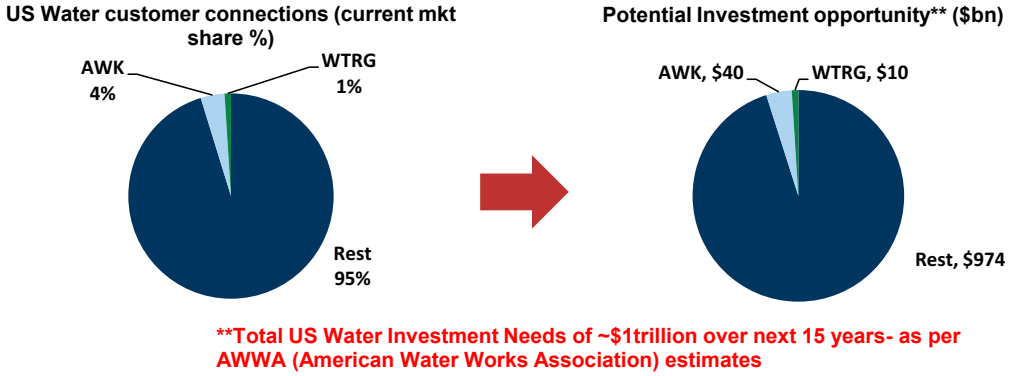
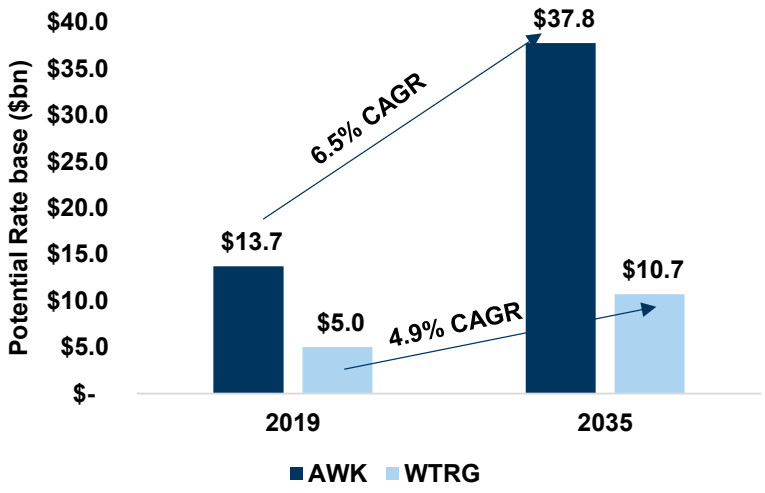
infrastructure, which we believe will continue to extend and expand organic investment opportunities. We view this long-term investment visibility as a key justifying factor for water utilities' relative premium valuations.

Exhibit 37: We see meaningful pipe replacement needs for both AWK/WTRG long-term...
Potential Investment Opportunity



Source: Company data, Goldman Sachs Global Investment Research, AWWA

Exhibit 38: ... that could support potential rate base growth of 6.5%/4.9% through 2035 for AWK/WTRG, not including potential upside from municipal acquisitions or new infrastructure spend
AWK/WTRG Potential rate base through 2035



Source: Company data, Goldman Sachs Global Investment Research, AWWA

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Upgrade AWK to Buy - Best-in-class growth, ESG-friendly profile justify premium

We view large-cap AWK's best-in-class 8.3% EPS growth, below-average beta, and its ESG-friendly profile as deserving of the highest premium valuation in our coverage universe and see 16% potential total return based on our $146 price target.

AWK	12m Price Target: $146	Price: $127.24			Upside: 14.7%
Buy	GS Forecast				
		12/19	12/20E	12/21E	12/22E
Market cap: $23.0bn	**Revenue ($ mn) New**	**3,610.0**	**3,800.8**	**3,992.0**	**4,175.0**
Enterprise value: $33.1bn	Revenue ($ mn) Old	3,610.0	3,800.8	3,992.0	4,175.0
3m ADTV :$187.1mn	EBITDA ($ mn)	1,752.0	1,947.1	2,097.8	2,240.3
United States	EBIT ($ mn)	1,170.0	1,335.6	1,443.7	1,544.3
America-Regulated Utilities:	**EPS ($) New**	**3.61**	**3.88**	**4.24**	**4.58**
	EPS ($) Old	3.61	3.88	4.24	4.58
M&A Rank: 3	P/E (X)	31.3	32.8	30.0	27.8
	Dividend yield (%)	1.7	1.7	1.9	2.0
	Net debt/EBITDA (X)	5.4	5.2	5.0	4.7
		12/19	**3/20E**	**6/20E**	**9/20E**
	EPS ($)	0.73	0.76	0.97	1.38

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 13 Apr 2020 close.

Source: Goldman Sachs Global Investment Research

We upgrade AWK from Neutral to Buy given 1) continued best-in-class earnings and dividend growth in our coverage universe, 2) long-term visibility of above-average growth from organic investments and municipal system acquisitions, 3) its ESG-friendly status as the only large-cap pure-play water utility, and 4) our updated target multiple and premium that imply a 16% total return.

We see a long runway of water infrastructure investment opportunities that should sustain AWK's above-average growth. The aging water and wastewater infrastructure in the United States is in need of replacement and modernization. In addition, increased regulation related to water quality and the management of water and wastewater residual discharges are also primary drivers for the need to modernize the country's water and wastewater infrastructure. We note AWK is well positioned to benefit from ~$40bn in potential investment over the next 15 years, given the company's ~4% market share (based on customers served) and AWWA's estimated $1 trillion in water investment needs. AWK already plans to invest almost $20 billion to the regulated utilities (pipe replacement, system upgrades) over the next 10 years, sustaining its 7-8% rate base CAGR target longer-term.

We expect municipal acquisitions continue to provide an additional growth layer. As mentioned in the previous sections, the water utility space is very fragmented, with the bulk of the customers in the U.S. still served by municipal utilities. With the majority of AWK's utility jurisdictions allowing fair market value (FMV) treatment for municipal acquisitions, we expect the company to continue its consistent acquisition track record

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that should contribute 1-2% of the 7-10% EPS CAGR guided range. Along with the inherent financial advantages of FMV, we note that acquisitions add incremental infrastructure investment opportunities to bolster AWK's rate base growth longevity.

AWK carries a stable balance sheet, improving through 2022. While we acknowledge AWK's relatively high ~60% debt/cap levels, management at the recent investor day announced plans to issue $500mn of equity at around the mid-point of the 2020-2024 investment plan. Our model continues to embed the $500mn issued by YE2022, resulting in a 58% debt/cap in 2022, and an improvement in FFO/debt from 15% in 2020 to 17% in 2022. Based on the current A/Baa1 credit rating, we do not anticipate any additional equity needs beyond the guided levels.

We keep our EPS estimates unchanged at $3.88/$4.24/$4.58 for 2020-2022 and see EPS growing at 8.3% CAGR from 2019-2022, at the mid-point of the company's 7-10% guidance range, contributed by 7-8% from regulated utilities and 1% from the market based business. Primary drivers of growth continue to include robust capital investments, customer growth (both organic and via municipal acquisitions), O&M management, with some dilution in 2022 from the $500mn equity issuance. We continue to assume 10% annual dividend through 2022, resulting in a 55%-57% payout.

We raise our 12-month price target to $146 (from $134 previously) derived using a 34.5x 2021E P/E multiple (vs 31.5x prior). Our revised P/E multiple incorporates our new water base P/E multiple of 30.0x (calculated in prior sections), as well as a 3x (10%) premium to account for AWK's above-average growth and favorable ESG profile. While the water utility peer group is fairly limited, AWK is currently trading at a 30.0x P/E on 2021E, largely in-line with peers. We believe AWK should trade at the highest multiple among water utilities and relative to our overall coverage universe.

Key downside risks include 1) water quality issues that result in customer health risks, leading to significant financial and regulatory impact, 2) inability to consistently manage operating costs, 3) unfavorable turn in regulatory environment that negatively impacts robust earnings growth potential, 4) lower-than-expected growth at the non-regulated segments, which lowers AWK's best-in-class growth rate, and 5) reduced ESG fund flows that impact further multiple expansion as investors turn to other qualifying investments.

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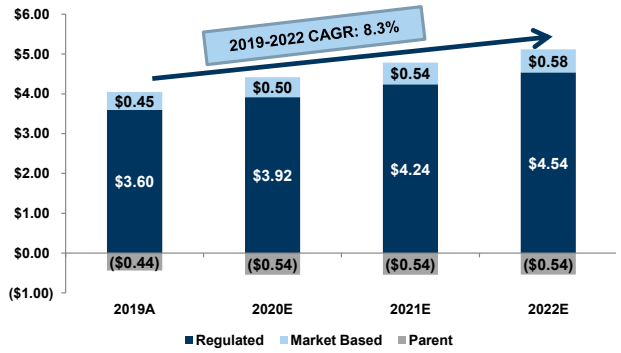
Exhibit 39: We keep our EPS estimates unchanged at $3.88/$4.24/$4.58 for 2020-2022 ...
GS new vs. old vs. consensus, 2019E-2022E

	EPS Estimates			% Difference	
	New	Old	Consensus	vs Old	vs Consensus
2020E	$3.88	$3.88	$3.85	0%	1%
2021E	$4.24	$4.24	$4.23	0%	0%
2022E	$4.58	$4.58	$4.56	0%	0%

Source: Goldman Sachs Global Investment Research, FactSet

Exhibit 40: ...reflecting 8.3% growth CAGR over 2019-2022...
EPS by segment, 2019A-2022E



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 41: We raise our TP to $146 using a 34.5x P/E multiple (vs 31.5x previously) using our revised base water multiple and a growth/ESP premium...
AWK Valuation

AWK Valuation	
AWK 2021 EPS	**$4.24**
GS Water Utility Base Multiple	30.0x
Premium / (Discount)	4.5x
Adjusted P/E	**34.5x**
Utility Valuation	**$146**
AWK Valuation	**$146**
Current Stock Price	$127.24
Price Return Potential	14.7%
Dividend Yield	1.4%
Total Return Potential	**16%**

Source: Goldman Sachs Global Investment Research

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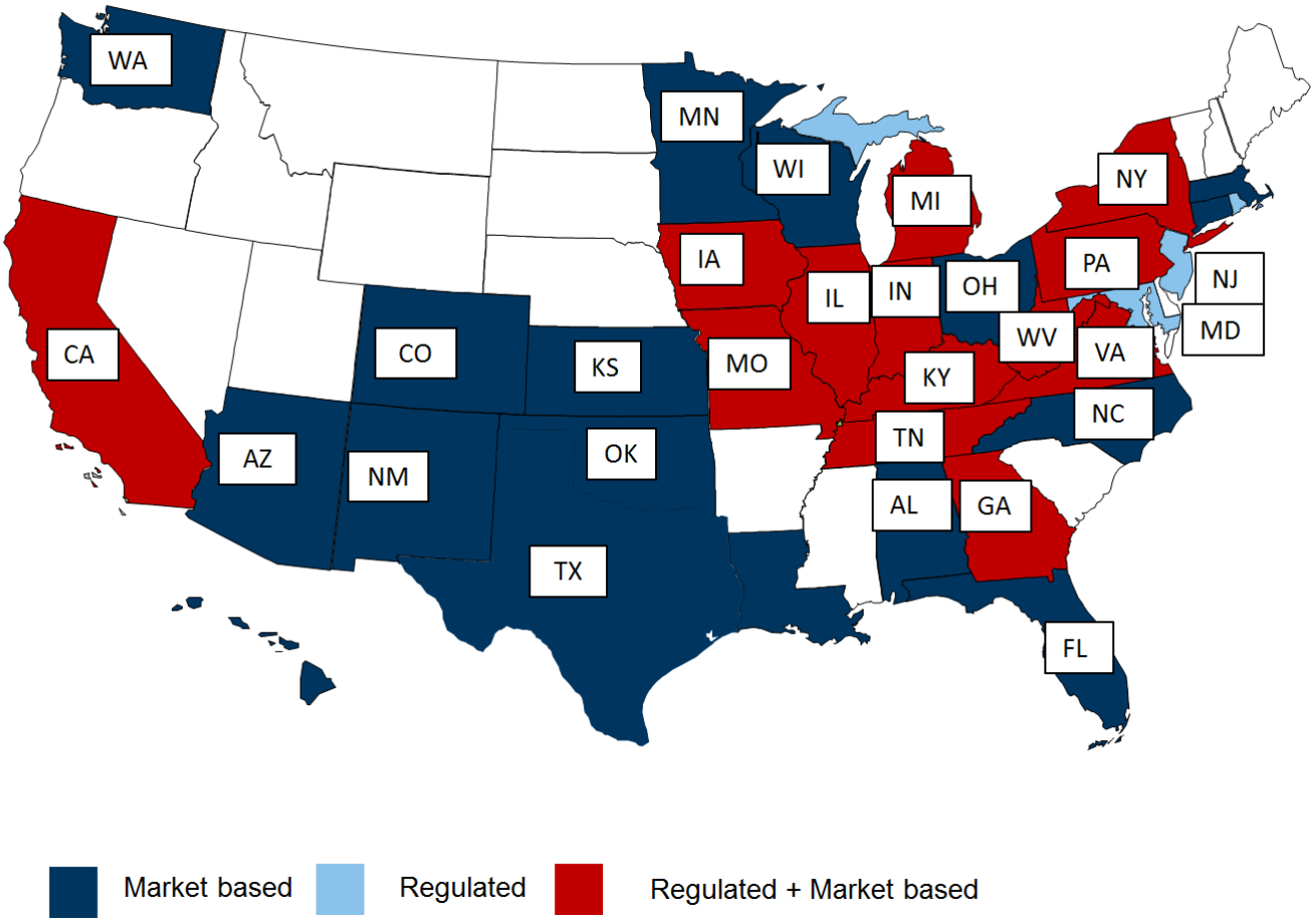
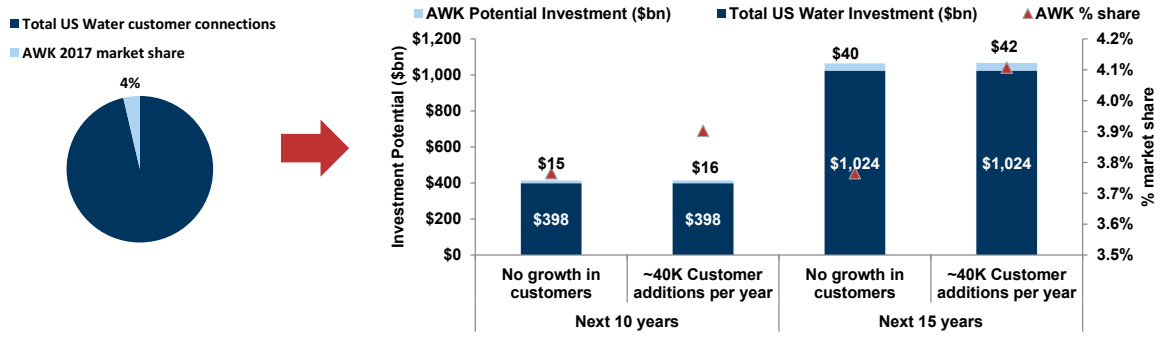
Exhibit 42: We see an impressive growth pipeline for AWK given its Regulated business presence in 16 U.S. states providing water and wastewater utility services to residential, commercial, industrial customers...
AWK Geographical footprint



*sale of NY Utility announced in 2019, currently not factored in our estimates

Source: Company data, Goldman Sachs Global Investment Research

Exhibit 43: ...and potential investment opportunity of ~$40bn over the next 15 years with potential upside from organic/inorganic customer additions.
AWK Potential Investment Opportunity



Source: Company data, Goldman Sachs Global Investment Research, AWWA

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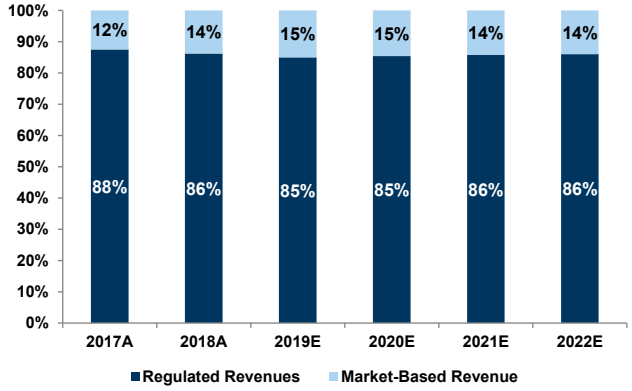
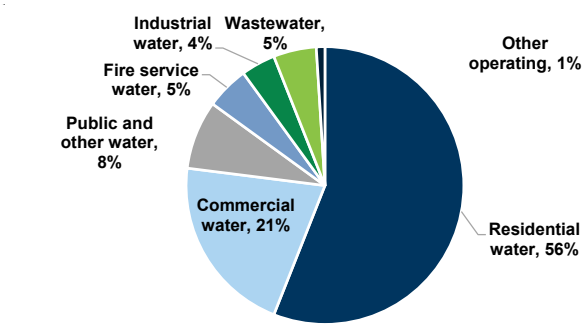
Exhibit 44: In addition to American Water's core regulated franchise, AWK owns and operates complementary water-related businesses with medium to long-term contracts, with low capital requirement fueling positive cash contribution
Regulated vs Unregulated Revenue mix (%)



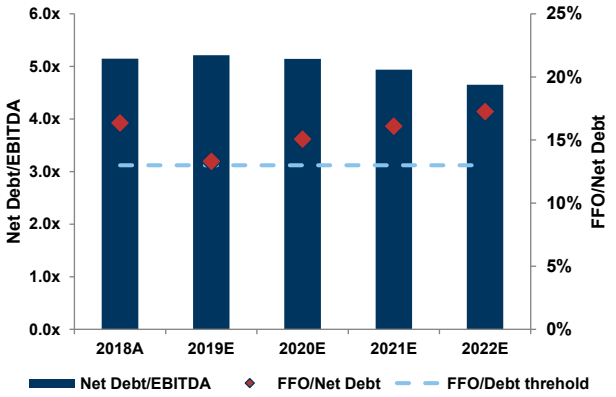
Source: Company data, Goldman Sachs Global Investment Research

Exhibit 45: AWK's regulated revenue base consists of 56% residential, 21% commercial and just 4% industrial
AWK Regulated Operating Revenue by customer class



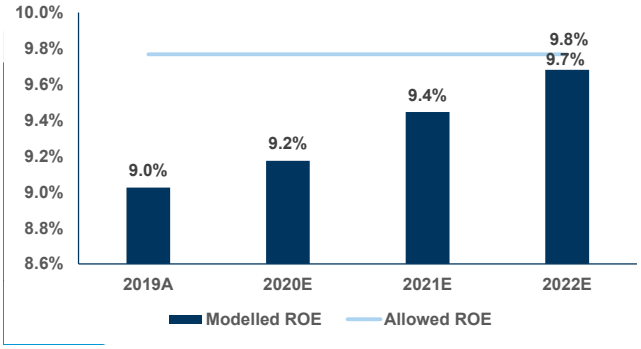
Source: Company data, Goldman Sachs Global Investment Research

Exhibit 46: We see FFO/debt improving through 2022, aided by $500mn of equity issuances across 2021-2022...
Net Debt/ EBITDA & FFO/Debt 2018A-2022E



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 47: ...and with AWK earning close to allowed by 2022
Earned vs Allowed ROE 2019A-2022E



Source: Company data, Goldman Sachs Global Investment Research

Company Overview

American Water Works (AWK), remains the largest publicly traded US water utility at more than $24bn in market cap, provides more than 14 million people with drinking water, wastewater and water-related services in almost 45 US states and 2 Canadian provinces. The company operates two divisions: (1) the Regulated segment, representing 86% of 2019 revenues and (2) the Market Based Operations segment, which comprises the remaining 14%. The key states served by AWK's regulated utilities are summarized in Exhibit 48.

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Exhibit 48: AWK's regulated segment exposure is distributed across sixteen states with bulk of earnings from seven states
State utility commission regulatory snapshot

AWK Regulatory Profile	New Jersey	Pennsylvania	Missouri	Illinois	California	Indiana	West Virginia
Commission Name	New Jersey Board of Public Utilities	Pennsylvania Public Utility Commission	Missouri Public Service Commission	Illinois Commerce Commission	California Public Utilities Commission	Indiana Utility Regulatory Commission	Public Service Commission of West Virginia
No. of Commissioners	5 of 5 (3 D, 2 R)	5 of 5 (3 D, 2 R)	5 of 5 (2 D, 3 R)	5 of 5 (1 D, 2 R, 2 Non-Partisan)	5 of 5 (5 D)	5 of 5 (3 D, 2 R)	3 of 3 (2 R, 1 D)
Test year for Rate Case	Historical test year	Future test year	Historical test year	Future test year	Future test year	Future test year	Historical test year
Infrastructure replacement surcharges	Yes	Yes	Yes	Yes	No	Yes	Yes
Revenue Stability mechanisms	No	No	No	Yes	Yes	No	No
Expense mechanisms	Yes	Yes	Yes	Yes	Yes	No	No
Utility plant recovery mechanisms	No	Yes	No	Yes	Yes	No	No
GS view on Regulation	Somewhat Restrictive	Constructive	Somewhat Restrictive	Constructive	Balanced	Somewhat Restrictive	Restrictive
Fair Market Legislation (FMV)	Yes	Yes	Yes	Yes	Yes	Yes	No
Company 2018 Revenue Exposure	AWK-24%	AWK-23%	AWK-10%	AWK-10%	AWK-7%	AWK-7%	AWK-5%

Infrastructure Replacement surcharges: Allows rates to change periodically, outside a general rate case proceeding, to reflect recovery of capital investments made to replace infrastructure necessary to sustain safe, reliable services for our customers. These mechanisms typically involve periodic filings and reviews to ensure transparency.
Utility plant recovery mechanisms: Allows recovery of the full return on utility plant costs during the construction period, instead of capitalizing an allowance for funds used during construction. In addition, some states allow the utility to seek pre-approval of certain capital projects and associated costs. In this pre-approval process, the PUC may assess the prudency of such projects.
Expense mechanisms: Allows changes in certain operating expenses, which may fluctuate based on conditions beyond the utility's control, to be recovered outside of a general rate case proceeding or deferred until the next general rate case proceeding.
Revenue stability mechanisms: Separates a utility's cost recovery from the amount of water it sells to recover its fixed costs and ongoing infrastructure investment needs. Such a mechanism adjusts rates periodically to ensure that a utility's revenue will be sufficient to cover its costs, regardless of sales volume, including recognition of declining sales resulting from reduced consumption, while providing an incentive for customers to use water more efficiently.
Future test year: A test period used for setting rates, which begins with the date new rates are effective. This allows current or projected revenues, expenses and capital investments to be collected on a timelier basis.
Fair Market Legislation(FMV): Allows regulated water companies to pay a fair market value for the purchase of water and wastewater systems. Before these changes, system values were determined by their depreciated original cost, which generally did not reflect a reasonable market value for those assets and became a barrier to a sale.

Source: SNL Financial, Company reports, Goldman Sachs Global Investment Research

In addition to American Water's core regulated franchise, AWK owns and operates complementary water-related businesses as part of its Market-based segment which include:

The Homeowner Services Group- which provides warranty protection programs to residential and smaller commercial customers to protect against repair costs for interior and exterior water and sewer lines, interior gas and electric lines, heating and cooling systems, water heaters and other home appliances, as well as power surge protection and other related services. The current porfolio includes the June 2018 acquisition of Pivotal Home Solutions, which increased the segment's customer base from 0.9mn to 1.5mn. The company also partners with municipalities, utilities and other organizations to offer protection programs to customers serviced by, or affiliated with, those municipalities, utilities and organizations. The term of these partnership agreements is typically three to five years, with mutual optional renewals; each customer generates around $20-$40mn of net income for this segment, which reflects around half or more of AWK's 14% market-based earnings. As of YE2019, the Homeowner Services Group had approximately 3 million customer contracts in 43 states.

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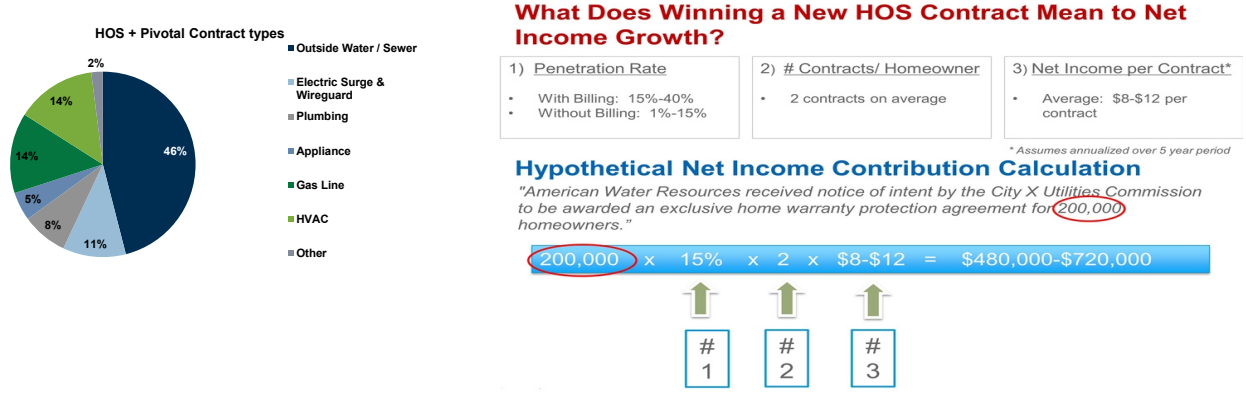
Exhibit 49: The Homeowner Services Group houses ~3 million contracts in 43 states, with a potential market opportunity of 30mn contracts...
Homeowner services business profile



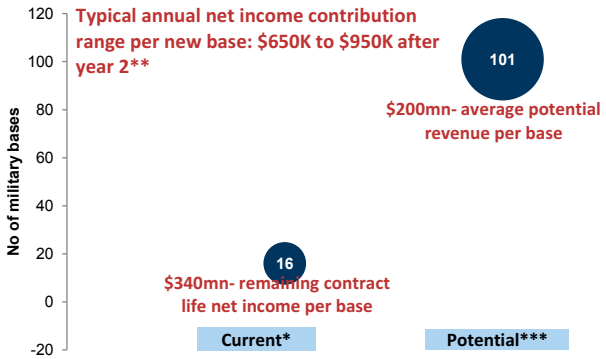
Source: Company data, Goldman Sachs Global Investment Research

Military Services Group - provides water and wastewater services to the U.S. government on military installations; operates on 16 military installations under 50-year contracts with the U.S. government as part of its Utility Privatization Program. The scope of these contracts generally includes the operation and maintenance of the installation's water and wastewater systems and a capital program focused on asset replacement and, in certain instances, systems expansion. The backlog of revenue associated with the current U.S. government contracts is approximately $4.3 billion, with an average remaining contract term of 42 years.

Exhibit 50: The Military Services Group generates stable revenues via 30-50 year contracts, with significant market expansion opportunities
Military services business profile

	Contract	Division	Contract Years remaining
1	Fort Sill	Army	35
2	Fort Leavenworth	Army	35
3	Fort Rucker	Army	36
4	Fort AP Hill	Army	39
5	Scott AFB	Air Force	39
6	Fort Hood	Army	40
7	Fort Polk	Army	40
8	Fort Belvoir	Army	41
9	Fort Meade	Army	42
10	Hill AFB	Air Force	46
11	Picatinny Arsenal	Army	46
12	Vadenberg AFB	Air Force	48
13	Wright- Patterson AFB	Air Force	50
14	Fort Leonard Wood	Army	50

2 more added in 2018-2019 as per latest 10K



*as per 2019 10K, ** as per Dec 2019 analyst presentation, ***as per Dec 2015 presentation

Source: Company data, Goldman Sachs Global Investment Research

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Initiate WTRG at Neutral – Robust water/gas growth already reflected in SOTP

While we see Aqua's recent acquisition of Peoples Gas providing upside to rate base and EPS growth longer-term, we view current valuations fairly crediting this growth in addition appropriately reflecting the company's water/gas utility mix (versus pure-play water prior). Our $45 price target implies an 7% total return versus 15% for Regulated Utilities.

WTRG	12m Price Target: $45	Price: $42.8			Upside: 5.1%
Neutral	GS Forecast				
		12/19	12/20E	12/21E	12/22E
Market cap: $9.2bn	**Revenue ($ mn) New**	**889.7**	**1,619.4**	**2,052.0**	**2,167.9**
Enterprise value: $14.9bn	Revenue ($ mn) Old	--	--	--	--
3m ADTV :$68.6mn	EBITDA ($ mn)	521.4	815.6	1,028.4	1,122.2
United States	EBIT ($ mn)	360.8	581.1	731.8	799.9
America-Regulated Utilities:	**EPS ($) New**	**1.47**	**1.56**	**1.65**	**1.78**
	EPS ($) Old	--	--	--	--
M&A Rank: 3	P/E (X)	27.6	27.5	26.0	24.0
	Dividend yield (%)	2.2	2.2	2.4	2.6
	Net debt/EBITDA (X)	2.3	7.0	6.2	6.2
		12/19	3/20E	6/20E	9/20E
	EPS ($)	0.29	0.57	0.17	0.27

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 13 Apr 2020 close.

Source: Goldman Sachs Global Investment Research

We initiate coverage on Essential Utilities, Inc. (WTRG) - formed by the merger of Aqua America and Peoples Gas - at Neutral with a 12-month price target of $45. We view the 9+% combined rate base growth (including municipal acquisitions) driving a robust 6.6% EPS CAGR from 2019A-2022E. However, we view current valuation already reflecting these positive qualities, with just 7% total return based on our water/gas SOTP price target, versus 15% for Regulated Utilities.

Peoples Gas acquisition provides additional growth...

Peoples Gas acquisition elevates rate base growth profile. We see 10%+ rate base growth at Peoples Gas from 2019A-2022E primarily driven by long-term visibility of pipeline replacement projects. We note that Peoples has identified more than 2,700 miles of bare steel and cast iron pipe to be replaced under its Long-term Infrastructure Improvement Plan (LTIIP) by 2034 in its PA service territory, which at ~180-200 miles/year of pipe replacement, implies more than 15 years of increased capital spending to support around 9% rate base CAGR during the period. Along with the majority of these investments eligible for distribution system improvement charge (DSIC) that help reduce regulatory lag, we expect Peoples Gas to benefit from favorable tax election, as detailed below.

Tax repairs election should help maintain robust EPS growth while providing incremental funding for investments. WTRG plans to elect tax repairs for Peoples

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Gas' PA utility, which comprises more than 90% of the gas customer base. **What is tax repair?** It essentially allows the company to expense certain utility asset improvement costs that were previously capitalized and depreciated for book and tax purposes. For PA, which allows flow-through accounting, the utility is able to keep the incremental earnings and cash from the lower tax rate (still collected in customer bills at the higher tax rate), supporting financing needs while reducing rate case cycles. We note WTRG's PA water utility elected tax repairs in 2012 (now expired), which enabled it to record robust earned ROEs while staying out of a rate case for almost 10 years. For the gas utility, we expect WTRG to allocate qualified assets over a longer investment period, reducing the sudden jump in earnings growth recorded when implemented for the water utility. Our model embeds ~10.5% earned ROEs for Peoples Gas through 2022 versus 10.2% allowed, reflecting the tax repairs benefit.

We expect merger synergies to benefit EPS through 2022. With the bulk of the Peoples Gas service jurisdictions - Pennsylvania - sitting on top of Aqua America's PA water utility area, we expect the combined company to benefit from merger synergies related to various operations and system integration. Our model embeds 5% of combined O&M as acquisition synergies, resulting in flat to 1% O&M CAGR from 2019A-2022E for both water and gas utilities.

...to a fundamentally robust water growth story

We expect combined 9.7% water rate base CAGR (including acquisitions) from 2019-2022 driven by a robust organic capital program... The water sector is extremely capital intensive, given its extensive pipe and main infrastructure system as well as treatment facilities, storage facilities, dams, wells and pumps. As shown in Exhibit 37, the American Water works Association's (AWWA), most recent estimates about $1 trillion will be needed in the next 15 years to upgrade the country's water systems, both public and private, to meet environmental standards. At the Water business, we expect ~$400-$500mn in capital spending each year underlying the company's 7% rate base growth CAGR.

...as well as growth via municipal transactions supported by FMV legislation. Given the fragmented nature of the water utility industry, as detailed in the prior sections of this note, we expect WTRG to continue its robust municipal acquisition strategy to support and sustain its growth. The vast majority of WTRG's jurisdictional states currently allow fair market value (FMV) accounting that should provide continued incentive for acquisitions. In 2018, Essential Utilities closed 6 municipal acquisitions, adding more than 13,700 customers and more than $100 million of rate base. In September 2019, the company entered into a purchase agreement to acquire the wastewater utility system assets of the Delaware County Regional Water Quality Control Authority ("DELCORA"), which consists of approximately 16,000 customers in 42 municipalities in Southeast Pennsylvania for $276,500. If approved by the Pennsylvania Public Utilities Commission (PUCO), this acquisition would be the largest water and wastewater deal in state history. We note that every $100 million in rate base from acquisitions that are added through municipals contributes ~$5 million in earnings, or $0.02 in EPS.

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Relatively stable balance sheet, although somewhat levered given Peoples acquisition

Following the Peoples Gas acquisition, we see WTRG maintaining around 50% debt/cap through 2022, along with FFO/debt at ~12% during the period. We note S&P's "A" issuer credit rating targets FFO/debt to remain at or above 12% longer-term, with sustained lower levels a potential risk for a downgrade. In addition, we note around 25-30% of debt resides at the parent, somewhat elevated in our view. However, we believe a one-notch credit downgrade would still place WTRG's rating around the utilities average; we do not see this as a meaningful risk.

Will ESG momentum continue post gas integration?

In recent years, the water industry has seen increased interest from ESG investors contributing to a significant expansion of water premium vs the average electric/gas multiple. During the period from 2014 to 2017, water utilities traded at an 11% to 28% premium to the regulated group. This premium expanded in 2018 and 2019 with the water premium currently at a 58% premium to the average regulated multiple. WTRG's premium also expanded from 19% in 2017 to 34% in 2019. However, we believe that a change in WTRG's profile from a pure play water utility to a gas/water utility could prove to be a headwind to this premium expansion going forward, in addition to investors' utilization of a more SOTP valuation approach (utilized in deriving our price target).

Robust growth largely priced in - Initiate Neutral

Our $45, 12-month price target is based on an SOTP valuation methodology. Our 2020-2022E EPS estimates of $1.56/$1.65/$1.78 reflects a 6.6% CAGR from 2019-2022E, with potential upside to growth beyond 2022 as WTRG reduces regulatory lag on both organic investments as well as added rate base from municipal acquisitions. To arrive at our SOTP-based price target, we apply our new 30x base water target P/E multiple to 2021E EPS for the water utility segment, along with a 22x P/E multiple to 2021E EPS for the gas utility segment. Our gas multiple reflects a 10% (or 2x) premium to our 20x base gas target P/E, which reflects above-average rate base and EPS growth, as well as our constructive view of PA regulation (which makes up over 90% of the gas utility customer base).

We view WTRG's current valuation as fairly representing the company's water/gas utility mix, with our $45 target reflecting a 27.3x P/E, a discount our 30x base water target P/E for pure-play water utilities like AWK. **Upside risks to our call** include: 1) Peoples Gas acquisition synergies exceed our expectations, elevating EPS growth profile, 2) tax repairs election for the PA gas utility elevates earned ROEs even above our estimate, and 3) WTRG continues to benefit from ESG fund flows, despite its water/gas utility mix profile on a pro-forma basis. **Downside risks to our call** include: 1) PA regulation turns less constructive, 2) growth from municipal acquisitions slows, and 3) WTRG credit rating is downgraded.

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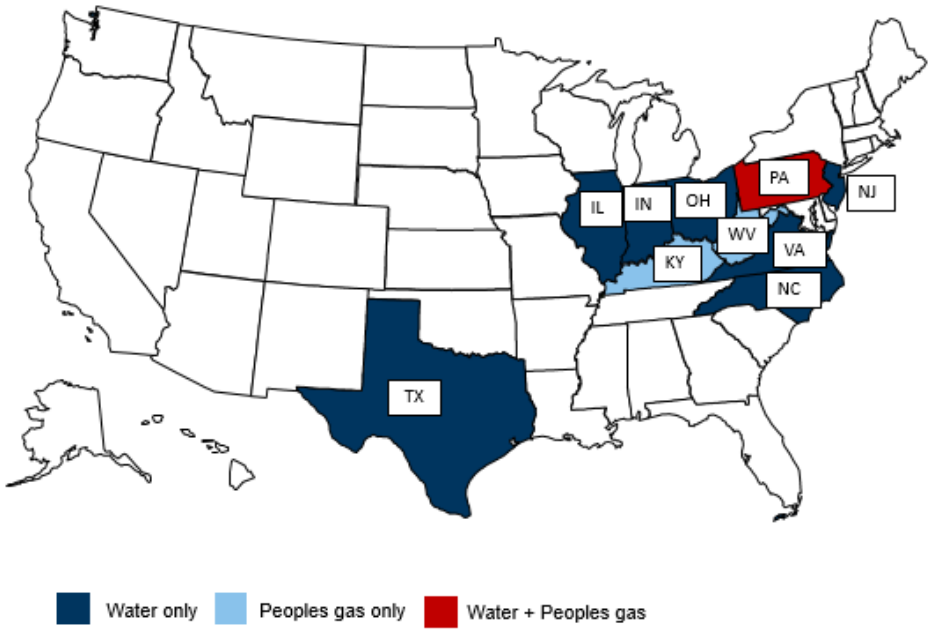
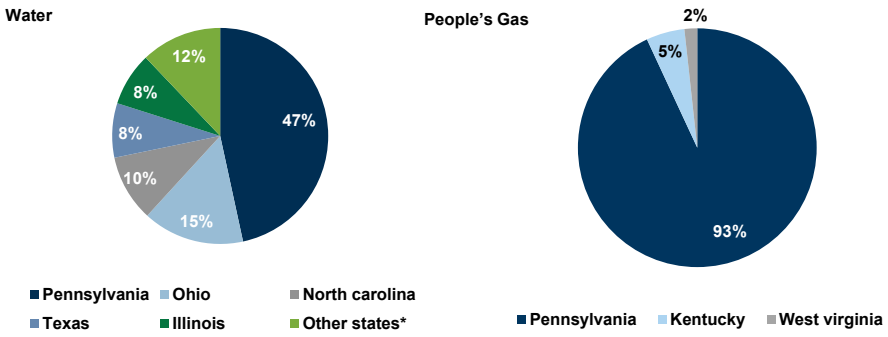
Exhibit 51: Essential Utilities is a Pennsylvania-based water and natural gas infrastructure company with a 10 state footprint...
Water + People's Gas Operating states for combined Essential Utilities



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 52: ... with combined 1.7 million regulated customers (1mn - water + 0.7mn gas), with PA as the biggest jurisdiction
Customer distribution across states Aqua + People's Gas



* Other states include New Jersey, West Virginia and Indiana

Source: Company data, Goldman Sachs Global Investment Research

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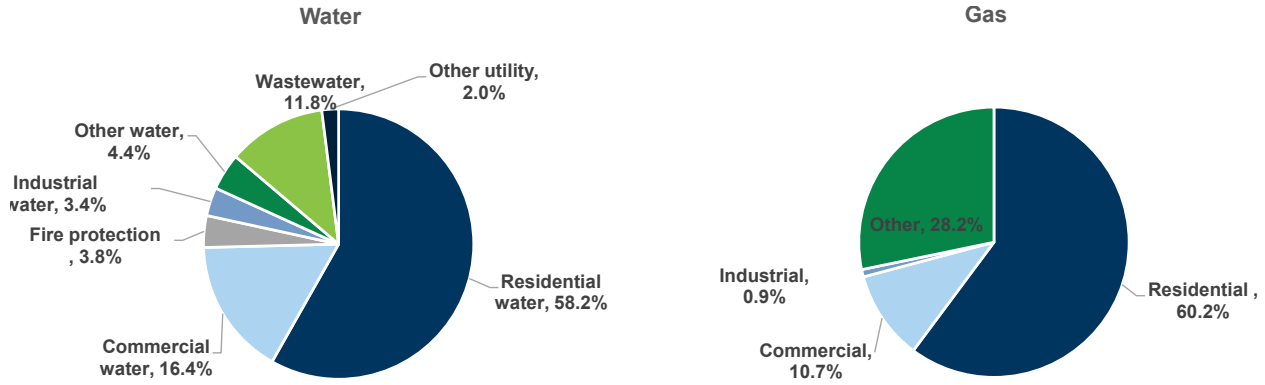
Exhibit 53: Residential revenues make up the bulk of both water and gas revenues...
Operating Revenue (2019) mix at the water/gas business by customer type



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 54: ... situated largely in constructive or balanced regulatory jurisdictions, especially its largest utility in PA.
State utility commission regulatory snapshot

WTRG Regulatory Profile							
	Pennsylvania	**Ohio**	**Illinois**	**Texas**	**North Carolina**	**Kentucky**	**West Virginia**
Commission Name	Pennsylvania Public Utility Commission	Public Service Commission of Ohio	Illinois Commerce Commission	Public Service Commission of Texas	North Carolina Utilities Commission	Kentucky Public Service Commission	Public Service Commission of West Virginia
No. of Commissioners	5 of 5 (3 D, 2 R)	5 of 5 (1 D, 2 R, 2 Non-Partisan)	5 of 5 (1 D, 2 R, 2 Non-Partisan)	3 of 3 (3 R)	4 of 7 (3 D, 1 R)	3 of 3 (3 R)	3 of 3 (2 R, 1 D)
Test year for Rate Case	Future test year	Historical test year	Future test year	Historical test year	Historical test year	Historical test year	Historical test year
Infrastructure replacement surcharges	Yes	Yes	Yes	No	Yes	Yes	Yes
Revenue Stability mechanisms	No	No	Yes	No	No	No	No
Expense mechanisms	Yes	Yes	Yes	Yes	Yes	Yes	No
Utility plant recovery mechanisms	Yes	No	Yes	No	No	Yes	No
DSIC Mechanism (applicable to Gas business)	Yes	NA	NA	NA	NA	Yes**	No
GS view on Regulation	Constructive	Balanced	Constructive	Somewhat Restrictive	Balanced	Balanced	Restrictive
Fair Market Legislation (FMV)	Yes	Yes	Yes	Yes	Yes	No	No
Company 2018 Revenue Exposure *% of total cutomers	**Water-53%; Peoples Gas*-93%**	**Water-13%**	**Water-9%**	**Water-9%**	**Water-7%**	**Peoples Gas*- 5%**	**Peoples Gas*- 2%**

Infrastructure Replacement surcharges: Allows rates to change periodically, outside a general rate case proceeding, to reflect recovery of capital investments made to replace infrastructure necessary to sustain safe, reliable services for our customers. These mechanisms typically involve periodic filings and reviews to ensure transparency.
Utility plant recovery mechanisms: Allows recovery of the full return on utility plant costs during the construction period, instead of capitalizing an allowance for funds used during construction. In addition, some states allow the utility to seek pre-approval of certain capital projects and associated costs. In this pre-approval process, the PUC may assess the prudency of such projects.
Expense mechanisms: Allows changes in certain operating expenses, which may fluctuate based on conditions beyond the utility's control, to be recovered outside of a general rate case proceeding or deferred until the next general rate case proceeding.
Revenue stability mechanisms: Separates a utility's cost recovery from the amount of water it sells to recover its fixed costs and ongoing infrastructure investment needs. Such a mechanism adjusts rates periodically to ensure that a utility's revenue will be sufficient to cover its costs, regardless of sales volume, including recognition of declining sales resulting from reduced consumption, while providing an incentive for customers to use water more efficiently.
Future test year: A test period used for setting rates, which begins with the date new rates are effective. This allows current or projected revenues, expenses and capital investments to be collected on a timelier basis.
Distribution System mprovement Charge ("DSIC") mechanism: Utilities are allowed to recover costs related to repair, replacement or improvement of eligible distribution property that has not previously been reflected in rates or rate base. Through a DSIC, subject to an earnings test, a utility may recover the fixed costs of eligible infrastructure incurred during the three months ended one month prior to the effective date of the charge, thereby reducing the historical regulatory lag associated with cost recovery through the traditional rate-making process.
Fair Market Legislation(FMV): Allows regulated water companies to pay a fair market value for the purchase of water and wastewater systems. Before these changes, system values were determined by their depreciated original cost, which generally did not reflect a reasonable market value for those assets and became a barrier to a sale.
**In Kentucky, Delta has a pipe replacement program tariff, which allows adjustment of regulated rates annually to earn a return on capital expenditures incurred subsequent to Delta's last rate case which are associated with the replacement of bare steel and vintage plastic pipe.

Source: SNL Financial, Company reports, Goldman Sachs Global Investment Research

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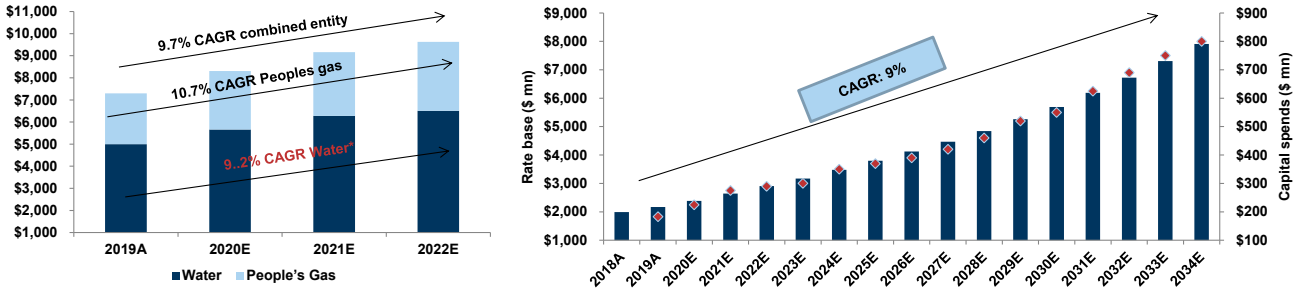
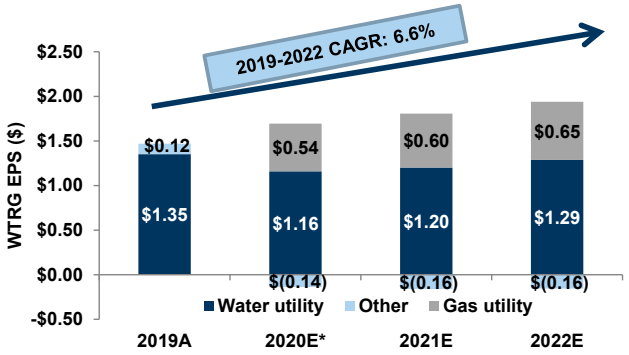
Exhibit 55: We expect WTRG to achieve 9.7% rate base CAGR from 2019-2022E across its utilities, with potential to sustain this level over the next 15 years based on organic investments and municipal acquisitions...
Rate base ($mn) 2019A-2022E



*includes $50mn/$75mn of capital in 2021/2022 at DELCORA

Source: Company data, Goldman Sachs Global Investment Research

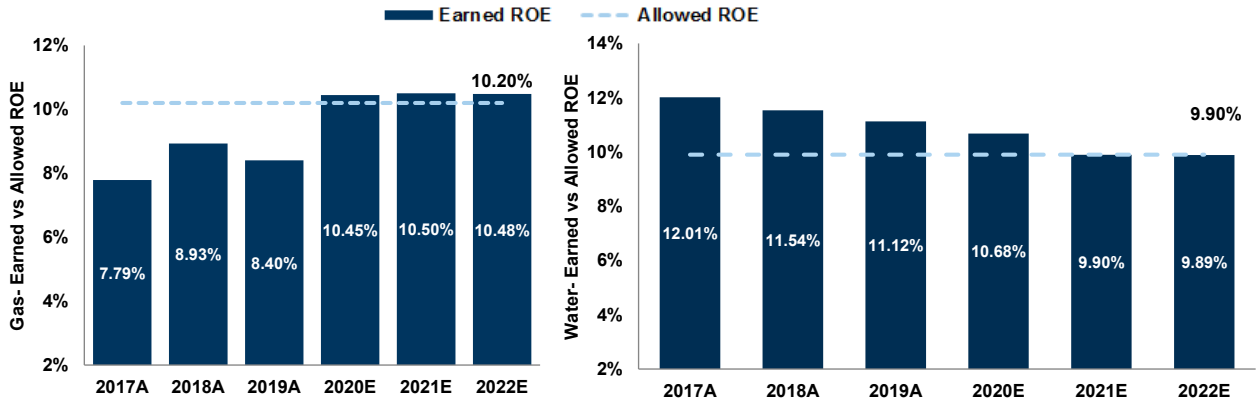
Exhibit 56: ...although we expect earnings growth to lag rate base growth at a larger rate through 2022 given acquisition earnings lag and water utilities transisiton away from tax repairs...
EPS 2019A-2022E



*2020 incorporates full-year of Peoples Gas earnings, comparable versus adjusted proforma company guidance ; 2021 summation for WTRG off by $0.01 due to rounding issue

Source: Goldman Sachs Global Investment Research, Company data

Exhibit 57: We model modest over-earning at gas utilities from expected PA tax repair benefits, versus closed to allowed ROE for water utilities after transitioning to more traditional ratemaking...
Water & Gas Utility Earned vs Allowed ROE



Source: Company data, Goldman Sachs Global Investment Research

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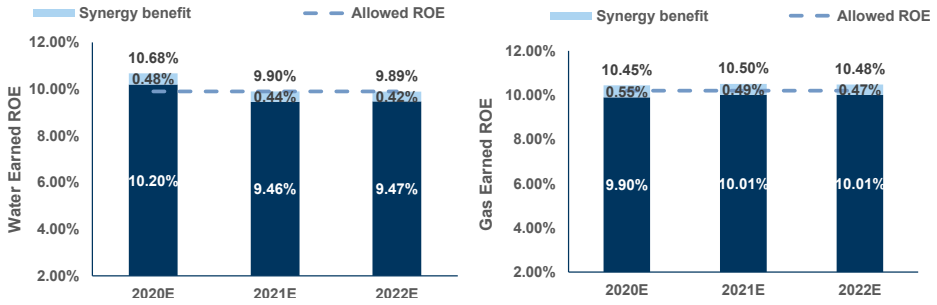
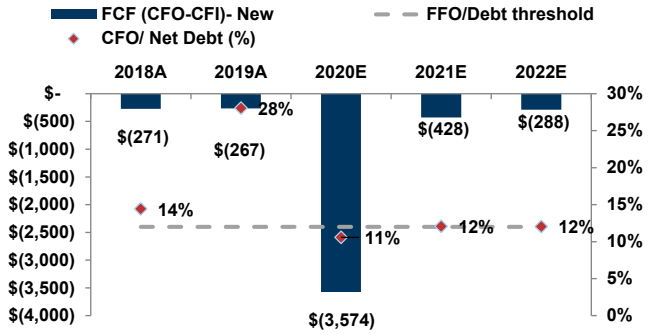
Exhibit 58: ...also supported by assumed Aqua-Peoples acquisition synergies.
Earned ROEs including and excluding merger synergies 2020E-2022E



Source: Goldman Sachs Global Investment Research

Exhibit 59: We expect FCF levels to improveing post acquisition financing, with FFO/debt near target threshold levels for its "A" rating by S&P
FCF (CFO-CFI $mn) & CFO/Net Debt (%)



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 60: Our EPS estimates are largely in line with consensus through 2022...
GS New vs Consensus

EPS Estimates			% Difference
	New	Consensus	vs Consensus
2019A	$1.47	$1.47	0%
2020E	$1.56	$1.57	-1%
2021E	$1.65	$1.65	0%
2022E	$1.78	$1.77	1%

Source: Goldman Sachs Global Investment Research, FactSet

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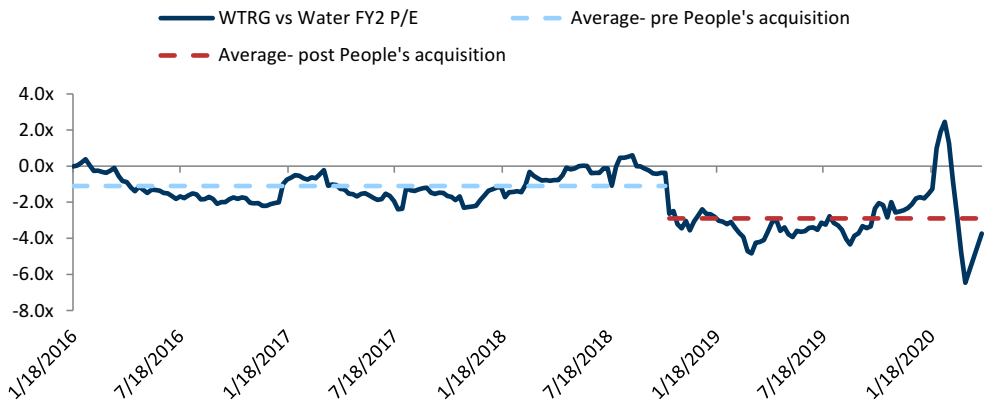
Exhibit 61: Our SOTP-based $45 price target reflects a 7% total return versus 15% for Regulated Utilities...
WTRG SOTP Valuation

VALUATION	
Water utility EPS 2021	**1.20**
Water utility multiple	30.00x
Assumed premium	0.00x
Adjusted P/E	30.0x
Water utility valuation	**36.08**
Gas utility EPS 2021	**0.60**
Gas utility multiple	20.00x
Assumed premium	2.00x
Adjusted P/E	22.0x
Gas utility valuation	**13.26**
Valuation - Other	**(0.16)**
2020 Blended multiple	27.33x
Other valuation	**(4.36)**
Total valuation	**45.00**
Current price per share	$42.80
Return potential	**5.14%**
Dividend yield	2.19%
Total return potential	**7%**

Source: Goldman Sachs Global Investment Research

Exhibit 62: ...and see WTRG's ~3-4x relative discount to pure-play water utilities as justified given its new gas utility exposure, which could affect ESG comparability
WTRG vs Regulated FY2 P/E



Source: Goldman Sachs Global Investment Research, FactSet

Company Overview

Essential Utilities Inc. (WTRG) formed from Aqua America's acquisition of privately owned Peoples Gas, completed on March 16, 2020. Essential's common stock

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began trading under the NYSE ticker symbol (WTRG) in early February. WTRG, with a market cap of $9.6 bn (as of 13th Apr close) market cap, serves more than 1 million water customers in 8 states and more than 740,000 gas customers in 3 states. WTRG projects 6-7% (ex. acquisitions) and 8-10% rate base growth for its water/gas utilities based on 2019 projected rate base of $5 billion and $2.3 billion, respectively. The key states served by WTRG are summarized in the Exhibit 52. The company operates through the following segments:

- **Regulated Water** (~70% of total operating revenues):
  - 2018 operating revenues were derived principally from the following states: ~53% in Pennsylvania, 9% in Ohio, 9% in Texas, 9% in Illinois, and 6% in North Carolina
  - The company's municipal growth strategy has accelerated significantly, largely due to the passage of Fair Market Value legislation(FMV) in several of its states. Aqua has added more than 33,000 new customers from 10 closed or signed municipal acquisitions in 2018
- **Regulated Gas** (~30% of total operating revenues):
  - The regulated gas business consists of 4 utility companies - Peoples Natural, and Peoples Gas (Formerly Peoples TWP) are regulated by the Pennsylvania Public Utility Commission. Peoples Gas – West Virginia is regulated by the West Virginia Public Service Commission. Peoples Gas – Kentucky is regulated by the Kentucky Public Service Commission
  - ~740,000 customers and 1,500 employees in western Pennsylvania, Kentucky and West Virginia
- **Market based business** (<1% of total operating revenues):
  - **Aqua Infrastructure**- provides non-utility raw water supply services for firms in the natural gas drilling industry
  - **Aqua Resources**- provides water service through O&M contracts with a municipal authority and another party close to utility companies' service territory; and offers, through a third-party, water and sewer line protection solutions and repair services to households

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Disclosure Appendix

Reg AC

I, Insoo Kim, CFA, hereby certify that all of the views expressed in this report accurately reflect my personal views about the subject company or companies and its or their securities. I also certify that no part of my compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

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Growth is based on a stock's forward-looking sales growth, EBITDA growth and EPS growth (for financial stocks, only EPS and sales growth), with a higher percentile indicating a higher growth company. **Financial Returns** is based on a stock's forward-looking ROE, ROCE and CROCI (for financial stocks, only ROE), with a higher percentile indicating a company with higher financial returns. **Multiple** is based on a stock's forward-looking P/E, P/B, price/dividend (P/D), EV/EBITDA, EV/FCF and EV/Debt Adjusted Cash Flow (DACF) (for financial stocks, only P/E, P/B and P/D), with a higher percentile indicating a stock trading at a higher multiple. The **Integrated** percentile is calculated as the average of the Growth percentile, Financial Returns percentile and (100% - Multiple percentile).

Financial Returns and Multiple use the Goldman Sachs analyst forecasts at the fiscal year-end at least three quarters in the future. Growth uses inputs for the fiscal year at least seven quarters in the future compared with the year at least three quarters in the future (on a per-share basis for all metrics).

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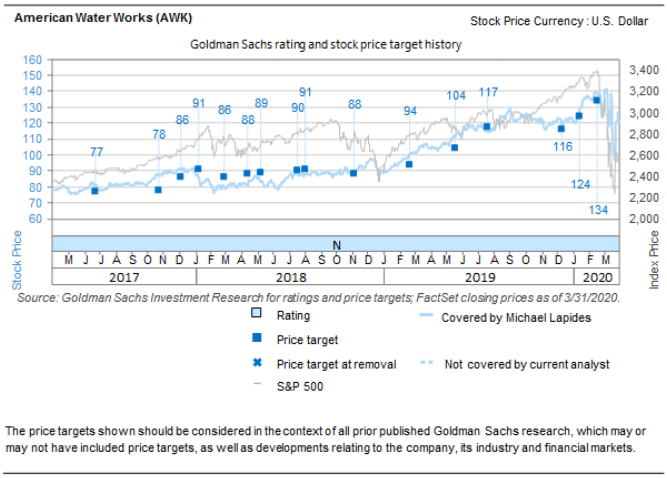
Price target and rating history chart(s)



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HSBC Global Research

26 April 2021

UK and US Water

New growth opportunities vs same old bond proxies

Equities
Utilities

UK and US

- Federal Water rehabilitation plans in the US and the Green Recovery scheme in the UK are new opportunities for growth
- US stocks are best placed for growth. Pennon may provide the M&A blueprint for the UK
- Downgrade UU to Reduce from Hold, Pennon to Hold from Buy; American Water and Essential, both Buy, offer more growth; Severn Trent remains Hold

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New opportunities for growth: Despite their ESG credentials, regulated UK and US utilities have performed less well than energy transition-focused stocks because of their status as bond proxies. The water proposals set out by the US government for accelerated investment and the UK's Green Recovery proposals show policy-makers are waking up to the need to improve resilience in water and waste water provision.

Opportunities from Federal Water spending plans: The US administration has proposed a USD111bn budget, of which USD10bn is for monitoring and cleaning up toxic (per and polyfluoroalkyl substances) and investing in rural water systems, household wells, and septic units. USD56bn is proposed for modernising drinking water, wastewater, and storm water conveyance and treatment. The remaining USD45bn will be used to remove lead drinking water pipes. We raise our target prices for both US water companies we cover, which are well placed to benefit from the focus on asset rehabilitation and their expertise in removing water contaminants to address historical municipal underinvestment.

UK has insufficient investment – M&A could be the way to grow: In contrast, Ofwat's PR19 price control focused on reducing customer bills rather than allowing RCV growth for the listed companies, except for Severn Trent. An announcement is due in May on whether it will allow the Green Recovery investment proposed by the companies or if it will be scaled back. We increase our risk-free rate in line with HSBC's new UK bond yield assumption, which reduces our DCF valuation for UU (UU/ LN, 968p, TP 910p vs 960p, downgrade to Reduce from Hold). We assume Pennon and Severn Trent can deliver higher long-term growth from their more ambitious Green Recovery plans. Severn Trent (SVT LN, 2,447p, TP 2,570p vs 2,450p) remains Hold but we downgrade Pennon (PNN LN, 1,030p, TP 1,090p) to Hold from Buy after its strong recent performance.

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Summary of rating and target price changes

Company	Ticker	Currency	Current price	TP Old	TP New	Rating Old	Rating New	Upside/ downside	Premium to RCV (%) (P/Bx) 2022e	Yield 2022e
Pennon	PNN LN	GBPp	1,030	1,090	1,090	Buy	Hold	5.9%	16.2%	2.3%
Severn Trent	SVT LN	GBPp	2,447	2,450	2,570	Hold	Hold	5.0%	21.0%	4.3%
United Utilities	UU/ LN	GBPp	968	960	910	Hold	Reduce	-6.0%	17.2%	4.6%
American Water	AWK US	USD	161.4	175	183	Buy	Buy	13.4%	3.9x	1.6%
Essential	WTRG US	USD	47.9	55	57	Buy	Buy	19.0%	1.9x	2.4%

Source: HSBC estimates, priced as at close on 22 April 2021

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Executive summary

- New growth opportunities in the US from USD111bn water system improvements
- UK's Green Recovery proposals not sufficient to avoid bond proxy status for stocks; M&A needed to accelerate growth
- US water stocks AWK and WTRG, both rated Buy, offer growth potential; in the UK, we downgrade PNN to Hold from Buy after a strong performance, SVT remains Hold, UU offers limited growth potential and we downgrade to Reduce from Hold

New growth opportunities in UK and US water

The water proposals set out by the US government and the UK's Green Recovery proposals show governments are waking up to the need to improve resilience in water

Regulated UK and US utilities have not performed as strongly as energy transition stocks, because of their perceived status as bond proxies. UK water stocks are down 21.6% over 12 months relative to the FTSE Utilities Europe index compared with Drax (DRX LN, 412p, Buy) up 40.3%. However, they too have strong ESG credentials. The water proposals set out by the US government for accelerated investment and the UK government's Green Recovery proposals show policy-makers are waking up to the need to improve resilience in water and waste water provision.

The UK water companies have bond proxy status unless accelerated growth can be proven. In HSBC's report *The Price is right*, 14 April 2021, our Fixed Income strategists increased their 10- year RfR assumptions. "We move our 10-year gilt year-end forecast to 50bp (from 30bp) because some MPC members are concerned about the risk of inflation proving more persistent than elsewhere, and we fear market expectations could overshoot". We increase our risk-free rate used in our UK water company valuations in line with HSBC's new bond yield assumption. This reduces our DCF valuation for United Utilities and leads us to downgrade our rating to Reduce from Hold. We assume that Pennon and Severn Trent can deliver higher long-term growth from their more ambitious Green Recovery plans, which offset the higher WACCs we calculate for each company. We retain our Hold rating on Severn Trent but downgrade Pennon to Hold from Buy after its strong recent share price performance.

The UK

DEFRA and Ofwat likely to provide preliminary guidance on the Green Recovery Initiative in May

We expect the Department for Environment, Food and Rural Affairs (DEFRA) and the water industry regulator Ofwat to provide preliminary guidance on the projects submitted by the water companies under the Green Recovery Initiative in May. For the three UK water companies under our coverage this will accelerate their regulated asset growth. Severn Trent has the largest Green Recovery proposal of GBP730m as a percentage of its current five-year investment programme among the listed UK water companies, which if approved would lead to a rise of 24% in its existing capex plans of cGBP3bn for the current AMP (alternative

performance measures). Pennon has a capex plan of GBP1bn for the current AMP and has submitted proposals for GBP92m worth of plans under the Green Recovery initiative to the regulator; if approved it would increase capex by c9%. United Utilities has proposed GBP135m of additional capex, marking a c7% increase in its existing plan of GBP2bn for the current AMP.

Downgrade Pennon to Hold after strong recent performance, TP of 1,090p unchanged; better to travel than to arrive

The ability to create value through M&A, as Pennon did with Bournemouth Water, is a much more arduous task

Pennon has had a strong share price performance recently, driven by M&A expectations and strong initial regulatory performance. Its reinvestment decisions will provide an interesting regulatory precedent depending on where it chooses to invest its waste proceeds for growth. It could be bold and buy a large water company and plan ambitious expansion or look at a smaller water-only company and give the proceeds back to shareholders. As the sector resilience needs are significant, we assume management may think big. The case for paying a premium to Regulatory Capital Value (RCV) – the regulated asset base has been strengthened by National Grid's (NG/ LN, 915p, Buy) premium paid in March 2021 for WPD (a fast-tracked sector leader). Many of Pennon's unlisted water potential targets have a combination of complicated (with derivatives) balance sheets with higher leverage, or significant operational challenges. The ability to create value as it did with Bournemouth Water is a much more arduous task.

Severn Trent remains Hold, raise TP to 2,570p from 2,450p on higher longer term growth and higher performance rewards

Severn Trent continues to set itself out as an innovator with underlying growth and ideas for green investment

Severn Trent has applied for a cGBP730m package under the Green Recovery initiative. This investment plan is above its base capex plan of GBP3bn for the period 2021-25 (on top of the 4% RCV growth target for AMP7, the highest of its peers). Severn Trent continues to set itself out as an innovator with underlying growth and ideas for green investment. Management said in 2020 that M&A was not part of its strategy. It still has much work to do on Hafren Dyfrdwy, the small water company it owns. Management said in its pre-close statement at the end of March that Severn Trent remains on or ahead of target for almost 80% of its customer performance measures and has increased its guidance for outperformance on customer performance incentives (ODIs) this year from 'at least GBP25m' to 'at least GBP50m'. Pennon and UU shares have outperformed Severn Trent but in our view both have had a higher profile: Pennon through M&A and United Utilities at its CMD. However, Severn Trent consistently trades at a premium to RCV to the other two listed stocks, currently at c20%, and therefore we do not see sufficient additional value to justify a Buy rating.

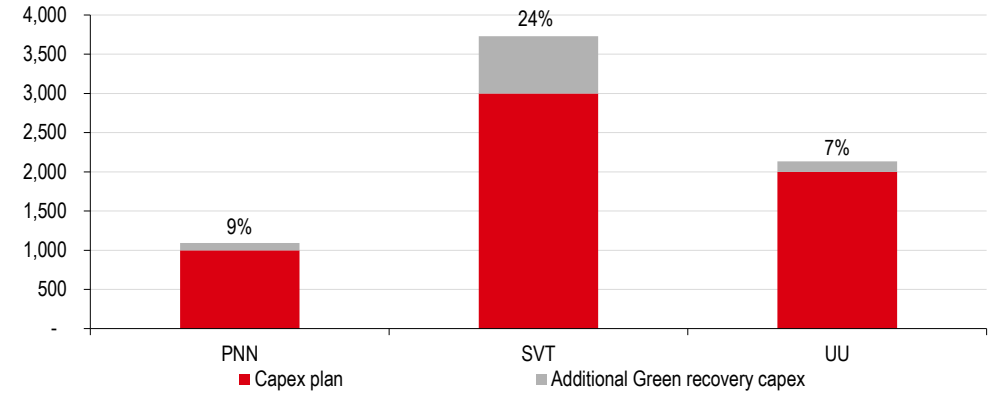
Downgrade United Utilities to Reduce from Hold, cut TP to 910p from 960p on higher gilt yield assumptions and brought forward phasing of investment

UU still struggles to avoid its bond proxy status. Of all the water stocks under our coverage it has the highest dividend yield and the lowest Green Recovery list of potential projects compared to its current investment. It continues to bring forward investment to drive ODI performance but management seems to have backtracked on exploring M&A opportunities in UK water despite a significant operational improvement.

Despite UU's significant operational improvements, its asset base is shrinking

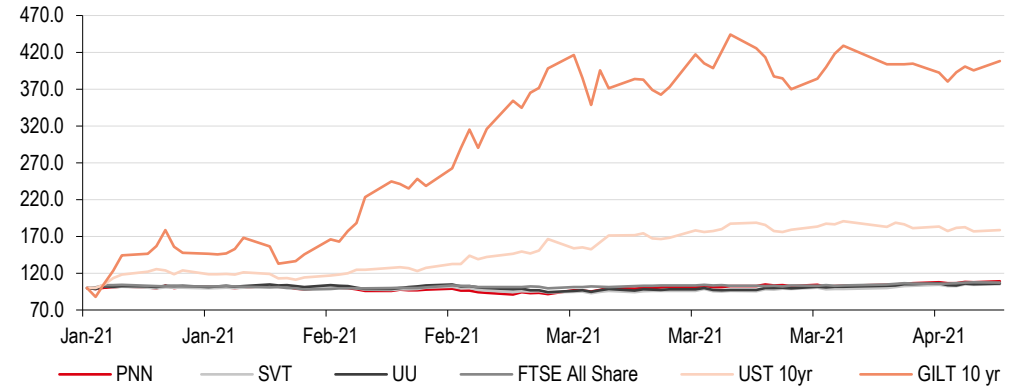
Despite UU's significant operational improvements, its asset base is shrinking. Ofwat is looking at the Haweswater Aqueduct Resilience Programme (HARP) project as a blueprint for attracting additional capital for major projects to the sector but it will have to prove convincingly that project finance without government guarantees with the additional cost of finance, lawyers, and cost duplication will deliver better value to shareholders. HARP in particular is a risky project because of the tunnelling required through hills in the Lake District, which is not a core competence for UU. We remain sceptical that it can be delivered at a lower cost to UU's customers bearing in mind that Thames Tideway, another significant project (Thames Water), needed a government guarantee. If HARP could be delivered more cheaply by United Utilities' management team it would form part of its regulatory asset growth post 2025.

Green Recovery capex acceleration (GBPm)



Source: Company data

Performance of AWK vs WTRG vs UST 10-year vs FTSE USA Growth Index vs S&P 500



Source: Refinitiv Datastream

The US

Federal proposal for USD111bn for water system improvements, most notably replacing lead pipes in drinking water systems

The US government set out its proposal, the 'American Jobs Plan', on 31 March 2021, which is a wide-ranging job creation and infrastructure rehabilitation plan. Among its many parts, it includes a proposal to allocate USD111bn for water system improvements, most notably replacing lead pipes in drinking water systems.

The larger privately held and investor-owned (IOU) water utilities including American Water Works and Essential Utilities, the two largest under our coverage, have the technological expertise to test and treat drinking water as additional federal and/or state contaminant levels are adopted. They also have the expertise in project management to rehabilitate waste water systems, which arguably have been neglected even more than the clean water network.

Funding aside, regulatory mechanisms such as Fair Market Value and the use of infrastructure charges have been major growth drivers for these listed companies

Funding aside, regulatory mechanisms such as Fair Market Value and the use of infrastructure charges have been a major growth driver for these listed companies. This has enabled them to:

- purchase regulated water systems at a premium to rate base (the appraised value),
- pay a premium for the municipality to redeploy the proceeds for other priorities,
- increase water rates incrementally each year in order to replace pipes.

The costs and risks of expansion within the states in which these two companies operate, has delivered savings through economies of scale and have also spread the cost of asset rehabilitation, especially for poor communities across the entire state rate base. US water assets are significantly underinvested compared to the UK. This underpins the mid-single digit earnings growth expected by the listed utilities.

Latest developments

HSBC's US Economics team on 15 April 2021 published *US Fiscal Policy*, updating on the Biden administration's latest proposals for spending on infrastructure and other areas of over USD2bn. We extract from this report below.

"Republican senators have indicated that they are preparing a smaller, counterproposal that would be focused on a narrower set of infrastructure investments compared to the American Jobs Plan. Republican Senator Shelley Moore Capito said on 14 April that the budgetary cost of such a plan could be in the range of USD600bn to USD800bn.

President Joe Biden is scheduled to address a joint session of Congress on 28 April. At that point, markets will be looking for some clarity about whether bipartisan discussions on infrastructure have yielded any progress or whether Democrats are likely to pursue enactment of American Jobs Plan proposals via budget reconciliation, relying on support strictly from Democratic lawmakers. In either case, it will be important to monitor the momentum of the discussions over the course of the early summer given that Congress typically goes on recess during the month of August".

American Water remains Buy, raise TP to USD183 from USD175 on higher growth

American Water plans to spend USD22-25bn over the next ten years on water quality, essential infrastructure replacement and regulated customer growth. This underpins regulated future revenue growth.

Its medium-term aim is for an EPS CAGR of 7-10% in 2021-2025. 1-2% growth is to come from Market-Based Businesses, 1-2% growth from Regulated Acquisitions and 5-7% growth from Regulated Investment (capex). Dividend growth is targeted at the high end of 7-10% while maintaining a payout ratio of 50-60% of earnings.

American plans to invest USD22-25bn of capital over the next ten years

It plans to maintain a predominantly regulated risk profile with capital-light, cash-generating Market-Based Businesses representing 12% of EPS in 2024.

Essential targets investment of USD3bn from 2021 to 2023 to maintain a 70/30 water to gas mix of business

Essential remains Buy, raise TP to USD57 from USD55 on higher growth

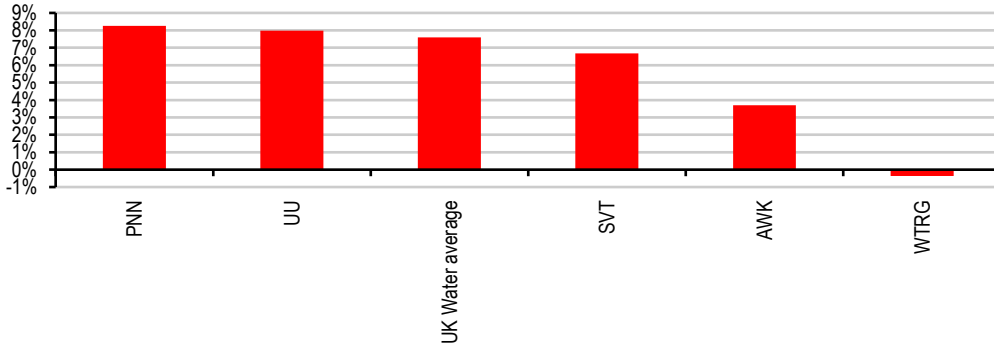
Essential Utilities' management targets investment of USD3bn from 2021 to 2023 to maintain a 70/30 water to gas mix of business measured by size of regulated rate base. To complement its infrastructure rehabilitation, Essential is also investing in municipal acquisitions in the US states in which it operates. We believe its recent performance has been muted because it remains embroiled in the political complexities of its Delcora acquisition, despite the legality of the contract. We think this could continue to depress its share price performance. Ultimately customers in Delaware will have to pay for asset rehabilitation even if Essential is not successful. There are other opportunities for expansion in water. In gas it has clear visibility for enhanced asset rehabilitation, which will also reduce carbon emissions.

Stock metrics

Company	Rating	PE			EV/EBITDA			Yield			FCF yield		
		2021e	2022e	2023e	2021e	2022e	2023e	2021e	2022e	2023e	2021e	2022e	2023e
PNN	Buy	35.6x	33.6x	30.6x	12.9x	12.6x	12.0x	2.1%	2.2%	2.3%	39.6%	2.2%	1.4%
SVT	Hold	23.2x	18.7x	15.8x	14.1x	13.1x	12.0x	4.1%	4.2%	4.3%	3.4%	1.3%	1.7%
UU	Reduce	17.6x	17.2x	15.9x	13.8x	13.7x	13.1x	4.4%	4.5%	4.6%	2.3%	3.9%	5.7%
WTRG	Buy	29.2x	26.7x	24.6x	19.1x	18.2x	16.5x	2.2%	2.4%	2.6%	-2.2%	-1.9%	0.8%
AWK	Buy	38.4x	35.3x	31.3x	18.8x	17.7x	17.0x	1.5%	1.6%	1.8%	-0.4%	-1.4%	-1.0%
UK average		**25.8x**	**23.3x**	**21.5x**	**13.6x**	**13.1x**	**12.4x**	**3.5%**	**3.6%**	**3.7%**	**15.1%**	**2.5%**	**2.9%**
Average		**28.8x**	**26.3x**	**23.6x**	**15.7x**	**15.1x**	**14.1x**	**2.9%**	**3.0%**	**3.1%**	**8.5%**	**0.8%**	**1.7%**

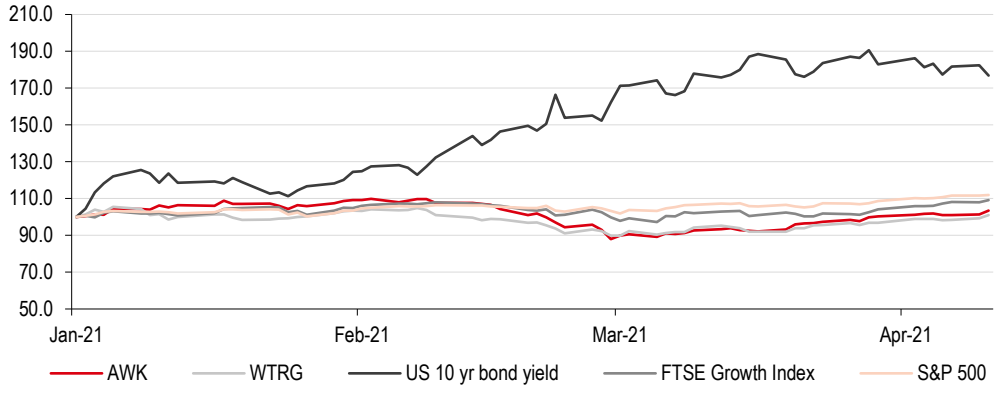
Source: HSBC estimates

Year-to-date share price performance



Source: Refinitiv Datastream

Performance of AWK vs WTRG vs UST 10yr vs FTSE USA Growth Index vs S&P 500



Source: Refinitiv Datastream

Opportunities from Federal Water spending plans

- The challenge of US water provision
- Lead pipe replacement and water contaminants removal are opportunities
- US water companies benefit from a highly fragmented, underinvested market

The challenge of US water provision

Clean water

Renewal and replacement of ageing water and wastewater infrastructure, as well as the financing for capital improvements, the top two issues facing the US water industry

Renewal and replacement of ageing water and wastewater infrastructure, as well as the financing for capital improvements, are the top two issues facing the US water industry according to the 2021 Infrastructure Report Card.

Funding for drinking water infrastructure has not kept pace with the growing need to address ageing infrastructure systems, and current funding sources do not meet the total needs. Since 2017, there have been signs of improvement with the modest expansion of federal financing programmes and water utilities are raising water rates to fund network investment.

The US Environmental Protection Agency's (EPA) drinking Water State Revolving Fund (DWSRF) provides low-interest loans to state and local drinking water infrastructure projects. The DWSRF programme grew from USD2bn in 2013 to nearly USD3bn in 2018. The EPA's Water Infrastructure Finance & Innovation Act (WIFIA) programme offers the sponsors of large projects (over USD20m) a new financing tool to leverage limited federal resources; stimulate additional investment in drinking water, wastewater, and stormwater infrastructure; and encourage greater private sector participation. By 2019, prospective borrowers had submitted letters of interest requesting over USD21bn in WIFIA loans, including USD3.9bn for drinking water projects. The US government increased its lending capacity from USD2.5bn in 2017 to USD6bn in 2019.

According to an American Society of Civil Engineers' (ASCE) 2020 economic study, the annual drinking water and wastewater investment gap will grow to USD434bn by 2029

US water customers have not paid tariffs, in our view, that allow the cost of infrastructure rehabilitation (in addition to water service provision) compared to markets such as France and the UK. The average nationwide monthly drinking water rate has increased 31% from 2012 to 2018 but more is needed. According to an American Society of Civil Engineers' (ASCE) 2020 economic study, the annual drinking water and wastewater investment gap will grow to USD434bn by 2029.

Wastewater

The majority of the nation's Wastewater Treatment Plants (WWTPs) were designed with an average lifespan of 40 to 50 years. Since the systems were constructed in the 1970s, around the passing of the Clean Water Act in 1972, they are reaching the end of their service lives.

Moreover, utilities face the challenge of meeting increasingly stringent surface water quality regulations for rivers and lakes. Significant infrastructure replacement is needed but clean water investment has tended to be prioritised compared to wastewater. Investor-owned utilities are experts in resilience-related planning and using technological and scientific innovations that produce profitable by-products such as sludge. They can also deliver cost savings from wastewater treatment relative to legacy plant. Today's waste water can be tomorrow's clean water in areas of water stress. In 2019, the federal government invited more than a dozen wastewater and water reuse projects to apply for over USD2.3bn in loans.

Federal Water spending plans

The US government set out its proposal, the 'American Jobs Plan', on 31 March 2021, which is a wide-ranging job creation and infrastructure rehabilitation plan. Among its many parts it includes a proposal to allocate USD111bn for water system improvements, most notably replacing lead pipes in drinking water systems.

The plan offers USD10bn for monitoring and cleaning up toxic (per and polyfluoroalkyl substances), a particular competence of the companies under our coverage

The plan offers USD10bn for monitoring and cleaning up toxic (per and polyfluoroalkyl substances or PFAS) and investing in rural water systems, household wells, and septic units. This is a major focus for US investors. A sum of USD56bn is proposed for modernising drinking water, wastewater, and storm water conveyance and treatment. The remaining USD45bn will be used to remove all of the country's estimated 6-10m lead drinking water pipes. Additionally, the plan provides funding for the 'western drought crisis' by investing in water efficiency and recycling programmes.

Where do the investor-owned utilities fit into these plans?
We look at what has happened historically when large Federal financial resources have been available. Federal money is expected to provide some support, but funding may not be available to all the municipalities in need.

Federal money is expected to provide some support, but funding may not be available to all the municipalities in need

Financially, municipal systems have been facing challenges with limited government funding and competing needs for other services. Operationally, due to a lack of expertise, smaller systems will find it difficult to keep up with increasingly stringent water quality standards over the medium term, even if they have money to replace their lead pipes in the short term. Municipal systems in the medium term will continue to weigh up the advantages of divesting assets for ongoing asset replacement needs and when the expense of testing and treating for higher standards of water is overly burdensome. This will continue to drive acquisition opportunities for the listed water stocks under our coverage.

The larger privately held and investor-owned (IOU) water utilities have the technological expertise to test and treat drinking water as additional federal and/or state contaminant levels are adopted. They also have the expertise in project management to rehabilitate waste water systems, which arguably have been neglected even more than the clean water network.

UK Water

- Announcement to deliver accelerated environmental growth expected next month
- Pennon – premium precedent by National Grid for regulated assets and CMA green light on increased leverage
- HSBC Fixed Income expects an increase in short-term gilt yields

Accelerated environmental growth through Green Recovery

DEFRA and Ofwat will provide preliminary guidance on the projects submitted by the water companies under the Green Recovery Initiative, we believe in May

DEFRA and Ofwat will provide preliminary guidance on the projects submitted by the water companies under the Green Recovery Initiative we believe in May. For all the companies under our coverage this will accelerate regulated asset growth. The UK water sector has lagged the performance of its UK electricity peers. The prospect of more growth and the strong ESG credentials of the listed water companies may lead to a better performance in calendar Q2.

M&A update – Pennon management could be tempted to pay up

M&A: Two recent events may encourage Pennon to pay up: National Grid's 60% premium payment for WPD; and the CMA's lack of endorsement for capital structure sharing with customers

The market is waiting for Pennon to conclude its strategic review on where to redeploy the GBP2.7bn of net proceeds from its waste sale. The easy option would be to enhance earnings through a share buyback and return the proceeds to shareholders. In our experience, water companies under our coverage have always found something to invest in. This is a once-in-a-lifetime to invest for environmental performance and growth. Two recent events may encourage Pennon to pay up:

- National Grid's 60% premium payment for WPD
- The CMA's lack of endorsement for capital structure sharing with customers.

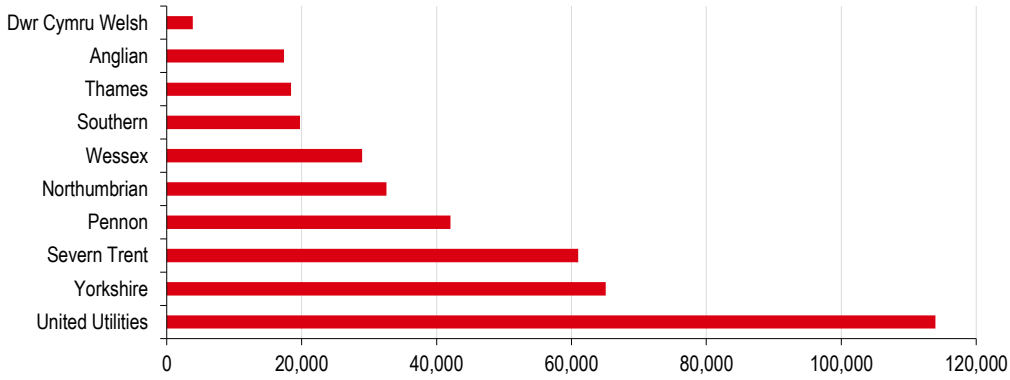
Both suggest that Pennon could pay more for one of the four companies that went to the CMA (Competition and Markets Authority) as it would not have to share the benefits of taking on more debt (to drive down the WACC) with shareholders.

Plenty of assets need accelerated investment – the UK's multiple sewage overflow numbers

According to an investigative report by the BBC's Panorama broadcast on 13 April, UK water companies have been illegally dumping untreated sewage into rivers. Panorama gathered detailed data from ten water companies in England and Wales through environmental information requests. The data suggests seven of the ten companies had treatment works that were breaching their permits by dumping sewage before they were treating the specified volumes. Water companies discharged untreated sewage into rivers more than 400,000 times lasting more than 3m hours last year.

To protect properties from flooding and prevent sewage from backing, treatment works are allowed to release sewage into rivers and streams after extreme weather, such as torrential rain, and when they are operating close to full capacity. This untreated sewage is normally screened and passed through storage tanks before it is dumped. Discharge permits issued by the Environment Agency specify the level of sewage each works has to treat before it can dump untreated sewage. But Panorama's report found some companies are discharging without a permit and/or providing incorrect information to the agency.

Number of storm water overflows, 2020



Source: Environment Agency

This is more an indication that even though the UK's water infrastructure has benefited from significant investment, more is needed

This chart does not imply that UU is exceeding its permitted discharge limits and this absolute chart does not reflect the size or geography of the companies. However, it does reflect that all the overflows were without permit. It merely demonstrates that further resilience investment is needed to reduce these numbers. This is more an indication that even though the UK's water infrastructure has benefited from significant investment, more is needed.

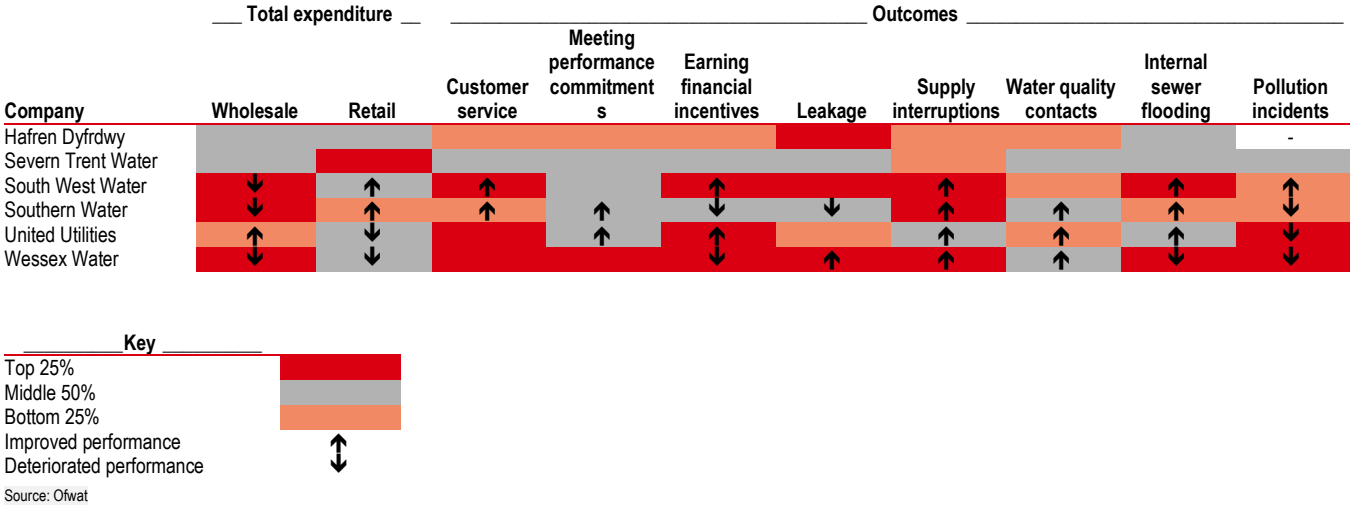
Customers may need to be prepared to accept increases in bills to ensure that less untreated sewage is released into rivers.

Bond proxy status unless accelerated growth can be proven

In HSBC Fixed Income's report *The Price is Right* published on 14 April 2021, the team increased its 10-year RfR assumptions. "We move our 10-year gilt year-end forecast to 50bp (from 30bp) because some MPC members are concerned about the risk of inflation proving more persistent than elsewhere, and we fear market expectations could overshoot".

We increase our RfR in line with HSBC's new UK bond yield assumption (we take an average of short and long-term gilt yields). This leads us to reduce our DCF valuation for United Utilities and we downgrade our rating to Reduce from Hold. We assume that Pennon and Severn Trent can deliver higher long-term growth from their more ambitious Green Recovery plans, which offset the higher WACC we now calculate for each company. We retain our Hold rating on Severn Trent but downgrade Pennon to Hold from Buy after its strong recent share price performance. United Utilities' RCV growth excludes the Haweswater Aqueduct project, which Ofwat is testing to see whether it can be financed more cheaply by project finance. This means its asset base is shrinking and it is hard to see how it will not continue to be seen as a bond proxy and command a yield premium to its peers. We downgrade United Utilities to Reduce from Hold on our higher RfR assumptions, not offset by significant Green Recovery Investment.

Overall Service Performance: Ofwat 2019-2020



Source: Ofwat

We reproduce above Ofwat's overall service performance table for 2019 to assess the task in hand for key companies in the sector. In terms of overall performance:

- Hafren Dyfrdwy, despite being owned by Severn Trent, is still a relatively poor performer on many measures.
- Severn Trent remains in the middle of the pack with an average performance but we know from its H1 presentation that it is working hard to alleviate its long-term weakness in supply interruptions.
- Southern Water is making progress but still has much work to do across many areas.
- South West Water still has to make better progress with water customer contacts, which was meant to be an area where its acquisition of Bournemouth Water was beneficial. It is already making improvements in reduction in pollution incidents.
- Wessex Water remains best in class across more measures than its peers.

Companies

American Water

- Acquisition-led growth accelerating
- Environmental credentials, especially in regard to removal of water contaminants
- Reiterate Buy rating, raise TP to USD183 from USD175

Investment thesis

American Water plans to spend USD22-25bn over the next ten years. This underpins its regulated future revenue growth.

Medium-term aims are for an EPS CAGR of 7-10% 2021-2025

The company's medium-term aims for an EPS CAGR of 7-10% from 2021-2025. adjusted EPS. 1-2% growth is to come from Market-Based Businesses, 1-2% growth from Regulated Acquisitions and 5-7% growth from Regulated Investment (capex). Dividend growth is targeted at the high end of a 7-10% range while maintaining a payout ratio of 50-60% of earnings.

It plans to maintain a predominantly regulated risk profile with capital-light, cash-generating Market-Based Businesses representing 12% of EPS in 2024. The company also plans to invest USD20-22bn of capital over the next ten years for water quality, needed infrastructure replacement and regulated customer growth.

Similarly, rate base growth of CAGR 7-8% is targeted for 2021-2025.

American is seen as one of the few regulated utilities with accelerated growth, which means it has not suffered as much as its peers from a bond proxy negative correlation with rising bond yields

Together this means American Water is regarded as one of the few regulated utilities with accelerated growth, which means it has not suffered as much as its peers from a bond proxy negative correlation with rising bond yields. Recent acquisitions have further underpinned its growth status.

2021 outlook

The outlook for 2021 was set out at the FY 2020 results on 25 February:

- 2021 earnings guidance range of USD4.18 to USD4.28 per diluted share.
- AWK has 44,000 customers in its pipeline through signed acquisitions following regulatory approval, which it expects to complete.
- The company is awaiting final orders for general rate cases in three states and filed for infrastructure surcharges in one state for a total annualised revenue request of USD126m.

Recent M&A activities underpin growth

American Water announced the acquisition of City of York wastewater systems in the state of Pennsylvania, through its subsidiary Pennsylvania American Water, for USD235m on 7 April. This acquisition will add roughly 45,000 connections. The agreement has received approval from York City Council and American Water plans to close the transaction by the end of 2021, assuming it receives the necessary approvals from the regulators. As part of the agreement, it will preserve current wastewater rates for a minimum of three years, offer employment to all of the city's wastewater system employees, establish an in-person customer service centre in

York, provide an upfront deposit of USD20m, and contribute at least USD50,000 in donations to non-profit organisations serving the city and its residents.

In another deal, American Water acquired the wastewater assets of Egg Harbour City in New Jersey for USD21.8m on 30 March. Under the terms of the deal, American Water will invest USD14m in the first ten years for necessary upgrades, including the construction of an emergency interconnection with the subsidiary's regional system. The deal is expected to be completed in the second half of the year, pending approval from the New Jersey Department of Community Affairs and the New Jersey Board of Public Utilities.

Performance against peers

The stock has underperformed the S&P 500 index by 8.5% and underperformed the FTSE USA growth index by 5.7% since 1 January 2021. In the same period, Essential Water's stock underperformed the S&P 500 index by 10.9% and FTSE USA growth index by 8.1%. Both American Water and Essential have performed as bond proxies since the start of the year. American Water appears to have a much greater correlation with the S&P 500 index than an inverse correlation with the US 10-year bond yield. As it accelerates its investment for growth, we expect the shares to continue to move in tandem with the FTSE USA Growth Index peers. This is in marked contrast to its regulated UK water peers, which have performed as bond proxies.

However, a falling UST 10-year yield has helped American Water's share price to move higher recently as it is the largest pure-play water company in the US with a clear growth trajectory and strong pipeline of acquisitive growth planned for the next few years.

Change in estimates

We update our model for the FY2020 results and introduce our 2023 estimates.

Change in estimates, introducing 2023e

	2021e	2022e	2023e
Revenues (USDm)			
Revised	3,942	4,193	4,456
Previous	3,957	4,203	-
Change	-0.4%	-0.2%	-
EBITDA (USDm)			
Revised	2,131	2,279	2,414
Previous	2,120	2,263	-
Change	0.5%	0.7%	-
EBIT (USDm)			
Revised	1,419	1,566	1,690
Previous	1,436	1,563	-
Change	-1.2%	0.2%	-
PBT (USDm)			
Revised	994	1,097	1,213
Previous	1,037	1,124	-
Change	-4.2%	-2.4%	-
Net income (USDm)			
Revised	763	842	958
Previous	778	843	-
Change	-2.0%	-0.1%	-
EPS (USD)			
Revised	4.20	4.58	5.15
Previous	4.21	4.57	-
Change	-0.2%	0.2%	-
DPS (USD)			
Revised	2.39	2.60	2.84
Previous	2.39	2.60	-
Change	0.0%	0.0%	-

Source: HSBC estimates

Valuation and risks

We value American Water via three approaches: DCF, target dividend yield, and sum of the parts (using the average of our rate base valuation and peer multiple valuation). Taking the average of the three fair values, which we update, we raise our target price to USD183 from USD175.

- **DCF:** We change our observed Bloomberg five-year beta to 0.79 from 0.5, reflecting volatility relating to interest rate rises in the US. We use a risk-free rate of 2.5%, equity risk premium of 3.0% and a cost of equity of 4.9%, resulting in a higher WACC of 4.2% (previously 3.7%). We update our earnings estimates. Despite the increased beta, recent deals mean we increase our terminal value growth rate by 50bp to 3.5%. This increases our DCF fair value to USD204.4 from USD175.5.
- **Target PE multiple and dividend yield:** We use the weighted average of the US water peer group (70%) and FTSE USA Growth index constituents (30%) to arrive at our PE multiple and target dividend yield. US water peers are now trading at a PE multiple of 36x with a yield of 1.45%, whereas the FTSE growth index is trading at a PE of 36x and yield of 1.25%. Hence, we use a 36x (unchanged) water peer multiple (for our SOTP valuation; see below) and a target dividend yield of 1.4% (unchanged in line with water peers), both in line with the above-mentioned methodology. The fair value from our yield approach is unchanged at USD170.9.
- **Sum of the parts:** In our SOTP approach, we continue to use the 2021e rate base to reflect the company's current growth trajectory (based on 2020e rate base numbers). In this we assume 8% annual growth of the rate base to 2021e. We then use the average of the sum-of-the-parts valuation based on the rate base with a small non-regulated element, and our peer multiple-based valuation of 3.5x price to regulated rate base (proxy for price to book in line with peers). Our new fair value from this method is USD173.3, down from USD179.9.

Our higher target price of USD183 implies upside of 13.4%. We retain our Buy rating as the company has a strong pipeline of accretive acquisitions to be completed in the next few years, which we expect to drive higher rate base growth than previously.

Summary of valuation

USD	New	Previous
Current price as on 22-Apr-21	**161.4**	**NA**
DCF	204.4	175.5
Yield 1.4% (unchanged)	170.9	170.9
Peer multiple	173.3	177.9
Target price (average rounded)	**183.0**	**175.0**
Implied upside to target price	13.4%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity valuation	USDm
Cost of debt		+ DCF value	46,361
Pre-tax cost of debt	3.1%	+ ST marketable assets	0
Marginal tax rate	23.3%	+ Value of associates	0
Cost of equity		+ Other assets	1,525
Risk-free rate	2.5%	**EV (asset side)**	47,886
Equity risk	3.0%	- Net debt (+ if net cash)	(10,368)
Additional risk	-	- Quasi debt (pension)	(388)
Beta (previously 0.5)	0.79	- Value of minorities	0
Debt - 28%	2.4%	**Total non-equity claims**	(10,756)
Equity - 72%	4.9%	Value of equity	37,130
Cost of capital	4.2%	**Value per share (USD)**	**204.4**

Source: HSBC estimates

SOTP valuation

Regulated rate base	2021e rate base USDm
California	581
Illinois	1,030
Indiana	1,238
Kentucky	517
Missouri	1,457
New Jersey	3,441
New York	321
Penn	3,689
Virginia	182
W Virginia	762
Total	**13,219**
Price to rate base valuation	46,265
Non-regulated 2020 (PE based valuation)	522
Net debt 2020e, pensions & Minority	-11,293
Total	**35,494**
NoS (m)	182
Value per share	**195**
2020 earnings (USD)	4.20
2020 PE sector average	36.0x
Value per share (USD)	**151**
Average of rate base and PE multiple (USD)	**173.3**

Source: HSBC estimates

Downside risks

If American Water fails to achieve the desired rate case revisions, this could impact its revenue and profit margins. The company may also fail to deliver organic growth. If it fails to keep its momentum in acquiring water systems or gaining O&M efficiency, it may not achieve our forecasts.

Financials & valuation: American Water Works

Buy

Financial statements

Year to	12/2020a	12/2021e	12/2022e	12/2023e
Profit & loss summary (USDm)				
Revenue	3,777	3,942	4,193	4,456
EBITDA	1,852	2,131	2,279	2,414
Depreciation & amortisation	-604	-712	-713	-724
Operating profit/EBIT	1,248	1,419	1,566	1,690
Net interest	-395	-425	-469	-477
PBT	924	994	1,097	1,213
Taxation	-215	-231	-255	-255
Net profit	709	763	842	958
Cash flow summary (USDm)				
Cash flow from operations	1,426	1,496	1,588	1,718
Capex	-1,822	-1,600	-2,000	-2,000
Cash flow from investment	-2,061	-1,600	-2,000	-2,000
Dividends	-389	-434	-478	-528
Change in net debt	999	537	190	810
FCF pre dividends	-396	-104	-412	-282
Balance sheet summary (USDm)				
Intangible fixed assets	1,559	1,559	1,559	1,559
Tangible fixed assets	20,837	21,725	23,013	24,289
Current assets	1,248	1,273	1,311	1,351
Cash & others	547	547	547	547
Total assets	24,137	25,051	26,376	27,692
Operating liabilities	3,097	3,144	3,216	3,292
Financial liabilities	10,944	11,481	11,671	12,481
Total liabilities	18,312	18,896	19,159	20,044
Net debt	10,397	10,934	11,124	11,934
Shareholders' funds	6,454	6,783	7,847	8,277

Ratio, growth and per share analysis

Year to	12/2020a	12/2021e	12/2022e	12/2023e
Y-o-y % change				
Revenue	4.6	4.4	6.4	6.3
EBITDA	5.7	15.0	6.9	6.0
Operating profit	6.7	13.7	10.4	7.9
PBT	10.9	7.6	10.4	10.6
HSBC EPS	7.8	7.8	9.0	12.5
Ratios (%)				
ROE	11.3	11.5	11.5	11.9
ROCE	6.1	6.1	6.4	6.6
EBITDA margin	49.0	54.0	54.3	54.2
Operating profit margin	33.0	36.0	37.3	37.9
Net debt/equity	161.1	161.2	141.8	144.2
CF from operations/net debt	13.7	13.7	14.3	14.4
Per share data (USD)				
EPS reported (diluted)	3.90	4.20	4.58	5.15
HSBC EPS (diluted)	3.90	4.20	4.58	5.15
DPS	2.19	2.39	2.60	2.84
Gross CFPS	8.40	8.12	8.46	9.04

Valuation data

Year to	12/2020a	12/2021e	12/2022e	12/2023e
EV/sales	10.5	10.2	9.6	9.2
EV/EBITDA	21.3	18.8	17.7	17.0
P/CF	19.2	19.9	19.1	17.8
PE*	41.4	38.4	35.3	31.3
FCF yield (pre div) (%)	-1.4	-0.4	-1.4	-1.0
Dividend yield (%)	1.4	1.5	1.6	1.8

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2019a
GHG emission intensity*	n/a
Energy intensity*	377.6
CO_2 reduction policy	Yes
Social Indicators	**12/2019a**
Employee costs as % of revenues	12.8
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	12/2020a
No. of board members	11
Average board tenure (years)	5.5
Female board members (%)	45.5
Board members independence (%)	45.5

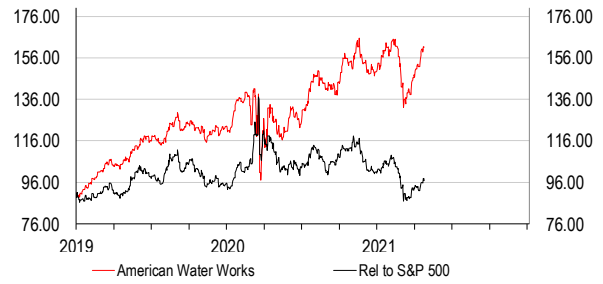
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	161.43	Free float	100%
Target price (USD)	183.00	Sector	Water Utilities
RIC (Equity)	AWK.N	Country/Region	United States
Bloomberg (Equity)	AWK US	Analyst	Verity Mitchell
Market cap (USDm)	29,294	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 22 Apr 2021

Essential Utilities

- The growth proposition with gas decarbonisation investment
- Next catalysts in the regulatory processes, Delcora uncertainty discount should unwind in 2021
- Reiterate Buy rating, raise TP to USD57 from USD55

Investment thesis

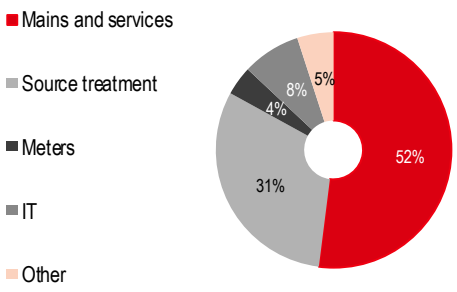
Essential Utilities' management set out its outlook for the period 2021-23 on 11 January, and confirmed it its FY2020 results on 24 February. It targets investment of USD3bn from 2021 to 2023 to maintain a 70/30 water (Aqua) to gas (Peoples) mix of business measured by size of regulated rate base. To complement its infrastructure rehabilitation, Essential is also investing in municipal acquisitions in the US states in which it operates. It has a pipeline of water acquisitions in these states and its accelerated investment programme in gas means it has not suffered as a bond proxy as much as some of its regulated peers. It has underperformed recently because of the well-publicised challenges to its acquisition of Delcora. We believe once either of these is resolved or indeed Essential walks away from the deal, this uncertainty discount should unwind.

2021 outlook

Management targets a range for 2021 EPS of USD1.64-1.69 with growth of 5-7% through to 2023. It will invest USD550m in regulated water and USD450m in its regulated gas segments.

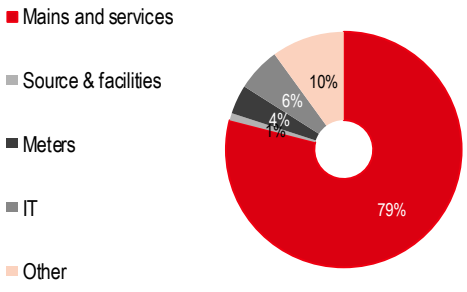
We discussed both its growth and this guidance in our report of 14 January: *Guidance update; ESG acceleration*. Management sees opportunities to add USD500m of rate base growth from a number of acquisition targets but the largest of these, Delcora, has faced a number of headwinds, as we discuss below.

Water segment capex plan through to 2023e



Source: Essential Utilities: Investors presentation – 11 January 2021

Gas segment capex plan through to 2023e



Source: Essential Utilities: Investors presentation – 11 January 2021

Caveat – why growth may not be linear

As with all regulated utilities under our coverage, it is important to note that asset and earnings growth should not be expected to be linear.

For example, Essential Utilities' management pointed out that this year, the company is preparing a water three-year rate case filing in Pennsylvania for its Aqua PA unit. Because the majority of Aqua's rate base is from Pennsylvania, this will result in a short-term earnings lag until it can recover the revenues at the new rates. Indeed, under- or over-recovery of revenues means adjustments are needed in subsequent years. However, M&A does provide some short-term support for earnings growth. Municipal acquisitions generally create a short-term earnings lag as these acquisitions rarely, if ever, earn a full return until they are included in a rate case.

Delcora – getting it done

In the light of uncertainty around the Delcora acquisition, Essential has excluded Delcora contributions from its 2021 guidance

In the light of the uncertainty around the Delcora acquisition, Essential has excluded Delcora contributions from its 2021 guidance. Post the ruling by a judge in favour of Essential's claims of legality of the purchase contract, the county has appealed to the Commonwealth Court. According to management, the ruling may take about six months. In a bid to make a better case for the deal, Essential says it will submit a rate stabilisation plan. Essential further updated that it will not delay the Aqua Pennsylvania rate case due to the pending Delcora deal.

Peoples Gas

According to management guidance, the rate base of gas segment will increase 8-10% pa to 2023

During its investor presentation in February, Essential disclosed an investment plan of USD3bn from 2021 to 2023, with USD1bn being invested in the current year to rehabilitate and strengthen water, wastewater and natural gas systems. According to the management guidance, the rate base of gas segment will increase at 8-10% per year to 2023. For the year 2021, Essential is planning to invest USD450m. Essential management hoped to used tax optimisation (using capital allowances on the balance sheet) to stay out of rates. It seems likely that this option may not be utilised for Peoples Gas. This suggests it will file for rate increases earlier. This will have no effect on earnings from an investor perspective but means customers will pay for the asset rehabilitation earlier than using balance sheet resources.

Performance against peers

Essential's stock has underperformed the S&P 500 index by 10.9% and FTSE USA growth index by 8.1% year-to-date. In our view, this is because of the newsflow on the regulatory and legal challenges to the Delcora acquisition. We believe that some of the issues have been resolved but there are still uncertainties. Essential raised 6,700,000 shares of equity in August 2020 on a forward sale basis which must be exercised by 10 August 2021. The proceeds from this equity raise was primarily for Delcora but also Essential management said, for general corporate purposes, including for water and wastewater utility acquisitions, working capital and capital expenditures.

Feedback from some investors is that the equity raise of USD300m on a deferred basis might still be drawn down even if the acquisition doesn't proceed. Essential management says it is confident there are other acquisition targets that could be funded by equity but a smaller amount of equity might be deployed. Investors need to be reassured that only the appropriate level of equity is raised for the investment needs of the business and Essential is not overcapitalised.

We believe certainty either of the success or failure of the Delcora deal should lead to the unwinding of the current uncertainty discount.

Change in estimates

We have updated our estimates post the company's FY2020 results and introduce our 2023 estimates.

Change in estimates, introducing 2023e

	2021e	2022e	2023e
EBIT (USDm)			
Revised	623	685	759
Previous	649	697	-
Change	-4%	-2%	-
Net income (USDm)			
Revised	428	467	519
Previous	420	456	-
Change	2%	2%	-
EPS (USD)			
Revised	1.64	1.79	1.94
Previous	1.67	1.81	-
Change	-2%	-1%	-
DPS (USD)			
Revised	1.07	1.15	1.23
Previous	1.07	1.15	-
Change	0%	0%	-

Source: HSBC estimates

Valuation and risks

We value Essential Utilities using the average of three approaches: DCF, dividend yield and the average of our PE multiple and rate-base valuations. After updating our earnings estimates and assumptions, we raise our target price to USD57 from USD55.

- In our DCF, we increase our Bloomberg observed five-year beta to 0.89 from 0.6. This reflects, we believe, the market volatility of interest rate rises in the US. This is the primary driver of the reduction in our DCF value to USD45.8 per share from USD56.5.
- For our yield-based valuation, we cut our target average yield to 1.64% from 2.25% in line with the water (70% of water peers' yield) and gas-related utilities peers (30% of gas peers' yield. This reflects Essential's business mix and leads us to increase our yield valuation to USD65.0 from USD47.7. This reflects the movement in peer group multiples as water and gas is seen as having more of a growth status compared to that of bond proxy stocks.
- For our approach using the average of our PE multiple and rate-base valuations, we keep our target multiple unchanged at 33.5x, in line with that of peers. We use a water and gas peer group PB average of 2.6x as a proxy for a rate-base valuation. This is consistent with all US utilities under our coverage and is a proxy for EV. Our new SOP and peer multiple value is USD58.7, down from USD61.4.

We increase our target price to USD57 from USD55, which implies 19.0% upside. We reiterate our Buy rating as we believe the combination of regulated investment growth and earnings growth remains attractive and there is scope for the current uncertainty discount to unwind.

Summary of valuation

USD	New	Previous
Current price as on 22-Apr-21	**47.9**	**NA**
DCF	45.8	56.5
Yield 1.64% (previously 2.25%)	65.0	47.7
SOP & peer multiple	58.7	61.4
Target price (average rounded)	**57.0**	**55.0**
Implied upside to target price	19%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity valuation	USDm
Cost of debt		+ DCF value	16,158
Pre-tax cost of debt	3.6%	+ ST marketable assets	0
Marginal tax rate	10.0%	+ Value of associates	0
Cost of equity		+ Other assets	1,369
Risk-free rate	2.5%	EV (asset side)	17,527
Equity risk premium	3.0%	- Net debt (+ if net cash)	(5,587)
Additional risk		- Quasi debt (pension)	0
Beta (previously 0.6)	0.89	- Value of minorities	0
Debt - 31%	3.2%	Total non-equity claims	(5,587)
Equity - 69%	5.2%	Value of equity	11,940
Cost of capital	5.2%	**Value per share (USD)**	**45.8**

Source: HSBC estimates

Average of rate base and peer multiple valuations

	2021e rate base USDm
Regulated water	
Pennsylvania	3,954
Ohio	393
Illinois	409
Texas	342
New Jersey	229
North Carolina	263
Indiana	96
Virginia	89
Regulated gas	2,634
Total	**8,409**
Price to rate base	21,864
Non-regulated 2020 PE multiple	10
Net debt 2021e, pensions & minority	(5,551)
Estimated equity value	16,323
Estimated equity value per share (USD)	**62.5**
PE multiple valuation	
2021e yield (%)	1.64
2021e PE sector average (USD)	33.5
Value per share (USD)	**54.9**
Average of rate base valuation and PE multiple valuation (USD)	**58.7**

Source: HSBC estimates

Downside risks

Essential Utilities failing to achieve the desired rate case upwards revisions and infrastructure surcharges; lacking organic growth from asset replacement; inability to take advantage of the Fair Market Value legislation opportunity; dividend growth at a lower rate than we assume; and inability to conclude the Delcora acquisition in 2021.

Financials & valuation: Essential Utilities

Buy

Financial statements

Year to	12/2020a	12/2021e	12/2022e	12/2023e
Profit & loss summary (USDm)				
Revenue	1,467	1,962	2,088	2,224
EBITDA	692	909	984	1,079
Depreciation & amortisation	-257	-286	-299	-320
Operating profit/EBIT	435	623	685	759
Net interest	-166	-168	-183	-201
PBT	265	455	502	558
HSBC PBT	268	455	502	558
Taxation	20	-27	-35	-39
Net profit	285	428	467	519
HSBC net profit	285	428	467	519
Cash flow summary (USDm)				
Cash flow from operations	508	740	773	847
Capex	-836	-1,000	-1,000	-750
Cash flow from investment	-4,334	-724	-1,000	-750
Dividends	-233	-280	-300	-328
Change in net debt	4,417	-36	526	-69
FCF equity	-328	-260	-227	97
Balance sheet summary (USDm)				
Intangible fixed assets	2,332	2,332	2,332	2,332
Tangible fixed assets	10,881	11,319	12,020	12,450
Current assets	375	449	476	504
Cash & others	5	5	5	5
Total assets	13,705	14,218	14,945	15,403
Operating liabilities	2,041	2,141	2,175	2,211
Gross debt	5,630	5,594	6,121	6,052
Net debt	5,625	5,589	6,116	6,047
Shareholders' funds	4,684	5,132	5,299	5,790
Invested capital	11,542	11,954	12,648	13,070

Ratio, growth and per share analysis

Year to	12/2020a	12/2021e	12/2022e	12/2023e
Y-o-y % change				
Revenue	64.9	33.7	6.4	6.5
EBITDA	39.2	31.4	8.3	9.6
Operating profit	27.8	43.3	10.0	10.7
PBT	25.3	71.9	10.2	11.2
HSBC EPS	7.6	46.7	9.1	8.6
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	5.3	5.0	5.2	5.5
ROE	6.7	8.7	9.0	9.4
ROA	4.2	4.2	4.4	4.7
EBITDA margin	47.2	46.3	47.1	48.5
Operating profit margin	29.6	31.8	32.8	34.1
EBITDA/net interest (x)	4.2	5.4	5.4	5.4
Net debt/equity	120.1	108.9	115.4	104.4
Net debt/EBITDA (x)	8.1	6.2	6.2	5.6
CF from operations/net debt	9.0	13.2	12.6	14.0
Per share data (USD)				
EPS Rep (diluted)	1.12	1.64	1.79	1.94
HSBC EPS (diluted)	1.12	1.64	1.79	1.94
DPS	1.00	1.07	1.15	1.23
Book value	18.39	19.67	20.31	21.67

Valuation data

Year to	12/2020a	12/2021e	12/2022e	12/2023e
EV/sales	11.8	8.8	8.6	8.0
EV/EBITDA	25.1	19.1	18.2	16.5
EV/IC	1.5	1.5	1.4	1.4
PE*	42.8	29.2	26.7	24.6
PB	2.6	2.4	2.4	2.2
FCF yield (%)	-2.8	-2.2	-1.9	0.8
Dividend yield (%)	2.1	2.2	2.4	2.6

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2019a
GHG emission intensity*	n/a
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social Indicators	**12/2019a**
Employee costs as % of revenues	n/a
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	12/2020a
No. of board members	8
Average board tenure (years)	7.0
Female board members (%)	25
Board members independence (%)	87.5

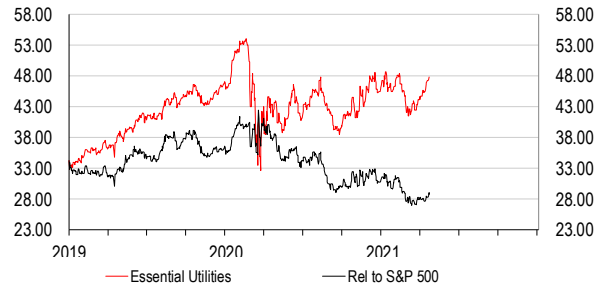
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	47.9	Free float	100%
Target price (USD)	57.00	Sector	Water Utilities
RIC (Equity)	WTRG.N	Country/Region	United States
Bloomberg (Equity)	WTRG US	Analyst	Verity Mitchell
Market cap (USDm)	11,751	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 22 Apr 2021

Pennon

- Trading update, positive FY21 guidance, possible news on cash deployment by June results
- Green Recovery push potential for cGBP92m of additional investment
- Downgrade to Hold from Buy with unchanged TP of 1,090p after strong performance; better to travel than to arrive

Investment thesis

The case for paying a premium to RCV has been strengthened by NG's premium paid for WPD (a fast-tracked sector leader). Many of Pennon's unlisted water potential targets have a combination of complicated (with derivatives) balance sheets with higher leverage, or significant operational challenges

Pennon shares have had a strong recent performance driven by M&A expectations and strong initial regulatory performance. Its reinvestment decisions will provide an interesting regulatory precedent depending on where it chooses to invest its waste proceeds for growth. It could be bold and buy a large water company and plan ambitious expansion or look for a smaller water-only company and give the proceeds back to shareholders. As the sector resilience needs are significant, we think management may think big. The case for paying a premium to RCV has been strengthened by National Grid's premium paid in March 2020 for WPD (a fast-tracked sector leader). Many of Pennon's unlisted water potential targets have a combination of complicated (with derivatives) balance sheets with higher leverage, or significant operational challenges as can be seen from the table on page 12 above. The ability to create value, as it did with Bournemouth Water, is a much more arduous task.

Trading update: growing regulatory return, M&A clarity in June

Pennon confirmed its FY2020/21 performance is in line with management expectations. It continues to expect a doubling of base RORE of 3.9% from total expenditure and financial outperformance, which remains in line with the H1 (April-September) number of 8%. The company anticipates a net ODI penalty (despite 80% ODIs on or ahead of targets) position for the year due to underperformance associated with pollution incidents. However, a COVID-19 financial impact is as anticipated. Pennon further suggested that cash collections in H2 have been robust and no new debtors provisions are added.

It confirmed that if a major deal is not completed, a substantial return of capital to shareholders will be made

There was no update on capital allocation plans, with clarity now expected at the FY2020/21 results in June. With GBP3bn cash and committed facilities, PNN is in a good financial position to carry out M&A. Pennon's management believes there is significant potential in the UK water sector and it continues to narrow down its review of potential growth opportunities to reinvest the proceeds from the Viridor sale in 2020. Moreover, Pennon has confirmed that if a major M&A opportunity is not available, a substantial return of capital to shareholders will be made.

Green Recovery initiative

Pennon has proposed a GBP92m Green Recovery investment for the period to 2025, which will mark a 10% increase in its existing GBP1bn investment programme for the period. It has proposed six projects focused on improving public health, protecting the environment and addressing climate change. Pennon has suggested that the impact on customer bills be paused until 2025. Ofwat will announce its preliminary views on the proposals in May.

Performance against peers

Pennon shares have underperformed the FTSE All share index by 19.4% year-to-date and underperformed other listed UK water companies. Lack of visibility on the deployment of cash may be driving this. It has announced it is evaluating M&A options in the UK water space and an update is expected during its full-year results in June. The current lack of visibility may hinder its performance in the short term, but management has confirmed a return of value is possible either through M&A or a share buyback in the medium term. It still appears to have some inverse correlation to gilt yields.

Change in estimates

We update our estimates post the trading update to reflect a slightly higher interest charge than we had assumed previously.

Change in estimates

GBPm	2021e	2022e	2023e
EBITDA			
Revised	327	336	355
Previous	327	336	355
Change	0%	0%	0%
EBIT			
Revised	205	218	233
Previous	205	221	235
Change	0%	-1%	-1%
PBT			
Revised	144	153	168
Previous	151	153	165
Change	-4%	0%	2%
Net income (continuing)			
Revised	121	128	141
Previous	127	128	139
Change	-4%	0%	1%
EPS (continuing, p)			
Revised	28.8	30.5	33.5
Previous	30.2	30.4	32.8
Change	-5%	0%	2%
DPS (p)			
Revised	21.7	22.5	23.4
Previous	21.8	22.6	23.5
Change	-0.5%	-0.5%	-0.5%

Source: HSBC estimates

Valuation and risks

We value Pennon shares using three valuation approaches: DCF, dividend yield and sum-of the-parts. We assign a 50% weight to yield and 25% each to DCF and SOTP, rounded, to arrive at our target price of 1,090p (unchanged).

- In the DCF valuation, we change our forward estimates for 2021 and onwards to reflect the guidance by management during the trading update for FY2020/21. We also update our tax rate and interest rate as per company guidance. We take the five-year Bloomberg observed beta of 0.70 (unchanged). We revise our RfR to reflect the HSBC Fixed Income team view of 10-year gilt rates to 50bp from 30bp previously. To this we add a 150bp premium. This increases our RfR to 2.0% from 1.83% previously. This increases our WACC to 3.8% from 3.6%. Because of the Green Recovery potential additional growth, we increase our terminal growth value in our DCF to 1.25% from 1.0%. We also update the pension deficit for the H1 results. These changes lead to a net increase in our DCF valuation to 1,439p from 1,249p.
- In the yield valuation, we add an unchanged premium of 0.25% to our revised RfR, increasing our yield to 2.55% from 2.08%. This reduces our yield value to 1,001p from 1,088p.
- In the SOTP valuation, we continue to assume net proceeds of GBP2.7bn from the sale of Viridor. We use South West Water's RCV to March 2022 for the basis of our SOTP. The higher WACC leads to a lower value creation assumption than previously but is offset by the assumption that Pennon is able to earn a 10% return on the Green Recovery investment (the same proportion we calculate for our value creation relative to its RCV) which we add to our value creation assumption. These changes lead us to increase in our SOTP valuation to 928p from 925p.

Our target price of 1,090p is unchanged and implies upside of 5.9%. We downgrade our rating to Hold from Reduce reflecting the strong recent share price performance.

Summary of valuation (p)

	New	Previous
Current price as on 22-Apr-21	**1,030**	**NA**
DCF	1,439	1,249
Yield 2.55% (vs 2.08%)	1,001	1,088
SOP	928	925
Target price (average rounded)	**1,090**	**1,090**
Implied upside to our TP	5.9%	NA
Rating	**Hold**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity valuation	GBPm
Cost of debt		**DCF value**	**5,996**
Pre-tax cost of debt	2.5%	Viridor net assets	0
Marginal tax rate	19.0%	**EV (asset side)**	**5,996**
Cost of equity		- Net debt (+ if net cash)	101
Risk-free rate (previously 1.83%)	2.0%	- Quasi debt (pension)	(52)
Equity risk premium	4.0%	- Value of minorities	(0)
Beta (unchanged)	**0.70**	- hybrid	0
Cost of debt - 37%	2.0%	Total non-equity claims	48
Cost of equity - 63%	4.9%	Value of Equity	6,045
Cost of capital	**3.8%**	**Value per share (p)**	**1,439**

Source: HSBC estimates

SOP valuation

	GBPm	EV RCV (combined)	GBPm
South West Water RCV 2022e	3,493	Net debt	2,612
Allowed return	355	Market cap	4,377
Total SWW	**3,848**	Less non-regulated	(2,700)
Total Viridor		Market implied utility value	4,289
PNN enterprise value	**3,848**	**Premium**	**22.8%**
Net debt 2022e, pensions & minority	52		
Estimated equity value	3,900		
Equity value per share (p)	**928**		

Source: HSBC estimates

Upside risks

- Pennon acquires a regulated water company that demonstrates a clear value creation proposition to shareholders
- Pennon cannot create shareholder value through acquisition and returns the proceeds to shareholders, enhancing earnings and yield through a share consolidation.

Downside risks

- For SWB, not being able to achieve the efficiency challenges in its business plan for 2020-25 and not being able to achieve the ODI rewards needed to support the dividend policy.
- Bad debts may continue to rise in SWB and Pennon Water Services from the current challenging economic conditions.
- Pennon is unable to expand profitably in UK water from a lack of opportunities that create value.
- It provides no clarity on its reinvestment strategy of return of proceeds by the time of the FY 2021 results in May.

Financials & valuation: Pennon Group

Hold

Financial statements

Year to	03/2020a	03/2021e	03/2022e	03/2023e
Profit & loss summary (GBPm)				
Revenue	637	603	615	633
EBITDA	365	327	336	355
Depreciation & amortisation	-120	-122	-118	-122
Operating profit/EBIT	246	205	218	233
Net interest	-63	-60	-65	-65
PBT	277	144	153	168
Taxation	-71	-14	-24	-27
Net profit	206	1,793	128	141
Cash flow summary (GBPm)				
Cash flow from operations	366	1,856	293	260
Capex	-323	-145	-198	-201
Cash flow from investment	-323	1,774	-198	-201
Dividends	-173	-184	-91	-95
Change in net debt	-31	-3,149	-3	36
FCF pre dividends	43	1,711	95	59
Balance sheet summary (GBPm)				
Intangible fixed assets	44	44	44	44
Tangible fixed assets	3,172	3,194	3,274	3,353
Current assets	861	2,979	2,938	2,909
Cash & others	666	2,712	2,715	2,680
Total assets	4,081	6,220	6,260	6,310
Operating liabilities	1,073	328	331	335
Financial liabilities	3,715	2,612	2,612	2,612
Total liabilities	5,050	3,202	3,205	3,208
Net debt	3,049	-101	-104	-68
Shareholders' funds	1,712	3,025	3,062	3,108

Ratio, growth and per share analysis

Year to	03/2020a	03/2021e	03/2022e	03/2023e
Y-o-y % change				
Revenue	-56.9	-5.4	2.0	2.9
EBITDA	-29.8	-10.5	2.8	5.6
Operating profit	-24.5	-16.7	6.7	6.8
PBT	6.4	-47.8	5.9	9.7
HSBC EPS	-32.5	-18.1	5.9	9.7
Ratios (%)				
ROE	8.7	5.1	4.2	4.6
ROCE	4.7	33.4	3.2	3.4
EBITDA margin	57.4	54.3	54.7	56.1
Operating profit margin	38.6	33.9	35.5	36.8
Net debt/equity	178.1	-3.3	-3.4	-2.2
CF from operations/net debt	12.0			
Per share data (GBPp)				
EPS reported (diluted)	61.71	28.20	30.50	33.46
HSBC EPS (diluted)	35.17	28.80	30.50	33.46
DPS	43.77	21.70	22.52	23.44
Gross CFPS	0.99	4.55	0.58	0.62

Valuation data

Year to	03/2020a	03/2021e	03/2022e	03/2023e
EV/sales	11.6	7.0	6.9	6.7
EV/EBITDA	20.2	12.9	12.6	12.0
P/CF	10.4	2.3	17.5	16.4
PE*	29.1	35.6	33.6	30.6
FCF yield (pre div) (%)	1.0	39.6	2.2	1.4
Dividend yield (%)	4.3	2.1	2.2	2.3

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	03/2020a
GHG emission intensity*	2,644.9
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social Indicators	**03/2020a**
Employee costs as % of revenues	13.5
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	03/2021a
No. of board members	7
Average board tenure (years)	5.6
Female board members (%)	42.9
Board members independence (%)	57.1

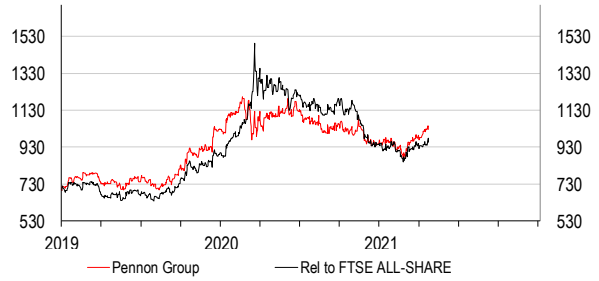
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (GBPp)	1,030	Free float	100%
Target price (GBPp)	1,090	Sector	Water Utilities
RIC (Equity)	PNN.L	Country/Region	United Kingdom
Bloomberg (Equity)	PNN LN	Analyst	Verity Mitchell
Market cap (USDm)	6,025	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 22 Apr 2021

Severn Trent

- Analysing the trading update, Green Recovery capex plans
- Still commands RCV premium relative to peers, despite Hafren Dyfrdwy performance and lack of M&A aspirations
- Retain Hold rating and raise TP to 2,570p from 2,450p on higher growth potential from Green Recovery

Investment thesis

Severn Trent continues to set itself out as an innovator with underlying growth and ideas for green investment. Management said in 2020 that M&A was not part of its strategy. It still has much work to do on Hafren Dyfrdwy, the water company it owns. We understand from the pre-close statement that management is focused on improvement in many areas. Severn Trent consistently trades at a premium to RCV to the other two UK listed stocks, currently at c20%, reflecting its higher RCV growth and recently its significant Green Recovery investment plans. We do not see therefore sufficient additional value to justify a Buy rating and remain at Hold.

Trading update for FY21

Company increased guidance for outperformance on Customer ODIs this year from GBP25m to at least GBP50m

SVT said at its trading update on 4 February 2021 that it remained on or ahead of its target for almost 80% of its customer performance measures. The company has therefore increased its guidance for outperformance on Customer ODIs this year from GBP25m to at least GBP50m.

Green Recovery initiative

SVT has applied for a cGBP730m package under Green Recovery

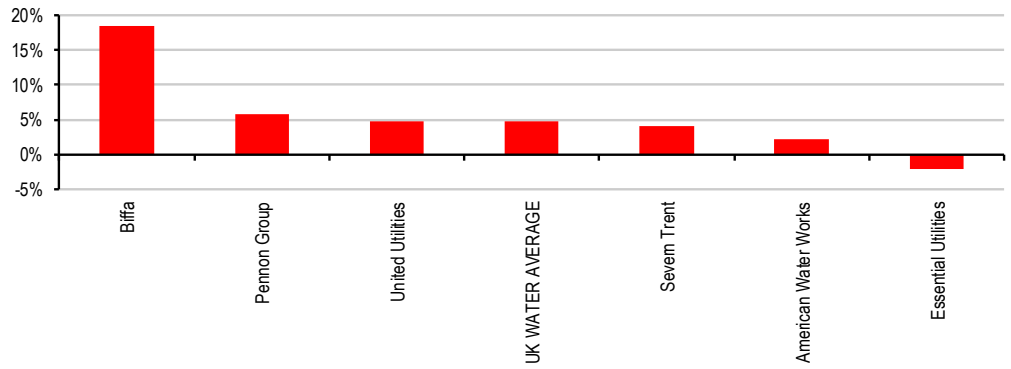
Severn Trent has applied for a cGBP730m package under Green Recovery. This investment plan is above the base capex plan of GBP3bn for the period 2021-25 (which would have delivered 4% RCV growth target for AMP7, the highest of its peers).

The water company said that only 15% of the cost would go directly onto customers' bills – Severn Trent will provide 85% of the funding needed upfront by raising new finance, which will then be recovered over a longer time period. Severn Trent estimates the extra cost to customers will be GBP6 per year on average.

Performance against peers

Pennon and UU shares have outperformed Severn Trent but in our view both have had a higher profile: Pennon through M&A and United Utilities at its CMD. However, Severn Trent consistently trades at a premium to RCV to the other two listed stocks, currently at c20%, and so we do not see sufficient additional value to justify a Buy rating. Our higher target price of 2,570p implies 5.0% upside and we maintain our Hold rating.

Relative return vs sector benchmark index y-t-d



Source: Refinitiv Datastream

Change in estimates

We update our estimates post trading update for FY2020/21.

Change in estimates

GBPm	2021e	2022e	2023e
EBIT			
Revised	476	548	625
Previous	492	546	607
Change	-3%	0%	3%
PBT			
Revised	279	352	422
Previous	289	350	404
Change	-3%	1%	4%
EPS (p)			
Revised	105.5	131.0	154.6
Previous	109.3	131.6	151.4
Change	-3%	0%	2%
DPS (p)			
Revised	100.58	102.38	104.50
Previous	100.71	102.51	104.63
Change	-0.1%	-0.1%	-0.1%

Source: HSBC estimates

Valuation and risks

We value Severn Trent shares using three valuation approaches: DCF, dividend yield and sum of the parts. We assign a 50% weight to yield and 25% each to DCF and SOTP, rounded to arrive at our new target price of 2,570p from 2,450p, after adjusting our earnings estimates and assumptions.

- In the DCF valuation, we change our forward estimates for 2021 and onwards to reflect the guidance given by management during the trading update for FY2020/21. We also update our tax rate as well as interest rate as per company guidance. We take an observed Bloomberg five-year beta of 0.71 (changed from 0.75 from the previous Bloomberg estimates used in December 2020). We revise our RfR to reflect the HSBC Fixed Income view of 10-year gilt rates to 50bp from 30bp previously. To this we add at 150bp premium. This increases our RfR to 2.0% from 1.83% previously. This increases our WACC to 3.9% from 3.8%. Because of the Green Recovery potential additional growth, we increase the

terminal growth value in our DCF to 1.5% from 1.0%. We also update the pension deficit for the H1 results. This increases our DCF to 3,190p from 2,452p.

- In the yield valuation, a premium of 1.75% is added to our revised RfR (2%) resulting in a yield of 3.75% (previously 3.58%). The higher RfR reduces our yield valuation to 2,730p from 2,860p.
- In our sum of the parts we assume that Severn Trent is able to earn a 6% return on the Green Recovery investment (the same proportion we calculate for our value creation relative to its RCV) which we add to our value creation assumption. This increases the SoP value to 1,637p from 1,625p.

Our new target price of 2,570p implies upside of 5.0%. We maintain our Hold rating as we think the accelerated Green Recovery potential and underlying RCV growth are fully reflected in its price. We also note the relatively weaker financial profile of Severn Trent vs peers.

Summary of valuation (p)

	New	Previous
Current price as on 22-Apr-21	**2,447**	**NA**
DCF	3,190	2,452
SOP	1,637	1,625
Yield 3.75% (previously 3.58%)	2,730	2,860
Target price (average rounded)	**2,570**	**2,450**
Implied upside to target price	5.0%	NA
Rating	**Hold**	**Hold**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity valuation	GBP m
Cost of debt		**+ DCF value**	**14,590**
Pre-tax cost of debt	3.3%	+ ST marketable assets	0
Marginal tax rate	11.0%	+ Value of associates	0
Cost of equity		+ Other assets	0
Risk-free rate (previously 1.83%)	2.0%	**EV (asset side)**	**14,590**
Equity risk	4.0%	- Net debt (+ if net cash)	(6,378)
Additional risk	0.00	- Quasi debt (pension)	(613)
Beta (vs 0.75)	**0.71**	- Value of minorities	0
Debt - 53%	2.9%	Total non-equity claims	(6,992)
Equity - 47%	4.9%	Value of Equity	7,598
Cost of capital	3.9%	**Value per share (p)**	**3,190**

Source: HSBC estimates

SOP valuation

	GBPm	EV RCV	GBPm
2021e RCV	9,730	Net debt	6,598
Value creation	611	Market cap	5,860
Total	10,478	Less non reg	(624)
Business Services	624	Market implied utility RCV	11,834
EV	11,100	RCV	9,730
Other assets	0	RCV premium	21.6%
Net debt 2021e, pensions & minority	(6,598)		
Total estimated equity value	3,899		
Equity value per share (p)	1,637		

Source: HSBC estimates

Upside risks

Severn Trent delivers additional operational total expenditure (totex) and ODI savings, driving higher EPS for FY 2020/21; property disposals above Severn Trent's GBP100m commitment; and growth in its Business Services division above our assumption.

Downside risks

Severn Trent faces higher costs than we assume, driving lower EPS for 2020/21; it may need to take remedial efforts to strengthen its balance sheet towards the end of the five-year period, which would be dilutive to shareholders.

Financials & valuation: Severn Trent

Hold

Financial statements

Year to	03/2020a	03/2021e	03/2022e	03/2023e
Profit & loss summary (GBPm)				
Revenue	1,741	1,786	1,797	1,904
EBITDA	908	860	940	1,041
Depreciation & amortisation	-367	-385	-392	-416
Operating profit/EBIT	541	476	548	625
Net interest	-206	-187	-198	-205
PBT	284	279	352	422
HSBC PBT	284	279	352	422
Taxation	-152	-55	-69	-83
Net profit	132	251	313	371
HSBC net profit	132	251	313	371
Cash flow summary (GBPm)				
Cash flow from operations	865	776	692	745
Capex	-804	-577	-614	-644
Cash flow from investment	-802	-633	-669	-699
Dividends	-228	-239	-243	-249
Change in net debt	371	154	220	203
FCF equity	61	198	78	101
Balance sheet summary (GBPm)				
Intangible fixed assets	245	245	245	245
Tangible fixed assets	9,581	9,774	9,995	10,223
Current assets	760	832	819	864
Cash & others	49	49	49	49
Total assets	10,780	11,100	11,364	11,693
Operating liabilities	1,925	1,939	1,943	1,978
Gross debt	6,433	6,587	6,807	7,010
Net debt	6,224	6,378	6,598	6,801
Shareholders' funds	1,244	1,171	1,212	1,303
Invested capital	8,613	8,863	9,067	9,306

Ratio, growth and per share analysis

Year to	03/2020a	03/2021e	03/2022e	03/2023e
Y-o-y % change				
Revenue	4.3	2.6	0.6	6.0
EBITDA	5.6	-5.2	9.2	10.7
Operating profit	-0.6	-12.0	15.1	14.0
PBT	-22.4	-1.5	26.1	19.9
HSBC EPS	-56.1	91.9	24.2	18.1
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	3.0	4.4	4.9	5.5
ROE	10.9	20.8	26.3	29.5
ROA	2.1	3.7	4.2	4.6
EBITDA margin	52.1	48.2	52.3	54.7
Operating profit margin	31.1	26.7	30.5	32.8
EBITDA/net interest (x)	4.4	4.6	4.8	5.1
Net debt/equity	500.5	544.8	544.9	522.6
Net debt/EBITDA (x)	6.9	7.4	7.0	6.5
CF from operations/net debt	13.9	12.2	10.5	11.0
Per share data (GBPp)				
EPS Rep (diluted)	54.97	105.49	130.98	154.63
HSBC EPS (diluted)	54.97	105.49	130.98	154.63
DPS	100.08	100.58	102.38	104.50
Book value	522.56	491.78	506.77	542.57

Valuation data

Year to	03/2020a	03/2021e	03/2022e	03/2023e
EV/sales	6.9	6.8	6.9	6.6
EV/EBITDA	13.3	14.1	13.1	12.0
EV/IC	1.4	1.4	1.4	1.3
PE*	44.5	23.2	18.7	15.8
PB	4.7	5.0	4.8	4.5
FCF yield (%)	1.1	3.4	1.3	1.7
Dividend yield (%)	4.1	4.1	4.2	4.3

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	03/2020a
GHG emission intensity*	160.8
Energy intensity*	920.9
CO_2 reduction policy	Yes
Social Indicators	**03/2020a**
Employee costs as % of revenues	19.8
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	03/2021a
No. of board members	9
Average board tenure (years)	4.1
Female board members (%)	55.6
Board members independence (%)	66.7

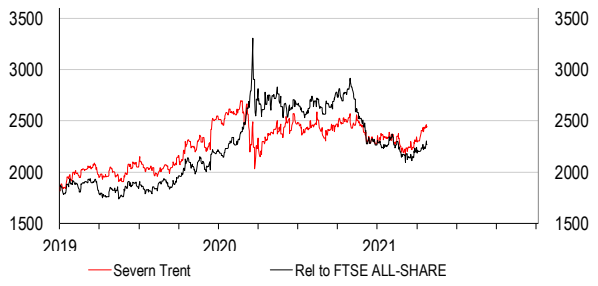
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (GBPp)	2,447	Free float	100%
Target price (GBPp)	2,570	Sector	Water Utilities
RIC (Equity)	SVT.L	Country/Region	United Kingdom
Bloomberg (Equity)	SVT LN	Analyst	Verity Mitchell
Market cap (USDm)	8,093	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 22 Apr 2021

United Utilities

- Trading update: FY21 revenue 3% lower, earnings 10% higher due to lower finance costs, Tallinn sale impact moves to next year
- Technology-driven GBP20m ODI outperformance, still ex-growth – most at risk of bond proxy correlation
- Downgrade to Reduce from Hold and cut TP to 910p from 960p on higher RfR assumption

Investment thesis

It has the highest dividend yield and the lowest Green Recovery list of potential projects compared to its current investment

United Utilities still struggles to avoid its bond proxy status. Of all the water stocks under our coverage it has the highest dividend yield and the lowest Green Recovery list of potential projects compared to its current investment. It continues to bring forward investment to drive ODI performance but management seems to have backtracked on exploring M&A opportunities in UK water despite a significant operational improvement.

Despite UU's significant operational improvements, its asset base is shrinking

Despite UU's significant operational improvements, its asset base is shrinking. Ofwat is looking at the Haweswater Aqueduct Resilience Programme (HARP) project as a blueprint for attracting additional capital for major projects to the sector but it will have to prove convincingly that project finance without government guarantees with the additional cost of finance, lawyers, and cost duplication will deliver better value to shareholders. HARP in particular is a risky project. We remain sceptical that it can be delivered at a lower cost to UU's customers, bearing in mind that Thames Tideway, another significant project (Thames Water), needed a government guarantee.

Trading update for FY21

UU issued a trading update on 25 March 2021. Management expects 3% lower revenue for FY 2020/21. Volumes have recovered in H2, compared to an H1 decline of 5%. Underlying operating profit for FY2020/21 is expected to be lower than in FY2019/20, largely reflecting the lower revenue and an increase in infrastructure renewals expenditure (IRE). The company expects its finance expenses to be cGBP100m lower than last year due to lower inflation applied to the group's index-linked debt. It has now adopted alternative performance measures (APMs) excluding what it says are non-core finance charges such as interest related to pensions. The recovery in H2 has also led to no extra provisions for bad debt, with only GBP17m bad debts aged more than a year. UU updated on its stake sale in Tallinn for EUR100m. The deal is pending regulatory clearance and realisation will move to next year.

Technology-driven GBP20m ODI outperformance

UU reiterated its ODI guidance of GBP20m announced during the capital markets day in early March

United Utilities reiterated its ODI guidance of GBP20m announced during the capital markets day in early March. The rewards are a result of accelerated investments in technology, automation and machine intelligence developed over the last five years. Moreover, UU recorded the lowest ever level of leakage and interruptions to water supply, which more than halved in the last 12 months.

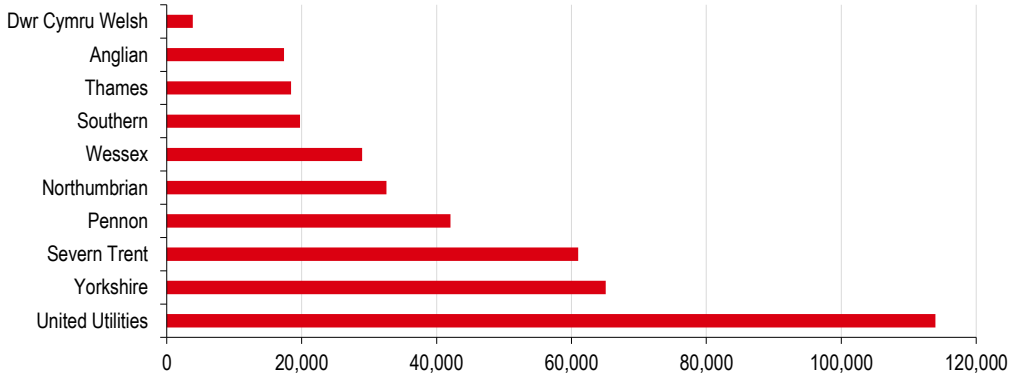
Green Economic Recovery spend

UU has proposed to DEFRA and Ofwat a total of a further GBP135m investment in AMP7 (2020-2025) pending regulatory approval as part of the Green Economic Recovery. Of this GBP135m, GBP119m is enhancement expenditure, which UU is proposing to bring forward from future AMP8 plans into AMP7. The proposal also includes delaying the recovery through customer bills until 2025-2030.

Panorama investigation highlights a continuing weakness in UU's infrastructure

Although the BBC Panorama broadcast on 13 April highlighting UK water companies have been illegally dumping untreated sewage into rivers is arguably investigative journalism of an emotive nature, United Utilities remains a significant outlier. Whether this is from the nature of its Lake District geography or insufficient funding provided in price reviews, it still detracts from its reputation as an environmental company. Unlike Pennon, which has made very public statements about the focus from top management on reducing pollution incidents, UU has said little about this publicly.

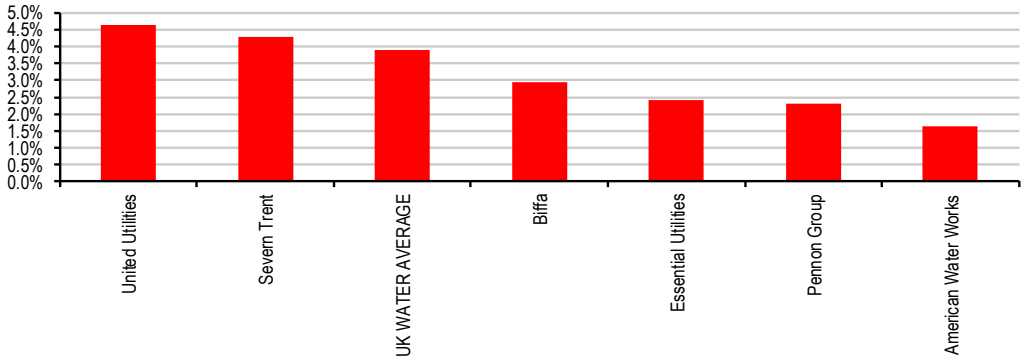
Number of storm water overflows, 2020



Source: Environment Agency

Performance against peers

2022e dividend yield for UK water and waste companies under our coverage



Source: HSBC estimates

Change in estimates

We update our estimates post trading update for FY2020/21.

Change in estimates

GBPm	2021e	2022e	2023e
EBITDA			
Revised	1,017	1,032	1,067
Previous	998	1,018	1,051
Change	*1.9%*	*1.4%*	*1.5%*
EBIT			
Revised	596	603	634
Previous	565	582	612
Change	*5.5%*	*3.7%*	*3.5%*
EPS (new method - pre deferred tax)			
Revised	55.3	56.6	61.3
Previous	45.5	46.5	49.2
Change	*21.6%*	*21.8%*	*24.5%*
DPS			
Revised	42.93	43.70	44.60
Previous	42.87	43.63	44.54
Change	*0.1%*	*0.2%*	*0.1%*

Source: HSBC estimates

Valuation and risks

We value United Utilities shares using three valuation approaches: DCF, dividend yield and sum of the parts. We assign a 50% weight to yield and 25% each to DCF and SOTP, rounded, to arrive at our lower target price of 910p from 960p.

- In our DCF valuation, we revise our RfR to reflect the new HSBC Fixed Income team view of 10-year gilt rates to 50bp from 33bp previously. To this we add a 150bp premium. This increases our RfR to 20% from 1.83% previously. We change our five-year Bloomberg observed beta to 0.73 from 0.75 because of share price movements since our last update in December 2020. We update our DCF estimates to reflect the phasing of capex that UU has brought forward in order to drive more ODI rewards. We increase our terminal value by 10bp to 1.10% because of the additional Green Recovery investment. This together reduces our DCF value to 939p from 1,064p.

- In our yield valuation we have updated our yield assumption to 4.25% from 4.58% based on higher RfR the premium of 2.25% remains unchanged. This reduces our valuation to 971p from 1,098p.
- In our SOP valuation, we assume that UU is able to earn a 4% return on the Green Recovery investment (the same proportion we calculate for our value creation relative to its RCV) which we add to our value creation assumption. This leads to an increase in our SOP valuation to 770p from 751p.

Overall, we reduce our target price to 910p from 960p, implying 6.0% downside from the current share price. We downgrade to Reduce from a Hold rating. We believe as a bond proxy with the most limited scope for Green Recovery of its peers, it is most at risk from rate increases.

Summary of valuation

	New	Previous
Current price on 22-Apr-21	**968**	**NA**
DCF (updated estimates)	939	1,064
Yield 4.25% (vs 4.58%)	971	1,098
SoP (updated estimates)	770	751
Target price (average rounded)	**910**	**950**
Implied downside to target price	-6.0%	NA
Rating	**Reduce**	**Hold**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs	`	Equity valuation	GBP m
Cost of debt		**+ DCF value**	13,870
Pre-tax cost of debt	3.2%	+ ST marketable assets	-
Marginal tax rate	18.0%	+ Value of associates	0
Cost of equity		+ Other assets	0
Risk-free rate (previously 1.83%)	2.0%	**EV (asset side)**	13,870
Equity risk premium	4.0%	- Net debt (+ if net cash)	(7,464)
Additional risk	0.0	- Quasi debt (pension)	0
Beta (previously 0.75)	0.73	- Value of minorities	-
Debt - 56%	2.6%	Total non-equity claims	(7,464)
Equity - 44%	5.0%	Value of Equity	6,406
Cost of capital	3.6%	**Value per share (GBp)**	939

Source: HSBC estimates

SOP valuation

	GBPm	EV RCV	GBPm
2021e RCV	12,073	Net debt	7,497
NPV of spread between achieved return and WACC	518	Market cap	6,635
Total	12,591	Less non-regulated	-
		Market implied utility value	14,132
Extra capex (not included in RCV)	100	Premium	17.1%
United Utilities EV	**12,691**	**Utility equity value**	**671**
Net debt 2021e, pensions & Minority	(7,497)		
Total estimated equity value	5,250		
Equity value per share (p)	**770**		

Source: HSBC estimates

Upside risks

(1) UU may reduce its bad debt provision potentially because better debt management at the end of the furlough scheme having not increased it at the H1; (2) UU delivers operational savings, decreasing its total expenditure (totex) over the five-year period relative to its regulatory allowances and increasing its ODI net rewards; and (3) in the medium term the HARP project is considered not to be achievable on a competitively tendered basis at a lower cost and risk to customers and the investment is then added back to UU's RCV, delivering accelerated growth from 2025 onwards.

Financials & valuation: United Utilities

Reduce

Financial statements

Year to	03/2020a	03/2021e	03/2022e	03/2023e
Profit & loss summary (GBPm)				
Revenue	1,859	1,802	1,793	1,813
EBITDA	1,113	1,017	1,032	1,067
Depreciation & amortisation	-483	-421	-429	-433
Operating profit/EBIT	630	596	603	634
Net interest	-284	-147	-149	-150
PBT	341	439	449	486
Taxation	-235	-70	-72	-78
Net profit	107	373	382	413
Cash flow summary (GBPm)				
Cash flow from operations	810	781	815	851
Capex	-680	-629	-554	-471
Cash flow from investment	-594	-629	-466	-471
Dividends	-285	-290	-293	-298
Change in net debt	294	103	32	-83
FCF pre dividends	130	152	260	381
Balance sheet summary (GBPm)				
Intangible fixed assets	189	189	189	189
Tangible fixed assets	11,511	11,719	11,844	11,882
Current assets	828	872	871	874
Cash & others	528	528	528	528
Total assets	13,290	13,542	13,578	13,619
Operating liabilities	1,240	1,266	1,264	1,268
Financial liabilities	8,507	8,610	8,555	8,472
Total liabilities	11,082	11,215	11,162	11,088
Net debt	7,361	7,464	7,497	7,414
Shareholders' funds	2,962	2,980	3,069	3,184

Ratio, growth and per share analysis

Year to	03/2020a	03/2021e	03/2022e	03/2023e
Y-o-y % change				
Revenue	2.2	-3.1	-0.5	1.1
EBITDA	8.0	-8.6	1.5	3.4
Operating profit	-0.7	-5.5	1.3	5.0
PBT	-20.5	28.5	2.4	8.1
HSBC EPS	-16.8	25.0	2.4	8.1
Ratios (%)				
ROE	10.0	12.5	12.6	13.2
ROCE	1.8	4.4	4.4	4.7
EBITDA margin	59.9	56.4	57.6	58.8
Operating profit margin	33.9	33.1	33.7	35.0
Net debt/equity	248.5	250.4	244.2	232.8
CF from operations/net debt	11.0	10.5	10.9	11.5
Per share data (GBPp)				
EPS reported (diluted)	44.24	54.67	55.98	60.54
HSBC EPS (diluted)	44.24	55.31	56.64	61.25
DPS	42.60	42.93	43.70	44.60
Gross CFPS	1.35	1.17	1.20	1.25

Valuation data

Year to	03/2020a	03/2021e	03/2022e	03/2023e
EV/sales	7.5	7.8	7.9	7.7
EV/EBITDA	12.5	13.8	13.7	13.1
P/CF	7.2	8.3	8.1	7.8
PE*	22.0	17.6	17.2	15.9
FCF yield (pre div) (%)	2.0	2.3	3.9	5.7
Dividend yield (%)	4.4	4.4	4.5	4.6

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	03/2020a
GHG emission intensity*	119.1
Energy intensity*	416.6
CO_2 reduction policy	Yes
Social Indicators	**03/2020a**
Employee costs as % of revenues	15.5
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	03/2021a
No. of board members	11
Average board tenure (years)	6.2
Female board members (%)	27.3
Board members independence (%)	72.7

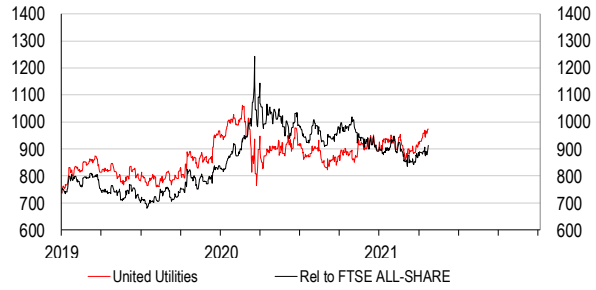
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (GBPp)	968	Free float	100%
Target price (GBPp)	910	Sector	Multi-Utilities
RIC (Equity)	UU.L	Country/Region	United Kingdom
Bloomberg (Equity)	UU/ LN	Analyst	Verity Mitchell
Market cap (USDm)	9,264	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 22 Apr 2021

Disclosure appendix

Analyst Certification

The following analyst(s), economist(s), or strategist(s) who is(are) primarily responsible for this report, including any analyst(s) whose name(s) appear(s) as author of an individual section or sections of the report and any analyst(s) named as the covering analyst(s) of a subsidiary company in a sum-of-the-parts valuation certifies(y) that the opinion(s) on the subject security(ies) or issuer(s), any views or forecasts expressed in the section(s) of which such individual(s) is(are) named as author(s), and any other views or forecasts expressed herein, including any views expressed on the back page of the research report, accurately reflect their personal view(s) and that no part of their compensation was, is or will be directly or indirectly related to the specific recommendation(s) or views contained in this research report: Verity Mitchell and Adam Dickens

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Equities: Stock ratings and basis for financial analysis

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From 23rd March 2015 HSBC has assigned ratings on the following basis:

The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

Prior to this date, HSBC's rating structure was applied on the following basis:

For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

As of 23 April 2021, the distribution of all independent ratings published by HSBC is as follows:

Buy	58%	(29% of these provided with Investment Banking Services)
Hold	34%	(28% of these provided with Investment Banking Services)
Sell	8%	(25% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

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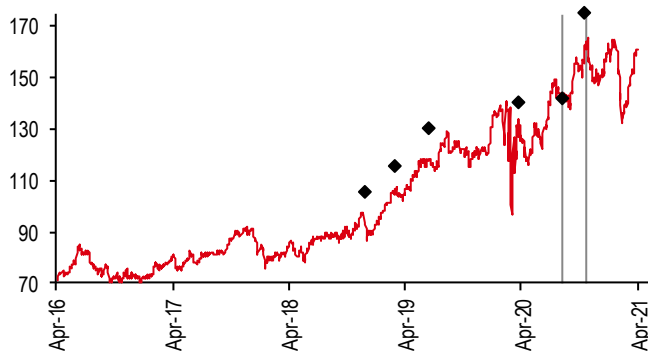
Share price and rating changes for long-term investment opportunities

American Water Works (AWK.N) share price performance USD Vs HSBC rating history



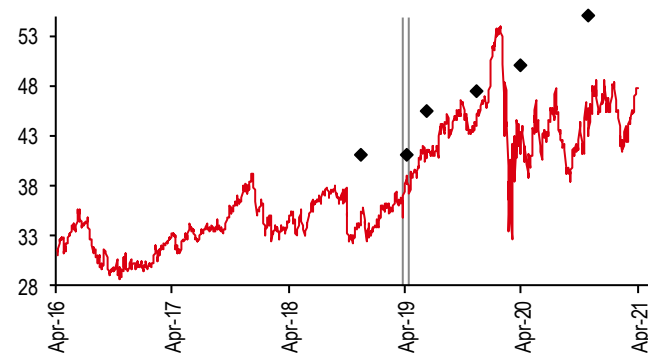
Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Hold	28 Aug 2020	Verity Mitchell
Hold	Buy	09 Nov 2020	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	105.00	17 Dec 2018	Verity Mitchell
Price 2	115.00	22 Mar 2019	Verity Mitchell
Price 3	130.00	08 Jul 2019	Verity Mitchell
Price 4	140.00	14 Apr 2020	Verity Mitchell
Price 5	142.00	28 Aug 2020	Verity Mitchell
Price 6	175.00	09 Nov 2020	Verity Mitchell

Source: HSBC

Essential Utilities (WTRG.N) share price performance USD Vs HSBC rating history



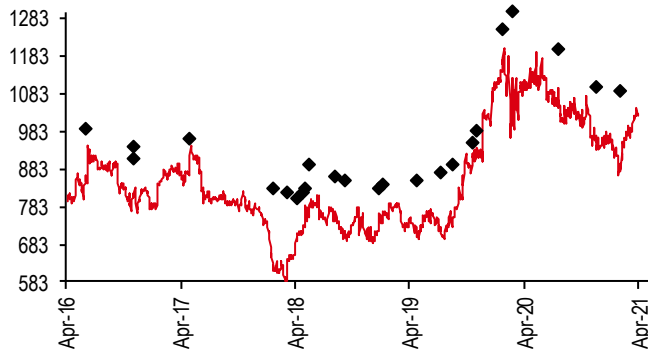
Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	41.00	06 Dec 2018	Verity Mitchell
Price 2	Restricted	15 Apr 2019	
Price 3	41.00	30 Apr 2019	Verity Mitchell
Price 4	45.50	28 Jun 2019	Verity Mitchell
Price 5	47.50	06 Dec 2019	Verity Mitchell
Price 6	50.00	22 Apr 2020	Verity Mitchell
Price 7	55.00	16 Nov 2020	Verity Mitchell

Source: HSBC

Pennon Group (PNN.L) share price performance GBp Vs HSBC rating history



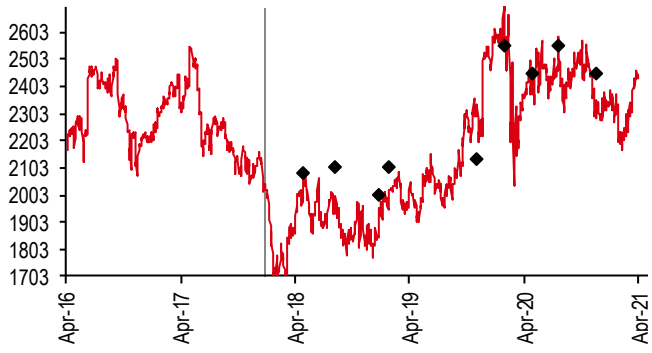
Source: HSBC

Rating & target price history

From	To	Date	Analyst
Overweight	Buy	31 Mar 2015	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	970	17 Apr 2015	Verity Mitchell
Price 2	950	06 Jul 2015	Verity Mitchell
Price 3	915	22 Oct 2015	Verity Mitchell
Price 4	950	15 Jan 2016	Verity Mitchell
Price 5	990	24 Jun 2016	Verity Mitchell
Price 6	910	21 Nov 2016	Verity Mitchell
Price 7	940	25 Nov 2016	Verity Mitchell
Price 8	960	24 May 2017	Verity Mitchell
Price 9	830	12 Feb 2018	Verity Mitchell
Price 10	820	26 Mar 2018	Verity Mitchell
Price 11	800	27 Apr 2018	Verity Mitchell
Price 12	820	17 May 2018	Verity Mitchell
Price 13	830	25 May 2018	Verity Mitchell
Price 14	890	08 Jun 2018	Verity Mitchell
Price 15	860	28 Aug 2018	Verity Mitchell
Price 16	850	28 Sep 2018	Verity Mitchell
Price 17	830	18 Jan 2019	Verity Mitchell
Price 18	840	31 Jan 2019	Verity Mitchell
Price 19	850	20 May 2019	Verity Mitchell
Price 20	870	31 Jul 2019	Verity Mitchell
Price 21	890	10 Sep 2019	Verity Mitchell
Price 22	950	12 Nov 2019	Verity Mitchell
Price 23	980	26 Nov 2019	Verity Mitchell
Price 24	1250	14 Feb 2020	Verity Mitchell
Price 25	1300	20 Mar 2020	Verity Mitchell
Price 26	1200	13 Aug 2020	Verity Mitchell
Price 27	1100	14 Dec 2020	Verity Mitchell
Price 28	1090	23 Feb 2021	Verity Mitchell

Source: HSBC

Severn Trent (SVT.L) share price performance GBp Vs HSBC rating history



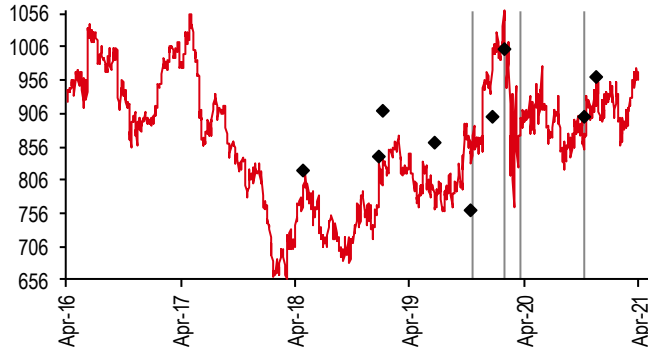
Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Hold	17 Jan 2018	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	2080	17 May 2018	Verity Mitchell
Price 2	2100	28 Aug 2018	Verity Mitchell
Price 3	2000	18 Jan 2019	Verity Mitchell
Price 4	2100	20 Feb 2019	Verity Mitchell
Price 5	2130	25 Nov 2019	Verity Mitchell
Price 6	2550	20 Feb 2020	Verity Mitchell
Price 7	2450	18 May 2020	Verity Mitchell
Price 8	2550	13 Aug 2020	Verity Mitchell
Price 9	2450	14 Dec 2020	Verity Mitchell

Source: HSBC

United Utilities (UU.L) share price performance GBp Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Hold	Reduce	07 Nov 2019	Verity Mitchell
Reduce	Hold	20 Feb 2020	Verity Mitchell
Hold	Buy	08 Apr 2020	Verity Mitchell
Buy	Hold	02 Nov 2020	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	820	17 May 2018	Verity Mitchell
Price 2	840	18 Jan 2019	Verity Mitchell
Price 3	910	01 Feb 2019	Verity Mitchell
Price 4	860	12 Jul 2019	Verity Mitchell
Price 5	760	07 Nov 2019	Verity Mitchell
Price 6	900	15 Jan 2020	Verity Mitchell
Price 7	1000	20 Feb 2020	Verity Mitchell
Price 8	900	02 Nov 2020	Verity Mitchell
Price 9	960	14 Dec 2020	Verity Mitchell

Source: HSBC

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Company	Ticker	Recent price	Price date	Disclosure
AMERICAN WATER WORKS	AWK.N	161.43	22 Apr 2021	6
ESSENTIAL UTILITIES	WTRG.N	47.88	22 Apr 2021	6
PENNON GROUP	PNN.L	10.29	22 Apr 2021	6, 7
SEVERN TRENT	SVT.L	24.47	22 Apr 2021	6, 7
UNITED UTILITIES	UU.L	9.68	22 Apr 2021	1, 4, 5, 6, 7

Source: HSBC

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2 HSBC expects to receive or intends to seek compensation for investment banking services from this company in the next 3 months.

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12 As of 19 Apr 2021, HSBC beneficially held a net long position of more than 0.5% of this company's total issued share capital, calculated according to the SSR methodology.

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AQUA AMERICA INC

Aqua America, Inc. is a publicly traded water and wastewater utility holding company with operating subsidiaries serving approximately three million people in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana, and Virginia. It has recently purchased Peoples, a natural gas distribution utility, which will diversify Aqua America's income.

Analyst's Notes

Analysis by Jacob Kilstein, CFA, and Justin Giacobbe, June 4, 2019

ARGUS RATING: BUY

- Raising target by $2 to $43 on relative valuation
- WTR shares trade at 27.1-times our 2019 EPS estimate, below the peer average P/E of 29.5. Our revised target values the stock in line with peers, which makes sense given WTR's above-average profitability.
- We think that Aqua America will continue to provide shareholders with solid risk-adjusted returns as it stands to benefit from an expected investment of more than $700 billion in the nation's water and wastewater infrastructure over the next two decades.
- On May 2, Aqua America reported 1Q19 adjusted income of $50 million, a 2% decline from 1Q18, partly due to higher operating and maintenance expenses. EPS of $0.28 missed our estimate of $0.29 and the consensus of $0.30.
- In October, the company announced that it would acquire Peoples, a natural gas distribution utility, for $4.3 billion in cash. The acquisition will diversify the company away from water distribution and is expected to close mid-2019.

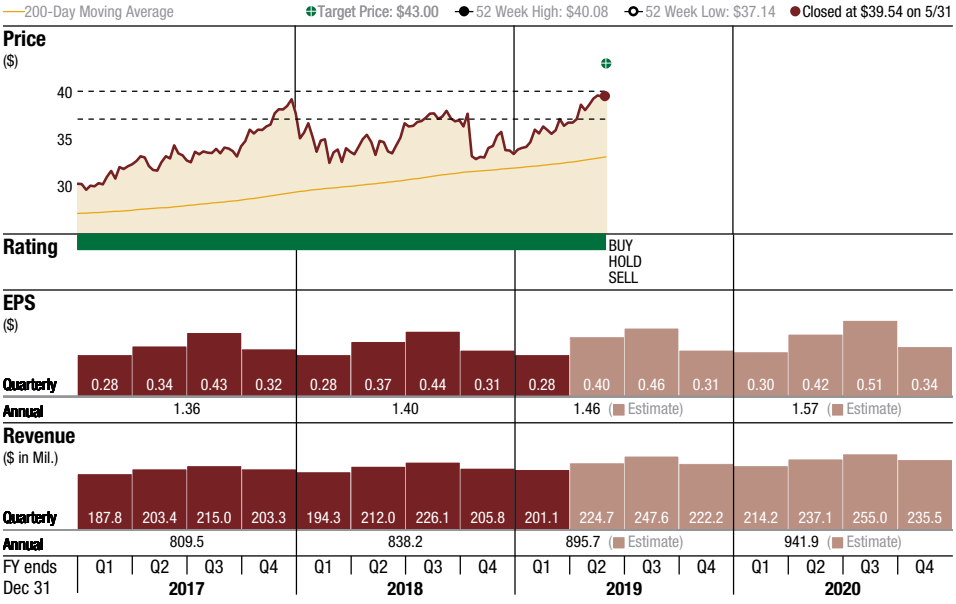
INVESTMENT THESIS

BUY-rated Aqua America Inc. (NYSE: WTR) has a solid business model, a history of steady earnings growth, and a growing dividend. We think the company will continue to provide shareholders with solid risk-adjusted returns as it stands to benefit from an expected investment of more than $700 billion in the nation's water and wastewater infrastructure recommended by the EPA over the next two decades. The company expects to grow its customer base not only through acquisitions but also organically, as it is well positioned in states such as North Carolina and Texas, where population growth is above the national average. The company also benefits from an experienced management team and balanced rate regulation. Lastly, we like the company's consistent earnings and rising dividend. We are increasing our 12-month price target to $43 from $41, which values the stock's P/E in line with its less profitable peers.

RECENT DEVELOPMENTS

Market Data

Pricing reflects previous trading week's closing price.



Argus Recommendations

Twelve Month Rating	SELL	HOLD	**BUY**
Five Year Rating	SELL	HOLD	**BUY**
Sector Rating	**Under Weight**	Market Weight	Over Weight

Argus assigns a 12-month BUY, HOLD, or SELL rating to each stock under coverage.

- BUY-rated stocks are expected to outperform the market (the benchmark S&P 500 Index) on a risk-adjusted basis over the next year.
- HOLD-rated stocks are expected to perform in line with the market.
- SELL-rated stocks are expected to underperform the market on a risk-adjusted basis.

The distribution of ratings across Argus' entire company universe is: 65% Buy, 34% Hold, 1% Sell.

Key Statistics

Key Statistics pricing data reflects previous trading day's closing price. Other applicable data are trailing 12-months unless otherwise specified

Market Overview

Price	**$39.82**
Target Price	**$43.00**
52 Week Price Range	**$32.09 to $40.08**
Shares Outstanding	**215.74 Million**
Dividend	**$0.88**

Sector Overview

Sector	**Utility**
Sector Rating	**UNDER WEIGHT**
Total % of S&P 500 Market Cap.	**3.00%**

Financial Strength

Financial Strength Rating	**MEDIUM**
Debt/Capital Ratio	**56.1%**
Return on Equity	**13.1%**
Net Margin	**18.7%**
Payout Ratio	**0.62**
Current Ratio	**0.37**
Revenue	**$844.88 Million**
After-Tax Income	**$158.07 Million**

Valuation

Current FY P/E	**27.27**
Prior FY P/E	**28.44**
Price/Sales	**10.17**
Price/Book	**3.56**
Book Value/Share	**$11.17**
Market Capitalization	**$8.59 Billion**

Forecasted Growth

1 Year EPS Growth Forecast
4.29%
5 Year EPS Growth Forecast
9.00%
1 Year Dividend Growth Forecast
7.06%

Risk

Beta	**0.62**
Institutional Ownership	**48.14%**

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Analyst's Notes...Continued

WTR shares have outperformed the S&P MidCap 400 over the last quarter, rising 9% compared to a 3% loss for the index. The shares have also outperformed over the past year, rising 13%, compared to a gain of less than 1% for the S&P MidCap 400 and a loss of 6% for the index. WTR shares have a beta of 0.62, in line with peers.

On May 2, Aqua America reported 1Q net income of $17 million or $0.09 per share, compared to $51 million or $0.29 per share in the prior-year period. The decrease was driven by losses on interest rate swaps and expenses related to WTR's acquisition of Peoples, a natural gas distribution utility. Adjusted income fell 2% to $50 million, or $0.28 per share, which missed our estimate of $0.29 and the consensus forecast of $0.30. Revenue rose 4% to $201 million, below our estimate of $202 million but in line with the consensus.

Operations and maintenance expenses rose 7% to $79 million. As such, the operating margin narrowed to 33.5% from 35.7% in 1Q18.

Along with the 1Q earnings release, management reiterated its 2019 EPS guidance of $1.45-$1.50, excluding transaction costs for the Peoples acquisition. Management's guidance assumes total customer growth of 2.0%-3.0%, in line with last year, and $550 million in capital spending. Management expects to spend $1.4 billion on capital projects through 2021.

In October, the company announced that it would acquire Peoples, a natural gas distribution utility, for $4.2 billion in cash, including the assumption of $1.3 billion in debt. Peoples serves about 740,000 customers in Pennsylvania, Kentucky, and West Virginia. The combined company's stock will trade under a new name. Management expects earnings accretion in the first full year after the closing and looks for 7% annual rate base growth in its water business and 8%-10% in natural gas through 2021. The Peoples deal is expected to close in mid-2019. Aqua America's revenue will still be 99% regulated following the acquisition.

WTR expects to spend an additional $50 million on system upgrades over the next 10 years. It expects to add 16,750 customers through the end of 2019 through additional acquisitions.

EARNINGS & GROWTH ANALYSIS

To date in 2019, WTR obtained rate increases or imposed surcharges in Ohio, Illinois and Pennsylvania, providing $5 million in revenue. Pending rate cases in New Jersey, Ohio, and North Carolina are seeking an additional $6 million of revenue.

During 1Q19, the company completed three acquisitions of water and wastewater systems, which added 572 customer connections. WTR financed those acquisitions with debt.

We are maintaining our 2019 EPS estimate of $1.46, which implies 4% growth and assumes higher rates in the company's regulated operations. We are also maintaining our 2020 estimate of $1.57.

We think the company will control costs and improve the

Growth & Valuation Analysis

GROWTH ANALYSIS

($ in Millions, except per share data)	2014	2015	2016	2017	2018
Revenue	780	814	820	810	838
COGS	289	309	305	287	308
Gross Profit	491	505	515	522	530
SG&A	—	—	—	—	—
R&D	—	—	—	—	—
Operating Income	314	321	326	329	323
Interest Expense	76	77	81	88	99
Pretax Income	239	217	255	257	178
Income Taxes	25	15	21	17	-14
Tax Rate (%)	11	7	8	7	—
Net Income	233	202	234	240	192
Diluted Shares Outstanding	178	178	178	178	178
EPS	1.31	1.14	1.32	1.35	1.08
Dividend	0.63	0.69	0.74	0.79	0.85
GROWTH RATES (%)					
Revenue	2.4	4.4	0.7	-1.3	3.5
Operating Income	4.2	2.1	3.8	0.2	-3.2
Net Income	5.4	-13.5	16.1	2.4	-19.9
EPS	4.3	-5.0	15.8	2.3	-20.0
Dividend	8.6	8.2	7.7	7.2	7.0
Sustainable Growth Rate	6.9	6.6	4.7	5.2	5.1
VALUATION ANALYSIS					
Price: High	$28.22	$31.09	$35.83	$39.55	$39.38
Price: Low	$22.40	$24.40	$28.03	$29.41	$32.09
Price/Sales: High-Low	6.4 - 5.1	6.8 - 5.3	7.8 - 6.1	8.7 - 6.5	8.4 - 6.8
P/E: High-Low	21.5 - 17.1	27.3 - 21.4	27.1 - 21.2	29.3 - 21.8	36.5 - 29.7
Price/Cash Flow: High-Low	13.8 - 11.0	14.9 - 11.7	16.9 - 13.2	18.1 - 13.5	18.0 - 14.7

Financial & Risk Analysis

FINANCIAL STRENGTH	2016	2017	2018
Cash ($ in Millions)	4	4	4
Working Capital ($ in Millions)	-173	-153	-252
Current Ratio	0.43	0.46	0.37
LT Debt/Equity Ratio (%)	93.9	102.6	119.4
Total Debt/Equity Ratio (%)	103.1	109.7	127.8
RATIOS (%)			
Gross Profit Margin	63.8	65.1	63.2
Operating Margin	40.7	41.2	38.6
Net Margin	28.6	29.6	22.9
Return On Assets	3.9	3.8	2.9
Return On Equity	13.1	12.6	9.7
RISK ANALYSIS			
Cash Cycle (days)	-21.3	-22.0	-33.7
Cash Flow/Cap Ex	1.0	0.8	0.7
Oper. Income/Int. Exp. (ratio)	—	—	—
Payout Ratio	53.8	60.4	58.5

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Analyst's Notes...Continued

efficiency of acquired assets, invest in infrastructure projects, and grow its customer base both organically and through acquisitions. The company plans to invest $550 million in infrastructure in 2019, following subsequent record investments of $478 million in 2017 and $500 million in 2018. WTR will use the funds to replace pipes, enhance water quality, and strengthen service reliability.

FINANCIAL STRENGTH & DIVIDEND

Our financial strength rating for Aqua America is Medium, the midpoint on our five-point scale. Our three main criteria include debt levels, fixed-cost coverage and profitability.

The company's total debt/total capitalization ratio was 57% at the end of 1Q, above the peer average of 55%. EBITDA covered interest expense by a factor of 5.5 in 1Q, below the peer average of 5.7. The 1Q adjusted net margin of 24.6% was well above the peer average of 12.3%. As of May 2, WTR had $4 million in cash and $2.7 billion in debt.

WTR pays a quarterly dividend of $0.219, or $0.876 annually, for a yield of about 2.3%, above the peer average of 1.8%. WTR has grown its dividend at a 7.6% average annual rate over the last five years. It has paid consecutive quarterly dividends for 74 years, and has raised the dividend 28 times in the past 27 years. Our 2019 dividend estimate is $0.91 per share and our 2020 estimate is $0.99.

MANAGEMENT & RISKS

Christopher Franklin has been CEO since July 2015. Mr. Franklin is a 25-year veteran of the company, and previously served as president and chief operating officer of its regulated operations.

The U.S. water industry is fragmented, with more than 53,000 individual water systems. Many of these systems cannot afford to meet the EPA's increasingly stringent standards, and have put themselves up for sale. In fact, several companies have sought to be acquired by Aqua America. The range of acquisition targets has also grown as cash-strapped municipalities look to monetize their utility assets. We believe that WTR will be able to acquire additional municipal water systems in the coming years at attractive prices.

Key risks for water utilities include the effect of adverse weather on revenues, regulatory issues (especially related to construction cost recovery), and potential environmental and safety-related liabilities. In addition, the utility's heavy capital needs create ongoing liquidity risk.

COMPANY DESCRIPTION

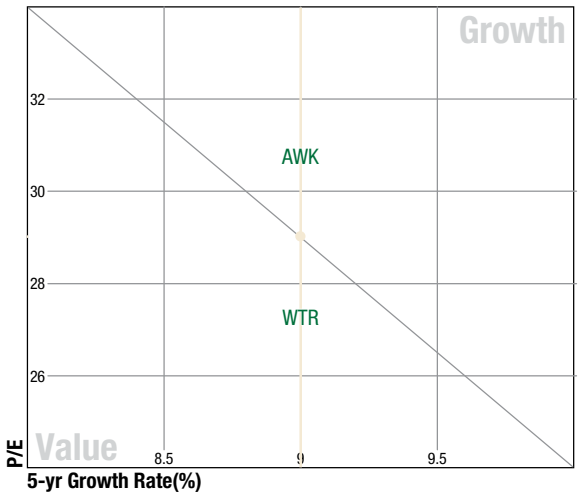
Aqua America, Inc. is a publicly traded water and wastewater utility holding company with operating subsidiaries serving approximately three million people in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana, and Virginia. It has recently purchased Peoples, a natural gas distribution utility, which will diversify Aqua America's income.

VALUATION

Peer & Industry Analysis

The graphics in this section are designed to allow investors to compare WTR versus its industry peers, the broader sector, and the market as a whole, as defined by the Argus Universe of Coverage.

- **The scatterplot shows how WTR stacks up versus its peers on two key characteristics: long-term growth and value. In general, companies in the lower left-hand corner are more value-oriented, while those in the upper right-hand corner are more growth-oriented.**
- **The table builds on the scatterplot by displaying more financial information.**
- **The bar charts on the right take the analysis two steps further, by broadening the comparison groups into the sector level and the market as a whole. This tool is designed to help investors understand how WTR might fit into or modify a diversified portfolio.**



Ticker	Company	Market Cap ($ in Millions)	5-yr Growth Rate (%)	Current FY P/E	Net Margin (%)	1-yr EPS Growth (%)	Argus Rating
AWK	American Water Works Co. Inc.	20,547	9.0	30.8	16.4	7.0	BUY
WTR	Aqua America Inc.	8,591	9.0	27.3	18.7	7.5	BUY
Peer Average		**14,569**	**9.0**	**29.0**	**17.6**	**7.3**	

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Analyst's Notes...Continued

WTR shares appear attractively valued at current prices near $39. Over the past 52 weeks, the shares have traded between $32 and $40.

WTR shares are trading at a discount to peers on a P/E basis, but at a premium based on price/book and price/sales, which we feel is justified by the company's solid long-term fundamentals. The shares trade at 27.1-times our 2019 EPS estimate which is below the peer average of 29.5. In our view, the company's financial strength, favorable risk profile, visible forward earnings stream and attractive integrated structure make WTR a compelling investment. We are increasing our 12-month price target to $43, which values the stock's P/E in line with less profitable peers.

On June 4, BUY-rated WTR closed at $39.82, down $0.22.

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About Argus

Argus Research, founded by Economist Harold Dorsey in 1934, has built a top-down, fundamental system that is used by Argus analysts. This six-point system includes Industry Analysis, Growth Analysis, Financial Strength Analysis, Management Assessment, Risk Analysis and Valuation Analysis.

Utilizing forecasts from Argus' Economist, the Industry Analysis identifies industries expected to perform well over the next one-to-two years.

The Growth Analysis generates proprietary estimates for companies under coverage.

In the Financial Strength Analysis, analysts study ratios to understand profitability, liquidity and capital structure.

During the Management Assessment, analysts meet with and familiarize themselves with the processes of corporate management teams.

Quantitative trends and qualitative threats are assessed under the Risk Analysis.

And finally, Argus' Valuation Analysis model integrates a historical ratio matrix, discounted cash flow modeling, and peer comparison.

THE ARGUS RESEARCH RATING SYSTEM

Argus uses three ratings for stocks: BUY, HOLD, and SELL. Stocks are rated relative to a benchmark, the S&P 500.

- A BUY-rated stock is expected to outperform the S&P 500 on a risk-adjusted basis over a 12-month period. To make this determination, Argus Analysts set target prices, use beta as the measure of risk, and compare expected risk-adjusted stock returns to the S&P 500 forecasts set by the Argus Market Strategist.
- A HOLD-rated stock is expected to perform in line with the S&P 500.
- A SELL-rated stock is expected to underperform the S&P 500.

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ESSENTIAL UTILITIES INC

Essential Utilities Inc., formerly Aqua America, Inc. is a publicly traded water and wastewater utility holding company with operating subsidiaries serving approximately five million people in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana, Kentucky, West Virginia and Virginia. In addition to its water/wastewater utilities, the company purchased the Peoples natural gas distribution utility in March 2020. The combined company has roughly 2,000 employees.

Analyst's Notes

Analysis by Angus Kelleher-Ferguson, June 18, 2021

ARGUS RATING: BUY

- Reiterating BUY and $55 price target
- Essential Utilities recently reported first-quarter results that exceeded analyst's expectations. On May 6, the company reported GAAP and non-GAAP EPS of $0.72 per share, up from non-GAAP EPS of $0.60 in 1Q20. The stronger results reflected contributions from Peoples, the natural gas utility that was acquired in March 2020.
- We are maintaining our 2021 EPS forecast of $1.68 from $1.66, implying 6% growth this year. We are maintaining our 2021 EPS forecast of $1.68. We look for continued gains in 2022 and are also reiterating our estimate of $1.80 per share, which assumes 7% growth from our 2021 forecast.
- The company has a long record - 75 years - of paying dividends. The current yield is about 2.1%.

INVESTMENT THESIS

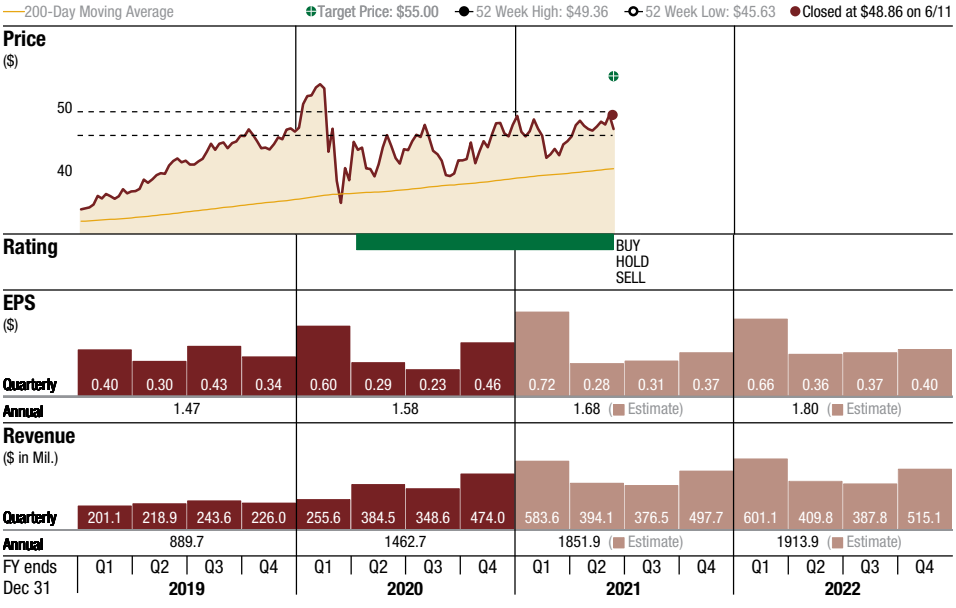
BUY-rated Essential Utilities Inc. (NYSE: WTRG) has a solid business model, a history of steady earnings growth, and a growing dividend. We think the company will continue to provide shareholders with solid risk-adjusted returns. Essential stands to benefit from aging water infrastructure that, according to industry observers, will soon require substantial investment to upgrade to safe levels. We also expect increased revenue and earnings following the March 2020 acquisition of Peoples, a gas distribution utility. We note that Essential has operations in states such as North Carolina and Texas, where population growth is above the national average. The company also benefits from an experienced management team and balanced rate regulation. Our 12-month price target is $55.

RECENT DEVELOPMENTS

WTRG shares have outperformed the S&P over the last three months, climbing 12% while the index has climbed 7%. The stock has underperformed over the past year, however, with a gain of 11% compared to a 35% increase for the market. The shares have roughly matched the performance of the Utility industry ETF IDU over the past year, but

Market Data

Pricing reflects previous trading week's closing price.



Argus Recommendations

Twelve Month Rating	SELL	HOLD	**BUY**
Five Year Rating	SELL	HOLD	**BUY**
Sector Rating	Under Weight	**Market Weight**	Over Weight

Argus assigns a 12-month BUY, HOLD, or SELL rating to each stock under coverage.

- BUY-rated stocks are expected to outperform the market (the benchmark S&P 500 Index) on a risk-adjusted basis over the next year.
- HOLD-rated stocks are expected to perform in line with the market.
- SELL-rated stocks are expected to underperform the market on a risk-adjusted basis.

The distribution of ratings across Argus' entire company universe is: 72% Buy, 28% Hold.

Key Statistics

Key Statistics pricing data reflects previous trading day's closing price. Other applicable data are trailing 12-months unless otherwise specified

Market Overview

Price	**$46.63**
Target Price	**$55.00**
52 Week Price Range	**$38.28 to $49.36**
Shares Outstanding	**245.64 Million**
Dividend	**$1.00**

Sector Overview

Sector	**Utility**
Sector Rating	**MARKET WEIGHT**
Total % of S&P 500 Market Cap.	**2.00%**

Financial Strength

Financial Strength Rating	**MEDIUM**
Debt/Capital Ratio	**55.2%**
Return on Equity	**8.6%**
Net Margin	**23.3%**
Payout Ratio	**0.62**
Current Ratio	**0.63**
Revenue	**$1.79 Billion**
After-Tax Income	**$416.76 Million**

Valuation

Current FY P/E	**27.76**
Prior FY P/E	**29.51**
Price/Sales	**6.40**
Price/Book	**2.38**
Book Value/Share	**$19.58**
Market Capitalization	**$11.45 Billion**

Forecasted Growth

1 Year EPS Growth Forecast	**6.33%**
5 Year EPS Growth Forecast	**6.00%**
1 Year Dividend Growth Forecast	**7.22%**

Risk

Beta	**1.05**
Institutional Ownership	**72.61%**

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Analyst's Notes...Continued

have outperformed over longer time horizons. The beta on WTRG shares is 0.53.

Essential Utilities recently reported first-quarter results that exceeded analyst's expectations. On May 6, the company reported GAAP and non-GAAP EPS of $0.72 per share, up from non-GAAP EPS of $0.60 in 1Q20. The stronger results reflected contributions from Peoples, the natural gas utility that was acquired in March 2020. Higher volume and favorable rates were secondary drivers, with an increase in Other expenses partially offsetting the strength. Revenue rose 128% to $586 million, with Peoples accounting for substantially all of this growth. Water usage per customer increased a modest 2% year-over-year as customers spent more time at home.

In March 2020, the company closed on the acquisition of Peoples Natural Gas for $4.3 billion in cash, including the assumption of $1.1 billion in debt. (The Canada Pension Plan invested $750 million into the company to help it close the deal.) Peoples serves about 740,000 customers in Pennsylvania, Kentucky, and West Virginia. The deal is partly synergistic, given that Essential was already providing water service to Peoples. Additionally, Peoples and Essential Water are the largest players in their respective industries in Pennsylvania, which is the company's biggest market.

Essential stands to benefit from aging water infrastructure that, according to industry observers, will soon require substantial investment. In August 2020, the American Society of Civil Engineers released a report detailing chronic underinvestment in drinking water and wastewater systems. The report highlighted the difficulties plaguing legacy systems, with many treatment facilities nearing the end of their design lives of 75-100 years. More recently, the $2.3 trillion Biden infrastructure bill earmarked roughly $111 billion over the next ten years to modernize water infrastructure. The bill still has a long way to go, and a size reduction looks increasingly more likely, but it remains a positive in any event. Looking ahead, we expect Essential to benefit from both new investment in water infrastructure and upgrades of existing systems.

Along with the 1Q21 earnings release, management reiterated its 2021 guidance calling for EPS of $1.64-$1.69. Management also stated that it expects compound annual earnings growth of 5%-7% through 2023.

EARNINGS & GROWTH ANALYSIS

The company's top-line growth is driven by acquisitions, organic customer count increases, volume increases, and rate increases. In 1Q21, revenue was up substantially due to inorganic growth from the March 2020 acquisition of Peoples. Excluding the impact of Peoples, revenue rose 4.7%. The growth in organic water utility revenue reflected better rates and higher volume.

We note that 2Q21 earnings will offer an appropriate year-over-year comp, as the Peoples acquisition will be fully annualized.

On growth, the company pursues a blended strategy of growth

Growth & Valuation Analysis

GROWTH ANALYSIS

($ in Millions, except per share data)	2016	2017	2018	2019	2020
Revenue	820	810	838	890	1,463
COGS	297	282	308	333	694
Gross Profit	523	527	530	557	768
SG&A	—	—	—	—	—
R&D	—	—	—	—	—
Operating Income	333	334	323	340	435
Interest Expense	81	88	99	100	183
Pretax Income	255	257	178	212	265
Income Taxes	21	17	-14	-13	-20
Tax Rate (%)	8	7	—	—	—
Net Income	234	240	192	225	285
Diluted Shares Outstanding	178	178	178	216	255
EPS	1.32	1.35	1.08	1.04	1.12
Dividend	0.74	0.79	0.85	0.91	0.97
GROWTH RATES (%)					
Revenue	0.7	-1.3	3.5	6.2	64.4
Operating Income	3.8	0.2	-3.2	5.3	27.8
Net Income	16.1	2.4	-19.9	17.0	26.9
EPS	15.8	2.3	-20.0	-3.7	7.7
Dividend	7.7	7.2	7.0	7.0	7.0
Sustainable Growth Rate	4.7	5.2	5.1	-1.1	0.2
VALUATION ANALYSIS					
Price: High	$35.83	$39.55	$39.38	$47.33	$54.52
Price: Low	$28.03	$29.41	$32.09	$32.70	$30.40
Price/Sales: High-Low	7.8 - 6.1	8.7 - 6.5	8.4 - 6.8	11.5 - 7.9	9.5 - 5.3
P/E: High-Low	27.1 - 21.2	29.3 - 21.8	36.5 - 29.7	45.5 - 31.4	48.7 - 27.1
Price/Cash Flow: High-Low	16.9 - 13.2	18.1 - 13.5	18.0 - 14.7	31.3 - 21.6	25.6 - 14.3

Financial & Risk Analysis

FINANCIAL STRENGTH	2018	2019	2020
Cash ($ in Millions)	4	1,869	5
Working Capital ($ in Millions)	-252	1,692	-224
Current Ratio	0.37	6.23	0.63
LT Debt/Equity Ratio (%)	119.4	76.1	118.8
Total Debt/Equity Ratio (%)	127.8	79.8	123.2
RATIOS (%)			
Gross Profit Margin	63.2	62.6	52.5
Operating Margin	38.6	38.2	29.7
Net Margin	22.9	25.2	19.5
Return On Assets	2.9	2.8	2.5
Return On Equity	9.7	7.6	6.7
RISK ANALYSIS			
Cash Cycle (days)	-33.7	-36.4	-13.9
Cash Flow/Cap Ex	0.7	0.6	0.6
Oper. Income/Int. Exp. (ratio)	2.8	2.7	2.4
Payout Ratio	58.5	59.5	120.5

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Analyst's Notes...Continued

through acquisitions and organic growth from its core operations (core ops include its regulated water utility and, more recently, a gas utility.) A key aspect of its acquisition strategy involves purchasing municipal water or wastewater utility assets. As of quarter end, there were seven pending acquisitions underway mixed between water and wastewater. Across the seven pending acquisitions, total purchase price came to $450.5 million and customer count totaled 231,000 dwelling units.

In 2020, Essential posted adjusted EPS of $1.58, up from $1.47 in 2019. Revenue of $1.46 billion rose from $890 million in 2019.

We are maintaining our 2021 EPS forecast of $1.68. We look for continued gains in 2022 and are also reiterating our estimate of $1.80 per share, which assumes 7% growth from our 2021 forecast. Our long-term earnings growth rate forecast is 6%.

FINANCIAL STRENGTH & DIVIDEND

Our financial strength rating for Essential Utilities is Medium, the midpoint on our five-point scale. Our three main criteria are debt levels, fixed-cost coverage, and profitability. Moody's rates the company's debt at Baa2 with a stable outlook and S&P rates it as A.

At the end of the quarter, WTRG had $18 million in cash and cash equivalents, up from $5 million at the end of 2020. The company had $5.8 billion in debt, up from $5.7 billion at the end of 2020. The total debt/total capitalization ratio was 54%, below the peer average of 58%. During the trailing twelve months, the interest coverage ratio was 4.4-times, below the peer average of 6.2. The company has $724 million in borrowing capacity on various credit facilities.

In August 2020, the Essential Utilities board approved a dividend hike. The quarterly cash dividend is now $0.2507, up from $0.2343. The annual distribution of roughly $1.00 yields about 2.1%. WTRG has grown its dividend at a 7% average annual rate over the last five years. It has paid consecutive quarterly dividends for 75 years, and has raised the dividend 30 times in the past 29 years. Our 2021 dividend estimate is $1.04 and our 2022 estimate is $1.12.

MANAGEMENT & RISKS

Christopher Franklin has been the company's CEO since July 2015, and is also chairman of the board. Mr. Franklin is a 25-year company veteran, and previously served as president and COO of its regulated operations. The COO is Richard Fox, who has served in the role since 2015, and the CFO is Daniel J. Schuller, who has been in the position since 2018. In August 2020, management announced that Mike Huwar would succeed Joe Gregorini as president of Peoples. Mr. Huwar has more than 30 years of industry experience and an established reputation with Pennsylvania regulators.

The U.S. water industry is fragmented, with more than 53,000 individual water systems. Many of these systems cannot afford to meet the EPA's increasingly stringent standards, and have put

Peer & Industry Analysis

The graphics in this section are designed to allow investors to compare WTRG versus its industry peers, the broader sector, and the market as a whole, as defined by the Argus Universe of Coverage.

- **The scatterplot shows how WTRG stacks up versus its peers on two key characteristics: long-term growth and value. In general, companies in the lower left-hand corner are more value-oriented, while those in the upper right-hand corner are more growth-oriented.**
- **The table builds on the scatterplot by displaying more financial information.**
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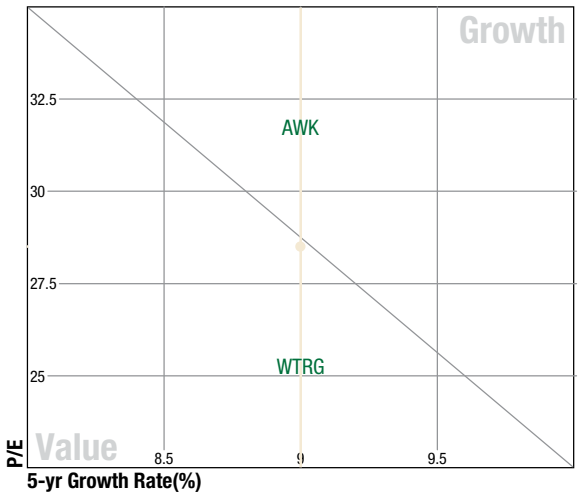
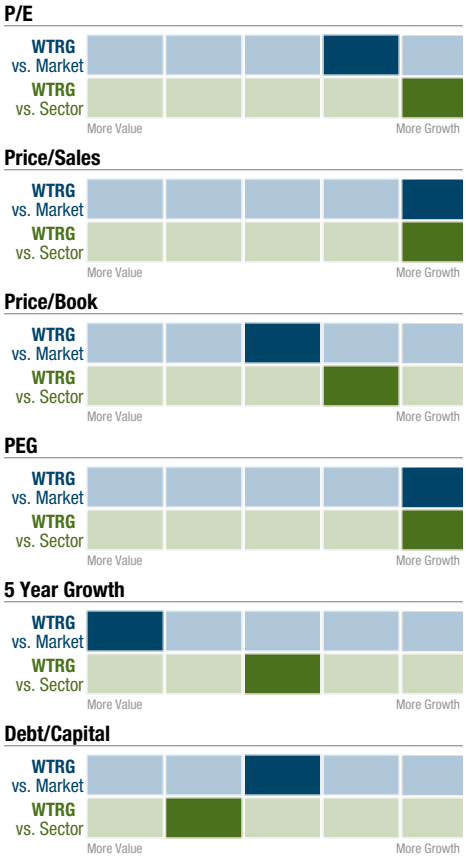


Ticker	Company	Market Cap ($ in Millions)	5-yr Growth Rate (%)	Current FY P/E	Net Margin (%)	1-yr EPS Growth (%)	Argus Rating
AWK	American Water Works Co. Inc.	25,104	9.0	31.7	18.8	10.1	BUY
WTRG	Essential Utilities Inc	10,417	9.0	25.3	19.5	7.1	BUY
Peer Average		**17,760**	**9.0**	**28.5**	**19.1**	**8.6**	



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Analyst's Notes...Continued

themselves up for sale. Several companies have even sought to be acquired by Essential Utilities. The range of acquisition targets has also grown as cash-strapped municipalities look to monetize their utility assets. We believe that WTRG will be able to acquire additional municipal water systems in the coming years as cities look to raise cash to deal with the impact of the pandemic.

Key risks for water utilities include the effect of adverse weather on revenues, regulatory issues (especially related to construction cost recovery), and potential environmental and safety-related liabilities. In addition, the utility's heavy capital needs create ongoing liquidity risk.

COMPANY DESCRIPTION

Essential Utilities Inc., formerly Aqua America, Inc. is a publicly traded water and wastewater utility holding company with operating subsidiaries serving approximately five million people in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana, Kentucky, West Virginia and Virginia. In addition to its water/wastewater utilities, the company purchased the Peoples natural gas distribution utility in March 2020. The combined company has roughly 2,000 employees.

VALUATION

WTRG shares appear attractively valued at current prices near $49. Over the past 52 weeks, the shares have traded between $38 and $49. WTRG trades at 29.0-times our 2021 EPS estimate and at 27.1-times our 2022 forecast. The shares are trading at premiums to electric and gas distribution peers on P/E, price/sales, and price/book, but in line on PEG, reflecting the company' stronger-than-average growth outlook. Compared to a basket of water utility peers, the shares trade at a discount versus the peer average of 33.2. We believe that premiums to electric utility peers are justified by the company's solid long-term fundamentals, and that WTRG shares should trade closer to the peer average of water utility peers. In our view, the company's financial strength, favorable risk profile, visible forward earnings stream, and attractive integrated structure make WTRG a compelling investment. Our target price is $55, implying a reasonable 2021 PE multiple of 32.7 - still below the water utility peer average.

On June 18, BUY-rated WTRG closed at $46.63, down $2.14.

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About Argus

Argus Research, founded by Economist Harold Dorsey in 1934, has built a top-down, fundamental system that is used by Argus analysts. This six-point system includes Industry Analysis, Growth Analysis, Financial Strength Analysis, Management Assessment, Risk Analysis and Valuation Analysis.

Utilizing forecasts from Argus' Economist, the Industry Analysis identifies industries expected to perform well over the next one-to-two years.

The Growth Analysis generates proprietary estimates for companies under coverage.

In the Financial Strength Analysis, analysts study ratios to understand profitability, liquidity and capital structure.

During the Management Assessment, analysts meet with and familiarize themselves with the processes of corporate management teams.

Quantitative trends and qualitative threats are assessed under the Risk Analysis.

And finally, Argus' Valuation Analysis model integrates a historical ratio matrix, discounted cash flow modeling, and peer comparison.

THE ARGUS RESEARCH RATING SYSTEM

Argus uses three ratings for stocks: BUY, HOLD, and SELL. Stocks are rated relative to a benchmark, the S&P 500.

- A BUY-rated stock is expected to outperform the S&P 500 on a risk-adjusted basis over a 12-month period. To make this determination, Argus Analysts set target prices, use beta as the measure of risk, and compare expected risk-adjusted stock returns to the S&P 500 forecasts set by the Argus Market Strategist.
- A HOLD-rated stock is expected to perform in line with the S&P 500.
- A SELL-rated stock is expected to underperform the S&P 500.

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ESSENTIAL UTILITIES INC

Essential Utilities Inc., formerly Aqua America Inc., is a publicly traded water and wastewater utility holding company with operating subsidiaries serving approximately five million people in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana, Kentucky, West Virginia and Virginia. In addition to its water/wastewater utilities, the company purchased a natural gas utility in March 2020. The combined company has roughly 2,000 employees.

Analyst's Notes

Analysis by Angus Kelleher-Ferguson, October 13, 2020

ARGUS RATING: BUY

- Reiterating BUY with target of $50
- WTRG shares remain 23% below their all-time high and currently offer investors a favorable entry point.
- In a transformative deal, the company recently acquired Peoples, a natural gas utility, for $4.2 billion in cash. It has also received regulatory approval for rate hikes and infrastructure surcharges in a range of states.
- The company has a long record - 75 years - of paying dividends. The current yield is about 2.4%.

INVESTMENT THESIS

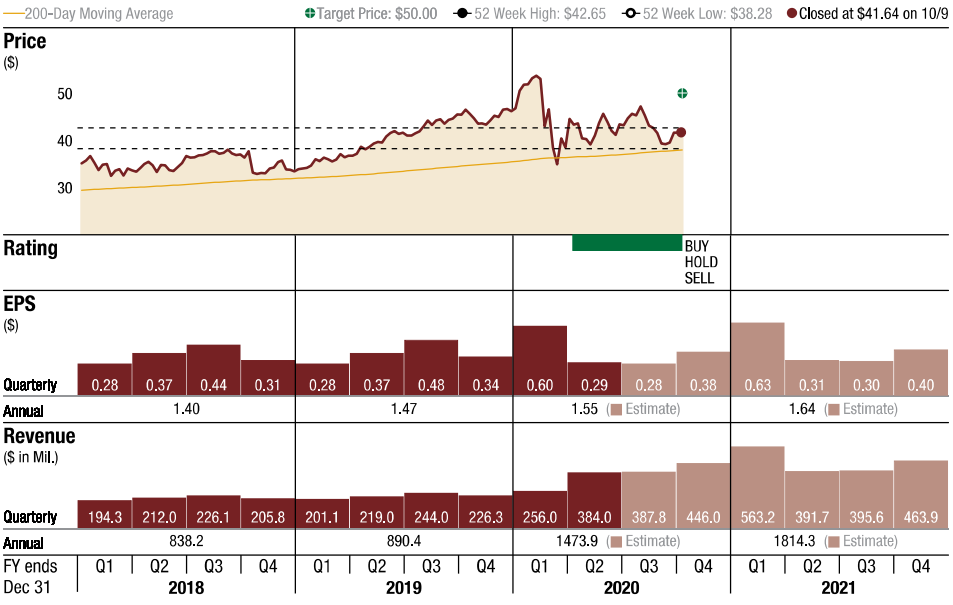
BUY-rated Essential Utilities Inc. (NYSE: WTRG) has a solid business model, a history of steady earnings growth, and a growing dividend. We think the company will continue to provide shareholders with solid risk-adjusted returns. Essential stands to benefit from aging water infrastructure that, according to many industry observers, will soon require substantial investment. In 2019, EPA Chief Andrew Wheeler projected that $700 billion would be needed over the next 20 years to upgrade/overhaul U.S. water infrastructure. Similarly, in August 2020, the American Society of Civil Engineers released a report detailing chronic underinvestment in drinking water & wastewater systems. The report highlighted the difficulties plaguing legacy systems, with many treatment facilities nearing the end of their design lives of 75-100 years. Looking ahead, we expect Essential Utilities to benefit from both new investment in water infrastructure and upgrades of existing systems.

In addition, Essential expects to grow its customer base, helped by operations in states such as North Carolina and Texas, where population growth is above the national average. The company also benefits from an experienced management team and balanced rate regulation. Our 12-month price target is $50.

RECENT DEVELOPMENTS

Market Data

Pricing reflects previous trading week's closing price.



Argus Recommendations

Twelve Month Rating	SELL	HOLD	**BUY**
Five Year Rating	SELL	HOLD	**BUY**
Sector Rating	Under Weight	Market Weight	**Over Weight**

Argus assigns a 12-month BUY, HOLD, or SELL rating to each stock under coverage.

- BUY-rated stocks are expected to outperform the market (the benchmark S&P 500 Index) on a risk-adjusted basis over the next year.
- HOLD-rated stocks are expected to perform in line with the market.
- SELL-rated stocks are expected to underperform the market on a risk-adjusted basis.

The distribution of ratings across Argus' entire company universe is: 63% Buy, 36% Hold, 1% Sell.

Key Statistics

Key Statistics pricing data reflects previous trading day's closing price. Other applicable data are trailing 12-months unless otherwise specified

Market Overview

Price	**$42.25**
Target Price	**$50.00**
52 Week Price Range	**$30.40 to $54.52**
Shares Outstanding	**245.15 Million**
Dividend	**$1.00**

Sector Overview

Sector	**Utility**
Sector Rating	**OVER WEIGHT**
Total % of S&P 500 Market Cap.	**3.00%**

Financial Strength

Financial Strength Rating	**MEDIUM**
Debt/Capital Ratio	**44.4%**
Return on Equity	**8.2%**
Net Margin	**25.2%**
Payout Ratio	**0.63**
Current Ratio	**6.31**
Revenue	**$1.11 Billion**
After-Tax Income	**$279.13 Million**

Valuation

Current FY P/E	**27.26**
Prior FY P/E	**28.74**
Price/Sales	**9.33**
Price/Book	**2.23**
Book Value/Share	**$18.91**
Market Capitalization	**$10.36 Billion**

Forecasted Growth

1 Year EPS Growth Forecast	**5.44%**
5 Year EPS Growth Forecast	**9.00%**
1 Year Dividend Growth Forecast	**6.59%**

Risk

Beta	**0.97**
Institutional Ownership	**67.73%**

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Analyst's Notes...Continued

WTRG shares have underperformed the S&P over the last quarter, falling 2% while the S&P 500 has climbed 9%. The stock has also underperformed over the past year, with a decline of 7% compared to a 17% advance for the broad market. The shares have outperformed the Utility industry ETF IDU over the past year. The beta on WTRG shares is 0.47.

On August 5, the company reported 2Q adjusted EPS of $0.29, above the consensus forecast of $0.24 but down from $0.37 in 2Q19. On a GAAP basis, EPS rose to $0.29 from $0.25 in 2Q19. Revenue rose 76% to $384 million, primarily reflecting contributions from Peoples, a natural gas utility acquired in March.

The company acquired Peoples for $4.2 billion in cash, including the assumption of $1.3 billion in debt. Peoples serves about 740,000 customers in Pennsylvania, Kentucky, and West Virginia. During Essential's second-quarter conference call, management announced that Mike Huwar would succeed Joe Gregorini as president of Peoples. Mr. Huwar has over 30 years of industry experience and is well regarded by Pennsylvania regulators.

Along with its 2Q earnings, management reiterated its 2020 guidance calling for adjusted EPS of $1.53-$1.58. The guidance assumes compound annual earnings growth of 5%-7% through 2022, infrastructure investments of $2.8 billion through 2022, and customer growth of 2%-3% per year in the regulated water segment.

EARNINGS & GROWTH ANALYSIS

The company's top-line growth is driven by acquisitions, volume increases and rate increases. In 2Q20, revenue rose significantly due to the Peoples acquisition. Excluding the acquisition, revenue still rose an impressive 9%, reflecting increased residential water usage, partially offset by lower usage from commercial and industrial customers.

On the regulatory front, to date in 2020, Essential's regulated water segment has received approval for higher rates or infrastructure surcharges in Illinois, Indiana, North Carolina, Ohio, Virginia and Pennsylvania. The changes will provide an estimated $10.2 million in additional annualized revenue. The company has additional proceedings pending in Indiana, New Jersey, Virginia and Ohio for its regulated water segment, which could provide another $5.2 million in revenue. Essential's regulated natural gas segment has also received approval for higher rates or infrastructure surcharges in Kentucky and Pennsylvania that will generate approximately $1 million in annualized revenue.

Below the top line, O&M expense rose 49% from 2Q19 due to new Peoples O&M, partially offset by merger-related synergies.

Turning to our estimates, we are maintaining our 2020 non-GAAP EPS estimate of $1.55, near the midpoint of management's guidance range and implying growth of 5% this year. We think the company will control costs and improve the efficiency of acquired assets, invest in infrastructure projects, and grow its customer base both organically and through acquisitions. The company plans to invest $950 million in gas and water

Growth & Valuation Analysis

GROWTH ANALYSIS

($ in Millions, except per share data)	2015	2016	2017	2018	2019
Revenue	814	820	810	838	890
COGS	309	297	282	308	333
Gross Profit	505	523	527	530	557
SG&A	—	—	—	—	—
R&D	—	—	—	—	—
Operating Income	321	333	334	323	340
Interest Expense	77	81	88	99	100
Pretax Income	217	255	257	178	212
Income Taxes	15	21	17	-14	-13
Tax Rate (%)	7	8	7	—	—
Net Income	202	234	240	192	225
Diluted Shares Outstanding	178	178	178	178	216
EPS	1.14	1.32	1.35	1.08	1.04
Dividend	0.69	0.74	0.79	0.85	0.91
GROWTH RATES (%)					
Revenue	4.4	0.7	-1.3	3.5	6.2
Operating Income	2.1	3.8	0.2	-3.2	5.3
Net Income	-13.5	16.1	2.4	-19.9	17.0
EPS	-5.0	15.8	2.3	-20.0	-3.7
Dividend	8.2	7.7	7.2	7.0	7.0
Sustainable Growth Rate	6.6	4.7	5.2	5.1	-1.1
VALUATION ANALYSIS					
Price: High	$31.09	$35.83	$39.55	$39.38	$47.33
Price: Low	$24.40	$28.03	$29.41	$32.09	$32.70
Price/Sales: High-Low	6.8 - 5.3	7.8 - 6.1	8.7 - 6.5	8.4 - 6.8	11.5 - 7.9
P/E: High-Low	27.3 - 21.4	27.1 - 21.2	29.3 - 21.8	36.5 - 29.7	45.5 - 31.4
Price/Cash Flow: High-Low	14.9 - 11.7	16.9 - 13.2	18.1 - 13.5	18.0 - 14.7	31.3 - 21.6

Financial & Risk Analysis

FINANCIAL STRENGTH	2017	2018	2019
Cash ($ in Millions)	4	4	1,869
Working Capital ($ in Millions)	-153	-252	1,694
Current Ratio	0.46	0.37	6.31
LT Debt/Equity Ratio (%)	102.6	119.4	76.1
Total Debt/Equity Ratio (%)	109.7	127.8	79.8
RATIOS (%)			
Gross Profit Margin	65.1	63.2	62.6
Operating Margin	41.2	38.6	38.2
Net Margin	29.6	22.9	25.2
Return On Assets	3.8	2.9	2.8
Return On Equity	12.6	9.7	7.6
RISK ANALYSIS			
Cash Cycle (days)	-22.0	-33.7	-36.4
Cash Flow/Cap Ex	0.8	0.7	0.6
Oper. Income/Int. Exp. (ratio)	3.9	2.8	2.7
Payout Ratio	60.4	58.5	59.5

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Analyst's Notes...Continued

infrastructure in 2020, following investments of $550 million in water infrastructure in 2019. WTRG will use the funds to replace pipes and strengthen service reliability, among other projects. We look for continued growth in 2021 and are maintaining our EPS forecast of $1.64.

FINANCIAL STRENGTH & DIVIDEND

Our financial strength rating for Essential Utilities is Medium, the midpoint on our five-point scale. Our three main financial strength criteria are debt levels, fixed-cost coverage, and profitability. Moody's rates the company's debt at Baa2 with a stable outlook. S&P's rating is A.

WTRG had $7 million in cash and $5.2 billion in debt at the end of 2Q20. The company's total debt/capitalization ratio was 53%. On April 13, the company completed a $1.1 billion public debt offering, with $500 million of 10-year 2.7% notes and $600 million of 30-year 3.3% notes, for a weighted-average maturity of 20.9 years and a weighted-average coupon of 3.0%. On April 14, the company priced $175 million of first mortgage bonds for Aqua Pennsylvania. The proceeds were used to pay off short-term borrowings and to fund an acquisition. As of May 1, after considering the effects of these financings, the company had $1.1 billion in borrowing capacity on various credit facilities.

On August 4, the Essential Utilities board approved a dividend hike. The quarterly cash dividend is now $0.2507, up from $0.2343. The annual distribution of roughly $1.00 yields about 2.4%. WTRG has grown its dividend at a 7% average annual rate over the last five years. It has paid consecutive quarterly dividends for 75 years, and has raised the dividend 30 times in the past 29 years. Our 2020 dividend estimate is $0.97, down from $0.98, and our 2021 estimate is $1.04, up from $1.02.

MANAGEMENT & RISKS

Christopher Franklin has been CEO since July 2015. Mr. Franklin is a 25-year veteran of the company, and previously served as president and COO of its regulated operations. The current COO is Richard Fox, who has served in the role since 2015, and the CFO is Daniel J. Schuller, who has been in the position since 2018.

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Key risks for water utilities include the effect of adverse weather on revenues, regulatory issues (especially related to construction cost recovery), and potential environmental and safety-related liabilities. In addition, the utility's heavy capital needs create

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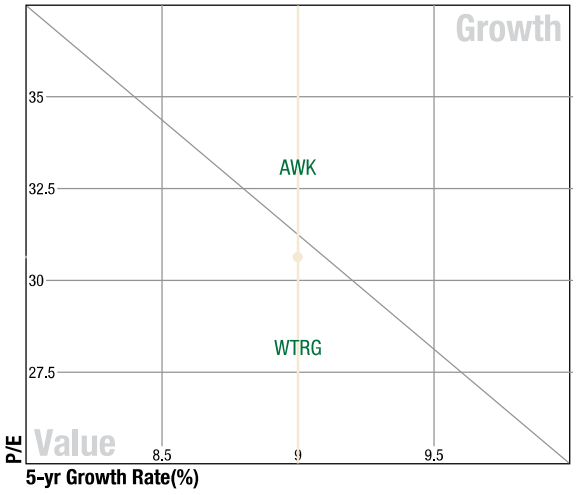
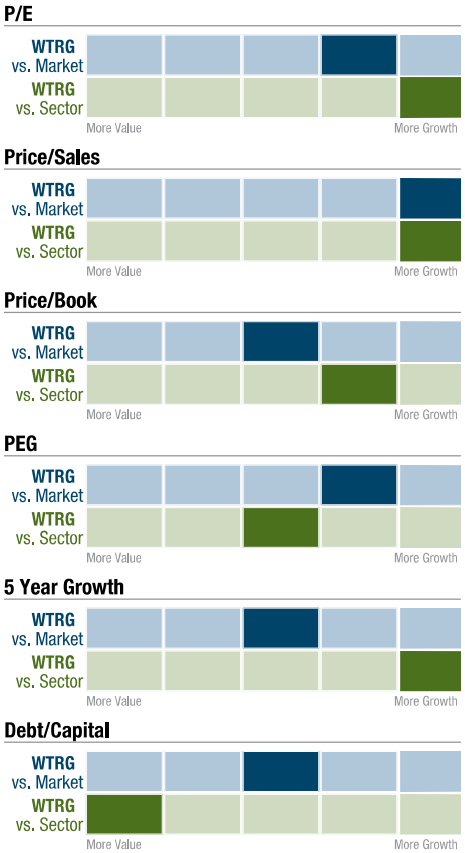


Ticker	Company	Market Cap ($ in Millions)	5-yr Growth Rate (%)	Current FY P/E	Net Margin (%)	1-yr EPS Growth (%)	Argus Rating
AWK	American Water Works Co. Inc.	23,721	9.0	33.1	17.4	10.1	BUY
WTRG	Essential Utilities Inc	10,703	9.0	28.2	27.5	5.8	BUY
Peer Average		**17,212**	**9.0**	**30.6**	**22.4**	**8.0**	



Please see important information about this report on page 5

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Analyst's Notes...Continued

ongoing liquidity risk.

COMPANY DESCRIPTION

Essential Utilities Inc., formerly Aqua America Inc., is a publicly traded water and wastewater utility holding company with operating subsidiaries serving approximately five million people in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana, Kentucky, West Virginia and Virginia. In addition to its water/wastewater utilities, the company purchased a natural gas utility in March 2020. The combined company has roughly 2,000 employees.

VALUATION

WTRG shares appear attractively valued at current prices near $42. Over the past 52 weeks, the shares have traded between $30 and $55. They are currently about 23% below their all-time high.

WTRG shares are trading at a discount to peers on P/E and price/book, but at a premium based on price/sales, which we feel is justified by the company's solid long-term fundamentals. The shares trade at 27.3-times our 2020 EPS estimate, below the peer average of 32.2. In our view, the company's financial strength, favorable risk profile, visible forward earnings stream and attractive integrated structure make WTRG a compelling investment. Our target price is $50.

On October 13 at midday, BUY-rated WTRG traded at $41.99, down $0.26.

Please see important information about this report on page 5

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About Argus

Argus Research, founded by Economist Harold Dorsey in 1934, has built a top-down, fundamental system that is used by Argus analysts. This six-point system includes Industry Analysis, Growth Analysis, Financial Strength Analysis, Management Assessment, Risk Analysis and Valuation Analysis.

Utilizing forecasts from Argus' Economist, the Industry Analysis identifies industries expected to perform well over the next one-to-two years.

The Growth Analysis generates proprietary estimates for companies under coverage.

In the Financial Strength Analysis, analysts study ratios to understand profitability, liquidity and capital structure.

During the Management Assessment, analysts meet with and familiarize themselves with the processes of corporate management teams.

Quantitative trends and qualitative threats are assessed under the Risk Analysis.

And finally, Argus' Valuation Analysis model integrates a historical ratio matrix, discounted cash flow modeling, and peer comparison.

THE ARGUS RESEARCH RATING SYSTEM

Argus uses three ratings for stocks: BUY, HOLD, and SELL. Stocks are rated relative to a benchmark, the S&P 500.

- A BUY-rated stock is expected to outperform the S&P 500 on a risk-adjusted basis over a 12-month period. To make this determination, Argus Analysts set target prices, use beta as the measure of risk, and compare expected risk-adjusted stock returns to the S&P 500 forecasts set by the Argus Market Strategist.
- A HOLD-rated stock is expected to perform in line with the S&P 500.
- A SELL-rated stock is expected to underperform the S&P 500.

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February 28, 2020

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	**Outperform/Moderate**
Price:	$46.34
Target Price ($US):	$50.00
Market Cap ($US millions):	$10,002
ADTV (US$ millions):	$67.5

Price as-of Prior Day Close

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2018A	$1.08	-	$838.1	-	42.9x
2019A	$1.00	-	$889.7	-	46.3x
2020E*	$1.10	$1.56	$1,384	$1,871	42.2x
2021E	$1.65	$1.70	$1,662	$2,086	28.0x

FYE 12/30; Revenue in USD millions.

*Assumes 3/16/2020 closing for Peoples acquisition.

Source: Capital IQ, B&S Estimates

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Analyst Day Highlights: 2020 guidance just OK, but M&A, three-year growth targets affirm thesis.

Essential Utilities hosted an analyst day at the NYSE, the company's first high-profile public appearance since receiving key PA regulatory approval for the impending acquisition of Peoples Gas. Major topics included the Peoples transaction (reaffirmation of strategic rationale and progress update), municipal acquisition pipeline, 4Q19 earnings, and forward guidance and growth targets. Overall, we came away reinforced in our favorable view of the fundamental story.

With the critical Pennsylvania regulatory approval now secured, the acquisition of Peoples is set to close on 16 March. The regulatory approval process took longer than expected due to the Goodwin-Tombaugh situation (see prior research), and as a result the first full quarter with Peoples on the P&L will be 2Q20. Still, we continue to view the addition of Peoples, which buttresses Essential's already robust regulatory presence in PA and enhances consolidated rate base growth, as a major strategic differentiator vs. peers.

Essential continues to shine on the municipal deal front not only in absolute terms, but also in terms of moving the needle relative to its size. Notable deals include the purchase of Cheltenham WW for $50 million and the pending acquisition of DELCORA for $276 million, which together with several smaller deals provide a material tailwind to customer growth. We expect Essential to remain highly active on municipal M&A, with deals outside PA likely to accelerate.

Essential issued 2020 EPS guidance of $1.53-$1.58, although given the later than expected Peoples closing, it is on an "illustrative pro forma adjusted" basis (i.e as if Peoples were in for a full 1Q, which it is not). While this means incoming 2020 consensus of $1.56 could come down, the run-rate pro forma guidance reflects the sustainable go-forward earnings power of the combined enterprise.

Essential initiated three-year growth targets for EPS (5%-7%) and rate base (6%-7% for Aqua, 8%-10% for Peoples). We see these as highly credible targets that Essential can achieve without sowing the seeds of longer-term problems in terms of regulatory/OCA relations, ratepayer affordability in acquired territories, and long-term customer growth. Importantly, Essential's long-term growth targets do NOT include acquisitions, which represent potential upside.

We reiterate our Outperform rating for Essential, which we see as a best-of-breed player in the regulated water utility space with notable catalysts. Our price target of $50 reflects a forward P/E multiple of 30.5 times, in-line with the current peer group average.

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Disclosure Appendix

Rating and Price Target History:

Risk Factors

The realization of any or all of the following risk factors, among others, may adversely affect the company's stock price and prevent it from reaching our price target: the economic cycle, concentration in energy sector, foreign currency exposure, and client concentration.

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- ***Underperform (Sell):*** The security's total return over the next year or longer is expected to be less than the total return of the S&P 500™ over the identical period.

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- ***High:*** The security has lower-than-average fundamental predictability and/or higher-than-average price volatility.
- ***Speculative:*** The security has very inconsistent fundamental predictability and/or very high relative price volatility.

Ratings Distribution (12/31/19):

Coverage Universe (a)	% of Universe
Outperform (Buy)	29%
Neutral (Hold)	58%
Underperform (Sell)	0%
Not Rated	12%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	14%
Neutral (Hold)	21%
Underperform (Sell)	0%
Not Rated	10%

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Aqua America, Inc.

(WTR-NYSE)

June 12, 2019

Water | Environment

Rating/Risk:	Outperform/Low
Price:	$40.58
Target Price:	$43.00

Aqua/Peoples regulatory process enters litigation in PA, but last-minute (non-unanimous) settlement reached; We expect PUC approval despite I&E objection.

Summary: Yesterday, we were in Harrisburg to attend evidentiary hearings for the Aqua/Peoples deal, which entered formal litigation in PA this week due to disagreement among key parties to the case regarding how to deal with certain high-risk gas gathering systems. While the unexpected delay in the regulatory approval process is by no means a positive, yesterday's hearing began with the news that terms of a non-unanimous settlement have been agreed to, with the formal settlement agreement to be filed with the PUC by June 26. We expect the PA PUC to approve the Peoples acquisition, and maintain our Outperform rating for WTR, with our $43 target price based on our proprietary regulation-weighted valuation model (click HERE for rankings and model).

Key Points:

- **PA regulatory approval dragging out, but settlement reached.** The Pennsylvania regulatory approval process for Aqua/Peoples is taking longer than initially expected, with actual litigation beginning with yesterday's hearings in Harrisburg. There appears to be light at the end of the tunnel, however, with parties telling the ALJ yesterday that terms have been reached on a non-unanimous settlement. The proposed timeline calls for a formal settlement agreement filing by June 26, with opposing party briefs due July 11 (the next two PUC Public Meetings are July 11 and August 8). The PUC's Bureau of Investigation and Enforcement (I&E) and the PA Office of the Small Business Advocate (OSBA) are opposing the non-unanimous settlement.
- **Handling of Equitable gas gathering assets the sticking point.** The main issue of contention is how to handle certain gas gathering assets acquired by Peoples as part of the 2013 Equitable deal – specifically the "Goodwin and Tombaugh" system. This gathering system serves roughly 1,600 customers, but has very high leakage rates and is a non-regulated asset that has been the subject of ongoing controversy since the Equitable acquisition (it was noted during yesterday's hearing that Aqua factored this issue into its negotiated purchase price). Fixing the G&T system would cost $122 million (or $75,000 per customer), and the non-unanimous settlement (which includes OCA) would allow Aqua/Peoples single-tariff rate recovery on this investment.
- **I&E opposes settlement, prefers abandonment of G&T system.** As it has since the Peoples/Equitable merger in 2013, I&E continues to strongly oppose allowing the sizable per customer investments to fix G&T into rate base, on the basis that this is not in the public interest and that it would amount to excessive subsidization by existing Peoples customers. Instead, I&E prefers abandoning the G&T system and moving these customers to propane, noting that Peoples CEO Morgan O'Brien has indicated that in some cases abandonment is in the public interest (for his part, O'Brien stressed he said *in some cases*, and this may not be one of those cases). Discussion of rate recovery vs. abandonment of the G&T system dominated yesterday's hearing.
- **PUC approval likely, clearing the way for closing.** We anticipate the PUC approving the non-unanimous settlement despite I&E's opposition. G&T is a problem asset that must be addressed regardless of owner, and the settlement lays out clear plan with a defined timeline (7 years), to be executed by a credible counterparty in Aqua with manageable impact on existing ratepayers (a 1% bill increase). In our view, a PUC rejection of the settlement would represent a de facto endorsement of abandoning the G&T customers, which would be unpopular politically, further tipping the scales toward approval. Of note, I&E lacks the ability to appeal a PUC ruling, so approval by the PUC would likely stand (OSBA can appeal, but rarely does), clearing the way for the Aqua/Peoples deal to close according to the existing "midyear" timetable.

EPS

Current	Q1	Q2	Q3	Q4	FY
2018A	$0.29	$0.37	$0.44	($0.02)	$1.08
2019E*	$0.09	$0.40	$0.50	$0.28	$1.28
Prior	**Q1**	**Q2**	**Q3**	**Q4**	**FY**
2019	$0.09	$0.40	$0.50	$0.28	$1.28
Consensus	**Q1**	**Q2**	**Q3**	**Q4**	**FY**
2018	$0.29	$0.36	$0.43	$0.31	$1.41
2019	$0.30	$0.39	$0.46	$0.32	$1.44
2020	$0.31	$0.42	$0.50	$0.33	$1.56

**1Q represents actual results.*

Revenue	Current	Prior	Consensus
2018A	$838	$838	$847
2019E	$894	$894	$900

Market Data	
Current Price	$40.58
52-Week Range:	$32.09 - $41.51
Market Cap. (M)	$8,755
Shares Out. (M):	215.7
Float Shs. (M):	215.2
Inst. Ownership:	49%
Short Interest (M)	10.4
Avg. Daily Vol. (Shs.Th.):	967.8
ADTV (M):	$39.27
Valuation	
P/E 2019E	31.8x
Capitalization	
Book Value / Share:	$9.37
Net Cash / Shares:	$0.02
Enterprise Value (M):	$11,515.3
Dividend / Share:	$0.88
Dividend Yield:	2.2%

Note: All estimates reflect stand-alone Aqua. We have discontinued stand-alone Aqua estimates for 2020 given our expectation of the Peoples acquisition closing in 2019.

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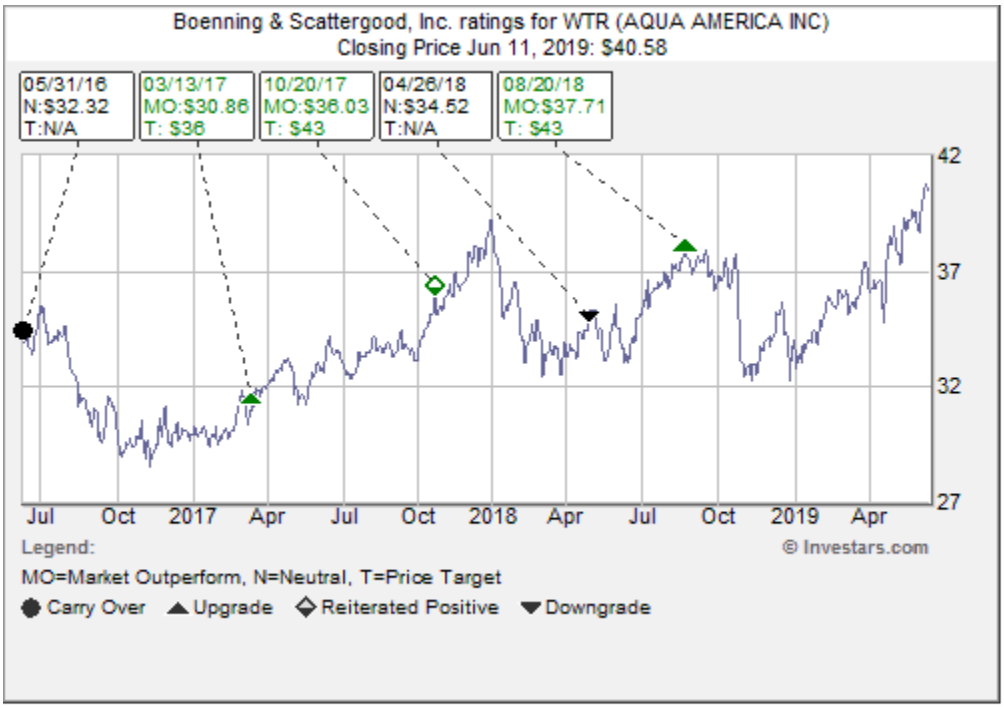
Disclosure Appendix

Rating and Price Target History:



Risk Factors:

The realization of any or all of the following risk factors, among others, may adversely affect the company's stock and prevent it from reaching our target price: regulatory lag; economic regulation; environmental law; water availability; weather; funding; and inputs.

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Ratings Distribution (3/31/19):

Coverage Universe (a)	% of Universe
Outperform (Buy)	43%
Neutral (Hold)	48%
Underperform (Sell)	0%
Not Rated	9%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	13%
Neutral (Hold)	18%
Underperform (Sell)	0%
Not Rated	13%

(a) Total may not add up to 100% due to rounding.
(b) Related to services provided within the past 12 months.

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July 1, 2019

Heads Up

Research Flash Update

Aqua America, Inc.
(WTR/NYSE)

Rating/Risk:	Outperform/Moderate
Price*:	$41.37
Target Price ($US):	$43.00
Market Cap ($US millions):	$8,925
ADTV (US$ millions):	$4.6

Price as-of Prior Day Close

*Target Price and Rating are for 12 months.

EPS	Q1	Q2	Q3	Q4	FY	P/E
2018A	$0.29	$0.37	$0.44	($0.02)	$1.08	38.3x
2019E	$0.09	$0.40	$0.50	$0.28	$1.28	32.4x
2020E	$0.25	$0.41	$0.52	$0.30	$1.49	27.8x

FYE 12/31; Q1-19 represents actual EPS.

Source: Capital IQ, B&S Estimates

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PA-PUC approval of Peoples deal inches closer; Peoples rate case settlement appears imminent.

Last week, Aqua formally filed the non-unanimous settlement agreement with the PA-PUC for its pending acquisition of Peoples Natural Gas, and overall the terms include no major incremental surprises and read favorably from a shareholder perspective.

Notable provisions include:

- A 7-year, $120 million plan to rehabilitate the Goodwin/Tombaugh gas gathering assets, to be recovered via base rates (not DSIC).
- $23 million in rate credits shared across Peoples and Aqua water/WW customers, to be applied by year-end 2019. This is below the $30-$40 million typical in such cases, and keeps the EPS impact within 2019, which is rife with deal-related noise anyway.
- Plans to accelerate replacement of gas distribution pipe within the Peoples system by $30 million a year (which translates into an enhanced rate base growth opportunity).

Based upon statutory timing parameters and precedent, we expect the ALJ to render a proposed decision within 3-4 weeks and for the settlement to come before the PUC for a vote in the September-October timeframe (of note, we believe the potential still exists for a unanimous settlement, which would accelerate this timing).

Separately, evidentiary hearings for the Peoples Gas rate case were abruptly cancelled, suggesting a settlement agreement is imminent. We expect a settlement to be announced in the days/weeks ahead, creating a positive catalyst for WTR shares.

With the Peoples close likely slipping into the fall, visibility on 2020 earnings is likely to remain extremely limited into late 2019. Repair tax treatment is a key variable impacting 2020 expectations, and it remains to be seen how this will affect earnings over the next 12-18 months. Aqua's 2012 adoption of flow-through accounting for repairs on the water side created an immediate and sizable earnings boost, but the company may take a different approach on Peoples.

Overall, WTR remains our top idea in the water utility space due to the combination of discount valuation and fundamental catalysts. We rate WTR shares Outperform, with our $43 target price based on our proprietary regulation-weighted relative valuation model (click HERE for RCI rankings report and valuation model).

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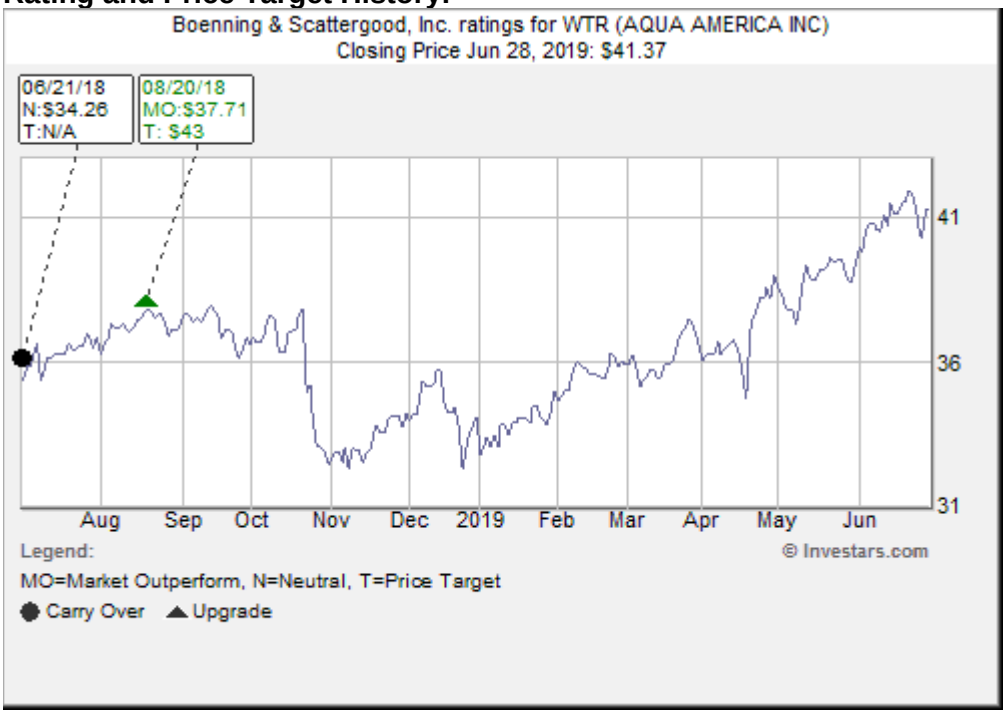

Risk Factors

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Our four-tier risk ratings are based on a mix of price volatility and fundamental factors relative to the market and peer group.

- ***Low:*** The security has higher-than-average fundamental predictability and/or lower-than-average price volatility.
- ***Moderate:*** The security has average fundamental predictability and/or average price volatility.
- ***High:*** The security has lower-than-average fundamental predictability and/or higher-than-average price volatility.
- ***Speculative:*** The security has very inconsistent fundamental predictability and/or very high relative price volatility.

Ratings Distribution (03/31/19):

Coverage Universe	% of Universe	Investment Banking Clients (a)	% of Rating Group
Outperform (Buy)	43%	Outperform (Buy)	13%
Neutral (Hold)	48%	Neutral (Hold)	18%
Underperform (Sell)	0%	Underperform (Sell)	0%
Not Rated	9%	Not Rated	13%

(a) Related to services provided within the past 12 months.

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Top 10 Ideas: 3Q19

July 24, 2019

A look at our Top Ten picks for 3Q19 and the investment thesis behind each.

- **Aqua America (WTR): Top-flight utility with catalysts, at a discount.** With 85% of revenue coming from the attractive regulatory jurisdictions of Pennsylvania, Ohio, and Illinois, Aqua is well positioned to deliver consistent growth in its core regulated water business. Meanwhile, management is pursuing a compelling strategy of doubling-down on these favorable regulatory areas with the pending acquisition of PA-based gas LDC Peoples. The result is a combination of stable underlying growth and compelling catalysts, with the impending regulatory approval of the Peoples deal likely to drive the stock higher in our view. Like most utilities, Aqua has seen its P/E multiple rise of late, but the stock trades at a ~10% discount to peers (our $43 target price based on our proprietary regulation-weighted relative valuation model (click HERE for RCI rankings report and valuation model). B&S Analyst: Ryan M. Connors.
- **Argo International (ARGO): Strong growth and execution, attractive valuation.** ARGO produced strong operating results in 1Q19, including solid premium growth and improved core loss and expense ratios. Management continues to enhance ARGO's operations via investments in technology and people, and we believe the company's operating performance is poised to further benefit from these investments. We compare ARGO to a peer group of 12 specialty insurers. The peer group is trading at a higher price-to-book multiple than ARGO (1.6x vs. 1.3x), but peers have generated only modestly stronger returns. ARGO's shares have returned 20% since mid-2018 but, relative to expected ROE, the shares still appear undervalued. Our $82 target is 1.4 times our forward BVPS estimate. B&S Analyst: Bob Farnam.
- **Bridge Bancorp (BDGE): A differentiated strategic model in an attractive area.** In a region (Long Island, NY) full of banks with high loan-to-deposit ratios and compressing net interest margins, Bridge Bancorp stands out as a differentiated model with a 91% L/D and expanding NIM. Combined with an attractive footprint, a long runway for above-average organic growth, and the ability to grow tangible book value 10% annually, we believe the risk/reward profile is favorable today, with shares trading at a discount to peers on a P/E basis (10.3x 2019E vs. 11.9x). Our $34 target price incorporates a forward (2020) P/E multiple of approximately 11.3 times. B&S Analyst: Erik Zwick.
- **Ecolab: Margin tailwinds set stage for upward revision cycle.** After battling higher oil-based raw material costs for years, Ecolab is finally seeing the price/cost situation turn in its favor, and we expect margin expansion to drive solid bottom-line growth in 2H19 and into 2020. Ecolab also represents a compelling "offense plus defense" story: top-line growth and margin expansion set the stage for the company to thrive if the economy continues to expand, while the "razor/razor-blade" nature of the company's consumables chemistry business makes the story low-beta to a potential recession scenario over the next 12-18 months. Our $210 target price for ECL reflects an Economic Value Added (EVA) yield of 1.3%, roughly in-line with the water infrastructure peer group average. B&S Analyst: Ryan M. Connors.
- **Employers Holdings (EIG): Compelling pure-play on workers' comp.** Employers booked favorable loss reserve development in each of the last eight quarters and, based on our review of the company's loss reserves at YE18, we believe the company will continue to recognize prior year reserve redundancies near-term. Given ongoing initiatives to improve efficiency and expand distribution capabilities, we also expect the company to gradually grow its top line (despite pricing headwinds) and maintain strong underwriting margins (although initiative-related expenses will be higher in the near-term). Loss trends remain favorable in the workers' compensation market. EIG's shares appear attractively priced trading at 1.1 times adjusted BVPS versus a median of 1.6x for a peer group of other specialty insurers. Our target price of $50 reflects a forward price/adjusted BVPS multiple of 1.25 times. B&S Analyst: Bob Farnam.

Boenning & Scattergood

Top 10 Best Ideas: 3Q19
(In alphabetical order)

Aqua America, Inc.
WTR-$41.12-Outperform; TP: $43.00

Argo Group International
ARGO-$70.30-Outperform; TP: $82.00

Bridge Bancorp
BDGE-$28.58- Outperform; TP: $34.00

Ecolab, Inc.
ECL-$197.24-Outperform; TP: $210.00

Employers Holdings
EIG-$42.84-Outperform; TP: $50.00

Flagstar Bancorp
FBC-$33.17-Outperform; TP: $39.00

Kingstone Companies
KINS-$8.37-Outperform; TP: $13.00

Middlefield Bancorp
MBCN-$41.16-Outperform; TP: $51.50

SB One Bancorp
SBBX-$22.44-Outperform; TP: $28.00

Xylem Inc.
XYL-$80.33-Outperform; TP: $90.00

*In alphabetical order.

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- **Flagstar Bancorp (FBC): Credit hiccup creates buying opportunity.** Flagstar disclosed an isolated credit issue that we expect to result in sizeable losses in 2Q, which partially explains the stock's steep discount. The situation involved a commercial loan to a reverse mortgage lender that declared bankruptcy, which we do not believe is indicative of larger problems with the loan portfolio or underwriting standards. Mortgage revenue comprises ~50% of earnings and given our more optimistic outlook for origination activity via lower market interest rates, we believe there is upside potential to current estimates. FBC trades at 10.5x our 2019 estimate and 132% of tangible book value. Our $39 target is based on a takeout-based valuation and peer multiples using a blend of banks and mortgage lenders. B&S Analyst: Scott Beury.
- **Kingstone (KINS): Solid insurer oversold after modest reserve charge.** Kingstone's shares are down 35% since late April when the company preannounced 1Q catastrophe losses ($0.37/share after tax) and a claims department restructuring/reserve charge ($0.37/share after tax). The stock price has declined 50% YTD, with the P/B multiple contracting to 1.1x from 2.1x – the dividend yield is 4.5% at the current price. We believe the shares have been oversold and think the market has overreacted to the company needing to boost reserves after seeing deteriorating trends in a handful of older liability claims, mostly in the company's small commercial lines book rather than in its core personal lines book. In our view, Kingstone remains one of the industry's top underwriters and we believe the company's long-term story remains intact (although results may continue to be pressured in the near-term until the commercial lines book is cleaned up). Our $13 target is 1.6 times our forward BVPS estimate. B&S Analyst: Bob Farnam.
- **Middlefield Banc Corp. (MBCN): Russell sell-off creates opportunity.** Middlefield was removed from the Russell 2000 index last month, which was preceded by a sustained sell-off in the shares, resulting in a discounted valuation. We believe the company is capable of generating consistent mid-single digit loan growth while maintaining stable credit metrics, and modest margin compression. The stock currently trades at 10x 2019e EPS and 114% of tangible book value, both representing a sizeable discount to peer multiples (11.5x, 155%). We believe this is unwarranted given the company's fundamental trends and expect the stock to drift higher through the remainder of the year. Our $51.50 target price is based on a blended valuation of peer multiples and a discounted acquisition analysis. B&S Analyst: Scott Beury.
- **SB One Bancorp (SBBX): Strong management team, winning culture.** SB One is a $1.9 billion community bank lead by a talented management team with big bank pedigrees. They operate the bank with a pervasive entrepreneurial spirit aimed at enhancing franchise value. We continue to see multiple catalysts for the stock to close the valuation gap with peers, including: 1) successful execution of acquisition-related cost saves, 2) improving profitability, and 3) above-peer organic balance sheet growth. We believe the risk/reward profile is favorable today, with shares trading at a discount to peers on both, P/E (8.9x 2019E vs. 11.9x peers) and P/TBV (1.3x vs. 1.4x peers) basis. Our $28 target price reflects a multiple of 10.2 times our current 2020 EPS estimate. B&S Analyst: Erik Zwick.
- **Xylem (XYL): Secular drivers create long-tailed growth story.** A water sector bellwether, Xylem boasts the water sector's most comprehensive solutions portfolio, offering a wide range of water treatment, transport, test, and metering/AMI solutions for customers in the municipal, industrial, and construction channels. The company has an established track record of organic growth and compelling acquisitions, and recently removed a key tactical risk from the equation by pushing its ambitious long-term operating margin target to the right. Our recent checks suggest Xylem's recent product launches are gaining strong pricing traction, setting up a strong second half for the company. Our $90 target reflects a forward P/E of 24.5x times, in-line with the water infrastructure peer group average. B&S Analyst: Ryan M. Connors.

Disclosure Appendix

Rating and Price Target History:

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November 5, 2019

Heads Up

Research Flash Update

Aqua America, Inc.
(WTR/NYSE)

Rating/Risk:	**Outperform/Moderate**
Price:	$43.56
Target Price ($US):	$50.00
Market Cap ($US millions):	$9,829
ADTV (US$ millions):	$39.7

Price as-of Prior Day Close

Target Price and Rating are for 12 months.

EPS	Q1	Q2	Q3	Q4	FY	P/E
2018A	$0.29	$0.37	$0.44	($0.02)	$1.08	40.3x
2019E	$0.09	$0.25	$0.38	$0.24	$0.96	45.2x

FYE 12/31; Q1-Q3 2019 represent actual EPS.

Source: Capital IQ, B&S Estimates

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Third quarter report contains no big surprises; Peoples, DELCORA key growth catalysts.

Aqua America posted 3Q EPS of $0.38, a penny below our estimate of $0.39, as stronger than expected revenue growth was offset by higher O&M expenses. Revenue increased 7.7% year/year in the third quarter, above our model at +5%, with new base rates, organic customer growth, and acquisitions all contributing. O&M expenses rose 19.5% year/year, driven by Peoples-related merger costs and a tough comp (management notes core expense growth was in-line with the historic run-rate).Overall, it was a solid operating quarter for Aqua, with the robust top-line growth encouraging.

The ALJ handling the Aqua/Peoples merger application in PA issued a favorable recommended decision last week, paving the way for the PUC to issue a final ruling (potentially on December 5 or 19). We expect the Peoples acquisition to close in January 2020, providing a notable catalyst for Aqua that will set the company apart from peers. As we've written consistently since Aqua sought to acquire electric transmission utility ITC in 2016 (and again when Eversource (ES-$81.42-Not Rated) acquired water utility Aquarion in 2017), we are big believers in the multi-utility concept. We envision Aqua/Peoples evolving into a powerful regulated infrastructure growth platform once the two companies have been successfully integrated.

In addition, Aqua signed an agreement to acquire DELCORA in 3Q, setting the stage for one of the industry's largest municipal deals in years. DELCORA is a regional WW system serving 500,000 people (or roughly 165,000 connections) in the southwestern Philadelphia suburbs, and Aqua will pay $277 million for the system. Aqua also has an additional 22,600 customers in the near-term acquisition pipeline. Headlined by DELCORA, Aqua continues to execute well on its municipal acquisition program, a key growth driver.

Aqua's combination of organic rate base growth, steady pipeline of municipal deals, and addition of a Pennsylvania gas platform provide a strong mix of fundamental catalysts that we believe set the stage for strong shareholder value generation in the years ahead. WTR shares remain our top idea in the utility space due to a mix of valuation and these fundamental catalysts. We rate WTR shares Outperform, with our $50 target price based on our regulation-driven valuation model and the stock's premium dividend yield.

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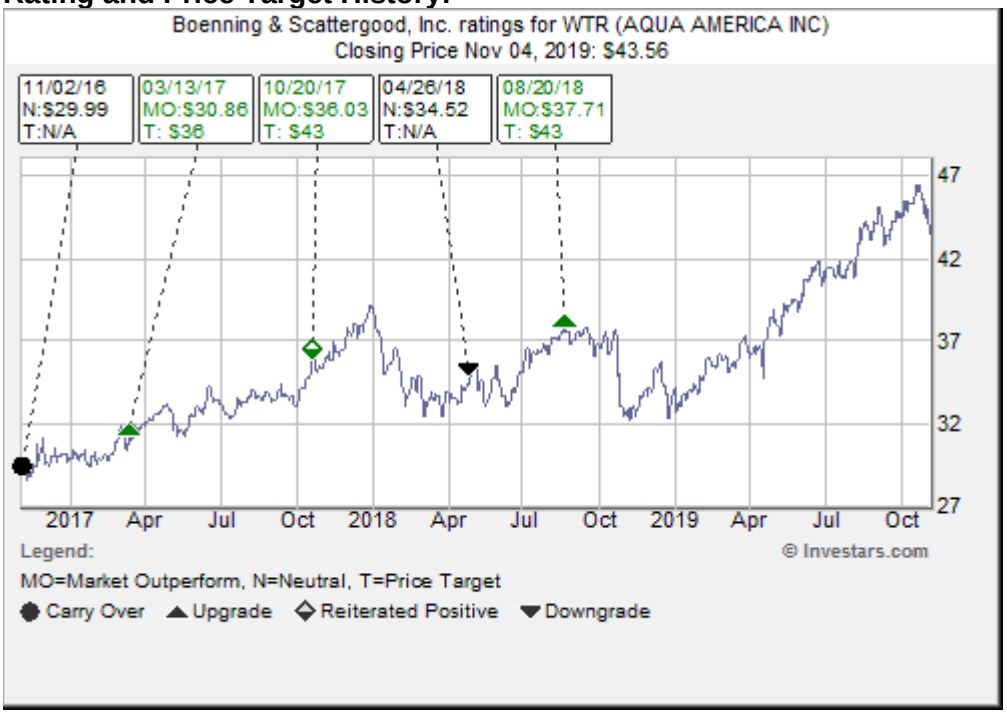
Rating and Price Target History:



Risk Factors

The realization of any or all of the following risk factors, among others, may adversely affect the company's stock price and prevent it from reaching our price target: the economic cycle, concentration in energy sector, foreign currency exposure, and client concentration.

Analyst Certification:

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Boenning & Scattergood received compensation for investment banking services from the subject company within the past 12 months.

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Ratings Distribution (9/30/19):

Coverage Universe (a)	% of Universe
Outperform (Buy)	33%
Neutral (Hold)	56%
Underperform (Sell)	0%
Not Rated	11%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	19%
Neutral (Hold)	20%
Underperform (Sell)	0%
Not Rated	22%

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October 7, 2019

Heads Up

Research Flash Update

Aqua America, Inc.
(WTR/NYSE)

Rating/Risk:	Outperform/Moderate
Price*:	$45.55
Target Price ($US):	$50.00
Market Cap ($US millions):	$9,829
ADTV (US$ millions):	$39.7

Price as-of Prior Day Close

*Target Price and Rating are for 12 months.

EPS	Q1	Q2	Q3	Q4	FY	P/E
2018A	$0.29	$0.37	$0.44	($0.02)	$1.08	42.2x
2019E	$0.09	$0.25	$0.39	$0.22	$0.95	47.9x

FYE 12/31; Q1 and Q2 2019 represent actual EPS.

Source: Capital IQ, B&S Estimates

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PA PUC approves Peoples rate case settlement, but silence deafening on merger application.

Update: Peoples Rate Case (Docket R-2018-3006818):

Last week, the Pennsylvania Public Utilities Commission approved the settlement agreement in the Peoples rate case by a vote of 4-0. The company receives $59.5 million in new revenue, or 63% of the $94.9 million requested, a solid outcome relative to other recent cases. The new rates represent a 9% increase over Peoples' current PA regulated revenue, and will take effect on October 29.

Of note, the PUC ruled in Peoples' favor on the sole remaining issue of contention in the case (the proposed main line extension policy), overriding objections raised by the Office of the Small Business Advocate. We view the Peoples rate case settlement approval as a positive development for Aqua America, as it improves the returns and earnings power of a potential combined Aqua/Peoples entity.

Update: Aqua/Peoples Merger Application (A-2018-3006061):

While the Peoples rate case settlement approval is a clear positive, the Aqua/Peoples 's merger application continues to drag on longer than initially expected. We had expected an ALJ decision to come before the PUC as early as August, so the delay is significant, but it is difficult to interpret what the holdup means.

The "glass half empty" interpretation is that the delay suggests that the ALJ is leaning toward a negative ruling, with the rationale being that a denial of the merger would be highly controversial and therefore require an extremely high level of diligence and detail given the inevitable scrutiny and pushback it would trigger. Upgrade vs. abandonment of the Goodwin/Tombaugh gas gathering system is the key sticking point (see our June 20 note for details).

The "glass half full" read is that the PUC has finite resources, and the Peoples rate case was seen as the more urgent matter to be dealt with first. With the rate case resolved, the PUC will now move ahead with addressing the merger settlement agreement. In our view, the Peoples acquisition remains likely to close by year-end, creating a notable positive catalyst for WTR shares.

WTR remains our top idea in the water utility space due to a mix of discount valuation and fundamental catalysts. We rate WTR shares Outperform, with our $50 target price based on our regulation-driven valuation model and the stock's premium dividend yield.

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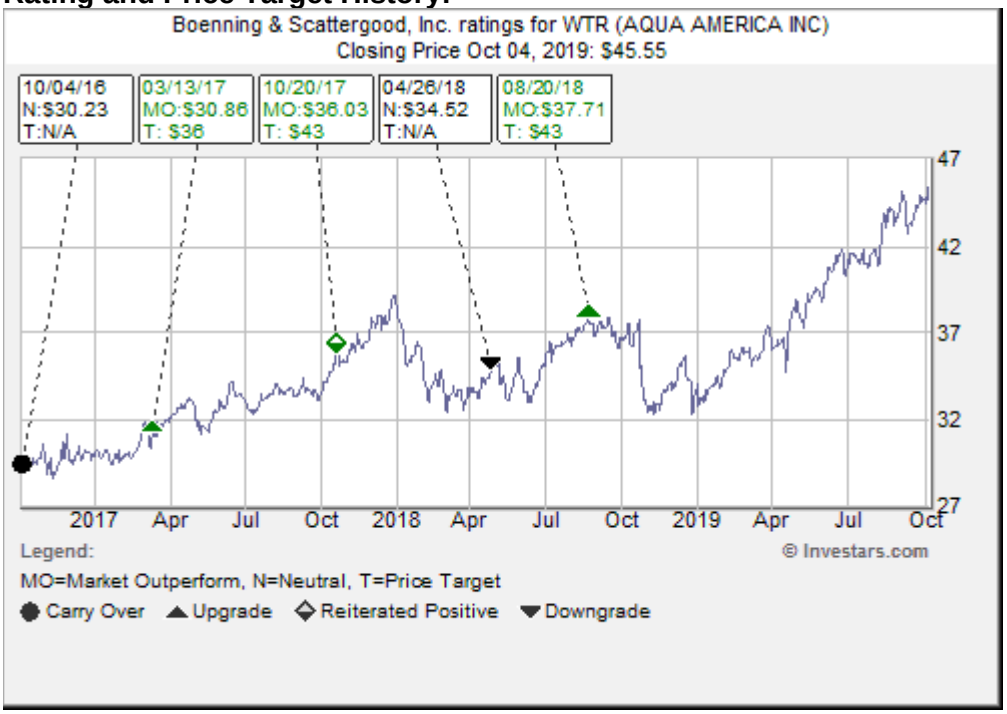

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Ratings Distribution (6/30/19):

Coverage Universe (a)	% of Universe
Outperform (Buy)	32%
Neutral (Hold)	56%
Underperform (Sell)	0%
Not Rated	13%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	20%
Neutral (Hold)	20%
Underperform (Sell)	0%
Not Rated	20%

(a) Related to services provided within the past 12 months.

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January 14, 2021

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	Outperform/Moderate
Price:	$46.88
Target Price ($US):	$54.00
Market Cap ($US millions):	$11,550
ADTV (US$ millions):	$61.0

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2018A	$1.08	-	$838.1	-	43.4x
2019A	$1.00	-	$889.7	-	46.8x
2020E*	$1.15	$1.59	$1,396	$1,639	40.8x
2021E	$1.68	$1.67	$1,625	$1,819	27.9x

FYE 12/30; Revenue in USD millions.

All historical EPS and B&S EPS estimates GAAP.

*Guidance: $1.53-$1.58 ("adjusted") reflects full year of Peoples.

Source: Capital IQ, B&S Estimates

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Surprise ALJ decision a setback, but DELCORA acquisition remains likely to move forward.

Yesterday, the administrative law judges dealing with Essential/Aqua acquisition of DELCORA issued a proposed decision recommending that the PUC reject the deal. The surprise decision comes just days after the Delaware County of Common Pleas issued a distinctly one-sided ruling in Essential/DELCORA's favor. While the recommended ALJ decision is tactical setback for the transaction, we continue to believe that the deal will ultimately move forward to a 2021 close.

There appear to be three primary points on which the ALJ bases the adverse recommendation, and we believe that all three issues are manageable and will ultimately turn in Essential's favor.

Rate Stabilization Fund. The ALJ decision notes that the novel rate stabilization trust that is part of the DELCORA deal is not included in the PUC application. Since the ultimate ratemaking details stemming from the trust remain to be determined in future rate cases, it is not surprising that this was left out, but this is an easy fix, as there are a number of ways to ensure that ratepayers are made whole.

Local Municipality Protests. The recommended decision also says that protest from some local municipalities is a problem, but sources close to the situation suggest that many are open to settling and on the path to doing so. Based on the players involved, this pushback appears driven in part by local politics/personalities rather than the public interest, a dynamic that will not escape the commission.

Potential DelCo ruling appeal. The ALJ cites "ongoing litigation" as an issue, since Delaware County is believed to be mulling an appeal despite the judge ruling in Aqua's favor. Our read of the DelCo ruling suggests it is very unlikely to be overturned, and there also remains the possibility of a settlement. The bottom-line is that whatever the ALJ says, the DelCo lawsuit has been going Essential's way.

While there have been adverse ALJ recommendations in the past, it is rare for the commission to actually rule against an acquisition between two willing parties. This is particularly the case when the acquirer is a well-known, established, and respected in-state player such as Essential/Aqua. As a result, we believe the DELCORA deal will ultimately move forward despite the ALJ recommendation.

WTRG and its peers have performed respectably on a risk-adjusted basis, but have lagged the broader market (S&P 500 +17% TTM) and the huge gains in the water industrial sector (+33% TTM). We believe that WTRG offers compelling reward/risk, with our $54 target price reflecting a P/E of 32 times, in-line with the peer group.

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Disclosure Appendix

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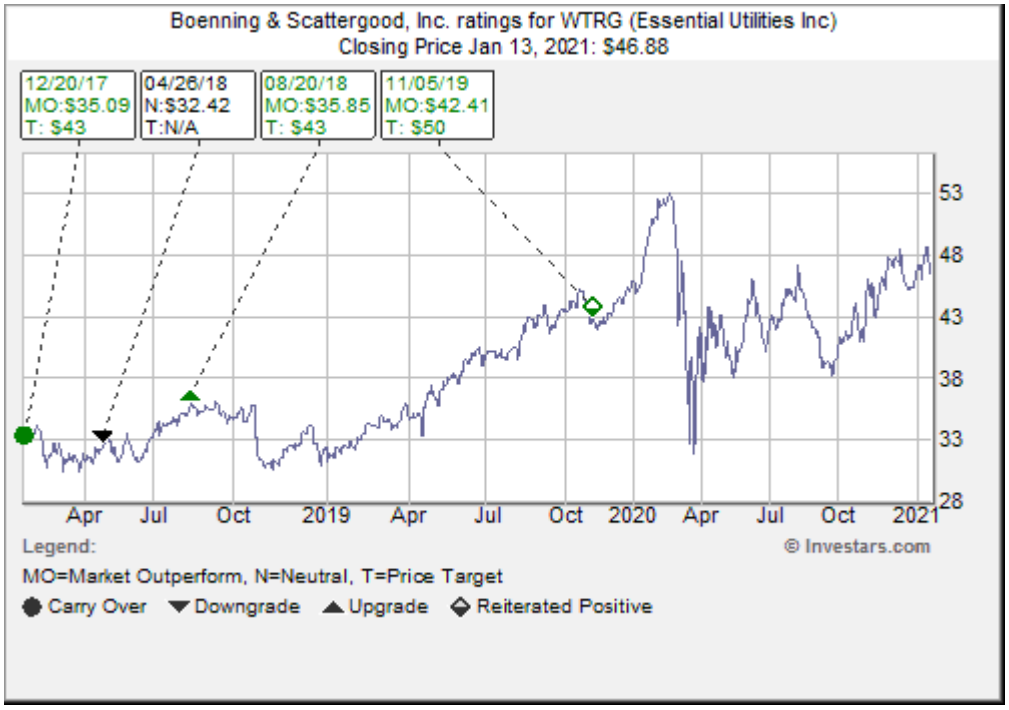

Risk Factors

The realization of any or all of the following risk factors, among others, may adversely affect the company's stock price and prevent it from reaching our price target: the economic cycle, concentration in energy sector, foreign currency exposure, and client concentration.

Analyst Certification:

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- ***High:*** The security has lower-than-average fundamental predictability and/or higher-than-average price volatility.
- ***Speculative:*** The security has very inconsistent fundamental predictability and/or very high relative price volatility.

Ratings Distribution (9/30/20):

Coverage Universe (a)	% of Universe
Outperform (Buy)	32%
Neutral (Hold)	46%
Underperform (Sell)	1%
Not Rated	20%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	21%
Neutral (Hold)	9%
Underperform (Sell)	100%
Not Rated	7%

(a) Related to services provided within the past 12 months.

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February 25, 2021

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	Outperform/Moderate
Price:	$44.09
Target Price ($US):	$54.00
Market Cap ($US millions):	$11,550
ADTV (US$ millions):	$61.0

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2019A	$1.00	-	$889.7	-	44.0x
2020A	$1.12	-	$1,463	-	39.4x
2021E	$1.68	$1.68	$1,877	$1,983	26.3x
2022E	$1.80	$1.81	$1,952	$2,163	24.4x

FYE 12/30; Revenue in USD millions.

All historical EPS and B&S EPS estimates GAAP.

Source: Capital IQ, B&S Estimates

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4Q solid yet anti-climactic after guidance update call; All eyes on PUC as DELCORA ruling looms.

Essential posted 4Q20 EPS of $0.40, up from $0.28 a year ago, with the upside driven by the addition of Peoples and organic growth also contributing. Revenue more than doubled year/year (+109.7%), with Peoples adding $240 million, or 106.4%. Ex-Peoples, revenue rose 3.3% on a combination of higher volumetric sales, rates/surcharges, and acquisitions. Seasonally high purchased gas costs ($93 million, or 20% of sales vs. 7% in 1Q-3Q) pressured margins, with operating margin down 220 bps sequentially to 28%. Of note, one-time credits to gas customers related to the Peoples deal hit EPS by $0.06.

Essential acquired six water/WW systems totaling 12,000 customers for $63 million in 2020, and currently has APAs in place for a further 227,000 in connections. The largest is the $276 million acquisition of DELCORA, which was dealt an adverse ALJ ruling last month. Still, we see the three major issues raised by the ALJ (rate stabilization fund, local municipality protests, and potential appeal of a favorable DelCo Ct. of Common Pleas ruling) ultimately turning in Essential's favor. Essential expects a PA PUC decision by March 2021.

Essential was awarded $21 million in base rates and surcharges in 2020, including in Illinois, Indiana, Kentucky, North Carolina, Ohio, Pennsylvania, and Virginia. Year-to-date, the company has received $8.5 in rates/surcharges across New Jersey, NC, OH, and PA, and has $1.8 million pending in IN and VA. Though not immaterial, this pipeline of rate activity is light by the company's historical standards, which we see as timely. Essential had just completed a number of major rate cases before COVID-19, and therefore does not have to seek major rate hikes during these difficult times for customers.

Essential's fourth quarter report is somewhat of a non-event, as the company stole its own thunder with its January 11 guidance release and conference call. Predictably, management reiterated the 2021 guidance of $1.64-$1.69 issued last month (one wildcard 2021 issue to watch is the EPS impact of the Texas situation). Essential also reiterated its 5%-7% EPS CAGR target through 2023, and we see the company as well positioned to deliver the top growth rate across the regulated water/multi-utility peer group over this timeframe.

WTRG and peers have underperformed notably in recent days due in part to rising inflation concerns, despite the fact that the data show utilities outperform the broader market during inflationary periods (for details, see our industry report today). We believe WTRG shares offer a compelling reward/risk equation, with our $54 target reflecting a P/E of 32 times, in-line with the water utility peer group.

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Disclosure Appendix

Rating and Price Target History:

Risk Factors

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- ***Speculative:*** The security has very inconsistent fundamental predictability and/or very high relative price volatility.

Ratings Distribution (12/31/20):

Coverage Universe (a)	% of Universe
Outperform (Buy)	38%
Neutral (Hold)	49%
Underperform (Sell)	1%
Not Rated	13%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	22%
Neutral (Hold)	3%
Underperform (Sell)	100%
Not Rated	0%

(a) Related to services provided within the past 12 months.

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May 7, 2020

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	**Outperform/Moderate**
Price:	$40.67
Target Price ($US):	$50.00
Market Cap ($US millions):	$9,965
ADTV (US$ millions):	$30.1

Price as-of Prior Day Close

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2018A	$1.08	-	$838.1	-	37.7x
2019A	$1.00	-	$889.7	-	40.6x
2020E*	$1.10	$1.46	$1,384	$1,655	37.0x
2021E	$1.65	$1.65	$1,662	$1,970	24.6x

FYE 12/30; Revenue in USD millions.

All historical EPS and B&S EPS estimates GAAP.

*Adjusted guidance of $1.53-$1.58 reflects full year of Peoples.

Source: Capital IQ, B&S Estimates

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*

Keep Calm, Carry On: Guidance, growth targets reaffirmed as regulated model shines amid crisis.

Essential Utilities posted 1Q EPS of $0.20, which include two weeks of the Peoples Gas acquisition which closed on March 16 (assuming a full quarter of Peoples, EPS would have been $0.60). In addition to the Peoples deal, Essential filed paperwork with the PUC in 1Q for the acquisition of the DELCORA regional wastewater system, which will be the largest municipal acquisition in the company's 134-year history as well as the biggest ever in the state of Pennsylvania.

In light of the solid first quarter report, Essential reiterated both its indicative (i.e. adjusted to include a full year of Peoples) 2020 EPS guidance of $1.53-$1.58 and its 5%-7% earnings CAGR through 2022. Given the strong organic growth dynamics and active M&A cadence, we believe Essential has the most compelling, sustainable growth story in the regulated environmental utility peer group.

Importantly for the intermediate-term outlook, Essential continues to move forward with its capital improvement program. Maintaining a robust capital investment level is key to sustaining rate base growth, which in turn is key to driving earnings and shareholder value. While affordability is a near-term concern, there is so far no evidence that COVID-19 is leading PUCs to lean on IOUs to cut capex to forestall future rate impacts. We believe that this is in part because regulated utilities provide timely offsetting infrastructure spending/stimulus at a time when state and local governments will be cutting budgets.

Like peers, Essential has suspended shut-offs during the COVID-19 crisis. This industry issue has been cited as a risk in the financial press, including a Wall Street Journal article this week (link HERE) saying households will "prioritize bills causing immediate disruptions to their lives if left unpaid. Cable TV and internet, which can still be cut off, are likely to rank higher on the payment hierarchy than electricity, gas and water". Such views misunderstand/ overstate the collection risks facing IOUs. Bills are being generated and will come due as the crisis stabilizes, and liabilities for basic utility services are unlikely to be forgiven except in cases of true financial hardship.

Essential's solid 1Q, guidance/growth target affirmation, active M&A pipeline, and continued execution on its capital investment program amid the huge COVID-19 economic shock epitomize the resilience of the regulated utility business model. We reiterate our Outperform rating for Essential, which we see as a best-of-breed player in the regulated utility space with notable near-term growth catalysts.

Our price target of $50 reflects a forward P/E multiple of 30.3 times, ~in-line with the current peer group average of 30.2 times.

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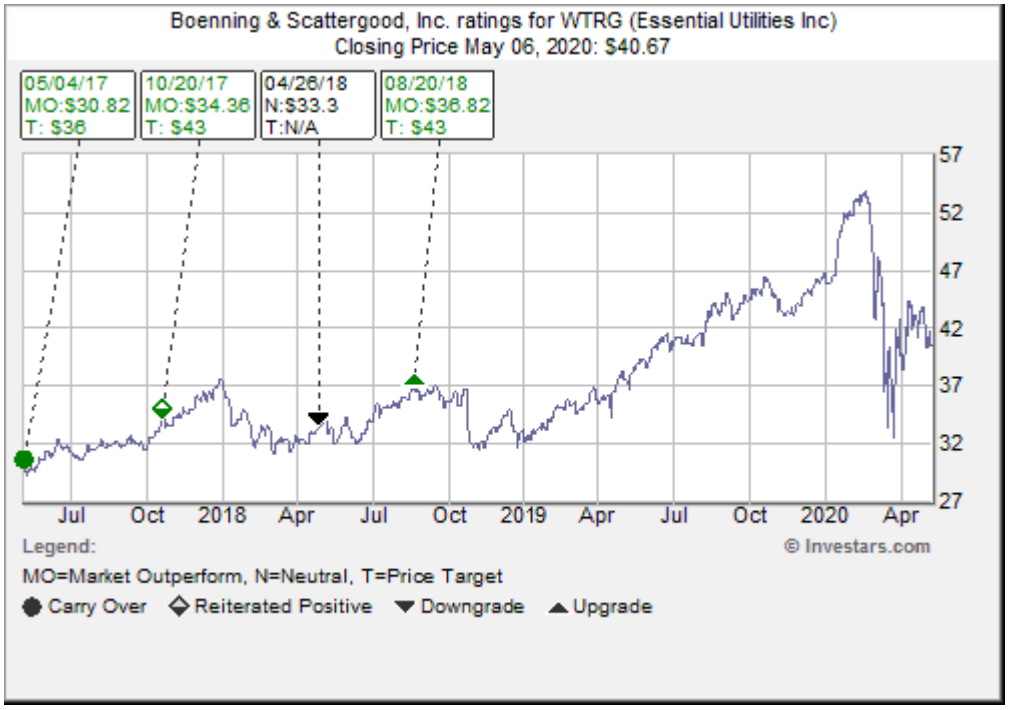

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- ***Speculative:*** The security has very inconsistent fundamental predictability and/or very high relative price volatility.

Ratings Distribution (3/31/20):

Coverage Universe (a)	% of Universe
Outperform (Buy)	28%
Neutral (Hold)	61%
Underperform (Sell)	0%
Not Rated	11%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	27%
Neutral (Hold)	13%
Underperform (Sell)	0%
Not Rated	22%

(a) Related to services provided within the past 12 months.

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Essential Utilities, Inc.

(WTRG-NYSE)

June 18, 2020

Water | Environment

Rating/Risk:	Outperform/Low
Price:	$43.14 (intra-day; 1:46pm)
Target Price:	$50.00

County of Delaware vs. DELCORA: Initial hearing suggests acquisition likely to close in 2020 despite shrill rhetoric, legal maneuvering by local officials.

Summary: We attended today's Delaware County Court of Common Pleas hearing in the County of Delaware (aka DelCo) vs. DELCORA, which has major ramifications on whether Essential's acquisition of DELCORA will go forward (and if so under what terms). Contrary to rhetoric from county officials assailing any deal and privatization generally, the county's legal positions focused primarily on the structure of the ratepayer stabilization fund, leaving us with the clear impression that the case is really about who gets the money and not an effort to block the deal altogether. The attorneys agreed on a path forward that includes follow-up hearings in July-August, with hopes to conclude in the fall, and we came away believing the acquisition is likely to close in 2020.

Key Points:

- **County walks back attack on sale, focuses on ratepayer trust.** Told by the judge that he read the initial complaint as an attack on the sale of DELCORA and the ratepayer stabilization fund, DelCo lawyers seemed to backpedal, saying the complaint is meant to attack the trust and that at this time it has no issue with the sale of DELCORA per se. DelCo also seemed to walk back the immediacy of its June 3 ordinance to dissolve DELCORA, saying the authority can only be terminated once key impediments are removed, which could take months. While a lot can still happen, DelCo's legal stance on the Aqua/DELCORA deal appears far less nuclear than recent rhetoric in the local press suggests, substantially increasing the odds of the deal going.
- **DELCORA: County must honor deal even if authority terminated.** DELCORA attorneys made a persuasive argument that while DelCo does have the ability to dissolve the authority, it can only do so after honoring all contracts, which in this case encompasses the sale agreement with Aqua. DelCo's lawyers did not appear to have a ready answer to this, and the issue did not engender much further discussion with the judge, suggesting that public statements from Aqua and DELCORA that the merger agreement and rate stabilization fund are enforceable no matter who owns DELCORA are on solid legal ground. This is key, since it would render draconian press reports on the ramifications of the termination of DELCORA essentially moot.
- **Judge steering parties toward agreeing on modifications to trust.** The judge acknowledged that the structure of the ratepayer stabilization fund, and not DELCORA's sale or termination, is the key issue, noting at one point that "we don't deal with rhetoric in the newspaper, we deal with representations in court". A key point came when, at the judge's prodding, DelCo attorneys said they would be amenable to opening discussions about how to improve upon the structure of the trust. In our view, this was the clearest evidence yet that the county's opposition is really about the money trail rather than the deal itself. We believe Aqua would be open to reasonable modifications of the trust, provided they do not result in a negative financial impact.
- **Deal looks more likely to close, creating positive EPS/stock catalyst.** The key take-away is that the hearing indicated a much less extreme position on the part of DelCo than suggested by recent public meeting comments and quotes in the press. In addition to appearing to back off of attacks on the sale itself and the immediate termination of DELCORA, the county did not raise any concerns regarding the sale process itself. As a result, we now believe the DELCORA deal is likely to close in 2020, giving Essential critical mass to go after additional WW deals in PA and creating a positive earnings tailwind for 2021. We reiterate our Outperform rating for shares of WTRG, with our $50 target price applying a P/E of 30 times, in-line with peers.

EPS	2018A	2019A	2020E	2021E	2022E
Current	$1.08	$1.00	$1.10	$1.65	$1.85
Prior	-	-	$1.10	$1.65	$1.85
Consensus	-	-	$1.38	$1.67	$1.79
Guidance*			$1.53-$1.58		

Revenue	Current	Prior	Consensus
2018A	$838	-	-
2019A	$881	-	-
2020E	$1,488	$1,488	$1,658
2021E	$1,668	$1,668	$1,948
2022E	$1,835	$1,835	$2,098

Market Data	
Current Price*:	$43.14
52-Week Range:	$30.40 - $54.52
Market Cap. (M)	$10,570
Shares Out. (M):	245.0
Float Shs. (M):	244.3
Inst. Ownership:	70%
Short Interest (M)	4.6
Avg. Daily Vol. (Shs.Th.):	383.9
ADTV (M):	$16.6
Valuation (Cons.)	
P/E 2020E	31.3x
P/E 2021E	25.8x
P/E 2022E	24.1x
Capitalization	
Book Value / Share:	$9.37
Net Cash / Shares:	$0.13
Enterprise Value (M):	$15,935.5
Dividend / Share:	$0.94
Dividend Yield:	2.2%

*Price as-of Prior Day Close
Target Price and Rating are for 12 months.
FYE 12/30; Revenue in USD millions.
Historical and B&S EPS estimates U.S. GAAP.
*Adj. 2020 guidance reflects full year of Peoples.
Source: Capital IQ, B&S Estimates

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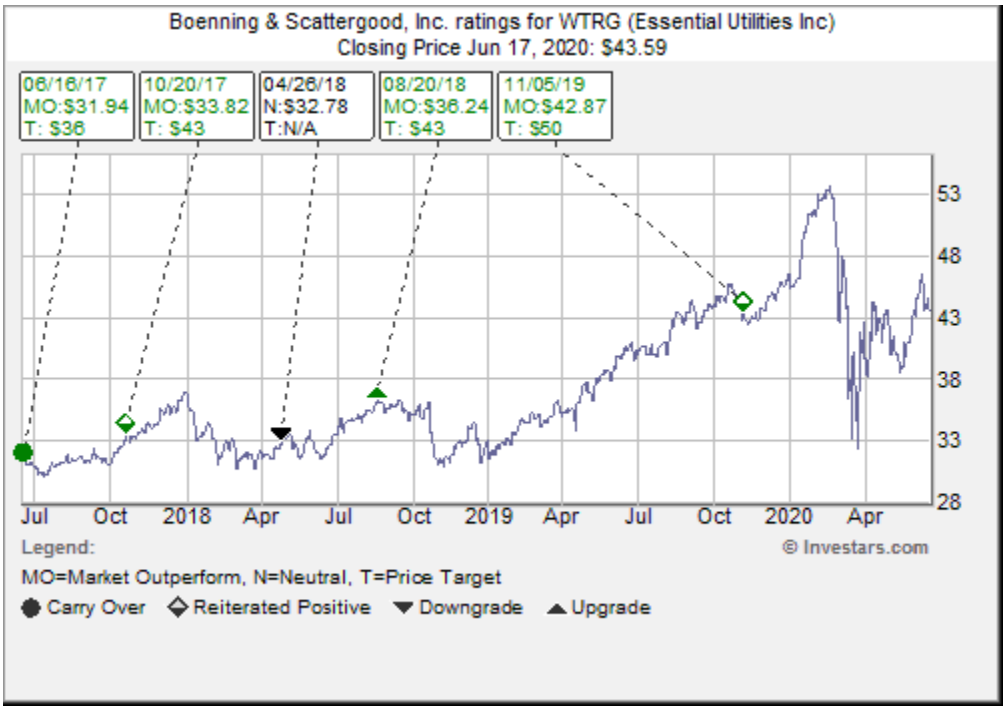
Disclosure Appendix

Rating and Price Target History:



Risk Factors:

The realization of any or all of the following risk factors, among others, may adversely affect the company's stock and prevent it from reaching our target price: regulatory lag; economic regulation; environmental law; water availability; weather; funding; and inputs.

Analyst Certification:

The research analyst whose name appears on this research report certifies that: (1) all of the views expressed in this research report accurately reflect their personal views about the subject security or issuer, and (2) no part of the research analysts' compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed by the research analysts in this research report.

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- ***High:*** The security has lower-than-average fundamental predictability and/or higher-than-average price volatility.
- ***Speculative:*** The security has very inconsistent fundamental predictability and/or very high relative price volatility.

Ratings Distribution (3/31/20):

Coverage Universe (a)	% of Universe
Outperform (Buy)	28%
Neutral (Hold)	61%
Underperform (Sell)	0%
Not Rated	11%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	27%
Neutral (Hold)	13%
Underperform (Sell)	0%
Not Rated	22%

(a) Total may not add up to 100% due to rounding.
(b) Related to services provided within the past 12 months.

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June 21, 2021

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	Outperform/Low
Price:	$46.63
Target Price ($US):	$54.00
Market Cap ($US millions):	$11,740
ADTV (US$ millions):	$63.0

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2019A	$1.00	-	$889.7	-	46.6x
2020A	$1.12	-	$1,463	-	41.7x
2021E	$1.68	$1.67	$1,839	$1,908	27.8x
2022E	$1.82	$1.80	$1,955	$2,010	25.6x

FYE 12/30; Revenue in USD millions.

All historical EPS and B&S EPS estimates GAAP.

Source: Capital IQ, B&S Estimates

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Tour of Aqua's state-of-the-art environmental lab affirms thesis as PA's teethier WQAA advances.

We toured Aqua's recently completed 14,700 sq. foot environmental lab, located at Essential's corporate headquarters in Bryn Mawr, PA. Led by Chief Environmental, Safety, and Sustainability Officer Chris Crockett, our tour affirmed several key aspects of the investment thesis for WTRG. In particular, the lab's opening is timely given the likely imminent passage of PA 597, PA's water quality accountability legislation (unlike in NJ, where WQAA is still not being enforced due to DEP foot-dragging, the PA law will be implemented by the PUC, which aims to enforce it vigorously). The Bryn Mawr lab positions Aqua well as a partner for local water systems as they struggle to meet WQAA testing and compliance reporting requirements.

While it's predictable that Essential itself touts the new lab, our in-person tour independently confirms that the lab is in fact impressive. We've toured environmental labs for peer companies and major, big city municipal water/WW utilities, and Aqua's is the largest and most advanced environmental water testing facility we've seen yet.

Below are some of the key attributes of the new facility:

- Certified for environmental compliance reporting in five states (Ohio, Pennsylvania, New Jersey, North Carolina, Virginia).
- Equipped for 300,000 tests annually on 30,000 water samples.
- Comprehensive microbiological, organic, and inorganic analysis.
- Liquid Chromotography tandem Mass Spectrometry (LC-MS-MS) capabilities test for PFAS at demanding parts per trillion levels.
- Dedicated space for piloting cutting-edge analytical technologies.
- 20 employees; room to expand as organization grows.

WTRG trades at a discount to water utility peers, and a trite refrain is that Essential's foray into gas makes the company "less sustainable" and inhibits a full "ESG multiple". We don't buy this, seeing Essential as among the most sustainable companies in the space, and the state-of-the-art Bryn Mawr lab affirms this, highlighting that this is not only still very much a water company, but one at the forefront of addressing difficult issues like PFAS. Meanwhile, environmentally sound natural gas is crucial to Western PA's energy mix, and years of observing the industry from the frontlines (not puffy ESG reports) inform our view of Essential's sound corporate governance and excellent employee/customer/community/regulatory relations.

Our $54 target reflects a P/E of 32 times, in-line with water peers.

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Disclosure Appendix

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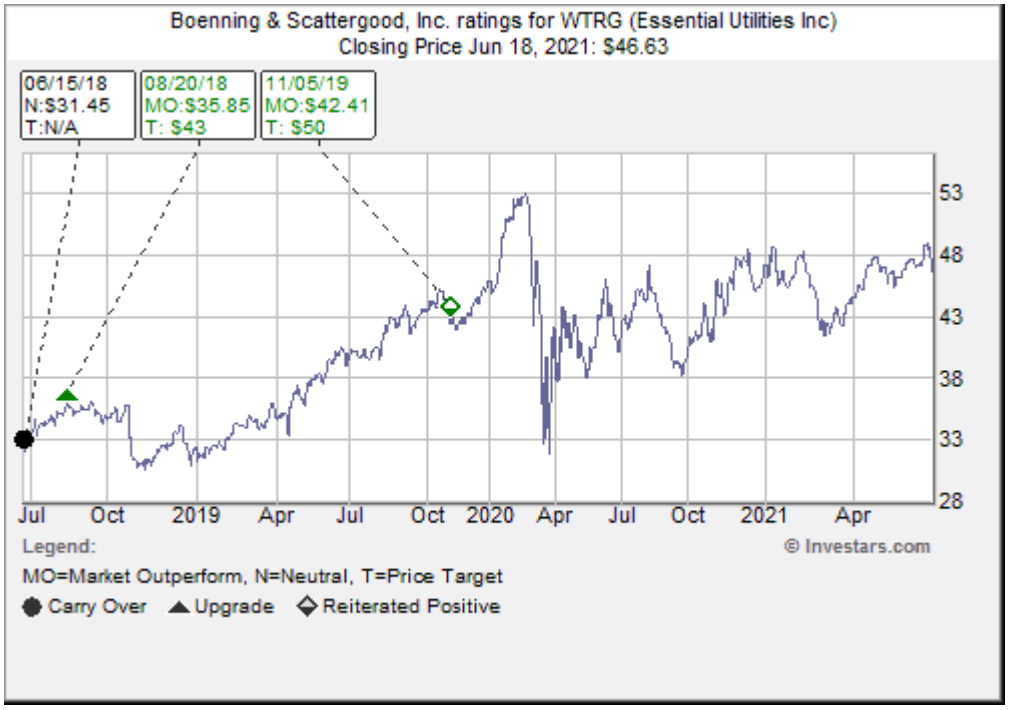

Risk Factors

The realization of any or all of the following risk factors, among others, may adversely affect the company's stock price and prevent it from reaching our price target: the economic cycle, concentration in energy sector, foreign currency exposure, and client concentration.

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Ratings Distribution (3/31/21):

Coverage Universe (a)	% of Universe
Outperform (Buy)	38%
Neutral (Hold)	47%
Underperform (Sell)	1%
Not Rated	14%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	7%
Neutral (Hold)	3%
Underperform (Sell)	100%
Not Rated	10%

(a) Related to services provided within the past 12 months.

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August 6, 2020

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	Outperform/Moderate
Price:	$44.69
Target Price ($US):	$50.00
Market Cap ($US millions):	$10,951
ADTV (US$ millions):	$46.6

Price as-of Prior Day Close

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2018A	$1.08	-	$838.1	-	41.4x
2019A	$1.00	-	$889.7	-	44.6x
2020E*	$1.40	$1.48	$1,485	$1,656	31.8x
2021E	$1.70	$1.66	$1,658	$1,813	26.3x

FYE 12/30; Revenue in USD millions.

All historical EPS and B&S EPS estimates GAAP.

*MOAP guidance of $1.53-$1.58 reflects full year of Peoples.

Source: Capital IQ, B&S Estimates

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EPS surge 17% as lockdowns drive residential demand; Growth outlook robust, highly visible.

Essential Utilities reported 2Q EPS of $0.29, up 17% year/year, with solid organic growth in the core water business and the addition of Peoples Gas driving a strong quarter, and management affirming its 2020 EPS guidance of $1.53-$1.58 (MOAP-basis). Excluding $150 million from Peoples, revenue rose 7.3% year/year in the core water business. Management says that higher residential demand due to COVID-19 quarantining more than offset the negative impact of the recession on commercial and industrial demand in the quarter.

An active rate pipeline is a usually a good thing for a regulated utility, but in the current environment, where rate increases are even more politically fraught than normal due to the impact of the COVID-19 recession on households, it pays to be off the radar. With just $5.2 million pending vs. annual revenue ~$1.5 billion, Essential's current rate pipeline is light. This is more a matter of being lucky than good (both Peoples and Aqua Pennsylvania recently wrapped up major rate cases), but either way it positions the company well to ride out the recession avoiding what could be meaningful regulatory lag.

Essential's $276 million DELCORA acquisition has seen unexpected delays due to a local legal challenge, but we believe the deal will close in 2020, creating a notable growth catalyst (see our June 18 note for details). Meanwhile, the municipal deal pipeline continues to expand, with Pennsylvania leading the way. In June, the city council in Norristown (pop. 35,000) approved the sale of the WW system to Aqua for $82 million. In addition to its size, Norristown is strategic because, with DELCORA, it would create a large PA WW ratepayer base, enabling future bolt-ons. Also, as the county seat in populous Montgomery County, Norristown is an anchor for peripheral deals.

After a brief lull at the onset of the COVID-19 pandemic, Essential is fully back up and running on its capital investment program, with the current 2020 capex target at $950 million (Aqua + Peoples). Early on in the pandemic, there were fears that rate base growth could slow (sapping future earnings growth), but this has not transpired.

Essential's solid 2Q, guidance/growth target affirmation, active M&A pipeline, and continued execution on its capital investment program amid the huge COVID-19 economic shock epitomize the resilience of the regulated utility business model. We reiterate our Outperform rating for Essential, which we see as a best-of-breed player in the regulated utility space with notable near-term growth catalysts.

Our price target of $50 reflects a forward P/E multiple of 30.1 times, ~in-line with the current peer group average of 29.5 times.

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Ratings Distribution (6/30/20):

Coverage Universe (a)	% of Universe
Outperform (Buy)	22%
Neutral (Hold)	40%
Underperform (Sell)	0%
Not Rated	38%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	24%
Neutral (Hold)	6%
Underperform (Sell)	0%
Not Rated	21%

(a) Related to services provided within the past 12 months.

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Aqua America, Inc. (WTR)

First Look at Q2 Results

Reiterate Outperform rating after Q2 earnings release. WTR reported results which were in line with consensus estimates, and the company reaffirmed adj. EPS guidance of $1.45 to $1.50 (excluding impacts of Peoples acquisition). Importantly, Peoples appears on track to close this fall (settlement filed in July), which we believe is the most important driver of the stock. Additionally, WTR has received $57.5M in annualized revenue increases YTD ($47M in Pennsylvania). We will look for additional information on the conference call.

- **Q2 results were in line with consensus EPS estimates due to rate increases and new customers from acquisitions and organic growth.** Q2 revenue was ~$218.9M vs. our/consensus estimates of $225M/$220M, as additional revenue from infrastructure surcharges contributed to ~3.3% growth y/y. Non-GAAP net income (excluding impacts of Peoples transaction-related expenses) was $66.8M vs. $70M/$66M, and EPS was $0.37 vs. $0.40/$0.37, respectively, due to rate increases and regulated growth.
- **WTR reaffirmed 2019 guidance.** WTR continues to expect $1.45 to $1.50 in EPS in 2019 (excluding impacts of Peoples transaction), total customer growth of ~2%-3%, and ~$550M in infrastructure investments.
- **Peoples appears on track to close in the fall.** Kentucky and West Virginia approved the Peoples acquisition in March and April, respectively, and WTR filed a settlement agreement in Pennsylvania which all but two intervenors chose not to oppose. The commission is expected to issue an order this fall.
- **Acquisition activity should continue to drive customer growth in the water business.** WTR has signed purchase agreements which are expected to add ~22.6k customer connections over the next two years (~$100M in rate base, on aggregate). Additionally, the company has a pipeline of ~400k water and wastewater customer connections it is actively pursuing across four states, which should help drive growth over time.
- **Rate increases and surcharges continue to contribute to revenue growth.** WTR has received $57.5M in annualized revenue increases thus far in 2019 due to favorable decisions in rate cases and infrastructure charges in five states, including ~$47M in Aqua Pennsylvania. Additionally, a decision on a total of ~$2.3M in annualized revenue increase is pending in Ohio, although the timing of potential regulatory approval remains unclear.
- **WTR's Q2 earnings call will be held today at 10:00 a.m. CT.** The call can be accessed at www.ir.aquaamerica.com.

RESEARCH UPDATE

1-Year Price Chart

Stock Data

Rating:	Outperform
Suitability:	Lower Risk
Price Target:	$44
Price (8/6/19):	$41.15
Market Cap (mil):	$7,341
Shares Out (mil):	178.4
Average Daily Vol (mil):	1.01
Dividend Yield:	2.1%

Estimates

FY Dec	2018A	2019E	2020E
Q1	0.29 A	0.28 A	
Q2	0.37 A	0.37 A	
Q3	0.44 A	0.47 E	
Q4	0.31 A	0.33 E	
Fiscal EPS	**1.41 A**	**1.48 E**	**1.57 E**
Fiscal P/E	29.2x	27.8x	26.2x

Chart/Table Sources: FactSet and Baird Data. Price chart reflects most recent closing price.

Please refer to Appendix - Important Disclosures and Analyst Certification

Aqua America is a holding company for numerous regulated water/waste water utilities serving almost 3.0 million people in the eastern half of the U.S.

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Investment Thesis

US water infrastructure needs should drive long-term earnings growth. The water infrastructure in the United States is in significant need of upgrade and expansion. We believe a significant long-term earnings growth driver for WTR comes from substantial capital investment opportunities, which contribute to rate base growth, and in turn, drives earnings.

Peoples acquisition, a natural gas utility, should add another platform for organic growth. The combined entity is expected to have ~$10.8B in assets and a rate base of >$7.2B, 70% in water and wastewater and 30% in natural gas. We estimate WTR paid ~14.8x EV/EBITDA (based on an enterprise value of $4.275B and 2019E EBITDA of $289M) for the assets. The transaction is subject to regulatory approvals, including approval by public utility commissions in Pennsylvania, Kentucky, and West Virginia, and is expected to close in mid-2019.

Planned capital investment should expand rate base and generate growth for the company in the long run. We expect Aqua America's long-term EPS growth to be fueled in part by the company's ~$500 million annual capex investment. $1.4B is expected to be invested into system upgrades (main, pipes, hydrants, etc.) over the next three years, which provides direct value to customers. Discretionary system investments are typically targeted for states with enhanced recovery mechanisms which help stabilize margin and earnings consistencies despite accelerated investment.

The majority of WTR's regulatory operations are located in states that maintain enhanced regulatory recovery mechanisms. The majority of WTR's current operating system employs infrastructure mechanisms, which allow a return on investment outside of a full rate case, substantially reducing regulatory lag time and minimizing rate case activity. These regulatory mechanisms include infrastructure investment riders, statewide rates and incentive mechanisms for acquisitions of troubled water systems. We believe such mechanisms provide a constructive regulatory environment in which to make capital investments, enabling improved and more consistent earned returns, which should lead to a premium peer valuation.

Continued municipal water acquisitions should help customer growth. The company targets 2-3% customer growth in 2019 driven by acquisitions of municipal utilities. Aqua has successfully acquired numerous water and waste water systems in the past decade to supplement its internal growth. Acquisitions also provide significant follow-on investment opportunities as WTR improves the quality of an acquired water system. The company is expected to be a key player in consolidating some of the 53,000 private water systems in the U.S., and rehabilitating those systems to improve water quality and drive investment growth.

Raising price target to $44. Our price target is based on a ~28x P/E multiple on our 2020 EPS estimate, which is in line with comps which are currently trading at a ~24x-31x multiple. We believe this is justified as WTR integrates the Peoples acquisition.

Risks & Caveats

Our suitability rating on Aqua America is Lower Risk. Key risks include the following.

Regulation. Regulated operations are subject to local, state and federal regulations. Changes in the regulatory environment can affect WTR's near-term and long-term performance.

Weather. WTR's businesses are sensitive to fluctuations in the weather. Particularly wet or dry weather can impact near-term financial results.

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Product quality. Unique among its sister regulated utility sectors, water utilities provide a product that is ingested. Despite robust mandated service quality standards that lower risk, a quality failure could materially impact the earnings and stock of WTR.

Company Description

Aqua America is a holding company for regulated utilities providing water and waste water services to nearly 3 million people located in the eastern half of the U.S. Over 50% of operating revenues and net income are derived from Pennsylvania.

Appendix - Important Disclosures and Analyst Certification

Approved on 06 August 2019 20:17EDT/ Published on 07 August 2019 01:02EDT.

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Aqua America, Inc. (WTR)

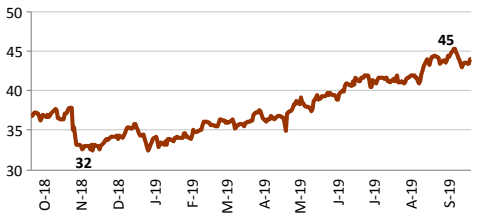
Announces Major Municipal Acquisition

Reiterate Outperform rating following acquisition announcement. WTR announced an agreement to acquire DELCORA's wastewater assets for $276.5M — the largest municipal acquisition in company and Pennsylvania history. With a prior estimated depreciated rate base of ~$240M, the acquired assets should drive significant rate base growth (~5%+ initially) with an opportunity for ~$1.2B of CapEx over the next 20 years. Financing will likely be the next questions for investors and we think WTR could look to issue an ATM to fund the deal. Remain buyers at current levels.

- **Last night, WTR announced an agreement to acquire DELCORA's wastewater assets for $276.5M, which will be the largest municipal acquisition in PA history.** Delaware Country Regional Water Quality Control Authority (DELCORA) serves ~500k people (estimated ~165k retail customers) in Southeast Pennsylvania; the acquisition is the largest ever municipal acquisition for WTR and the largest water/wastewater deal in Pennsylvania history. WTR previously announced it signed a letter of intent committing to exclusive discussions with DELCORA (see: Q2 Conference Call Highlights). The transaction is subject to approval by the Pennsylvania PUC.
- **Transaction significantly expands WTR's wastewater customer base; DELCORA assets to be aggregated into wastewater business.** For context, WTR serves ~3M people across its asset base— the DELCORA assets alone serve ~500k customers. The company currently has ~100k wastewater customers, so the addition of 165k new retail customers from acquired assets is significant. As part of the acquisition, Aqua will hire all 136 DELCORA employees and will aggregate all wastewater customers into what is effectively the company's new wastewater division.
- **DELCORA depreciated rate base previously forecast at ~$240M; should drive significant (~5%+) growth with an opportunity for further investment over time.** The depreciated rate base for the DELCORA assets was previously estimated at ~$240M and should immediately drive ~5% rate base growth (over YE:19 forecast of ~$5B in rate base for WTR's water assets). Additionally, WTR indicated CapEx need for the acquired assets is forecast at $1.2B through 2041, which should drive further rate base growth over time.
- **Financing likely next question for investors; we think it is possible WTR will look to issue an ATM to fund deal.** Particularly following the Peoples acquisition, we think investors will now focus on financing strategies for the large deal. Management previously indicated it could look to put out an at-the-market program to fund a municipal acquisition of this size, though we will look for more information on the Q3 conference call.

RESEARCH UPDATE

1-Year Price Chart



Stock Data

Rating:	Outperform
Suitability:	Lower Risk
Price Target:	$44
Price (9/17/19):	$43.90
Market Cap (mil):	$9,649
Shares Out (mil):	219.8
Average Daily Vol (mil):	1.03
Dividend Yield:	2.0%

Estimates

FY Dec	2018A	2019E	2020E
Q1	0.29 A	0.28 A	
Q2	0.37 A	0.37 A	
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Fiscal EPS	**1.41 A**	**1.48 E**	**1.57 E**
Fiscal P/E	31.1x	29.7x	28.0x

Chart/Table Sources: FactSet and Baird Data. Price chart reflects most recent closing price.

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Investment Thesis

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Price target $44. Our price target is based on a ~28x P/E multiple on our 2020 EPS estimate, which is in line with comps which are currently trading at a ~24x-31x multiple. We believe this is justified as WTR integrates the Peoples acquisition.

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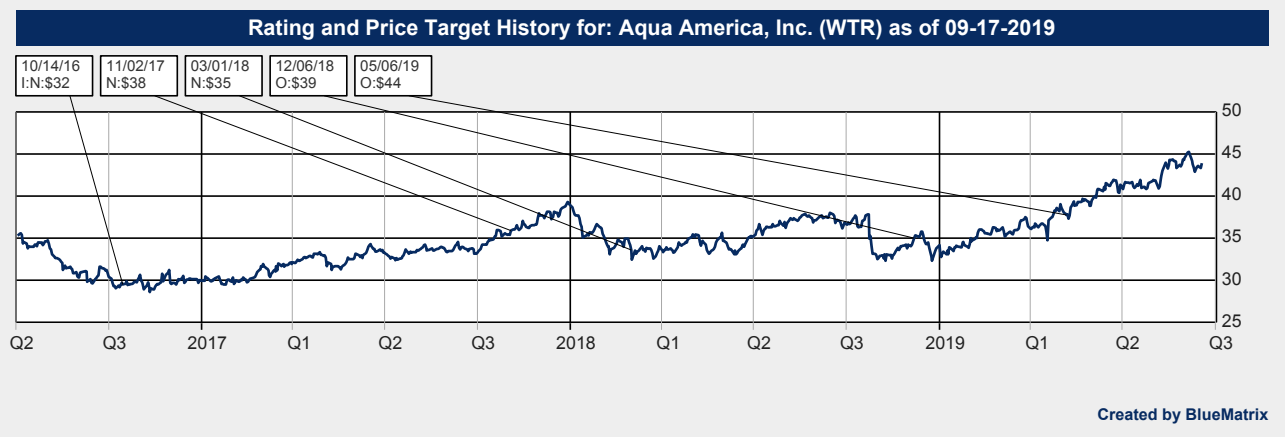
Approved on 18 September 2019 08:43EDT/ Published on 18 September 2019 08:48EDT.



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Aqua America, Inc. (WTR)

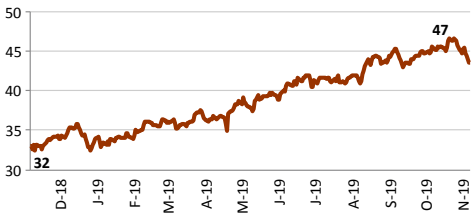
First Look at Q3 Results

Reiterate Outperform rating after Q3 earnings release. WTR reported results which were in line with consensus estimates, and the company reaffirmed adj. EPS guidance of $1.45 to $1.50 (excluding impact of Peoples acquisition). Importantly, the Peoples acquisition is now expected to close in late 2019 or early 2020 (vs. prior expectation of fall 2019), though WTR appears to be progressing through regulatory proceedings; we believe this is the most important driver of the stock. Additionally, WTR has received $59.8M in annualized revenue increases YTD.

- **Q3 results were in line with consensus EPS estimates due to rate increases and new customers from acquisitions and organic growth.** Q3 revenue was ~$243.6M vs. our/consensus estimates of $241M/$250M, as additional revenue from infrastructure surcharges contributed to ~7.7% growth y/y. Non-GAAP net income (excluding impacts of Peoples transaction-related expenses) was $85.6M vs. $86M/$88M, and EPS was $0.48 vs. $0.48/$0.44, respectively, due to rate increases and regulated growth.
- **WTR reaffirmed 2019 guidance, excluding impact of Peoples acquisition.** WTR continues to expect $1.45 to $1.50 in EPS in 2019 (excluding impacts of Peoples transaction), total customer growth of ~2%-3%, and ~$550M in infrastructure investments.
- **Peoples acquisition now expected to close in late 2019 or early 2020 (vs. prior expectation of fall 2019), though WTR appears to be progressing through regulatory proceedings.** Kentucky and West Virginia approved the Peoples acquisition in March and April, respectively. In Pennsylvania, the Administrative Law Judge issued a recommended decision determining WTR is fit to control Peoples and that the acquisition would be positive for the public; the Pennsylvania Utility Commission will now review the recommendation and issue a final order. WTR now expects the acquisition to close in late 2019 or early 2020.
- **Acquisition activity should continue to drive customer growth in the water business; WTR announced an agreement to acquire DELCORA's wastewater assets for ~$276.5M in Q3.** WTR has signed purchase agreements which are expected to add ~22.6k customer connections by early 2020 (~$110M in rate base, on aggregate). Additionally, WTR announced an agreement to acquire DELCORA's wastewater assets; the largest municipal acquisition in company and Pennsylvania history (see: Municipal Acquisition); we will look for more information on the conference call.
- **Rate increases and surcharges continue to contribute to revenue growth.** WTR has received $59.8M in annualized revenue increases thus far in 2019 due to favorable decisions in rate cases and infrastructure charges in five states.
- **WTR's Q3 earnings call will be held today at 10:00 a.m. CT.** The call can be accessed at www.ir.aquaamerica.com.

RESEARCH UPDATE

1-Year Price Chart



Stock Data

Rating:	Outperform
Suitability:	Lower Risk
Price Target:	$44
Price (11/4/19):	$43.56
Market Cap (mil):	$9,574
Shares Out (mil):	219.8
Average Daily Vol (mil):	1.15
Dividend Yield:	2.2%

Estimates

FY Dec	2018A	2019E	2020E
Q1	0.29 A	0.28 A	
Q2	0.37 A	0.37 A	
Q3	0.44 A	0.48 A	
Q4	0.31 A	0.35 E	
Fiscal EPS	**1.41 A**	**1.48 E**	**1.57 E**
Fiscal P/E	30.9x	29.4x	27.7x

Chart/Table Sources: FactSet and Baird Data. Price chart reflects most recent closing price.

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Aqua America is a holding company for numerous regulated water/waste water utilities serving almost 3.0 million people in the eastern half of the U.S.

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Investment Thesis

US water infrastructure needs should drive long-term earnings growth. The water infrastructure in the United States is in significant need of upgrade and expansion. We believe a significant long-term earnings growth driver for WTR comes from substantial capital investment opportunities, which contribute to rate base growth, and in turn, drives earnings.

Peoples acquisition, a natural gas utility, should add another platform for organic growth. The combined entity is expected to have ~$10.8B in assets and a rate base of >$7.2B, 70% in water and wastewater and 30% in natural gas. We estimate WTR paid ~14.8x EV/EBITDA (based on an enterprise value of $4.275B and 2019E EBITDA of $289M) for the assets. The transaction is subject to regulatory approvals, including approval by public utility commissions in Pennsylvania, Kentucky, and West Virginia, and is expected to close in late-2019.

Planned capital investment should expand rate base and generate growth for the company in the long run. We expect Aqua America's long-term EPS growth to be fueled in part by the company's ~$500 million annual capex investment. $1.4B is expected to be invested into system upgrades (main, pipes, hydrants, etc.) over the next three years, which provides direct value to customers. Discretionary system investments are typically targeted for states with enhanced recovery mechanisms which help stabilize margin and earnings consistencies despite accelerated investment.

The majority of WTR's regulatory operations are located in states that maintain enhanced regulatory recovery mechanisms. The majority of WTR's current operating system employs infrastructure mechanisms, which allow a return on investment outside of a full rate case, substantially reducing regulatory lag time and minimizing rate case activity. These regulatory mechanisms include infrastructure investment riders, statewide rates and incentive mechanisms for acquisitions of troubled water systems. We believe such mechanisms provide a constructive regulatory environment in which to make capital investments, enabling improved and more consistent earned returns, which should lead to a premium peer valuation.

Continued municipal water acquisitions should help customer growth. The company targets 2-3% customer growth in 2019 driven by acquisitions of municipal utilities. Aqua has successfully acquired numerous water and waste water systems in the past decade to supplement its internal growth. Acquisitions also provide significant follow-on investment opportunities as WTR improves the quality of an acquired water system. The company is expected to be a key player in consolidating some of the 53,000 private water systems in the U.S., and rehabilitating those systems to improve water quality and drive investment growth.

$44 price target. Our price target is based on a ~28x P/E multiple on our 2020 EPS estimate, which is in line with comps which are currently trading at a ~24x-31x multiple. We believe this is justified as WTR integrates the Peoples acquisition.

Risks & Caveats

Our suitability rating on Aqua America is Lower Risk. Key risks include the following.

Regulation. Regulated operations are subject to local, state and federal regulations. Changes in the regulatory environment can affect WTR's near-term and long-term performance.

Weather. WTR's businesses are sensitive to fluctuations in the weather. Particularly wet or dry weather can impact near-term financial results.

Acquisition risk. WTR may have the opportunity to purchase assets or companies in the near future. Acquisitions carry risks related to personnel, expected-versus-actual growth and a myriad of unforeseen hurdles, all of which can negatively affect earnings.

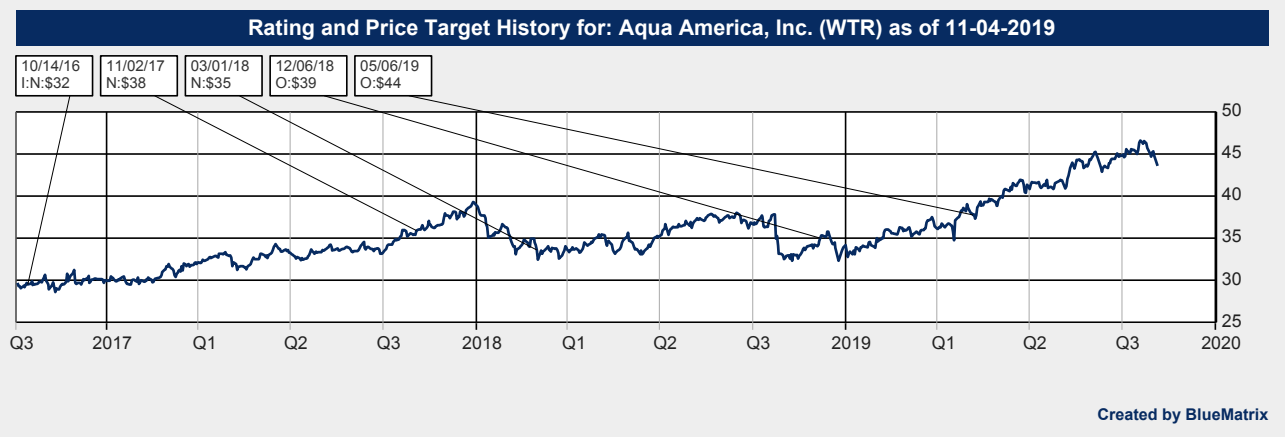
Product quality. Unique among its sister regulated utility sectors, water utilities provide a product that is ingested. Despite robust mandated service quality standards that lower risk, a quality failure could materially impact the earnings and stock of WTR.

Company Description

Aqua America is a holding company for regulated utilities providing water and waste water services to nearly 3 million people located in the eastern half of the U.S. Over 50% of operating revenues and net income are derived from Pennsylvania.

Appendix - Important Disclosures and Analyst Certification

Approved on 04 November 2019 21:49EST/ Published on 05 November 2019 01:05EST.



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Essential Utilities Inc., (WTRG)

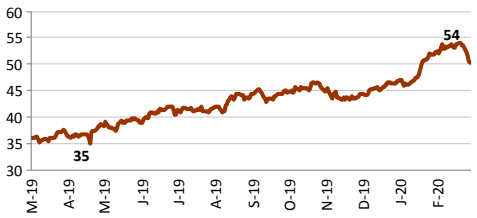
Brief Thoughts After Investor Day

Reiterate Outperform rating after investor day. WTRG issued 2020 and three-year EPS growth guidance which was largely in line with expectations and should help calibrate models following the close of the Peoples acquisition (expected mid-March). Importantly, we believe long-term growth drivers are on track: the accelerated pipeline replacement program and long-term water infrastructure need provides CapEx visibility and WTRG continues to execute on its municipal acquisition strategy. We think Essential Utilities is well-positioned for current market volatility, and remain buyers at current levels.

- **WTRG issued 2020 and three-year EPS growth guidance which was largely in line with expectations; EPS growth should align with rate base growth over the long run.** For 2020, WTRG guided to ~$1.53 - $1.58 of adj. EPS (largely in line with consensus of $1.58) and $1.05 - $1.10 of GAAP EPS (assuming 9.5 months of Peoples contribution and transaction expenses). EPS is expected to grow at a 5%-7% CAGR through 2022E, which compares favorably with water utility peers, and overtime management indicated EPS growth should mirror rate base growth (6%-7% growth for water, excluding acquisitions, 8%-10% for Gas).
- **Pipeline replacement at Peoples, along with substantial need for investment in water infrastructure, provides significant visibility on forward CapEx.** WTRG guided to ~$400M of annual CapEx for Peoples alone, as the company operates under an accelerated pipe replacement program; at ~189 miles replaced/year, the business has visibility on 15+ years of increased capital spending (recovered through DSIC). Separately, ongoing CapEx in the water business (~$550M expected in 2020) should drive rate base and earnings growth.
- **WTRG's municipal acquisition strategy is on track, and could help accelerate growth (particularly in the water business).** Since 2015, WTRG has added ~$237M of rate base through 57 acquisitions, and has signed municipal agreements (pending close) for ~$327M of aggregate purchase price, most significantly DELCORA (198k total customers, alone). Moving forward, the company has identified acquisition opportunities totaling ~320k customer additions (majority wastewater), which could contribute to rate base growth over time. As a reminder, every ~$100M of acquired rate base amounts to ~$5M of incremental annual earnings potential.
- **We think WTRG, and the other water utilities under our coverage, are well-positioned in the current macro environment and could be a safe haven during market volatility.** All four utilities under our coverage have significant growth visibility and little to no exposure to trade or the global economy, which we think is a key differentiating factor. Favorable regulatory dynamics, M&A activity and accelerating capital investment should continue to drive EPS growth regardless of broader macro uncertainty. We believe the space is well positioned to outperform the market if volatility and/or macro headwinds persist.

RAISING PRICE TARGET

1-Year Price Chart



Stock Data

Rating:	Outperform
Suitability:	Lower Risk
Price Target/Previous:	▲$50/$44
Price (2/27/20):	$46.34
Market Cap (mil):	$10,186
Shares Out (mil):	219.8
Average Daily Vol (mil):	1.36
Dividend Yield:	2.0%

Estimates

FY Dec	2019A	2020E	2021E
Q1	0.28 A	0.56 E	
Q2	0.37 A	0.19 E	
Q3	0.48 A	0.26 E	
Q4	0.34 A	0.53 E	
Fiscal EPS	**1.47 A**	**1.55 E**	**1.64 E**
Previous Est	1.48 A	1.57 E	
Fiscal P/E	31.5x	29.9x	28.3x

Chart/Table Sources: FactSet and Baird Data. Price chart reflects most recent closing price.

Please refer to Appendix - Important Disclosures and Analyst Certification

Essential Utilities is a holding company for numerous regulated water/waste water utilities serving almost 3.0 million people in the eastern half of the U.S.

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Investment Thesis

US water infrastructure needs should drive long-term earnings growth. The water infrastructure in the United States is in significant need of upgrade and expansion. We believe a significant long-term earnings growth driver for WTRG comes from substantial capital investment opportunities, which contribute to rate base growth, and in turn, drives earnings.

Peoples acquisition, a natural gas utility, should add another platform for organic growth. The combined entity is expected to have ~$10.8B in assets and a rate base of >$7.2B, 70% in water and wastewater and 30% in natural gas. We estimate WTR paid ~14.8x EV/EBITDA (based on an enterprise value of $4.275B and 2019E EBITDA of $289M) for the assets. The transaction is expected to close in mid-March.

Planned capital investment should expand rate base and generate growth for the company in the long run. We expect WTRG's long-term EPS growth to be fueled in part by the company's ~ $950M annual capex investment. Investments are typically targeted for states with enhanced recovery mechanisms which help stabilize margin and earnings consistencies despite accelerated investment.

The majority of WTRG's regulatory operations are located in states that maintain enhanced regulatory recovery mechanisms. The majority of WTRG's current operating system employs infrastructure mechanisms, which allow a return on investment outside of a full rate case, substantially reducing regulatory lag time and minimizing rate case activity. These regulatory mechanisms include infrastructure investment riders, statewide rates and incentive mechanisms for acquisitions of troubled water systems. We believe such mechanisms provide a constructive regulatory environment in which to make capital investments, enabling improved and more consistent earned returns, which should lead to a premium peer valuation.

Continued municipal water acquisitions should help customer growth. The company targets 2-3% customer growth in 2020 driven by acquisitions of municipal utilities. Aqua has successfully acquired numerous water and waste water systems in the past decade to supplement its internal growth. Acquisitions also provide significant follow-on investment opportunities as WTR improves the quality of an acquired water system. The company is expected to be a key player in consolidating some of the 53,000 private water systems in the U.S., and rehabilitating those systems to improve water quality and drive investment growth.

Raising price target to $50. Our price target is based on a ~29x P/E multiple on our 2022 EPS estimate, which is in line with comps which are currently trading at a ~24x-31x multiple. We believe this is justified as WTR integrates the Peoples acquisition.

Risks & Caveats

Our suitability rating on Essential Utilities is Lower Risk. Key risks include the following.

Regulation. Regulated operations are subject to local, state and federal regulations. Changes in the regulatory environment can affect WTRG's near-term and long-term performance.

Weather. WTRG's businesses are sensitive to fluctuations in the weather. Particularly wet or dry weather can impact near-term financial results.

Acquisition risk. WTRG may have the opportunity to purchase assets or companies in the near future. Acquisitions carry risks related to personnel, expected-versus-actual growth and a myriad of unforeseen hurdles, all of which can negatively affect earnings.

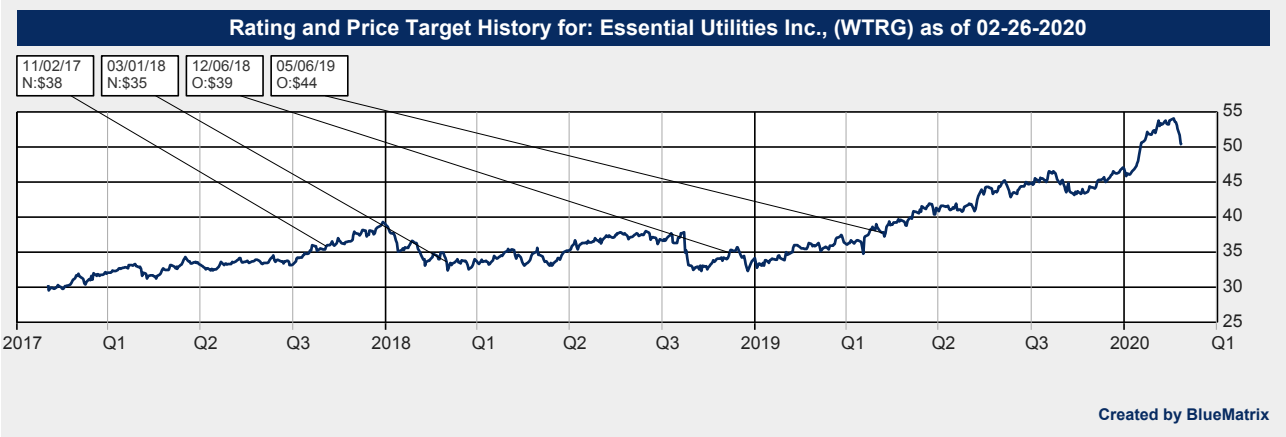
Product quality. Unique among its sister regulated utility sectors, water utilities provide a product that is ingested. Despite robust mandated service quality standards that lower risk, a quality failure could materially impact the earnings and stock of WTRG.

Company Description

Essential Utilities is a holding company for regulated utilities providing water and waste water services to nearly 3 million people located in the eastern half of the U.S. Over 50% of operating revenues and net income are derived from Pennsylvania.

Appendix - Important Disclosures and Analyst Certification

Approved on 27 February 2020 17:35EST/ Published on 28 February 2020 01:05EST.



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Essential Utilities Inc., (WTRG)

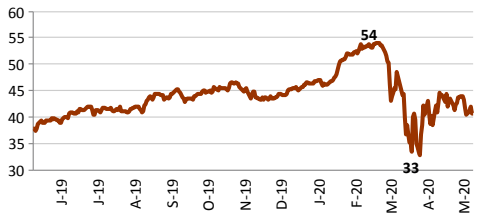
Solid First Quarter with Peoples, M&A Focus Now on DELCORA

Reiterate Outperform rating after Q1 earnings release. WTRG reported results which were slightly below our estimates, though the company reaffirmed 2020 adj. EPS guidance of $1.53 to $1.58 (excluding impact of Peoples acquisition). Following the close of Peoples on March 16, the M&A focus shifts to DELCORA wastewater assets, which is the largest municipal acquisition in company and Pennsylvania history. We will look for more information on the Q1 conference call, which will be held today at 10 a.m. CT.

- **Q1 results were slightly below our/consensus EPS estimates in the first quarter of Peoples contribution.** Q1 revenue was ~$255.6M vs. our/consensus estimates of $241M/$250M, driven by a $38.5M contribution from Peoples (from March 16 close to quarter end) and rate increases in the regulated water segment. Non-GAAP EPS (excluding contribution of Peoples and transaction-related expenses) was $0.60 vs. $0.65/$0.65, respectively, due to rate increases and regulated growth. On a GAAP basis, EPS of $0.20 exceeded our estimate of $0.08 on a larger Peoples contribution.
- **Importantly, WTRG reaffirmed 2020 guidance and continues to monitor potential impacts of COVID-19.** WTRG continues to expect $1.53 to $1.58 in adj. EPS in 2019 (excluding impacts of Peoples transaction, ~$1.05 - $1.10 on GAAP basis), total water customer growth of ~2%-3%, and ~$950M in infrastructure investments (~$550M in regulated water, ~$400M in natural gas).
- **Acquisition activity should continue to drive customer growth in the water business and WTRG filed the DECLORA wastewater acquisition request with the Pennsylvania PUC.** WTRG has signed purchase agreements which are expected to add ~205k customer connections by early 2020 (~$327M in rate base, on aggregate). These figures include the ~$276.5M (~198k retail customer) DELCORA acquisition, which is the largest municipal acquisition in company and Pennsylvania history.
- **Repair tax deduction for Peoples a ~$5.9M benefit in Q1; should enable further infrastructure investment and increase time between rate cases.** WTRG elected to employ the repair tax deduction for Peoples, which allows a tax deduction for qualifying infrastructure investments and reduces tax expense. The deduction allows WTRG to continue investing while increasing the time between rate cases and limiting the need for future rate increases.
- **Rate increases and surcharges continue to contribute to revenue growth.** The regulated water segment has received $5.2M in annualized revenue increases thus far in 2020 due to favorable decisions in rate cases and infrastructure charges in Illinois, North Carolina, Ohio, and Virginia. The gas segment has received ~$1M of annualized revenue increases.
- **WTRG's Q1 earnings call will be held today at 10:00 a.m. CT.** The call can be accessed at www.ir.aquaamerica.com.

ESTIMATE CHANGE

1-Year Price Chart



Stock Data

Rating:	Outperform
Suitability:	Lower Risk
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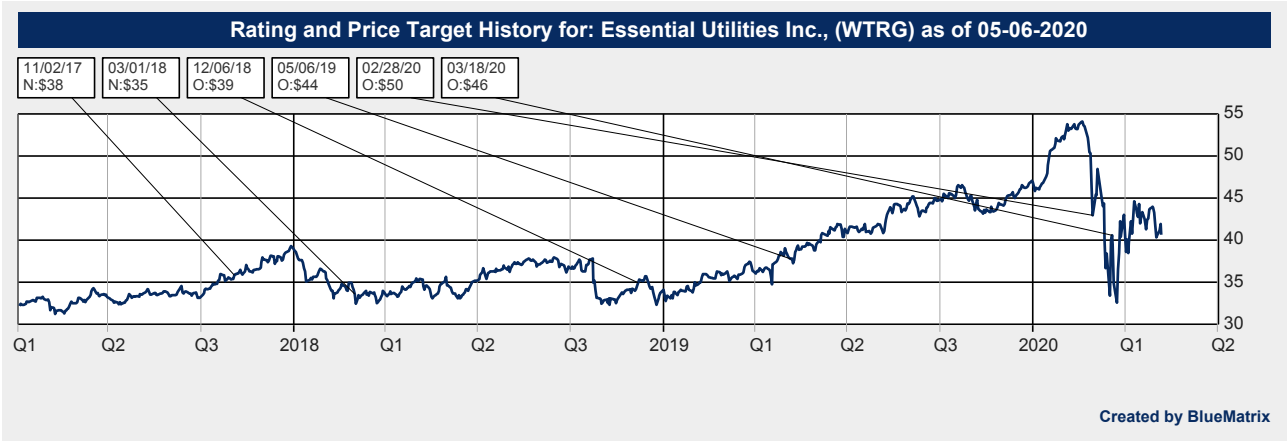
Approved on 06 May 2020 20:13EDT/ Published on 07 May 2020 01:05EDT.



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Essential Utilities Inc., (WTRG)

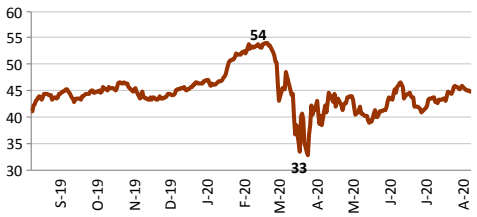
Strong Peoples Contribution Drives Earnings Beat

Reiterate Outperform rating after Q2 earnings release. WTRG reported results which exceeded our/consensus estimates driven by a better-than-expected contribution from Peoples. The company reaffirmed 2020 adj. EPS guidance, and continues to target ~$950M of regulated system investment for the year. We will look for an update on the DELCORA acquisition (transaction close previously expected early 2021), which should drive significant rate base and earnings growth, when completed. We will look for more information on the Q2 conference call, which will be held today at 10 a.m. CT.

- **Q2 results exceeded our/consensus EPS driven by a better-than-expected contribution from Peoples.** Q2 revenue was ~$384M vs. our/consensus estimates of $375M/$371M, driven by a $149.6M contribution from Peoples (we modeled $144M for the quarter) and rate increases & surcharges ($7.6M). EPS was $0.29 vs. $0.20/$0.23, largely related to lower-than-expected purchased gas costs ($43M in Q2, vs. our $60M estimate). We will look for more information on the Q2 earnings call.
- **Importantly, WTRG reaffirmed 2020 guidance; continuing to monitor COVID impacts, though volumes have been fairly resilient thus far.** WTRG continues to expect $1.53 to $1.58 in adj. EPS in 2020, ~$950M of regulated system investments ($550M in water, ~$400M in natural gas), and annual rate base growth of 6%-7% for water and 8%-10% for gas. Importantly, Q2 water sales increased 0.3% in Q2, as 10% growth in residential consumption (66% of quarterly consumption) more than offset the declines in commercial & industrial (-16% and -11%, respectively).
- **Substantial dividend increase (~7% annualized) highlights commitment to returning capital to shareholders and long-term value proposition.** WTRG recently increased its dividend ~7%; annualized dividend now amounts to a ~2.2% yield based on the August 5 closing price. WTRG has grown the dividend at a 7.2% CAGR since 2014, and we expect growth to continue, consistent with rate base and EPS growth.
- **Acquisition activity should continue to drive customer growth in the water business; will look for an update on DELCORA acquisition process (previously expected to close in early 2021).** WTRG has closed two acquisitions YTD (~$28.3M of cumulative rate base) and has signed purchase agreements totaling 203k customer connections (~$315M in rate base, on aggregate); we expect this will add ~$15M to annual earnings potential. These figures include the ~$276.5M (~198k retail customer) DELCORA acquisition, which is the largest municipal acquisition in company and Pennsylvania history; we will look for an update on potential transaction timing on the conference call.
- **WTRG's Q2 earnings call will be held today at 10:00 a.m. CT.** The call can be accessed at www.ir.aquaamerica.com.

ESTIMATE CHANGE

1-Year Price Chart



Stock Data

Rating:	Outperform
Suitability:	Lower Risk
Price Target:	$46
Price (8/5/20):	$44.69
Market Cap (mil):	$11,398
Shares Out (mil):	255.1
Average Daily Vol (mil):	1.14
Dividend Yield:	2.2%

Estimates

FY Dec	2019A	2020E	2021E
Q1	0.28 A	0.60 A	
Q2	0.37 A	0.29 A	
Q3	0.48 A	0.22 E	
Q4	0.34 A	0.43 E	
Fiscal EPS	**1.47 A**	**1.55 E**	**1.68 E**
Fiscal P/E	30.4x	28.8x	26.6x

Chart/Table Sources: FactSet and Baird Data. Price chart reflects most recent closing price.

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Essential Utilities is a regulated water, wastewater, and natural gas utility serving customers primarily in the eastern half of the U.S.

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Investment Thesis

US water infrastructure needs should drive long-term earnings growth. The water infrastructure in the United States is in significant need of upgrade and expansion. We believe a significant long-term earnings growth driver for WTRG comes from substantial capital investment opportunities, which contribute to rate base growth, and in turn, drives earnings.

Peoples acquisition, a natural gas utility, should add another platform for organic growth. The combined entity is expected to have ~$10.8B in assets and a rate base of >$7.2B, 70% in water and wastewater and 30% in natural gas. We estimate WTR paid ~14.8x EV/EBITDA (based on an enterprise value of $4.275B and 2019E EBITDA of $289M) for the assets. The transaction is expected to close in mid-March.

Planned capital investment should expand rate base and generate growth for the company in the long run. We expect WTRG's long-term EPS growth to be fueled in part by the company's ~ $950M annual capex investment. Investments are typically targeted for states with enhanced recovery mechanisms which help stabilize margin and earnings consistencies despite accelerated investment.

The majority of WTRG's regulatory operations are located in states that maintain enhanced regulatory recovery mechanisms. The majority of WTRG's current operating system employs infrastructure mechanisms, which allow a return on investment outside of a full rate case, substantially reducing regulatory lag time and minimizing rate case activity. These regulatory mechanisms include infrastructure investment riders, statewide rates and incentive mechanisms for acquisitions of troubled water systems. We believe such mechanisms provide a constructive regulatory environment in which to make capital investments, enabling improved and more consistent earned returns, which should lead to a premium peer valuation.

Continued municipal water acquisitions should help customer growth. The company targets 2-3% customer growth in 2020 driven by acquisitions of municipal utilities. Aqua has successfully acquired numerous water and waste water systems in the past decade to supplement its internal growth. Acquisitions also provide significant follow-on investment opportunities as WTR improves the quality of an acquired water system. The company is expected to be a key player in consolidating some of the 53,000 private water systems in the U.S., and rehabilitating those systems to improve water quality and drive investment growth.

$46 price target. Our price target is based on a ~26x P/E multiple on our 2022 EPS estimate, which is in line with comps which are currently trading at a ~24x-31x multiple. We believe this is justified as WTR integrates the Peoples acquisition.

Risks & Caveats

Our suitability rating on Essential Utilities is Lower Risk. Key risks include the following.

Regulation. Regulated operations are subject to local, state and federal regulations. Changes in the regulatory environment can affect WTRG's near-term and long-term performance.

Weather. WTRG's businesses are sensitive to fluctuations in the weather. Particularly wet or dry weather can impact near-term financial results.

Acquisition risk. WTRG may have the opportunity to purchase assets or companies in the near future. Acquisitions carry risks related to personnel, expected-versus-actual growth and a myriad of unforeseen hurdles, all of which can negatively affect earnings.

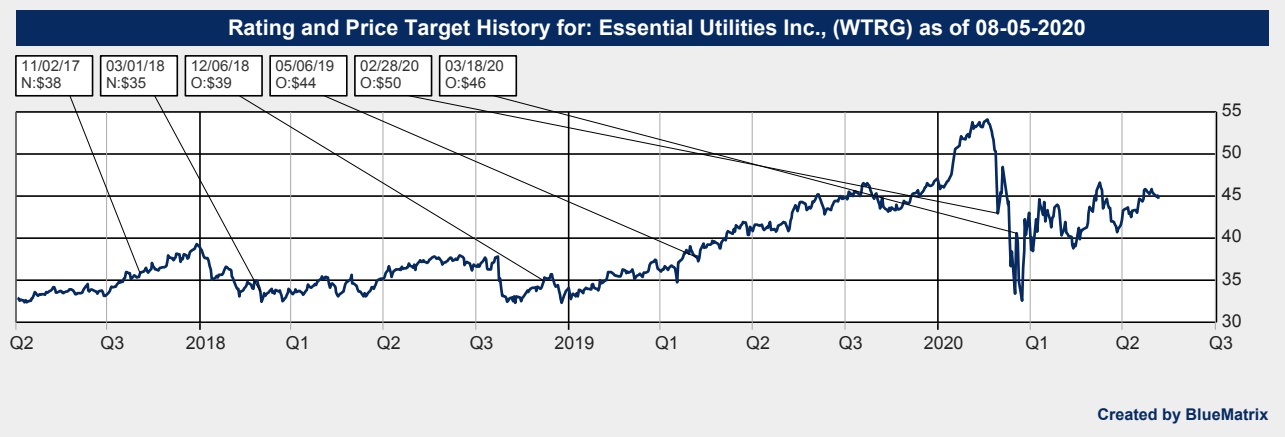
Product quality. Unique among its sister regulated utility sectors, water utilities provide a product that is ingested. Despite robust mandated service quality standards that lower risk, a quality failure could materially impact the earnings and stock of WTRG.

Company Description

Essential Utilities is a holding company for regulated utilities providing water and waste water services to nearly 3 million people located in the eastern half of the U.S. Over 50% of operating revenues and net income are derived from Pennsylvania.

Appendix - Important Disclosures and Analyst Certification

Approved on 05 August 2020 22:44EDT/ Published on 06 August 2020 01:05EDT.



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Risk Ratings: L - Lower Risk – Higher-quality companies for investors seeking capital appreciation or income with an emphasis on safety. Company characteristics may include: stable earnings, conservative balance sheets, and an established history of revenue and earnings. **A - Average Risk** – Growth situations for investors seeking capital appreciation with an emphasis on safety. Company characteristics may include: moderate volatility, modest balance-sheet leverage, and stable patterns of revenue and earnings. **H - Higher Risk** – Higher-growth situations appropriate for investors seeking capital appreciation with the acceptance of risk. Company characteristics may include: higher balance-sheet leverage, dynamic business environments, and higher levels of earnings and price volatility. **S - Speculative Risk** – High growth situations appropriate only for investors willing to accept a high degree of volatility and risk. Company characteristics may include: unpredictable earnings, small capitalization, aggressive growth strategies, rapidly changing market dynamics, high leverage, extreme price volatility and unknown competitive challenges.

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Aqua America

Overflowing Interest: Downgrading to Neutral

Rating Change: NEUTRAL | PO: 52.00 USD | Price: 50.57 USD

Transaction Approval, New Branding & Leadership

Following the PA PUC's approval of WTR's pending Peoples Gas transaction on Thursday, we are downgrading shares to Neutral. After a rather protracted process since announcing the acquisition in 2018, the commission finally voted 4-1 in favor of the deal, with Commissioner Place the lone commissioner opting against it. Following approval, the company put out a press release mid-afternoon on Thursday announcing their new name, ticker, and executive leadership team ahead of the transaction close. The name will become 'Essential Utilities' on February 3rd (the ticker is also set to transition to WTRG), with Chris Franklin remaining CEO & Chairman of the Pro Forma entity. Since our launch in July, shares are up 23%, outperforming the XLU by 1300bps. While the final commission approval helps to de-risk the earnings profile going forward, we see a more balanced setup into the upcoming Analyst Day (February 27th) when the company lays out their long term guidance (potentially *more smoothed*). We have confidence in the mgmt. team in place and note their ability to effectively deploy their currency for the deal. We further highlight the shares' ability to re-rate higher into the deal - despite the foray into gas - as helping to mitigate ESG concerns around gas utes more broadly. Further, gas is additive.

Updating our Valuation & Moving to the Sidelines

Our estimates remain unchanged following our broader 4Q water preview published last week. While we remain above the street, we see shares as less attractive given elevated expectations into the Analyst Day and caution the lack of clarity around the ability to smooth earnings with implementation of the repairs tax benefit. With our latest valuation, we mark to market our above street estimates for the latest water and gas peer multiples of 28.1x and 19.6x (vs. 26.2x and 19.0x respectively just last week). Even after applying higher premiums to both the water and gas segments – which we see as worthwhile given the purer composition (vs. closest peer AWK with meaningful non-reg) and clear muni-driven EPS growth opportunities - our PO only shifts to $52, implying just 5% TSR. With water multiples overall still quite elevated vs. peer utility asset classes & risk that mgmt. may seek to moderate near-term EPS in favor of a 'trajectory' we d/g.

Estimates (Dec)

(US$)	2017A	2018A	2019E	2020E	2021E
EPS	1.36	1.41	1.47	1.70	1.72
GAAP EPS	1.36	1.41	1.47	1.70	1.72
EPS Change (YoY)	3.0%	3.7%	4.3%	15.6%	1.2%
Consensus EPS (Bloomberg)			1.44	1.56	1.67
DPS	0.81	0.86	0.92	0.99	1.06

Valuation (Dec)

	2017A	2018A	2019E	2020E	2021E
P/E	37.2x	35.9x	34.4x	29.7x	29.4x
GAAP P/E	37.2x	35.9x	34.4x	29.7x	29.4x
Dividend Yield	1.6%	1.7%	1.8%	2.0%	2.1%
EV / EBITDA*	1.2x	9.1x	29.9x	18.7x	17.8x
Free Cash Flow Yield*	-0.9%	-1.2%	-1.4%	-1.2%	-0.9%

* For full definitions of IQmethod℠ measures, see page 8.

BofA Securities does and seeks to do business with issuers covered in its research reports. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of this report. Investors should consider this report as only a single factor in making their investment decision.
Refer to important disclosures on page 9 to 11. Analyst Certification on page 6. Price Objective Basis/Risk on page 6. 12085436

Timestamp: 21 January 2020 06:00AM EST

21 January 2020

Equity

Key Changes

(US$)	Previous	Current
Inv. Opinion	A-1-7	A-2-7
Inv. Rating	BUY	NEUTRAL
Price Obj.	47.00	52.00

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Stock Data

Price	50.57 USD
Price Objective	52.00 USD
Date Established	21-Jan-2020
Investment Opinion	A-2-7
52-Week Range	33.72 USD - 50.71 USD
Mrkt Val (mn) / Shares Out (mn)	10,915 USD / 215.8
Average Daily Value (mn)	57.60 USD
BofA Ticker / Exchange	WTR / NAS
Bloomberg / Reuters	WTR US / WTR.N
ROE (2019E)	8.4%
Net Dbt to Eqty (Dec-2018A)	127.1%

PUC: Public Utility Commission

TSR: Total Shareholder Return

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iQprofile℠ Aqua America

*iQ*method℠ – Bus Performance*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Return on Capital Employed	5.1%	3.9%	3.9%	5.1%	5.0%
Return on Equity	12.6%	9.7%	8.4%	8.3%	8.1%
Operating Margin	41.5%	38.7%	41.7%	68.9%	70.1%
Free Cash Flow	(97)	(127)	(154)	(135)	(95)

*iQ*method℠ – Quality of Earnings*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash Realization Ratio	1.6x	1.9x	1.7x	1.8x	1.9x
Asset Replacement Ratio	3.5x	3.4x	3.9x	2.6x	2.5x
Tax Rate	6.6%	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	108.3%	127.1%	95.9%	99.5%	102.6%
Interest Cover	3.9x	2.8x	3.4x	3.5x	3.3x

Income Statement Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Sales	805	835	902	949	966
% Change	0.6%	3.7%	8.0%	5.3%	1.7%
Gross Profit	810	838	905	1,572	1,638
% Change	-1.3%	3.5%	8.0%	73.7%	4.2%
EBITDA	14,226	1,941	590	942	990
% Change	-33.6%	-86.4%	-69.6%	59.7%	5.1%
Net Interest & Other Income	(88)	(99)	(115)	(193)	(210)
Net Income (Adjusted)	240	192	284	404	409
% Change	2.4%	-19.9%	48.1%	42.2%	1.2%

Free Cash Flow Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Net Income from Cont Operations (GAAP)	240	192	325	432	437
Depreciation & Amortization	137	147	163	330	356
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	14	(15)	0	0	0
Other Adjustments, Net	(9)	45	(3)	(32)	(3)
Capital Expenditure	(478)	(496)	(639)	(865)	(885)
Free Cash Flow	-97	-127	-154	-135	-95
% Change	NM	-31.5%	-21.4%	12.4%	29.6%

Balance Sheet Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash & Equivalents	4	4	3	5	5
Trade Receivables	99	101	109	190	198
Other Current Assets	28	42	44	56	57
Property, Plant & Equipment	5,400	5,930	9,132	9,667	10,196
Other Non-Current Assets	801	887	2,462	2,462	2,462
Total Assets	6,332	6,964	11,750	12,380	12,919
Short-Term Debt	117	160	287	310	332
Other Current Liabilities	167	239	245	307	313
Long-Term Debt	2,008	2,398	4,290	4,638	4,963
Other Non-Current Liabilities	2,083	2,158	2,158	2,158	2,158
Total Liabilities	4,375	4,955	6,979	7,412	7,765
Total Equity	1,958	2,009	4,771	4,968	5,154
Total Equity & Liabilities	6,332	6,964	11,750	12,380	12,919

* For full definitions of *iQmethod*℠ measures, see page 8.

Company Sector

Water Utilities

Company Description

Aqua America is a regulated water utility providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI. In Oct 2018, The company announced the acquisition of Peoples Gas in Oct 2018, which the PA PUC approved in January 2020. Peoples Gas is a gas utility providing distribution services to 740,000 customers in PA, WV, and KY.

Investment Rationale

We are Neutral rated on shares of WTR, seeing risk/reward as balanced at the current valuation. We have confidence in the mgmt. team in place and view the People's Gas deal constructively. The re- effective use of their currency can drive value, and the ability for shares to re-rate higher - despite the foray into gas - helps to mitigate ESG concerns around gas utilities more broadly.

Stock Data

Average Daily Volume	1,138,923

Quarterly Earnings Estimates

	2018	2019
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NA

Details of Pro Forma 'Essential Utilities' Revealed

Following approval from the Pennsylvania Public Utility Commission on Thursday for their pending acquisition of Peoples Gas, WTR put out a press release mid-afternoon announcing their new name, ticker and executive leadership team ahead of the close. The name will become "Essential Utilities" on Feb 3rd, with Chris Franklin remaining CEO and Chairman of the pro forma entity. The same day, the ticker is set to transition to WTRG. We include the full slate of leadership updates in the exhibit below. Mgmt. plans to host an Analyst Day in New York on February 27th with the release of full year results, which should provide an opportunity to interact and engage in Q&A with the newly introduced executive team.

Despite our more balanced view of shares, we have confidence in the mgmt. team in place and view the deal constructively; the re- effective use of their currency can drive value, and the ability for shares to re-rate higher - despite the foray into gas - helps to mitigate ESG concerns around gas utilities more broadly.

Table 1: WTR Leadership Team: Executives

'Essential Utilities' Executive Leadership Team	
Name	Title
Chris Franklin	Chairman, CEO
Richard Fox	EVP, COO
Christopher Luning	EVP, GC
Matthew Rhodes	EVP, Strategy and Corp Development
Dan Schuller	EVP, CFO
Ruth DeLost-Wylie	SVP, Business Transformation
Susan Haindl	SVP, Chief Administrative Officer
Christina Kelly	SVP, Chief HR Officer
Brian Dingerdissen	VP, Chief of Staff, IR & Communications
Kimberly Joyce	VP, Regulatory & Government Affairs

Source: BofA Global Research, company report

Table 2: WTR Leadership Team: Executives

'Essential Utilities' Operating Presidents	
Name	Title
Joseph Gregorini	President, Nat Gas Utilities
Colleen Arnold	President, Water & Wastewater Utilities

Source: BofA Global Research, company report

...but Repairs Tax Details Unaddressed

Despite the protracted timeline for the close of the transaction (we perceive around March 1st as a conservative expectation for final close), the company plans to elect to implement the repairs tax benefit in 2020. Under the strategy, earnings will see a large step up as the company expenses capital costs as opposed to depreciating them over a useful life for tax purposes. The magnitude of the initial increase will ultimately be determined by how much of the capital investment program qualifies for the treatment and whether the commission allows the company to use a catch up component for costs that are currently being depreciated. Our sense is that capital investments back to 2012 could potentially be privy to such treatment – albeit we perceive historical investment as likely more muted relative to future capital expenditures. With any approved catch up component, we also would expect the commission to be inclined to give at least part of the benefit back to customers.

While mgmt. has noted a desire to smooth out the impact from implementation as opposed to a large step up in '20 and minimal growth in future years, how they will approach this remains unclear. Bottom line, we see more execution risk to implementation given the elevated expectations implied by the current share price. Look for additional details at the upcoming Analyst Day on February 27th.

EPS Estimates

The exhibit below reflects our unchanged EPS estimates into the upcoming Analyst Day. We remain 3% above the street for '21 given what we perceive as strong earnings upside from the election of the Repairs Tax Benefit. That said, we perceive higher expectations from the buy side as largely priced in at the current valuation.

Table 1: EPS Estimates: still meaningfully above Street ests, but this moderates

EPS Estimates	2019E	2020E	2021E	2022E	2023E
PA	$1.05	$0.79	$0.77	$0.82	$0.86
OH	$0.09	$0.07	$0.07	$0.08	$0.08
IL	$0.10	$0.07	$0.08	$0.08	$0.09
TX	$0.08	$0.06	$0.06	$0.06	$0.06
NC	$0.05	$0.04	$0.04	$0.04	$0.05
Other States	$0.10	$0.08	$0.09	$0.09	$0.10
Water Utility	1.47	1.12	1.11	1.17	1.24
Peoples Gas		0.66	0.71	0.77	0.82
Parent & Other		*-0.08*	*-0.10*	*-0.12*	*-0.14*
EPS	1.47	1.70	1.72	1.82	1.92
YoY Growth		*16%*	*1%*	*6%*	*6%*
Guidance	1.45-1.50				
Shares O/S	*193*	*238*	*238*	*250*	*254*
Fully Diluted Shares O/S	*178*	*254*	*254*	*254*	*254*
Previous EPS		*$1.70*	*$1.72*	*$1.82*	
Consensus	1.44	1.56	1.67		

Source: BofA Global Research, Bloomberg

PO Shifts to $52: Downgrade to Neutral

The exhibit below reflects our latest SOTP. While our estimates remain unchanged, we mark to market for the latest utility peer multiples and update our premium/discount assumptions. Latest peer multiples shift to 28.1x and 19.6x for water and gas, respectively vs. 26.2x and 19.0x previously.

We now apply premiums to the water segment of 2x for PA (up from 1.5x previously), and add additional premiums of 2x, 3x, and 1x for OH, IL, and NC, respectively. We continue to highlight IL as a key state to watch for consolidation in the industry.

Following approval of the Peoples Gas transaction by the commission last week, we apply a 2x premium to the LDC peer group (compared to a -0.5x discount previously).

Despite the higher premiums ascribed in our valuation and our street-high estimates, our SOTP suggests limited upside after the latest run-up in share price. While our PO shifts to $52, we now see risk/reward as more fairly balanced at the current share price. Downgrade to Neutral.

We treat the blended entity with premium multiples still and see its fully regulated profile with sustained EPS growth as superior among water utility peers. We stress the ongoing municipal acquisition cycle appears to have accelerated of late (see our water preview) with datapoints suggesting this should indeed persist. We see the relative market cap size and breadth of state involvement as allowing larger market-cap companies to prove more nimble in pursuing municipal acquisitions.

Table 2: WTR SOTP

Water Utilities	2022 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*28.1x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		30.4x							
Water Utilities									
States	2022E EPS	ROE	embedded						
PA	$0.82	10.0%	2.0x	31.4x	32.4x	33.4x	$26	$27	$27
OH	$0.08	9.9%	2.0x	31.4x	32.4x	33.4x	$2	$3	$3
IL	$0.08	9.6%	3.0x	32.4x	33.4x	34.4x	$3	$3	$3
TX	$0.06	10.0%	0.0x	29.4x	30.4x	31.4x	$2	$2	$2
NC	$0.04	9.9%	1.0x	30.4x	31.4x	32.4x	$1	$1	$1
Other (including acquisitions)	$0.09	9.9%	0.0x	29.4x	30.4x	31.4x	$3	$3	$3
Water utilities total (ex-Peoples)	$1.17			*31.2x*	*32.2x*	*33.2x*	$37	$38	$39
Gas Utilities									
Peer Gas P/E		*19.6x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		20.7x							
	2022E EPS	ROE	embedded						
Peoples Gas	$0.77	13.5%	2.0x	21.7x	22.7x	23.7x	$17	$17	$18
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			-811	50%			($406)	($406)	($406)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($402)	($371)	($433)
50/50 Weighted Drag from HoldCo Drag							($808)	($777)	($839)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							$50.00	$52.00	$54.00
Current Price								$50.57	
Dividend Yield								2%	
Total Return								4.65%	

Source: BofA Global Research, Bloomberg

Price objective basis & risk

Aqua America (WTR)
Our price objective is $52 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 2.0x premium to Peoples Gas given the organic growth opportunities.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Risks to the upside include upward revisions to street estimates and further accretion from implementation of the Repairs Tax Benefit

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	AES	AES	AES US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Aqua America	WTR	WTR US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
RSTR				

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith
	Pattern Energy Group	PEGI	PEGI US	Julien Dumoulin-Smith

iQmethod℠ **Measures Definitions**

Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

iQ*method*℠is the set of BofA Global Research standard measures that serve to maintain global consistency under three broad headings: Business Performance, Quality of Earnings, and validations. The key features of iQmethod are: A consistently structured, detailed, and transparent methodology. Guidelines to maximize the effectiveness of the comparative valuation process, and to identify some common pitfalls.

iQ*database*® is our real-time global research database that is sourced directly from our equity analysts' earnings models and includes forecasted as well as historical data for income statements, balance sheets, and cash flow statements for companies covered by BofA Global Research.

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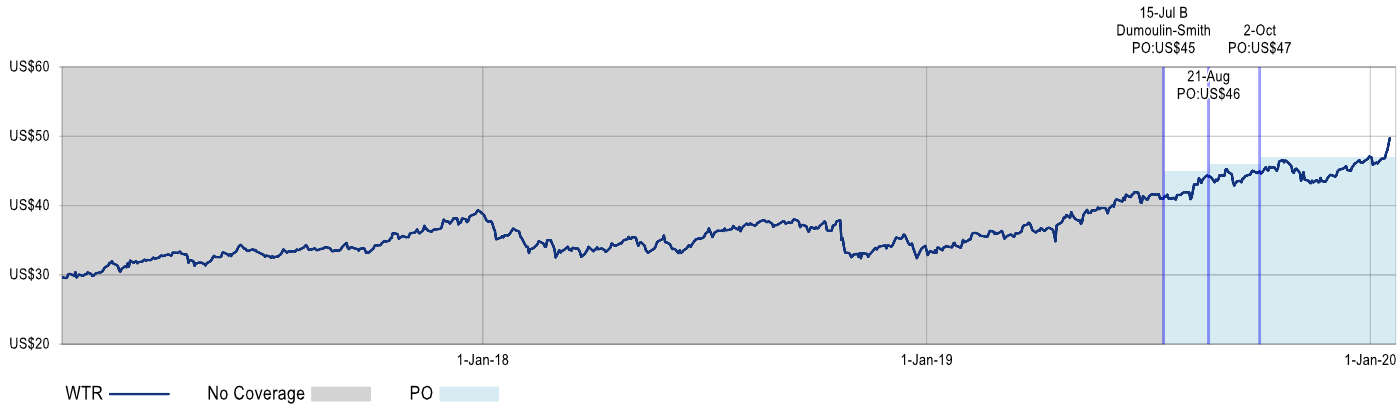
Disclosures

Important Disclosures

Aqua America (WTR) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Utilities Group (as of 31 Dec 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	63	44.06%	Buy	44	69.84%
Hold	43	30.07%	Hold	31	72.09%
Sell	37	25.87%	Sell	27	72.97%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1560	50.49%	Buy	991	63.53%
Hold	717	23.20%	Hold	461	64.30%
Sell	813	26.31%	Sell	415	51.05%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

FUNDAMENTAL EQUITY OPINION KEY: Opinions include a Volatility Risk Rating, an Investment Rating and an Income Rating. *VOLATILITY RISK RATINGS*, indicators of potential price fluctuation, are: A - Low, B - Medium and C - High. *INVESTMENT RATINGS* reflect the analyst's assessment of a stock's: (i) absolute total return potential and (ii) attractiveness for investment relative to other stocks within its *Coverage Cluster* (defined below). There are three investment ratings: 1 - Buy stocks are expected to have a total return of at least 10% and are the most attractive stocks in the coverage cluster; 2 - Neutral stocks are expected to remain flat or increase in value and are less attractive than Buy rated stocks and 3 - Underperform stocks are the least attractive stocks in a coverage cluster. Analysts assign investment ratings considering, among other things, the 0-12 month total return expectation for a stock and the firm's guidelines for ratings dispersions (shown in the table below). The current price objective for a stock should be referenced to better understand the total return expectation at any given time. The price objective reflects the analyst's view of the potential price appreciation (depreciation).

Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

***INCOME RATINGS*, indicators of potential cash dividends, are: 7 - same/higher (dividend considered to be secure), 8 - same/lower (dividend not considered to be secure) and 9 - pays no cash dividend.** *Coverage Cluster* is comprised of stocks covered by a single analyst or two or more analysts sharing a common industry, sector, region or other classification(s). A stock's coverage cluster is included in the most recent BofA Global Research report referencing the stock.

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North American Utilities & IPPs

1Q20 Regulated Utility Preview: Who is key in COVID resiliency?

Price Objective Change

20 April 2020

Equity
North America
Utilities & IPPs

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Prospects for 1Q20: COVID, oil prices and mild weather

We present our 1Q20 regulated preview including LNT, AEE, AEP, AWK, ED, DTE, DUK, EIX, ETR, WTRG, EVRG, ES, FE, PNW, PPL, WEC, and XEL. Overall, we see the sector splitting into stocks well-suited to weather the storm that started in 1Q – and those that are less equipped. Key factors that distinguish between these include: Having decoupling and/or bad debt trackers to balance out decreases in demand from COVID, oil price, and mild weather pressures (**ES**, **ED**, **WEC**); revenues with a heftier reliance on resi or fixed-charges vs industrial or volumetric (**FE**, **AWK**, **WTRG**) strong FFO/debt metrics (**AEE**); and having room in original 2020 O&M projections for more savings given these pressures (both **LNT** and **XEL** had factored in increases YoY). We have updated our models and made a number of changes to our ests and POs using a 17.6x peer multiple for both electric and gas.

Key company views for 1Q

For 1Q, we expect **EIX** mgmt. to focus on wildfire mitigation execution as well as decoupling/other constructive regulatory mechanisms to offset COVID related pressures; focus remains on the equity overhang where mgmt. is likely to delay its '20 issuance into 2H - *'20* equity addresses mgmt.'s current expectations for wildfire related liabilities and timely recovery of memo accounts ($1.09bn in aggregate); we believe clarity on these outcome remain protracted and uncertain at best. For **DUK**, we see a weak 1Q with weather related headwinds; expect mgmt. to talk-up cost reductions up to $150mn to offset COVID related pressures (3-5% decline in load?); rate case risks in Carolinas remain with ROE and coal ash to be litigated with still wide bid-ask. Resi compositions of **AWK** and **WTRG** should help limit load degradation, they are largely not decoupled. LT, we would expect tailwinds for further industry consolidation as muni's face add'l budget pressure and see both base capital plans as intact over the forecast period with upside from tuck-ins. While **PPL** is decoupled in the UK, we stress a year two lag before true up and see the company as particularly exposed to load degradation in KY as near term rate relief seems less likely given the current rate paradigm and international crisis (albeit plans for timing not totally clear). UK risks appear to be improving but watch govt reactions to Covid on biz response. On top of O&M room (with -8c YoY), we see **LNT**'s Wisconsin regulatory env, confidence in getting renewables online (w/ two of four already commissioned), and credit metrics ($1.17bn of available liquidity) as strengths. **XEL** too could have more O&M savings and push out rate cases expected this year depending on if spend can be tracked. **AEP** is sensitive given it already factors in significant O&M savings in 2020 guide, but the company has noted it could bend the curve further to mitigate demand impacts from COVID and oil prices; some reprieve at Indiana (still underway) and confidence on North Central have us remain at Buy. **FE** is expected to have a quiet quarter as the Street awaits updates of the the New Jersey rate cases; the rest of the year is quiet on the reg front (a pos). For **AEE** we look for any sign of accelerated coal retirement given this fall's integrated resource plan (IRP) but note federal coal quality regulations have been eased of late. Finally, **ES** may start to give a (further) sense of incremental grid mod spend and is largely one of the lease impacted companies as it is almost fully decoupled. **Click for our other previews: SMID-cap (PacNW), SMID-cap (rest of country), PEG & EXC, AGR & NEE, Gas LDCs and Other Diversifieds**

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1Q Summary and PO Changes

We include a brief summary of our 1Q estimates compared vs Street as well as PO changes reflected in this report.

Table 1: PO Changes

Company	Ticker	New PO	Old PO
Alliant Energy Corp	LNT	$56.00	$58.00
Ameren Corp.	AEE	$85.00	$80.00
American Electric Power, Inc	AEP	$93.00	$89.00
American Water	AWK	$133.00	$128.00
Consolidated Edison	ED	$93.00	$100.00
DTE Energy Co.	DTE	$112.00	$116.00
Duke Energy	DUK	$93.00	$93.00
Edison International	EIX	$69.00	$61.00
Entergy Corp.	ETR	$122.00	$108.00
Essential Utilities	WTRG	$47.00	$50.00
Evergy, Inc	EVRG	$69.00	$70.00
Eversource Energy	ES	$83.00	$93.00
FirstEnergy Corp.	FE	$47.00	$47.00
Pinnacle West Capital Co.	PNW	$84.00	$105.00
PPL Corporation	PPL	$29.00	$36.00
WEC Energy Group Inc.	WEC	$85.00	$95.00
Xcel Energy Inc.	XEL	$66.00	$70.00

Source: BofA Global Research

Table 2: 1Q Estimate Summary: only significant beat remains Sempra

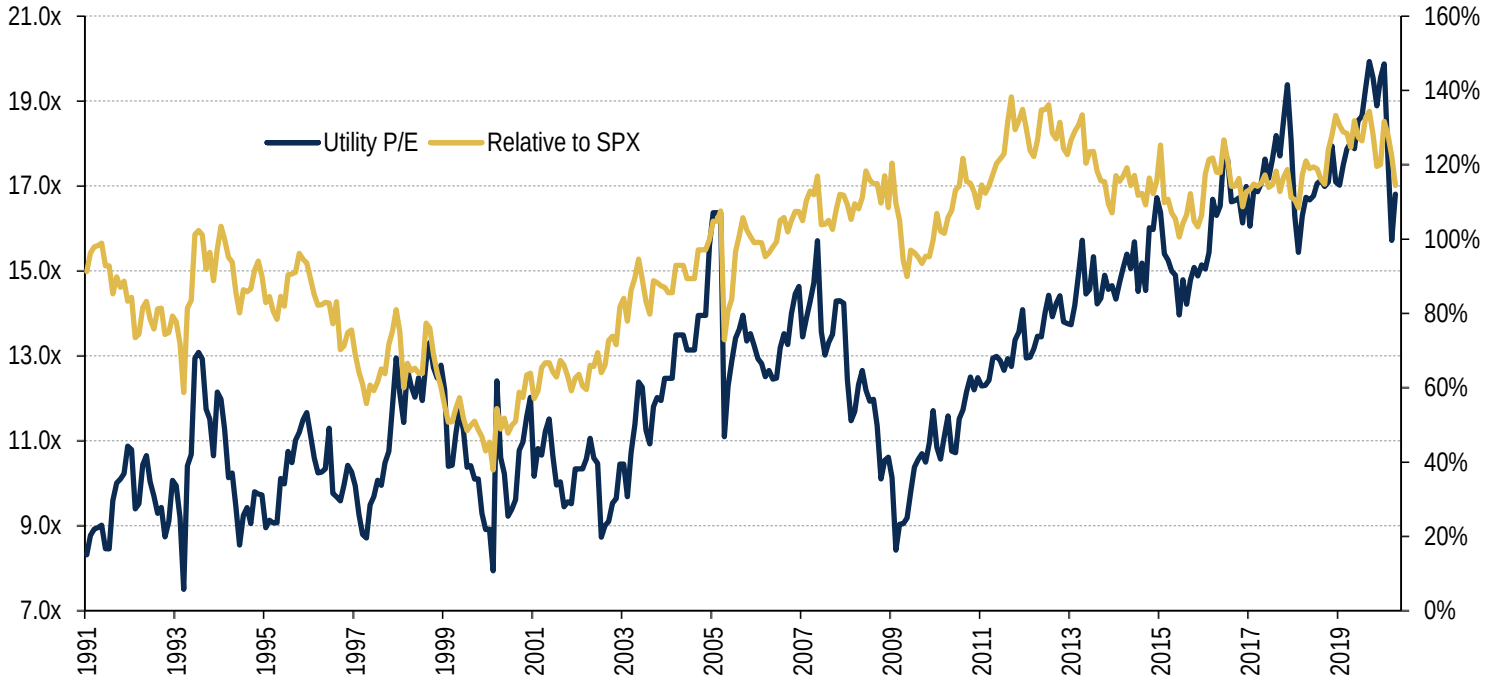
Diversified		1Q20 - BofAe	1Q20 - Cons	Delta
Avangrid Inc.	AGR	$0.71	$0.76	-7%
CenterPoint Energy Inc	CNP	$0.47	$0.46	2%
Dominion Resources	D	$1.11	$1.13	-2%
Exelon Corp.	EXC	$0.86	$0.85	1%
NextEra Energy	NEE	$2.24	$2.20	2%
Public Service Enterprise Group	PEG	$1.05	$1.06	-1%
Sempra Energy	SRE	$2.35	$1.97	19%
Southern Company	SO	$0.72	$0.73	-1%
Regulated		1Q20 - BofAe	1Q20 - Cons	Delta
Alliant Energy Corp	LNT	$0.55	$0.55	0%
Ameren Corp.	AEE	$0.67	$0.73	-8%
American Electric Power, Inc	AEP	$1.03	$1.15	-10%
American Water	AWK	$0.67	$0.67	0%
Consolidated Edison	ED	$1.33	$1.41	-6%
DTE Energy Co.	DTE	$1.80	$1.93	-7%
Duke Energy	DUK	$1.14	$1.23	-7%
Edison International	EIX	$0.81	$0.84	-4%
Entergy Corp.	ETR	$1.01	$1.01	0%
Essential Utilities	WTRG	$0.61	$0.58	5%
Evergy, Inc	EVRG	$0.40	$0.47	-15%
Eversource Energy	ES	$1.02	$1.02	0%
FirstEnergy Corp.	FE	$0.62	$0.63	-2%
Pinnacle West Capital Co.	PNW	$0.15	$0.16	-6%
PPL Corporation	PPL	$0.73	$0.72	1%
WEC Energy Group Inc.	WEC	$1.32	$1.32	0%
Xcel Energy Inc.	XEL	$0.53	$0.62	-15%
SMID		1Q20 - BofAe	1Q20 - Cons	Delta
Avista Corp	AVA	$0.62	$0.63	-2%
Black Hills Corp	BKH	$1.60	$1.66	-4%
CMS Energy	CMS	$0.79	$0.86	-8%
Hawaiian Electric Industries	HE	$0.42	$0.45	-7%
Idacorp, Inc	IDA	$0.77	$0.81	-5%
NorthWestern Corp	NWE	$1.23	$1.27	-3%
OGE Energy Corp	OGE	$0.18	$0.21	-14%
PNM Resources	PNM	$0.18	$0.36	-50%
Portland General Electric Company	POR	$0.90	$0.90	0%
Unitil Corp	UTL	$0.93	$1.05	-11%

Source: BofA Global Research, FactSet

Macro Backdrop

We believe investors are generally skeptical of current sector valuations – and see the continued upward trajectory of the sector as still showing an expensive backdrop from a high level perspective. The chart below shows the latest mark-to-market of the group on an absolute basis and against the SPX; utilities are now trading below their all-time highs on both a relative and absolute basis.

Chart 1: Utility PE vs SPX

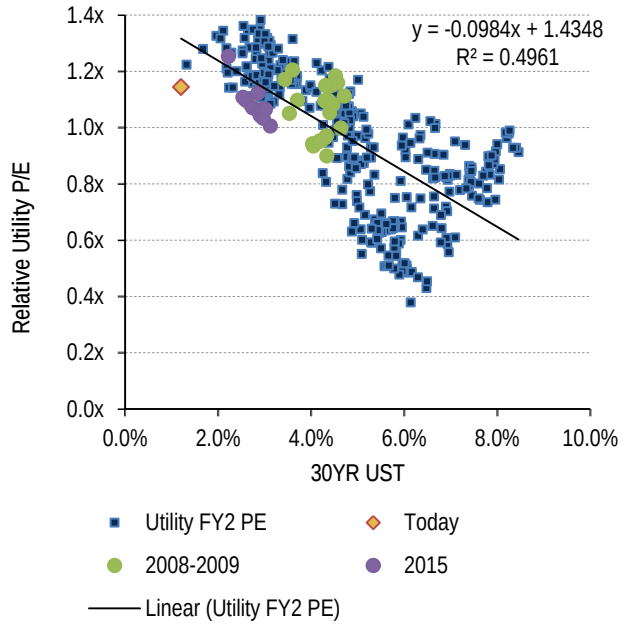


Source: BofA Global Research Estimates, company report, Bloomberg

When adjusting for the S&P itself *and* the treasury environment: different story

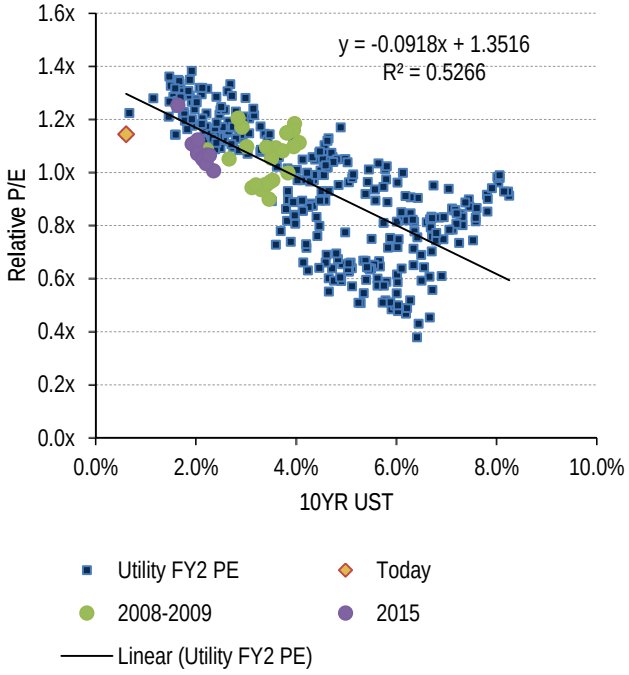
In the exhibits below, we show a time series of where the sector has traded relative to the linear regression on a relative and absolute basis for Treasuries to illustrate the premium; the group has started to trade more in line with its historical linear relationship with 10Yr and 30 Yr Treasuries on a relative basis and could argue somewhat cheap vs historical relationships.

Chart 2: Relative Utility PE vs. 30 YR UST



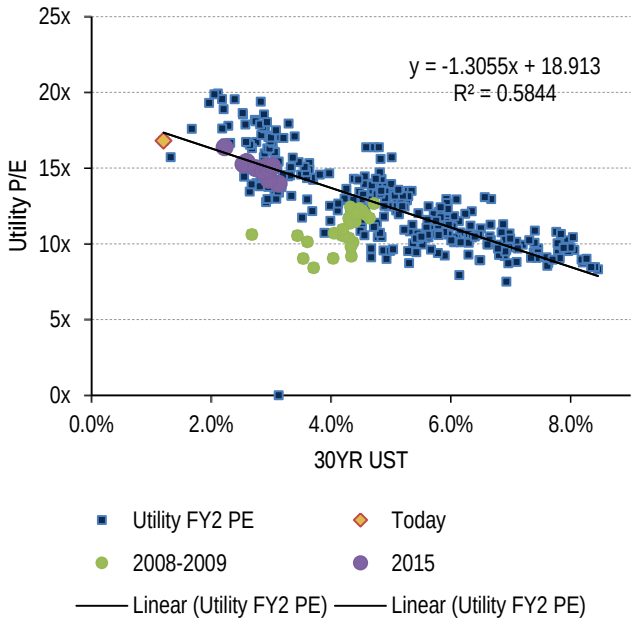
Source: BofA Global Research, Bloomberg

Chart 3: Relative Utility PE vs. 10 YR UST



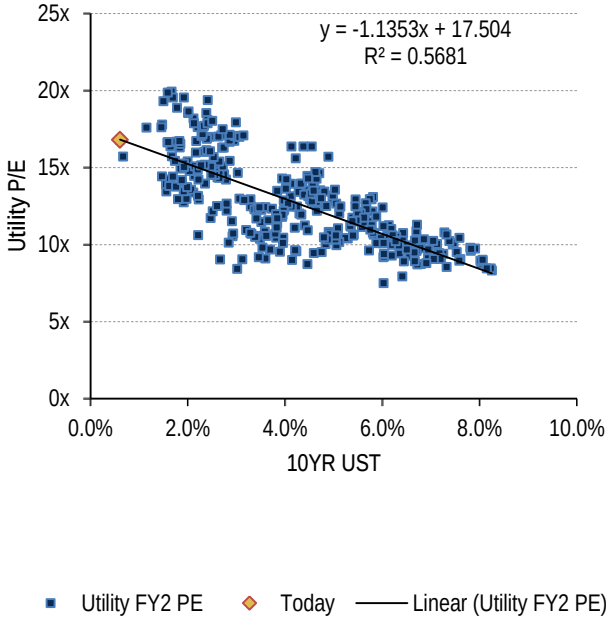
Source: BofA Global Research, Bloomberg

Chart 4: Absolute Utility PE vs. 30 YR UST



Source: BofA Global Research, Bloomberg

Chart 5: Absolute Utility PE vs. 10 YR UST

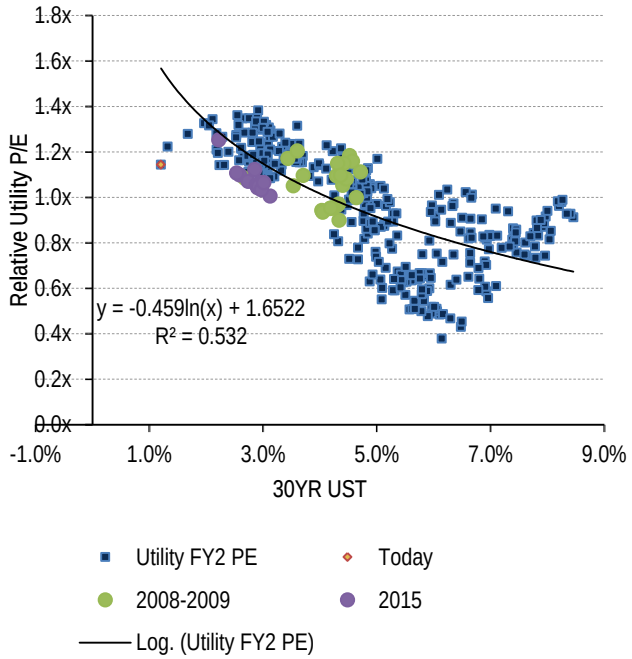


Source: BofA Global Research, Bloomberg

Non-linear makes more sense to us...

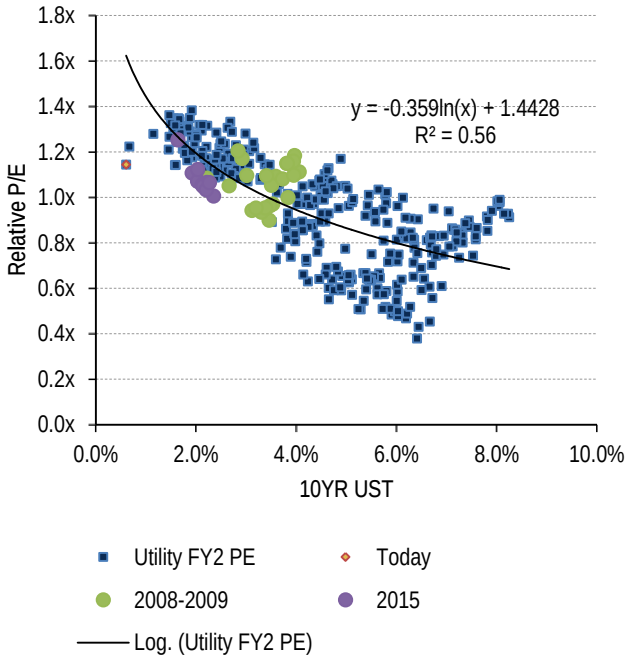
We provide the non-linear relationship below as well given the greater percent change on valuations for every 1% move. We emphasize the limited shift in authorized returns through the cycle also argues that value creation should accelerate with rates declining too. On this basis, the sector looks much less expensive.

Chart 6: Relative Utility PE vs. 30 YR UST



Source: BofA Global Research, Bloomberg

Chart 7: Relative Utility PE vs. 10 YR UST



Source: BofA Global Research, Bloomberg

Alliant (LNT)

We reiterate our Buy going into the 1Q20 call. We adjust down '20 and '21 ests -2c to reflect potential demand impacts from COVID, oil, and 1Q weather – balanced by our expectation that LNT has room for O&M savings as -8c YoY is included in the co's original '20 ests. This takes into account the co's recently disclosed electric sales sensitivity (1% change correlates with an EPS impact of 2c for resi, 1c for industrial, and 1c for commercial), the forecast of 1% sales increasing this yr, and the class breakdown ('19 margins 46% resi, 28% commercial, 26% industrial – with 30-40% of industrial demand fixed, and a hefty chunk agriculture focused that we see as more resilient). We see the company as having stronger credit metrics as well, with $1.17bn of available liquidity as of April 2, 2020. Also recall LNT executed on equity in March. We see other positives for the company including its regulatory relationship in Wisconsin (having deferral of bad debts approved), its ongoing renewable deliveries for the two wind projects to commission in 3Q-4Q (two already commissioned in 1Q), and West Riverside to commission next quarter. Finally, we anticipate the company discusses its forthcoming Wisconsin rate case and solar case. We forecast a 1Q20 estimate of $0.55/sh (the same as Consensus).

LNT 1Q20 Walk

Below we forecast a $0.55/sh 1Q20 EPS, compared to a $0.55/sh Consensus and a $0.53/sh 1Q19 EPS the prior year.

- **Drivers**: We expect about +19c of benefits from the IPL Gas and Electric base rate increases and WPL Electric's as well.
- **Other**: We expect a few of the drivers that LNT provided in its 2020 annual walk (e.g. depreciation, AFUDC, interest expense, other expenses) will be weighted to later quarters, meaning less of an impact of 1Q. Note LNT also has some equity dilution.
- **Wildcard**: As for most companies, the mild winter was noticeable for LNT. We note that 1Q19 saw a +5c benefit (to be reversed now) associated with 800 heating degree days more than average; as such, we expect a -3c hurt in 1Q20 from the mild winter that was 500 days below average. COVID shouldn't impact LNT in a big way yet, since stay at home started mid-March; we expect that the leap day benefit largely counter-balances demand impact since LNT doesn't have decoupling.

Table 3: LNT 1Q20 walk

1Q20 EPS Walk	Notes	EPS Impact
1Q19 Starting Point		$0.53
Weather impact 1Q19	*Had positive*	($0.05)
Weather impact 1Q20	*Very mild*	($0.03)
IPL Base rate increase	*IPL Electric effective 1/8/20; IPL Gas effective 12/18/19*	$0.10
WPL Electric	*New rates at WPL*	$0.09
Depreciation	*-$0.18/sh for full year; weighted more heavily later in yr*	($0.03)
AFUDC increases	*-$0.13/sh for full year*	($0.02)
Other items / O&M / ATC	*-$0.08/sh for full year*	($0.02)
Int Expense	*Debt issuance at WPL and IPL - less neg impact: some was later / intr rates better*	($0.01)
COVID	*Stay at home mid-March balanced by leap yr extra day*	$0.00
Dilution	*Incremental equity dilution*	($0.02)
1Q20 EPS		$0.55
Consensus		$0.55
2020 EPS		$2.44
2020 Consensus EPS		$2.41
2020 Guidance		2.34-2.48
1Q19 Sharecount		237
1Q20 Sharecount		245

Source: BofA Global Research estimates, company report, Bloomberg

Items to track going into 1Q20 call

Key COVID considerations

- **Retail electric margins and sensitivities**: LNT provided sales sensitivities in early April, indicating that a +1% change in electric sales in '20 correlates with a $0.02/sh resi impact, a $0.01/sh commercial impact, and a $0.01/sh industrial impact. It also shared that its 2019 retail electric margins were split such that 46% were resi, 28% commercial, and 26% industrial. Also importantly, LNT acknowledged that 40% of Iowa and 30% of Wisconsin C&I margins are demand-based charges.

- **Diverse industrial customers not all equally impacted**: LNT has a number of C&I customer types, diversifying demand impact. In Iowa, customers are particularly focused on food/agriculture – as well as some chemicals, and manufacturing. In Wisconsin, customers are focused on metals, chemicals, petroleum and plastics (i.e. biofuels), and food. We expect that ethanol has of course been pressured by oil and gas prices, but note that electric demand from farmers should still stays strong as it is too soon to decrease long-term food demand expectations (which would require decisions now to plant less crops for a lower yield this fall).

- **Not decoupled (*for now*) *but* Wisconsin grants bad debt mechanism**: LNT is not decoupled and in its original 2020 guidance expected about 1% sales growth; this included the leap year and industrial customers with operational issues in '19 coming back to normal in '20. Importantly, we see Wisconsin as a positive regulatory environment for LNT, particularly as the state regulators recently approved deferral of bad debts above the revenue requirement. We highlight that the state is evaluating how to proceed with impacts to demand, and we look for future commentary around decoupling in the future.

- **Space for more O&M cuts**: LNT has some room in its earnings for more O&M savings, particularly as it baked in -$0.08/sh YoY in its annual 2020 walk. We expect that the company has some leverage to increase O&M savings in 2020 making the company more resilient to COVID impacts.

- **We expect more demand data to come**: LNT has real-time demand data for resi and commercial customers since AMI exists in both WI & IA, but LNT has about a month lag for industrial data given the meter technology. We expect LNT to provide more customer class-specific impacts from COVID on demand during the 1Q call.

Wisconsin

- **Rate case**: LNT is still analyzing how to file its Wisconsin rate case during this sensitive time, such that it is mindful of its customers during the economic hardship COVID presents to many. We expect to hear more details on requests on the call.

- **Solar filing**: LNT continues to plan to file for about half of its targeted 1Q solar build in 2Q. The company is wrapping up development activity since Wisconsin requires exact sites pre-filing (Iowa allows the site to be named after). While details might be ready on the 1Q call, some more details might come after.

- **West Riverside Energy Center**: LNT's 730MW gas plant is still expected to commission next quarter (2Q20).

Iowa

- **Renewables on schedule**: Amidst the rush to commission wind by year-end to effortlessly qualify for the production tax credit (PTC), LNT is in good shape. Two IPL projects are already in service (201MW Whispering Willow North, and 200MW Golden Plains), and the remaining 130MW Richland project (expected in service 3Q20) is currently receiving timely equipment deliveries. This on time delivery applies for the Wisconsin wind farm too (150MW Kossuth expected in service 4Q20)

- **Multi-year cases**: We still think there's a potential for multi-year cases in the future, but doubt this will take up much of the conversation on the 1Q call.

Estimates

We include our latest EPS estimates and ROEs below by subsidiary. We tweak down our estimates by a few pennies in '20 and '21 to reflect how LNT is not decoupled and could see EPS impacts from lower demand – but with our expectation the company has some ability to ramp up O&M cuts. We are at the middle of the 5-7% guidance range for LNT looking at '18-'23 CAGR.

Table 4: LNT EPS Estimates

EPS by Segment	2017A	2018A	2019E	2020E	2021E	2022E	2023E
IPL	$0.94	$1.13	$1.19	$1.41	$1.47	$1.56	$1.58
WPL	$0.80	$0.89	$0.97	$0.98	$1.05	$1.11	$1.19
ATC	$0.11	$0.13	$0.13	$0.13	$0.14	$0.14	$0.15
Parent/Other	$0.09	$0.02	$0.01	-$0.08	-$0.08	-$0.07	-$0.07
Total	$1.93	$2.17	$2.31	$2.44	$2.59	$2.74	$2.85
Prior Estimates	$1.93	$2.17	$2.31	$2.46	$2.61	$2.74	$2.85
EPS Guidance							
IPL +WPL		*2.04 - 2.07*	*2.21 -2.23*				
ATC		*0.10 - 0.12*	*0.11 - 1.13*				
Parent/Other		*(0.01) - 0.00*	*(0.05) - (0.03)*				
Guidance	$1.89-$1.97	$2.13-$2.19	2.27-2.33	2.34-2.48			
Non-GAAP EPS Growth Off $2.26 in '19 (5-7%)				7.94%	6.97%	6.67%	5.96%
Consensus	$1.95	$2.16	$2.30	$2.41	$2.58	$2.72	$2.84
Consensus CAGR					6.88%		
Mid				$2.41	$2.56	$2.71	$2.87
High				$2.48	$2.65	$2.84	$3.04
Low				$2.34	$2.46	$2.58	$2.71
Model Embedded ROEs / Equity	2017A	2018A	2019E	2020E	2021E	2022E	2023E
IPL							
Regulatory ROE (Avg)	9.2%	9.8%	9.0%	9.2%	9.4%	9.7%	10.0%
GAAP ROE (AVG)	8.4%	8.9%	8.5%	9.6%	9.5%	9.6%	9.3%
WPL							
Regulatory ROE (Avg)	10.5%	10.1%	10.1%	9.9%	9.9%	9.6%	9.7%
GAAP ROE (AVG)	10.1%	10.3%	10.3%	9.9%	10.4%	10.7%	11.1%
ATC							
Earned ROE	10.5%	10.8%	10.5%	10.2%	10.2%	10.2%	10.2%

Source: BofA Global Research estimates, company report, Bloomberg

Valuation

We update the peer multiple to 17.6x for electric and update our WPL peer multiple to 3x (prev 2x) to reflect the regulatory ability to defer bad debt. We reiterate Buy with a $56/sh PO.

Table 5: LNT SOTP Valuation

2022E SotP Analysis - BofAe										
All figures in USD millions except per share										
Regulated Utilities	2022E Net Income	EPS	P/E Multiple					Equity Value		
			Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric			-	17.6x	-	-	-	-	-	-
Group EPS '18-'22 CAGR - Electric			-	5.00%	-	-	-	-	-	-
			-	-	-	-	-	-	-	-
Relative Utility Group P/E Multiple				18.5x						
IPL	$385	$1.56	19.5x	18.5x	2.0x	20.5x	21.5x	$7,500	$7,885	$8,270
WPL	$275	$1.11	20.5x	18.5x	3.0x	21.5x	22.5x	$5,636	$5,911	$6,186
ATC (LNT Share)	$36	$0.14	19.5x	18.5x	2.0x	20.5x	21.5x	$697	$732	$768
EPS (w/o Parent)	$696	$2.82						$13,832	$14,528	$15,224
Parent NI	-$18	-$0.07	18.5x	18.5x	1.0x	19.5x	20.5x	($330)	($348)	($366)
Add Back: Parent Interest Exp	$14	$0.06	18.5x	18.5x	1.0x	19.5x	20.5x	$252	$133	$279
Less: Parent Debt (Term Loan AEF)					*50% weighting*			($500)	($500)	($500)
								($578)	($715)	($587)
Total Implied			19.5x			20.4x	21.6x	$13,254	$13,813	$14,637
Shares Outstanding (2022E)								247	247	247
Total Equity Value Per Share								$54.00	$56.00	$59.00
Total Return Analysis										
Current Share Price									$51.61	
Price Objective									$56.00	
Implied Return									8.51%	
Dividend Yield									2.75%	
Total Return									11.26%	

Source: BofA Global Research estimates, company report, Bloomberg

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Alliant Energy Corporation: Our favorite defensive utility idea	Julien Dumoulin-Smith	11 March 2020
Alliant Energy Corporation: Watching the solar front with carbon goal announcements later this yr; reiterate Buy	Julien Dumoulin-Smith	25 February 2020
Alliant Energy Corporation: Constructive update with more strength ahead: Raise EPS & Reiterate Buy	Julien Dumoulin-Smith	08 November 2019
Alliant Energy Corporation: Iowa resolution, financing updates, and spend all coming up; Maintain Buy	Julien Dumoulin-Smith	05 August 2019

Ameren (AEE)

Our latest EPS projections of $3.43/sh (vs '20 guidance of $3.40-3.60/sh) factor in lower 30-year Treasury assumptions starting at 1.5% in 2020, a lower base ROE for FERC jurisdiction (10.38% with 50bps adder), and our expectation that there is room for cost savings since AEE in its 2020 guidance acknowledged O&M would be increasing at Missouri and Illinois Gas (the exact amount not disclosed). We note that AEE is decoupled in IL, which we think will be a clear benefit; note this leaves about ½ of ratebase (in MO) not decoupled. Although more exposed in MO, we view the company's low portion of industrial energy demand as a positive as well (class break down: 50% margins resi, 40% commercial, 10% industrial), and note that impact of commercial demand is typically more protracted given many billing cycles are 12-month trailing. More specifically, we would expect O&M savings balance out MO commercial sales impact for '20. This still leaves us at ~7% for '20-24 EPS CAGR. Outside of COVID and demand, we expect 1Q commentary to highlight the strong pipeline opportunities the company has outside of its five-year and ten-year capex projections. We specifically watch for any hinting toward potential accelerated retirement of unscrubbed coal, but note that with the outstanding 8th Circuit Case on EPA regulations and lack of securitization legislation will indicate a later update here. Finally, we note the company has strong FFO/debt metrics that sets it apart from peers. As for 1Q20, we expect a $0.67/sh quarter impacted by mild winter, limited COVID impact on demand (due to shoulder month), and lower energy efficiency benefits. Maintain Buy.

1Q20 Walk

We expect a $0.67/sh 1Q20 estimate, versus a Consensus of $0.74/sh and a prior year's 1Q19 est of $0.78/sh.

- **Drivers**: We expect the 1Q result of the Treasury will bring down Illinois Electric ROEs by -2c; this is largely counteracted by ratebase growth (balancing ROE revisions) in IL Electric, IL Growth, and Transmission (+2c).

- **Other**: Note that 1Q19 included $0.03/sh of weather and $0.06/sh of energy efficiency that need to be backed out. The 2019 spring Callaway outage mostly impacted 2Q19, and new rates in AEE Missouri will be a 2Q20 item as well. The company benefited from two refi's in 2019: One March 6th that replaced a $329mn 6.7% with a 450mn 3.5%, and one Oct 1st that replaced a $244mn 5.10% with a $330 3.25%. Lower tax benefits with share-base comp usually benefits 1Q (+3c) and dilution from the $100mn drip is nearly flat.

- **Wildcard**: We see 1Q20 as a mild winter. Looking at heating degree days (HDD) of 2019 and 2020 versus the 10-year average (2009-2018) in Saint Louis, we find 236 more days in 1Q19 and 202 less days in 1Q20. As 1Q19 benefited AEE by +3c, we adjust 1Q19 by -3c. O&M will be another wildcard: We factor in -1c compared to 2019. Finally, COVID impacts on demand are unknown but likely limited in 1Q given the shoulder month it would have impacted (i.e. March).

Table 6: AEE 1Q20 Walk

Ameren 1Q20 Earnings Walk	Notes	EPS
1Q19 EPS		$0.78
Return to normal weather	Cold	($0.03)
1Q20 weather impact	Mild	($0.03)
AEE Illinois		
IL Electric	2019 Average 30 YR UST was 2.58% vs. Current @ 1.368%	($0.02)
IL Gas		$0.01
IL Transmission/Dist./ATXI	Ratebase growth largely balanced by ROE change	$0.01
AEE Missouri		
New Rates	Effective 2Q20	$0.00
Callaway refueling	Roughly 9c for 2019, mostly in 2Q	$0.01
PISA Benefit	Depreciation exp and int exp typically balance out	$0.00
MEEIA Benefits	Lower energy efficiency performance incentive (-11c for 2019)	($0.06)
O&M, Other	Higher O&M over the year (no guide yet)	($0.01)
Interest Refinancings	Two 2019 refi's (March & Oct)	$0.01
Parent Company income tax exp	2020 lower tax benefits w/ share-base comp (3c in 2020 all 1Q)	$0.03
Dilution	Dividend reinvestment plan and employees - $100Mn/yr	($0.00)
COVID	Reduced demand (1Q shoulder months)	($0.01)

Table 6: AEE 1Q20 Walk

Ameren 1Q20 Earnings Walk	Notes	EPS
Other	Donations at AEE Parent more in line w/ normal level, some for COVID	$0.00
1Q20 BofA Adjusted EPS		$0.67
1Q20 BofA Modeled EPS		$0.67
1Q20 Consensus		$0.74
BofA 2020E EPS		$3.43
2020 Consensus		$3.46
1Q19 Shares outstanding		246
1Q20 Shares outstanding		248

Source: BofA Global Research estimates, company report, Bloomberg

Key considerations

We see AEE as well suited to recover on the rebound more than peers.

- **Strong growth yet to come**: AEE showed its growth strength at 4Q19 when it added $3bn to its five-year capex & disclosed a substantial 10-year $36bn runway of 'business as usual' investments. We perceive some slight risks to further acceleration previously contemplated this Fall with IRP update, but overall see among the best positioned longer-term ratebase growth stories. Bottom line we see capex backdorp as securing EPS growth of the 7-8% range (with DPS growth that should beat that given the lower payout ratio), but it will help AEE achieve of on the best 'rate of change' ESG stories in the sector to come. We acknowledge potential pressures on ’20 EPS guide from 30-year treasuries in tandem.

- **Potential accelerated coal retirements & rate-based replacements**: We note AEE might have the opportunity to accelerate its ratebase plan this fall with is integrated resource plan (IRP) filing. Note, though, that actual timing of MO coal retirement could depend on securitization legislation (in '21) as well as Sept resource filing: both key upsides on capex.

- **Illinois is likely later-dated**: While AEE might have upside via more renewables in IL, an extension of formula rates in IL at a higher auth ROE, and more transmission projects, it will likely be a challenge this year. We expect social distancing makes getting to all legislative decisions in the May session difficult, and we could see other issues fill up the November veto session as well. Based on our latest industry conversations, we are expecting a little more difficulty for a broad energy reform involving nukes in the near-term – and could see further out legislation that includes more folks (e.g. labor, environmental) in the future with perhaps more modest gains for utilities (e.g. just formula rates rather than ratebasing renewables).

- **Good balance sheet**: Finally, it would be remiss to ignore AEE's stronger FFO/debt metrics, with projected 19.2% in '19-'25 vs. credit rating 17% min and regulated avg of 16.5% (& larger caps even lower).

- **COVID impact**: AEE in the near-term faces a lower COVID impact given seasonality (i.e. shoulder months limit heating/cooling) and given half of its rate base has limited exposure (i.e. IL electric has full decoupling; IL gas has full decoupling for resi & small commercial & a bad debt expense tracker). AEE faces exposure in MO outside of its energy efficiency mechanism; with 50% of margins resi, 40% commercial, and 10% industrial, increase in resi may offset some drop in commercial but with billing cycles this will likely impact '21 as well.

Estimates

Our estimates remain largely the same as we already adjusted down our EPS expectations for ’20 and beyond given COVID impact on demand (no decoupling in MO) as well as lowered IL ROEs given where 30-year Treasuries have fared thus far. We continue to expect a 1.5% +580bps IL Electric earned ROE.

Table 7: AEE EPS Estimates: towards the bottom end of '20 with risk it could drop below; our focus remains on longer-term compounding outlook

Consolidated EPS Projections	2016A	2017A	2018A	2019E	2020E	2021E	2022E	2023E	2024E	2025E	Segment CAGR ('20-'24)
Ameren Missouri	$1.48	$1.48	$1.94	$1.72	$1.89	$2.04	$2.15	$2.28	$2.41	$2.49	6.26%
Ameren Illinois	$1.05	$1.10	$1.25	$1.39	$1.34	$1.46	$1.64	$1.80	$2.01	$2.22	10.58%
ATXI	$0.23	$0.27	$0.31	$0.32	$0.32	$0.31	$0.30	$0.29	$0.28	$0.28	-2.92%
Other	-$0.07	-$0.02	-$0.13	-$0.09	-$0.12	-$0.12	-$0.11	-$0.11	-$0.11	-$0.11	
Total EPS	$2.68	$2.83	$3.37	$3.35	$3.43	$3.69	$3.97	$4.26	$4.59	$4.88	7.03%
Guidance		*$2.70 - $2.90*	*$3.35-3.45*		*$3.40-3.60*						
EPS CAGR off 2018 ($3.05)				9.86%	6.11%	6.51%	6.83%	6.90%	7.06%	6.95%	
EPS CAGR off 2020 ($3.50)						5.30%	6.54%	6.76%	7.03%	6.88%	
YoY Growth		5.39%	19.14%	-0.53%	2.49%	7.31%	7.80%	7.19%	7.83%	6.29%	
Prior Estimates	*2.68*	*2.83*	*3.37*	*3.35*	*3.43*	*3.69*	*3.97*	*4.26*	*4.59*	*4.88*	
Consensus		$3.46	$3.40	$3.29	$3.46	$3.76	$4.03	$4.30	$4.46		6.25%
Average Earned ROE (Auth in parenthesis)											
Missouri (Auth: electric 9.4-9.8%, gas 9.4-9.95%)		9.5%	12.2%	10.3%	10.0%	9.7%	9.7%	9.8%	10.0%	9.9%	
Illinois (Auth: electric 580bps + 30yr T, gas 9.87%)		9.9%	10.0%	10.0%	8.8%	9.0%	9.2%	9.2%	9.4%	9.5%	
BofA 30-yr Treasury assumption					*1.50%*	*1.75%*	*2.00%*	*2.25%*	*2.50%*	*2.75%*	
ATXI (9.88% plus 50bps adder)		10.82%	10.82%	10.82%	10.38%	10.38%	10.38%	10.38%	10.38%	10.38%	
Consolidated FFO/Debt			23.8%	20.9%	18.1%	18.5%	18.5%	18.7%	19.1%	19.4%	
Guidance (6-8% '18-'23 off of $3.05) --> *Midpoint*				$3.26	$3.49	$3.74	$4.00	$4.28			
Low Implied				$3.23	$3.43	$3.63	$3.85	$4.08			
High Implied				$3.29	$3.56	$3.84	$4.15	$4.48			
Guidance (6-8% '20-'24 off of $3.50) --> *Midpoint*					$3.50	$3.75	$4.01	$4.29	$4.59	$4.91	
Low Implied					$3.50	$3.71	$3.93	$4.17	$4.42	$4.68	
High Implied					$3.50	$3.78	$4.08	$4.41	$4.76	$5.14	

Source: BofA Global Research estimates, company report, Bloomberg

Valuation

We MtM the peer multiple (now 17.6x) and come to a price objective of $85/sh using the same 3x premiums at Missouri and Illinois (not transmission or parent). We reiterate our Buy rating.

Table 8: AEE SOTP Valuation

Ameren Sum of the Parts Valuation - 2022E BofA

All figures in $Mn except per share

Regulated Utilities	2022E EPS	P/E Multiple					Equity Value		
		Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric			17.6x	-	-	-	-	-	-
Group EPS '18-'22 CAGR - Electric			5.00%	-	-	-	-	-	-
				-	-	-	-	-	-
			18.5x	-	-	-	-	-	-
Ameren Missouri	$2.15	20.5x		3.0x	21.5x	22.5x	$44.02	$46.17	$48.32
Ameren Illinois	$1.64	20.5x		3.0x	21.5x	22.5x	$33.56	$35.20	$36.84
Ameren Transmission (ATXI)	$0.30	17.5x		0.0x	18.5x	19.5x	$5.22	$5.52	$5.81
Parent/Unallocated Items	-$0.11	17.5x		0.0x	18.5x	19.5x	-$1.99	-$2.11	-$2.22
Total Implied Utilities	$3.97						$80.81	$84.78	$88.76
Shares outstanding	262								
Implied P/E		21.4x							
Valuation							$81.00	$85.00	$89.00
BofAe Implied Multiple								21.4x	
Current Price								$77.83	
PO								$85.00	
Upside/Downside								9.21%	
NTM Dividend Yield								2.54%	
Total Return								11.76%	

Source: BofA Global Research estimates, company report, Bloomberg

American Electric Power (AEP)

We see the 1Q20 call quite important as it will set the stage for FY20 guidance. It is clear AEP will be negatively impacted by very mild winter as it is not fully decoupled (we factor in -10c for 1Q20 given an even more mild winter than 1Q17, which was -8c YoY). Shares remain among the most controversial of large-cap peers. On top of this, we expect AEP to face lower electric demand from low oil prices' impact on industrial customers (O&G represent 30% of this class) as well as its outcome of its pending Indiana rehearing request. Even so, AEP has been clear that even though it already factors in 'bending the curve' O&M cost cuts, it could factor in more later this year to balance out some of these impacts. The degree to which is so far unclear, so we await commentary to provide a sense. We weigh in the full North Central Wind into our valuation as we see it proceeding forward in key states, but look for any commentary on financing the project (if the asset rotation is possible to pay for the equity check). Upside includes repowering opportunities from the SRE portfolio. We reiterate Buy at a $93/sh PO with an updated peer multiple of 17.6x. Finally, we forecast $1.03/sh for 1Q20 EPS – lower than a $1.15/sh Consensus and 1Q19 results of $1.19/sh.

1Q20 AEP EPS Walk

We estimate EPS of $1.03/sh for 1Q20. This compares to Consensus of $1.15/sh and last year's 1Q19 EPS of $1.19/sh.

- **Drivers**: Apart from weather, 1Q will be driven by a -9c Ohio regulatory provision, YoY wholesale rate changes (+6c for wholesale with Michigan going into effect in February, West Virginia, Arkansas, and Oklahoma last year), and some improvements in O&M (although many are planned for later this year)

- **Other**: A number of 2020 full year walk items are weighted heavier towards other quarters. This includes the -10c for 2020 wholesale load (mostly in 2-3Q), +19c for 2020 O&M (mostly after 1Q), -3c Texas carrying charges (a 2Q item), and a -9c Transmission HoldCo true-up (a 2Q item).

- **Wildcard**: The mild weather will likely account for around -10c YoY for 1Q given that a slightly less mild winter in 1Q17 represented -8c YoY. Note that AEP also has a +1c to return to normal from 1Q19.

Table 9: AEP 1Q20 EPS Walk: street still a bit too high on '20

American Electric Power 1Q20 Earnings Walk	EPS
1Q19 adjusted earnings	$1.19
Vertically Integrated Utilities	($0.11)
Wholesale/Normal Load	($0.02)
Rate Changes	$0.06
Weather	
Return to Normal	$0.01
Current Quarter	($0.10)
Transmission revenues	$0.02
O&M	$0.01
Depreciation and Other	($0.04)
Int/AFUDC	$0.00
Other	($0.01)
Trans./Dist. Utilities	($0.08)
Rate Changes (AEP Ohio, TX DCRF)	$0.01
OH Legacy Riders	($0.01)
OH Reg Prov	($0.09)
Weather	
Weather (Texas) Normalization	$0.00
Weather (Texas) Impact	$0.00
AEP TX transmission revenues (T-cost filings pre-ratecase)	$0.02
O&M	$0.04
TX Carrying Chgs	$0.00
Depreciation and Other	($0.02)
Other Taxes	($0.02)
Other/AFUDC	($0.00)

Table 9: AEP 1Q20 EPS Walk: street still a bit too high on '20

American Electric Power 1Q20 Earnings Walk	EPS
Transmission Holdco	$0.04
Investment growth (ahead of schedule)	$0.04
O&M	$0.00
True-Up	$0.00
Other	$0.01
Generation and Marketing	$0.02
Corporate/Other	($0.02)
Dilution	($0.00)
1Q20E Adjusted EPS	$1.03
1Q20 BofA EPS	$1.03
1Q20 Consensus	$1.15
2020 BofA EPS	$4.25
2020 Consensus	$4.30
2020 Guidance	4.25-4.45

Source: BofA Global Research estimates, company report, Bloomberg

Key items for the 1Q20 call

- **Indiana**: The final outcome for I&M's rate case in Indiana is still underway. Previously, we highlighted that it was possible AEP face a -7c impact from loss of wholesale revenues ($46mn) associated with the case (on top of the ROE result). We note that at the end of March, the Indiana regulatory commission gave the company results of a compliance filing that updated the net impact of the case from $8mn to $26mn. The outcome of the rehearing to recoop the remaining portion associated with wholesale revenues is due 60 days from 3/31. Stay tuned here.

- **Exposure to Covid**: We could see AEP towards the lower end of its guided '20 range based on its exposure to the industrial sales (and specifically Oil & Gas prone growth assumptions). Note that 30% of industrial sales is based on O&G – and that looking at 4Q19, AEP's Industrial GWh growth was 3.5% for the oil & gas related sectors but -6.1% for others. With sensitivity of $0.015/sh for every 1% change in industrial volume (the same for every 1% change in commercial volume as well), we expect the potential loss (vs. the company's originally projected 3.2% growth YoY in industrial GWh Sales) could be a significant driver for a '20 EPS reduction. Flat industrial growth in '20 would bring down '20 EPS by -$0.05/sh alone, and an actual drop in industrial volumes (which we see more likely due to its oil biz dependency) could mean a revision closer to -$0.10 or more. Here, we acknowledge AEP's less decouple profile (largely just Ohio and Texas through regular use of TCOS/DCOS riders) leaves some greater risk vs other more pre play utilities.

- **O&M and mitigating factors**: AEP factors in +19c of O&M cost savings YoY (equates to $200mn of savings established last Nov at EEI) into its 2020 walk already. While not commenting on flexibility, the company noted that it would be evaluating yet further reductions to bend the O&M curve even more this year in effort to balance some of the impacts of lower demand. We see O&M as a mitigating factor to COVID / oil price impacts on demand, Indiana's rate case outcome, and poor 1Q weather. Other ways to mitigate could include filing new rate cases. Finally, we continue to perceive mgmt. strategy as among the best positioned vs. peers between its largely transmission oriented growth strategy and nascent renewable build efforts.

- **Load loss**: As AEP experienced some load loss on the industrial side last year, it factored in some load loss assumptions for 2020 in the residential segment given the normal business cycle for the utility usually sees trends lead by industrial and then followed by resi 12 months later. AEP had factored in a resi decrease of 1.4%. We watch here as COVID work from home mandates could result in more residential use of electric.

- **Wind catcher**: With Louisiana filing its settlement, we await more official certainty before AEP announces how it plans to finance the project. Prior calls have identified 50% to two-thirds financed with equity. We look for whether the company is still able to pursue asset rotations in this environment.

- **Liquidity**: We highlight that AEP had $2.1bn in liquidity at the end of 2019 and that it signed a $1bn credit agreement several weeks ago as well. We expect that the company addresses liquidity and credit concerns as all companies in the utility space have looked to do. Finally, we note that Moody's previously placed AEP on negative outlook last November, but that credit rating agency is well aware of North Central Wind (and the equity associated with the project) as well as measures to reduce O&M at AEP. Note that our FFO/debt reconciliations are roughly around 15% (the company guides to mid-teens).

Estimates

Below we include our estimates largely unchanged from before – still at the bottom of 2020 guidance. We already factored in negative impacts expected from oil price impact as well as COVID impact on industrial demand and the cautious result at Indiana (although still could be mitigated). We note other moving pieces include a further O&M push and 1Q weather pressures.

Table 10: AEP EPS Estimates

EPS	2017A	2018A	2019E	2020E	2021E	2022E	2023E	2024E	2025E
APCo	$0.67	$0.73	$0.78	$0.79	$0.82	$0.84	$0.89	$0.93	$0.97
I&M	$0.38	$0.53	$0.51	$0.52	$0.55	$0.55	$0.57	$0.58	$0.60
SWEPCO	$0.25	$0.30	$0.37	$0.36	$0.38	$0.41	$0.45	$0.47	$0.49
PSO	$0.15	$0.17	$0.25	$0.24	$0.27	$0.30	$0.33	$0.35	$0.36
Other Utes (incl. KY)	$0.17	$0.27	$0.24	$0.24	$0.25	$0.25	$0.26	$0.26	$0.26
KY break out	$0.13	$0.14	$0.15	$0.16	$0.17	$0.17	$0.17	$0.17	$0.18
North Central Wind					$0.02	$0.18	$0.17	$0.17	$0.17
Vertically Integrated	$1.64	$2.00	$2.17	$2.14	$2.28	$2.36	$2.49	$2.58	$2.69
Guidance		$2.00	$2.17	$2.19					
Ohio	$0.66	$0.66	$0.67	$0.58	$0.63	$0.65	$0.69	$0.74	$0.80
Texas	$0.39	$0.41	$0.41	$0.44	$0.53	$0.60	$0.69	$0.76	$0.83
T&D	$1.01	$1.05	$1.00	$1.01	$1.15	$1.26	$1.38	$1.50	$1.62
Guidance		$1.05	$1.00	$1.03					
Transmission HoldCo	$0.72	$0.75	$1.05	$1.07	$1.18	$1.28	$1.38	$1.50	$1.66
Guidance		$0.75	$1.05	$1.08					
AEP Energy Supply	$0.30	$0.29	$0.30	$0.33	$0.23	$0.24	$0.26	$0.27	$0.30
Guidance		$0.29	$0.30	$0.35					
Corp & Eliminations	$0.01	($0.14)	($0.28)	($0.30)	($0.31)	($0.31)	($0.30)	($0.31)	($0.32)
Guidance		($0.14)	($0.28)	($0.30)					
Consolidated EPS without North Central	$3.68	$3.95	$4.24	$4.25	$4.53	$4.83	$5.20	$5.56	$5.94
CONSOLIDATED EPS with NORTH CENTRAL WIND	$3.68	$3.95	$4.24	$4.25	$4.56	$5.01	$5.38	$5.73	$6.11
EPS Growth (%)		*7.5%*	*7.3%*	*0.2%*	*7.3%*	*9.9%*	*7.3%*	*6.5%*	*6.7%*
Previous EPS (without North Central)	*$3.68*	*$3.95*	*$4.24*	*$4.25*	*$4.54*	*$4.84*	*$5.21*	*$5.56*	*$5.95*
Consensus		$3.93	$4.22	$4.30	$4.63	$4.97	$5.31	$5.58	
BofAe CAGR without North Central (vs '18 mid)			10.2%	5.0%	5.6%	5.9%	6.2%	6.3%	6.4%
BofAe CAGR with North Central (vs '18 mid)			10.2%	5.0%	5.8%	6.8%	6.9%	6.8%	6.8%
Annual Guidance	3.55-3.68	3.88-3.98	4.14-4.24	4.25-4.45					
Guidance: 5-7% EPS CAGR off of '18 (or '19 orig midpt)		$3.85	$4.19	$4.35	$4.59	$4.86	$5.15	$5.46	$5.82
Low			$4.14	$4.25	$4.46	$4.68	$4.91	$5.16	$5.42
High			$4.24	$4.45	$4.72	$5.05	$5.40	$5.78	$6.18
Share Count	492	493	494	496	497	511	515	519	522

Source: BofA Global Research estimates, company report, Bloomberg

Valuation

We MtM the peer multiple to 17.6x and derive a $93/sh PO with the same premiums awarded per subsidiary. We reiterate our Buy rating.

Table 11: AEP SOTP Valuation

AEP SoTP	2022E EPS			P/E Multiple	Premium/ Discount	Value ($mn)	Value ($/Sh)
Group Peer Multiple - Electric				17.6x			
Group EPS '18-'22 CAGR - Electric				5.00%			
Vertically Integrated Utilities (SWEPCO, PSO, APCo) excl KY	$2.19			18.5x	0.0x	$20,673	$40.5
Kentucky Power break out	$0.17			18.5x	0.0x	$1,612	$3.2
T&D Utilities (Principally D) - TNC/TCC, Ohio Power	$1.26			18.5x	1.0x	$12,502	$24.5
Transmission-Only Utilities - Mostly FERC	$1.28			18.5x	1.0x	$12,735	$24.9
Parent & Other - Principally HoldCo Debt	($0.31)			18.5x	0.0x	($2,904)	($5.7)
Total Regulated & HoldCo Value	$4.59					$44,618	$87.4
Renewables							
Legacy Energy Supply + Marketing/ Increasingly Renewables	$0.24			18.5x	-3.0x	$1,934	$3.8
Total AEP Equity Value - Existing Assets							$91.1
Upside	**2022E EPS (or discounted)**	**Capex**	**FFO**	**Earnings Impact (50% Equity)**	**P/E Multiple**	**Premium**	**Probability Weighted**	
SWEPCO 1200MW RFP filing - in service '21 (mostly 80% PTC)	0.09	1,089	$75		18.5x	0.0x	100%	$1.7
PSO 1000MW RFP filing - in service '21 (mostly 80% PTC)	0.07	908	$55		18.5x	0.0x	100%	$1.3
Total	0.17	1,997						3.1
Probability-Weighted EPS	0.17							
Discount Factor by year	10%							
Total Capex (probability weighted)				1,997				
Total Equity Needed ($M) (assuming 50%)				799				
Issuance Price (current price)				86.38				
Shares Issued (mn)				9				
Dilution %				2%				
Value Dilution				($808)			($808)	($1.6)
Shares Outstanding								511
Total Equity Value Per Share								$93
							Price Appreciation	7.7%
							+2020 Dividend Yield	3.2%
							Total Return	10.8%

Source: BofA Global Research estimates, company report, Bloomberg

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
American Electric Power: Starting from the Top: Breaking down the COVID Impact on C&I Sales	Julien Dumoulin-Smith	25 March 2020
American Electric Power: All on the same 5-7% page: North Central, financing, and rate cases	Julien Dumoulin-Smith	21 February 2020
American Electric Power: Adding to the US1 List: Key utility opportunity in 2020	Julien Dumoulin-Smith	22 January 2020
American Electric Power: Still confident on '20 & Awaiting critical updates with EEI; Reiterate Buy	Julien Dumoulin-Smith	25 October 2019

American Water Works (AWK)

Amid the escalation of the COVID pandemic, we expect continued execution by AWK with their inaugural ten year capital forecast of $20-22Bn intact and the company recently taking action to proactively address NT liquidity. We don't perceive any meaningful delays in spend or regulatory filings (albeit note the timing shift for new rates to take effect for NYAW) and with recent changes in mgmt. taking effect in the beginning of the month, we have confidence in the team's ability to navigate the crisis with potential for a further acceleration in muni acquisitions during any recovery period. While we appreciate the scarcity element and higher sustained investment trajectory for the subsector, we ultimately see the steep premium as unwarranted. We reiterate our Underperform rating.

AWK 1Q20 Earnings Walk

We forecast 1Q20 adjusted EPS of $0.67, in line with consensus and a $0.06 uptick from 1Q19 results of $0.61.

- **Key Drivers:** The primary positive drivers y/y are new rates implemented across a number of states in their footprint as well as various infrastructure surcharges. Partially offsetting results at the regulated segment includes higher D&A and O&M, as well as a bit of a drag at the parent level offsetting MBB contributions.

Table 12: AWK 1Q20 Walk

AWK 1Q20 Earnings Walk		EPS
AWK 1Q19 EPS	$	0.61
Regulated		0.06
Rate Cases & Step Increases		0.07
Infrastructure Charges		0.03
Depreciation		-0.02
O&M		-0.02
MBB		0.02
Parent		-0.02
Interest/Other Impact		-0.02
1Q20 BofAe Adjusted EPS	$	0.67
In Model	*$*	*0.67*
Consensus		$0.67
BofAe 2020 EPS	$	3.85
Guidance		3.79-3.89
2020 Consensus		$3.84
AWK 1Q20 Shares Outstanding		181
AWK 1Q19 Shares Outstanding		181

Source: BofA Global Research, Bloomberg

Predictable Execution Amid Unpredictable Crisis

Amid the escalating COVID crisis, mgmt. of AWK has maintained a clear focus on liquidity: in addition to their $2.25Bn revolver, the company entered into a $750Mn term loan, drawing $500Mn to hold in cash for add'l flexibility. The company has no near term debt maturities and remains confident in its ability to access both debt & equity markets (no equity needed in '20) as they still expect to fully execute on their capital investment plan of $20-$22Bn over the next ten years (any 2020 delays are expected to be made up later this year). To date, the company hasn't seen major disruptions to the supply chain: key distributors have indicated excess inventory, while chemical providers are meeting needs and reporting no shortages. On the margin, we sense commercial trucking capacity as mgmt's only potential concern for transport of chemicals or bottled water in the event of a major service outage – and the company said it has secured contracts with two suppliers with relationships with gov't agencies in any event.

Reg., Leg., and Muni Prospects

We further perceive regulatory filings as generally proceeding as planned – while remote - with no anticipation of a delay in their ongoing NJ rate case. That said, late last month, NYAW announced postponement of the rate increase and improvement charge. We could also see a further uptick in bad debt expense with no real time tracker for recovery. With resi composing 69% of revenue, we see load impact as likely more muted, however. Given the already longer process of engaging in municipal transactions, mgmt hasn't seen particular delays on the acquisition front and we perceive a potential for further acceleration in industry consolidation under a recovery scenario as munis focus on the small businesses. Meanwhile, the capital light MBB is continuing to generate cash with no impacts yet to Military and an expectation that the customer base in homeowners services will be maintained in any economic downturn.

EPS Estimates

The exhibit below reflects our latest EPS estimates with annuals remaining unchanged ahead of our 1Q preview and as we await additional data points. We continue to expect sustained long term growth within their 7-10% LT EPS CAGR and 7% rate base growth longer term.

Table 13: EPS Estimates

AWK	2019A	2020E	2021E	2022E	2023E	2024E
Earnings Metrics						
Regulated Water EPS	3.60	3.84	4.19	4.43	4.66	4.98
Market Based EPS	0.45	0.47	0.51	0.53	0.57	0.63
Parent and Other EPS	-0.44	-0.46	-0.43	-0.40	-0.36	-0.39
Adjusted EPS	3.61	3.85	4.27	4.56	4.87	5.21
Consensus	3.61	3.84	4.23	4.53	4.92	
Guidance	3.56-3.64	3.79-3.89				
Midpoint of Guidance	3.60	3.84				
Implied Guidance - 2020-2024 off 2018 EPS base						
High	3.64	3.89	4.39	4.83	5.31	5.85
Low	3.56	3.79	4.04	4.33	4.63	4.95
Mid	3.60	3.84	4.22	4.58	4.97	5.40
EPS CAGR - BofA off 2018 EPS base - 2020-2024	*7.9%*					

Source: BofA Global Research, Bloomberg

Valuation

The exhibit below reflects our latest valuation: We mark to market our valuation for the latest water utility multiple of 26.3x (vs. 25.2x), with our PO shifting to $133. We maintain our Underperform rating given the large premium vs. electric & gas peers, which we see as unjustified given its only modest relative growth premium.

Table 14: AWK SOTP

Water Utilities	2022E EPS	P/E Multiple					Equity Value		
		Peer	Prem/ Discount	Low	Base	High	Low	Base	High
AWK Earnings		26.3x							
Group EPS '18-'22 CAGR		8.30%							
Water Utilities		28.5x							
NJ	$1.12		3.0x	30.5x	31.5x	32.5x	$34.13	$35.25	$36.37
PA	$1.27		3.0x	30.5x	31.5x	32.5x	$38.81	$40.08	$41.35
IL	$0.35		3.0x	30.5x	31.5x	32.5x	$10.57	$10.92	$11.26
MO	$0.50		2.0x	29.5x	30.5x	31.5x	$14.64	$15.14	$15.63
IN	$0.29		1.0x	28.5x	29.5x	30.5x	$8.27	$8.56	$8.85
CA	$0.19		-1.0x	26.5x	27.5x	28.5x	$5.03	$5.22	$5.42
Other	$0.71		0.0x	27.5x	28.5x	29.5x	$19.50	$20.21	$20.92
Regulated Water EPS	$4.43						$130.95	$135.38	$139.80
Parent/Other Drag	-$0.40		0.0x	27.5x	28.5x	29.5x	-$11.03	-$11.43	-$11.83
Market Based Business									
Military (40%)	$0.21	26.3x	-3.0x	22.3x	23.3x	24.3x	$4.74	$4.95	$5.17
Non Military (60%)	$0.32			11.0x	12.0x	13.0x	$3.51	$3.83	$4.15
Total Market Based Business	$0.53						$8.25	$8.78	$9.31
Valuation	$4.56						$128.00	$133.00	$137.00
Current Price as of 04/19/20								*$131.76*	
Dividend Yield								1.5%	
Total Return							-1.35%	2.45%	5.48%

Source: BofA Global Research, Bloomberg

See our other recent reports on AWK:

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
American Water Works: Takeaways from our latest fireside chat	Julien Dumoulin-Smith	07 April 2020
American Water Works: Adding detail to our valuation approach: Underperform	Julien Dumoulin-Smith	09 March 2020
American Water Works: Analyst Day Redux: A Splash of Deleveraging & More	Julien Dumoulin-Smith	16 December 2019

Consolidated Edison (ED)

ED is expected to deliver Q1 results down slightly from the prior-year quarter. Our 1Q20 estimate of $1.33/sh compared to adjusted EPS of $1.39/sh in 1Q19 and Street consensus of $1.42/sh – we see downside here as effects of Covid-related slowdown are more fully reflected in consensus estimates. ED's main electric and gas business at the Con Edison Company of New York (CECONY) and Orange & Rockland (O&R) is fully decoupled leaving its earnings relatively defensive in the face of Covid-related slowdowns amid ongoing shut-in orders, with the Steam business being the only one exposed to weather and load factors. ED's non-regulated business should see a modest uplift in 2020 on higher earnings from the ongoing Mountain Valley Pipeline (MVP) project as well as the normalizing effect of weather-curtailed renewable production in the Clean Energy Business (CEB).

1Q20 Quarterly Walk

We see Q1 EPS at $1.33/sh, slightly below Street at $1.42 though we perceive downside to consensus ests after weather and demand considerations are more fully factored in to forecasts. Weather is expected to be a drag (we estimate 5 cents, see below) due to milder weather in Q1 2020 affecting principally the Steam business (CECONY and O&R are decoupled for Electric and Gas) offset partially by normalization of the negative effect from 1Q19. We expect a $0.12/sh uplift from new rates at the gas and electric utilities in effect since January with new rates in place following the approval of the joint settlement in the CECONY rate case, and modest uplift at CEB from improving wind resource in Q1 (ex HLBV impact). Key unknown is the drag from stock-based compensation (SBC) which becomes incrementally larger depending on the y/y share price return as of the end of the quarter – given market volatility in Q1 this item is particularly difficult to estimate, though we assume some drag given the share price was higher *on average* during 1Q20 as compared to the prior year.

Table 15: ED 1Q20 Earnings Walk

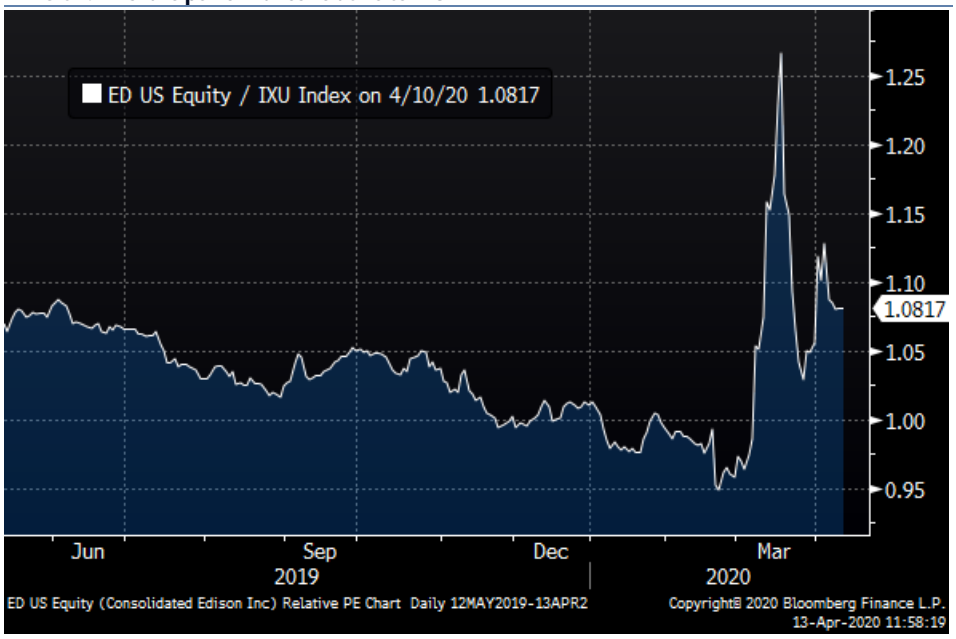
ConEd 1Q20 Earnings Walk		EPS
1Q19 Adjusted EPS	Notes	$1.39
Con Edison of New York (CECONY)		
Rate Changes		0.12
Gas	$84m increase effective Jan. 1, 2020	0.05
Electric	$113m increase effective Jan. 1, 2020	0.07
Impact of Steam 1Q19	Normalizing last year impact	0.01
Impact of Steam 1Q20	Warmer than normal weather; demand due to COVID	(0.05)
O&M		(0.03)
Stock based comp	Share price higher in Q1 2020 based on quarterly average	(0.03)
D&A / Property Taxes		(0.10)
Interest Expense		0.00
Orange & Rockland (O&R)		
Rate Changes		0.02
O&M		0.00
D&A / Property Taxes		(0.01)
Competitive Business		
CET	Flat y/y	0.00
CEB	Normalizing wind resource	0.04
Dilution		(0.03)
1Q20 Adjusted EPS		$1.33
1Q20 Consensus		$1.42
1Q20 in Model		$1.33
2020 BofAe		$4.38
2020 Consensus		$4.42
2020 Guidance		$4.30-$4.50
Share Count		
1Q19		323
1Q20		330

Source: BofA Global Research Estimates, company report, Bloomberg

Stock trading dynamics

Shares of ED have held up relatively well during the March market volatility which was kicked off by concerns about the economic effect of Covid. ED remains one of the more defensive names in our coverage owing to its largely decoupled business – both Electric and Gas distribution at CECONY and O&R are decoupled, leaving the much smaller Steam business along with the Rockland Electric Company (RECO) exposed to changes in load. The New York Independent System Operator (NYISO) has reported electricity demand in Zone J declining by as much as 18% during the weeks since the shut in orders began, largely driven by lower morning peaks as commercial customers are shut down and commuting has declined precipitously. While the timing of the Covid demand shock is more likely to impact Q2, we note that milder Q1 weather can be a negative driver for the steam business, though ED does not disclose sensitivities. ED has weather normalization at the CECONY and O&R gas businesses but not at the electric utility. While ED does not have a separate bad debt expense rider, each rate case creates an allocation for bad debt expense that is then recovered through rates. Nonetheless, on a 2-year forward PE relative to the IXU, ED shares continue to screen relatively expensive. Accordingly we remain comfortable with our Neutral rating, seeing risk and reward as largely balanced.

Exhibit 1: ED share performance relative to IXU



Source: Bloomberg

Weather should be more impactful than demand in Q1

We expect that despite ED's largely decoupled business, the impact of milder than normal weather in Q1 results will be more pronounced in 2020, on an order of magnitude more in line with Q1 2018. As measured by heating degree days at LaGuardia Airport, Q1 was 20% warmer than normal, a level of mild weather last approached in 2016 and 2017. ED's reported weather impact on the steam business includes both the normalization of the prior year's impact as well as that of the current year. As such it is more instructive to look at the total delta in deviation from normal from year to year – note that in 2016 HDDs swung from 18% above normal to 16% below normal, an aggregate change of -34% which resulted in a significant 12 cent impact on EPS. The change in 2020 is not as dramatic as 2019 was only slightly below normal in terms of HDDs, accordingly the total drop in HDDs including the impact of the current year is -18%. We therefore estimate that the impact on EPS from weather impacts on the Steam business is -$0.05. We not however that this impact is historically volatile and numerous factors affect the total EPS swing including the timing of when the biggest deltas from normal occur – HDDs in Jan-Feb are "worth more" in an EPS sense than

those in more shoulder months of Mar-Apr generally speaking. 2020 saw relatively consistent trends in weather, with each Q1 month recording double-digit percentage declines from normal including 20%/15% declines in Jan/Feb. In 2016 by contrast, Jan-Feb declines were approximately 10% while March HDDs were 30% below normal. Bottom line: we see weather as a likely negative driver in Q1 on an order of magnitude similar to 2018. We see this as a much more impactful Q1 event than Covid-related demand declines owing to the timing of state shut-in orders, though both will be Q1 headwinds with the mix shifting toward demand declines looking forward to Q2 and beyond.

Table 16: New York City HDD data

	Q1 2015	Q1 2016	Q1 2017	Q1 2018	Q1 2019	Q1 2020
NYC HDDs	3,057	2,171	2,132	2,406	2,530	2,062
Normal	2,582	2,582	2,582	2,582	2,582	2,582
% Above / Below	18%	-16%	-17%	-7%	-2%	-20%
% Delta		-34%	-2%	11%	5%	-18%
Steam impact ($/sh)		(0.12)	0.02	0.05	(0.01)	

Source: BofA Global Research Estimates, NYSERDA

Credit and financing update

ED's 3-year financing plan includes up to $1.8B of equity issuance in 2020-22. Needs in the current year are seen at up to $600m on top of $88m of equity forwards settled in January, while the forecast for the two following years calls for $1.1B. Street estimates were higher than our forecast. However, they still trail the announced issuance by ~$400m through 2022. On the credit side, Fitch lowered outlooks of ED and its subsidiaries CECONY and Orange and Rockland Utilities Inc. to negative from stable reflecting a weak financial profile associated with lower demand and higher than anticipated bad debt expense involving NY power market due to COVID 19. Admittedly, the companies have revenue recovery mechanisms in place to deal with such situations but Fitch expects those are not sufficient enough to protect the utilities. We continue to see ED's consolidated CFO pre-WC to net debt metric as bouncing back from the ~15% level at the end of 2019, increasing to 17-18% by 2024.

Table 17: ED credit update

Rating Agencies	2015A	2016A	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E	2025E
CFO		3,459	3,367	2,695	3,134	3,452	3,678	3,912	4,140	4,364	4,747
Add: Pensions		233	187	233	233	233	233	233	233	233	233
Add: Operating Leases		12	12	12	12	12	12	12	12	12	12
Less: Changes in WC		(150)	(83)	414	160	160	160	160	160	160	160
Adj CFO Pre-W/C	3,692	3,554	3,483	3,354	3,539	3,857	4,083	4,317	4,545	4,769	5,152
Long -Term Debt		14,774	16,029	18,970	19,973	20,484	20,989	21,222	21,731	22,103	22,182
Add: Short-Term Debt		1,054	577	1,741	1,692	1,692	1,692	1,692	1,692	1,692	1,692
Add: Pensions		1,623	1,262	1,262	999	999	999	999	999	999	999
Add: Operating Leases		180	180	180	880	880	880	880	880	880	880
Add: Non-Standard Adjustments			134	142	142	167	167	167	167	167	167
Adj Total Debt	17,170	17,765	18,190	22,295	23,711	24,222	24,727	24,960	25,469	25,841	25,920
(CFO Pre-W/C) / Debt	21.5%	20.0%	19.1%	15.0%	14.9%	15.9%	16.5%	17.3%	17.8%	18.5%	19.9%

Source: BofA Global Research estimates, company report, Bloomberg

EPS Estimates

We tweak our 2020 estimates lower on Covid and weather impact at the Steam business, reducing earned ROE to 8.8% (in line with authorized) from 8.9% while we continue to reflect 10 bps of over-earning at CECONY in 2021 and beyond. We also reflect a slight uptick in results at the CEB y/y as below-normal results from 2019 are normalized, though in the long-term growth in this business is expected to come principally via contractual escalators and investment in incremental projects. Our estimates are modestly below Street consensus in '20 and '22 and in-line in '21, reflecting a CAGR of ~4% over our 2019 estimate.

Table 18: ED updated estimates

EPS by Business	2019A	2020E	2021E	2022E	2023E	2024E	2025E
CECONY	$3.79	$3.71	$3.91	$4.07	$4.26	$4.51	$4.77
O&R	$0.21	$0.22	$0.22	$0.23	$0.24	$0.26	$0.27
Regulated	$4.01	$3.93	$4.14	$4.30	$4.50	$4.76	$5.04
Core Regulated Growth (Y/Y)	*-0.12%*	*-1.85%*	*5.22%*	*3.88%*	*4.71%*		
CED Development (Solar)	$0.21	$0.29	$0.31	$0.33	$0.35	$0.37	$0.39
CEE (Energy/Wholesale Marketing)	$0.02	$0.02	$0.02	$0.02	$0.02	$0.02	$0.02
CES (Solutions)	$0.01	$0.01	$0.01	$0.01	$0.01	$0.01	$0.01
Clean Energy Businesses	$0.24	$0.32	$0.34	$0.36	$0.38	$0.40	$0.42
Electric Transmission	$0.02	$0.03	$0.03	$0.03	$0.03	$0.03	$0.03
Midstream/Stagecoach	$0.08	$0.06	$0.06	$0.06	$0.06	$0.06	$0.06
MVP	$0.09	$0.11	$0.08	$0.05	$0.05	$0.05	$0.05
Consolidated Edison Transmission	$0.19	$0.20	$0.17	$0.13	$0.13	$0.13	$0.13
Parent	-$0.07	-$0.07	-$0.07	-$0.07	-$0.07	-$0.07	-$0.07
CONSOLIDATED EPS	$4.38	$4.38	$4.57	$4.72	$4.94	$5.22	$5.52
Prior EPS Estimates	$4.08	$4.49	$4.62	$4.78	$4.99		
Management guidance		$4.30-$4.50					
Midpoint		$4.40	$4.58	$4.76	$4.95	$5.15	$5.35
Long term CAGR (3-5% CAGR guide off 2020 guidance)			3.9%	3.6%	4.0%	4.4%	4.7%
Consensus	4.30	4.42	4.59	4.79			
BofAe CAGR '19 -'22	2.6%						
CECONY CAGR '19-22	2.4%						
O&R CAGR '19-22	2.3%						
Earned ROEs							
CECONY	9.2%	8.8%	8.9%	8.9%	8.9%	8.9%	8.9%
O&R	9.3%	9.1%	9.1%	9.1%	9.1%	9.1%	9.1%

Source: BofA Global Research Estimates, company report, Bloomberg

Valuation

We update our PO to $93 following mark to market of the latest peer group multiples of 17.6x for electric and 17.6x for gas. We remain Neutral on ED as the latest guidance provides a below-peer rate of return of 3-5% over a five year period based off 2020's guidance, which implies minimal growth over 2019 at the midpoint. While in our view shares are largely derisked in terms of rate case uncertainty with new rates in place for three years, we would expect the market to remain focused near-term impacts from warmer weather and Covid-related demand destruction in the near term along with a focus on the below-average growth trajectory and uncertain cadence of 2021-22 equity issuance in the medium term. Reiterate Neutral.

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Consolidated Edison: Cautious update as equity issuance exceeds expectations	Julien Dumoulin-Smith	21 February 2020
Consolidated Edison: Fine-tuning equity & renewable investments; reiterate Neutral	Julien Dumoulin-Smith	20 December 2019
Consolidated Edison: Moving to conservative ROE outlook following EEI; D/G to Neutral	Julien Dumoulin-Smith	14 November 2019
Consolidated Edison: '19 Narrowed Lower: Long-term still quite compelling despite NT Noise; Buy	Julien Dumoulin-Smith	05 November 2019

Table 19: ED SOTP

ConEd Valuation	Metric	Multiples				Equity Value		
	2022E EPS	Low	Prem/ Discount	Base	High	Bear	Base	Bull
	-	-	-	-	-	-	-	-
	-	-		-	-	-	-	-
Group Peer Multiple - Electric	-	-	17.6x	-	-	-	-	-
Group EPS '18-'22 CAGR - Electric	-	-	5.00%	-	-	-	-	-
	-	-		-	-	-	-	-
Group Peer Multiple - Gas	-	-	17.6x	-	-	-	-	-
Group EPS '18-'22 CAGR - Gas	-	-	5.10%	-	-	-	-	-
	-	-		-	-	-	-	-
Applied Multiple	-	-		-	-	-	-	-
Electric (& Steam)	-	-	18.5x	-	-	-	-	-
Gas	-	-	18.5x	-	-	-	-	-
Utilities		-	-	P/E	-	-	-	-
CECONY Electric	$2.85	18.5x	1.0x	19.5x	20.5x	$53	$56	$58
CECONY Steam	$0.19	18.5x	1.0x	19.5x	20.5x	$3	$4	$4
CECONY Gas	$1.03	18.5x	1.0x	19.5x	20.5x	$19	$20	$21
Total CECONY	$4.07					$75	$79	$83
O&R + RECO Electric	$0.16	18.5x	1.0x	19.5x	20.5x	$3	$3	$3
O&R Gas	$0.07	18.5x	1.0x	19.5x	20.5x	$1	$1	$1
Total O&R	$0.23					$4	$4	$5
Grand Total Utilities EPS	$4.30							
Competitive Businesses								
	2022E EPS			P/E				
CET Electric Transmission (NY Transco)	$0.03	15.5x	-2.0x	16.5x	17.5x	$0.40	$0.42	$0.45
CEE (Wholesale Energy)	$0.02	11.5x	-6.0x	12.5x	13.5x	$0.23	$0.25	$0.27
Infrastructure	2022E EPS			P/E				
Stagecoach Midstream	$0.06	15.5x	-2.0x	16.5x	17.5x	$0.89	$0.95	$1.01
	2022E EBITDA			Baseline	Adjusted			
Mountain Valley Pipeline (MVP)	$70	10.0x	-2.0x	11.0x	9.0x	$1.41	$1.81	$2.21
ConEd Development: Renewables	2022E EBITDA			EBITDA Multiple				
Legacy ED Portfolio	360	9.0x		10.0x	11.0x	3,240	3,599	3,959
Renewables Acquistion (60% of SRE portfolio)	211	9.0x		10.0x	11.0x	1,897	2,107	2,318
Total CEB EBITDA	571							
Less: CEB Project Level Debt						-2,806	-2,806	-2,806
Total Renewable Portfolio Equity Value						2,330	2,901	3,471
Implied Equity Value $/sh						$6.72	$8.36	$10.01
Parent + HoldCo Debt	2022E EPS							
Corp & Other Drag	-$0.07	17.5x	0.0x	18.5x	19.5x	-$1.18	-$1.25	-$1.32
Holding Company: 50% Weighting to Debt Subtraction & 50% Weighting to Interest Expense								
Current HoldCo Debt	-900					-450	-450	-450
Imputed MVP Debt @ 10% Ownership	-324					-324	-324	-324
Add Back: Interest expense (Tax effected)	41	17.5x	0.0x	18.5x	19.5x	361	382	403
Total Adjustment $/Sh						-$1.19	-$1.13	-$1.07
Shares Outstanding							347	
Total Equity Value						$87.00	$93.00	$100.00
Implied Consolidated P/E							19.7x	
Dividend Yield							3.31%	
Total Return						0.4%	7.1%	15.0%

Source: BofA Global Research Estimates, company report, Bloomberg

Duke Energy (DUK)

With DUK's upcoming 1Q call, we expect a sharp focus on cost reduction mitigation measures to offset in part COVID-19 related pressures. While mgmt. is still assessing the impact on load and delayed bad debt expense recovery, we could potentially see up to a -$0.14-16/sh headwind assuming just 2-3% load degradation (although could be materially higher than this) on C&I/wholesale customers and $20mn incremental bad debt similar to '09 levels if not for offsets. Specific details on cost cuts have yet to be delineated, although we look back to 2017 where weather was a significant headwind with mgmt. offsetting the impact through cost reductions of $100-150mn, which would translate to $0.11-$0.16/sh EPS benefit in 2020. Ability to bend the cost curve is notable and opportune following last year favorable weather and pull-ahead on O&M execution. Beyond 1Q details around load pressures and cost reduction, we look to discussions around the North Carolina rate cases where we remain cautious given litigated ROEs and coal ash pressures; perceive the risks of negative revisions to be largely known/priced-in. With potential for multi-year rates/ ROE banding in exchange for enhanced customer metrics the Carolina jurisdictions could be partially de-risked following rate case outcome. Longer-term, the NC IRP filing in Sept that could create additional opportunities for DUK in terms of clean energy and coal reduction opportunities, although we look for further discussion on natural gas build considerations given still uncertainty around ACP. Net-net, we maintain our Neutral rating.

DUK 1Q20 EPS walk

We forecast 1Q20 EPS of $1.14 compared to 1Q19 results of $1.24 and consensus estimates of $1.24. While our estimates are below consensus and down -3% YoY it includes -$0.08 of negative weather est in the quarter. With rate cases in the Carolinas/IN expected to be implemented in 2H and potential cost cuts upwards of $0.16/sh we see the ability to hold the line of 2020 guide.

- **Key drivers**: Positive YoY drivers include the implementation of rates and riders at the electric utilities (+$0.08), the wholesale contract moving to formula rates (+$0.01), new rates at Piedmont (+$0.04), AFUDC on Atlantic Coast Pipeline (+$0.01), other gas utility growth (+$0.01), Offsetting results are regulatory lag (-$0.04), impacts from COVID on load growth (-$0.02), the tax true-up reversal at the gas segment (-$0.06), higher interest expense (-$0.01), preferred coupon interest expense (-$0.04), share dilution (-$0.01), and increased O&M expense due to the Feb. storms in the Carolinas (-$0.03).

- **Unknowns**: Weather is expected to be unfavorable driver in the quarter with HDDs 20% below the norm and 15-18% below the prior year, although slightly offset by more favorable CDDS; the exact magnitude is unclear. Another unknown impact is the decline in load growth from COVID19; while mgmt. provides sensitivity that every 1% decline in load equates to a $0.15/sh impact with industrial load ~20% of retail sales, which has lower margins compared to the other customer classes and Commercial load ~30% of retail, and the ~15% from wholesale, the exact extent of the decline is difficult to discern in 1Q. Further, it remains unclear if the company was able to bend the cost curve on O&M costs, which could be a potential offset, although likely to show up in 2Q.

Table 20: DUK 1Q20 EPS walk

DUK 1Q20 Earnings Walk	EPS
DUK 1Q19 EPS	1.24
Weather - normalize from 1Q19	$0.06
Weather- 1Q20	-$0.11
Electric	$0.03
Rate implementation:	
DEC SC rates (full quarter)	$0.01
DEP SC rates (full quarter)	$0.01
Florida - multi-year plan	$0.01
SOBRA - FL	$0.01
Other Riders - IN and OH	$0.04
Regulatory lag	-$0.04
Load Growth - 1%	-$0.02
AFUDC equity	$0.00
Wholesale - fixed to formula rates	$0.01
Gas	$0.00
LDC Growth	$0.01
New Rates - PNY	$0.04
AFUDC for ACP	$0.01
Tax true-up reversal	-$0.06
Renewables	$0.00
Palmer (60MW) – 2Q in-service	$0.00
Other	-$0.08
O&M - Feb. storms	-$0.03
Interest expense	-$0.01
Other - preferred	-$0.04
Dilution	-$0.01
DUK 1Q BofAe Adjusted EPS	$1.14
Consensus	$1.25
BofAe 2020 EPS	5.21
Guidance	5.05-5.45
2020 Consensus	5.17
DUK 1Q20 Shares Outstanding	732
DUK 1Q19 Shares Outstanding	728
Tax Rate	12%

Source: BofA Global Research estimates, company report, Bloomberg

Bending the O&M cost curve

Given the potential implications from a decline in load with the electric utility largely exposed as several C&I customers have announced closures in its service territory (see further below), we expect mgmt. to look to mitigate these impacts through reductions in O&M. While the company has not yet announced these mitigating measures, we look back to 2017 where weather was a severe headwind with mgmt. able to offset that by $100-150mn in cost reductions. We could very well see mgmt. announce similar cost reductions (relative to flat growth yoy) that would result in a $0.11-$0.16/sh EPS benefit in 2020 to offset (or at least partially) the below headwinds to load. Additionally, mgmt. executed on pulling cost forward with favorable weather last year, including $0.04/sh for foundation giving that could be a benefit as well. While details on where these O&M levers are going to come from have yet to be disclosed, we look forward to additional commentary from mgmt. to see if these are more transitory (i.e. at the utility level) or through sustainable corp. overhead reductions. Net-net, we see this as a positive as it would be able to offset headwinds from load this year.

Load growth considerations and decoupling

DUK's electric utilities & infrastructure jurisdiction (~83% of 2020 adjusted EPS contribution according to guidance) does not have decoupling and is much more exposed to load. On a sensitivity basis, every +/- 1% change in electric load across all customer classes equates to +/- $0.15 change in EPS. Note DUK's industrial load is ~20% of its retail business, which has lower margins compared to the other customer classes driving a lower impact to EPS ($0.02/sh for every 1% change). Commercial load accounts for ~30% of retail, residential is ~35% and the remaining ~15% is wholesale. As we've mentioned before, the residential market may be set up to benefit from COVID-19 as people continue to self-quarantine in their homes (especially true as we enter peak

cooling demand with more residential customers utilizing air conditioning). We also highlight that wholesale represents 15% of its load with every 1% load loss in retail, equating to $0.02-0.03/sh impact to EPS; although this is likely overestimating the impact to some extent as its largest wholesale customers in the Carolinas are residential. Also, the impact for wholesale would only impact the current year as volumes get reset in the following year's rates automatically.

While mgmt. is still assessing the impacts to load, there have been several announced closures in DUK's service territory: BMW in NC and Fiat in IN announced closures in mid-march while many schools and small businesses have also announced closures. See our assumptions below for potential headwinds to EPS from a 2% decline in load (w/ a partial offset by 0.5% increase in residential load), although see this offset in part from increased O&M cost cuts.

Table 21: DUK EPS Load Sensitivity and Assumptions

DUK Load Sensitivity	Every 1% change	Assume 2% decline in load (ex-residential)
Industrial	$0.02	-$0.04
Commercial	$0.05	-$0.09
Residential	$0.09	$0.04
Wholesale	$0.03	-$0.05
Total Headwind		-$0.14

Source: BofA Global Research estimates, company report

Gas LDC's decoupled in NC with weather normalization in SC/TN

On the positive side, most of DUK's gas jurisdiction is decoupled or has weather normalization with only about 9% of total gas earnings exposed to load (~91% of Gas Utilities & Infrastructure business has mostly fixed margins). Piedmont is fully decoupled in North Carolina (75% of Piedmont gas business). South Carolina and Tennessee have weather protection only (25%). From an earnings contribution standpoint Gas Utilities & Infrastructure only accounts for ~12% of 2020 adj. EPS or ~10% excluding ACP's EPS per DUK's latest guidance.

Bad debt expense and recovery of COVID costs

DUK has a bad debt expense rider in Piedmont for fuel expenses (60% of the bill) and a full rider for all bad debt expense at Duke OH gas and electric. For Duke Ohio, bad debt expense is collected through annual uncollectible riders for both the gas and electric businesses, with true-ups. For the Piedmont businesses, these are collected in the fuel rider, and mgmt. can update the fuel costs as often as it needs, although tends to do it every six months driven by under or over-collection status as the cost of natural gas changes. For the other jurisdictions, mgmt. will be tracking incremental bad debt expenses and other COVID-19 related expenses, and if significant, would explore regulatory asset treatment similar to other extraordinary costs when material to the respective utility. *While the majority of the business does not have a bad debt expense rider/mechanism we continue to see a relatively minimal impact from incremental costs associated with bad debt: for context, the company experienced $20mn of incremental bad debt during the 2008/2009 financial recession, which would translate to $0.02-$0.03/sh today (assuming inflationary increase in today's dollars).*

NC rate cases remain key to watch: ROE and coal ash

We continue to expect DUK's rate case in the Carolinas to have a similar outcome to Dominion's coal ash order potentially further cautious for earned/recoverable ROEs where we already assume $0.10-$0.13/sh eventual drag. Further, we expect the ROE to be litigated in the Duke Energy Progress (DEP) case with intervenor testimony on April 13th likely to give further indication of staffs issue with ROE given the wide discrepancy between parties on the current interest rate environment and cost of capital (which has rebounded precipitously for DUK of late). Rate cases remain cautious although see risks of the negative revisions priced-in/largely known.

EPS estimates

We provide our EPS estimates below and see a 4.5% CAGR through '24 with estimates slightly below street and mgmt. guide for 5% growth at the mid-point. See headwinds in 2020 despite sizeable O&M reductions given weather headwinds and reduction in load. We don't expect a guidance cut to be clear with '20 despite 1Q pressures, particularly considering cost levers. DUK appears among the most confident in sourcing these offsets across the sector.

Table 22: DUK EPS Estimates: looking for consensus ests to come down a touch

EPS Estimates	2018A	2019A	2020E	2021E	2022E	2023E	2024E
Electric							
Carolinas	1.65	1.95	1.88	1.94	2.02	2.10	2.20
Indiana	0.57	0.60	0.61	0.62	0.65	0.67	0.69
Ohio - Electric	0.26	0.22	0.25	0.25	0.28	0.31	0.35
Progress- Carolinas	1.02	1.12	1.16	1.16	1.19	1.22	1.24
Progress- Florida	0.81	0.96	0.97	1.02	1.05	1.09	1.10
Commercial Transmission	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Eliminations	0.39	-0.04	0.00	0.00	0.00	0.00	0.00
Consolidated Earnings	4.70	4.81	4.86	4.99	5.19	5.38	5.58
Guidance		4.77	4.94				
Gas							
Ohio - Gas	0.13	0.12	0.14	0.16	0.19	0.20	0.21
Piedmont (PNY)	0.23	0.27	0.31	0.33	0.37	0.41	0.45
Midstream Pipelines	0.02	0.23	0.23	0.29	0.23	0.25	0.25
Eliminations	0.06	0.00	0.00	0.00	0.00	0.00	0.00
Consolidated Earnings	0.45	0.62	0.68	0.79	0.78	0.85	0.91
Guidance		0.51	0.72				
Commercial Renewables	0.14	0.27	0.33	0.33	0.30	0.28	0.29
Guidance		0.32	0.33				
Parent/Other	-0.57	-0.64	-0.73	-0.65	-0.60	-0.56	-0.53
Guidance		-0.60	-0.73				
Adjustments							
BofAe EPS	4.72	5.06	5.14	5.45	5.67	5.95	6.24
Previous Estimates		*5.06*	*5.21*	*5.45*	*5.67*	*5.95*	*6.24*
Guidance	4.65-4.85	*4.95-5.15*	*5.05-5.45*				
Consensus	4.76	5.02	5.16	5.47	5.70	5.97	
Mgmt EPS CAGR: 4-6% from 2019-2023E		5.00	5.25	5.51	5.79	6.08	6.39
Low End		4.80	5.05	5.41	5.62	5.85	6.08
High End		5.20	5.45	5.62	5.96	6.31	6.69
BofAe CAGR '19-'23e						4.5%	
BofAe CAGR '19-'24e							4.5%

Source: BofA Global Research estimates,, Bloomberg, company filings

Valuation: PO of $93

Our PO of $93 based on our latest EPS estimates and mark to market of peer utility multiples of 17.9x for gas and electric. Ability to turn the narrative in the NC jurisdiction would clearly help shares to re-rate on DUK shares although still look for execution.

Critically, the ability to implement PBR (Performance Based Rates) potentially in exchange for implementation of an ROE band/and or multi-year stay out of rate cases appears increasingly likely and among a handful of understated emerging positive trends for shares. We anticipate further discussion albeit beyond the scope of the near-term pressures and Covid related concerns.

Table 23: DUK SOTP Valuation

Duke Energy Sum of the Parts Valuation
2022E
All figures in $Mn except per share

	Metric	P/E Multiple						Equity Value	
	2022E EPS	Low	Peer	Prem/ Discount	Base	High		Low	Base	High
Group Peer Multiple - Electric	-	-	17.9x	-	-	-	-	-	-	-
Group EPS '18-'22 CAGR - Electric	-	-	5.00%	-	-	-	-	-	-	-
	-	-	-	-	-	-	-	-	-	-
Electric Utilities			18.8x							
Duke Energy Carolinas	$2.02	17.8x		0.0x	18.8x	19.8x		$36.02	$38.04	$40.07
Duke Energy Progress/Carolinas	$1.18	17.8x		0.0x	18.8x	19.8x		$21.07	$22.26	$23.44
Duke Energy Florida	$1.05	18.8x		1.0x	19.8x	20.8x		$19.80	$20.86	$21.91
Duke Energy Indiana	$0.65	18.8x		1.0x	19.8x	20.8x		$12.13	$12.77	$13.42
Duke Energy Ohio/Kentucky	$0.28	17.8x		0.0x	18.8x	19.8x		$4.98	$5.26	$5.54
Total Electric Utility Value	$5.19							$94.01	$99.19	$104.38
Group Peer Multiple - Gas			17.9x							
Group EPS '18-'22 CAGR - Gas			5.10%							
Gas Utilities	2022E EPS		18.8x							
Duke Energy Piedmont	$0.37	18.8x		1.0x	19.8x	20.8x		$6.88	$7.25	$7.61
Duke Energy Ohio/Kentucky Gas	$0.19	18.8x		1.0x	19.8x	20.8x		$3.53	$3.71	$3.90
Total Gas Utility Value	$0.55							$10.41	$10.96	$11.51
Commercial Segment	2022E EBITDA									
Midstream Infrastructure:							Weight			
ACP	$407	8.0x	9.0x	0.0x	9.0x	10.0x	50%	1,627	1,831	2,034
Add back ACP debt							50%	942	942	942
All Other	$61	8.0x	9.0x	0.0x	9.0x	10.0x		492	553	614
Transmission Segment	$6	8.0x	9.0x	0.0x	9.0x	10.0x		52	58	64
Segment Net Debt	-$5,055							-5,055	-5,055	-5,055
Add back Renewable Debt	$1,088							1,088	1,088	1,088
Renewables Segment NPV @ 8% Discount	$1,291							1,291	1,291	1,291
New Renewables NPV	$471							471	471	471
Net Infrastructure Equity								909	1,181	1,452
Net Infrastructure Equity Per Share								$1.25	$1.53	$1.99
Parent	2022E EPS									
NMC (Saudi Chemical JV)	$0.05	11.8x		-6.0x	12.8x	13.8x		$0.59	$0.64	$0.69
Parent Interest attributed to utility - 50%	-$0.60	20.2x		0.0x	19.2x	18.2x		-$6.08	-$5.78	-$5.48
Parent Debt- 50%	-$21,165							-$13.71	-$13.71	-$13.71
Total Equity Value								-$19.20	-$18.85	-$18.50
Shares Outstanding									772	
Total Equity Value								$86.00	$93.00	$99.00
Current Share Price								$90.10	$90.10	$90.10
NTM Dividend Yield									4.25%	
Total Return									7.47%	

Source: BofA Global Research estimates, company report, Bloomberg

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Title: Subtitle	Primary Author	Date Published
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Duke Energy: Upgrading to Neutral: Raising the bar with an improved regulated outlook	Julien Dumoulin-Smith	14 February 2020
Duke Energy: Raising the Ratebase & other nuances	Julien Dumoulin-Smith	13 February 2020

DTE Energy

We forecast 1Q20 adjusted EPS of $1.80 vs. $2.05 in 1Q19 and $1.98 consensus. Our estimate is well below last year's result due to this quarter's unique combination of weather, Covid impacts, and reversals of one time items. We expect consensus estimates to be revised substantially lower going into the Q1 print. We stress non-reg continues to garner disproportionate attention relative to its modest implied value after multiple contraction in midstream sector. We see shares as entirely fairly rated vs. peers (earlier shares offered a double-digit total return on utility-only values).The strategic question embedded is just how to view non-regulated when netting parent level debt against these businesses (with their depressed trading multiples/valuations of late). We appreciate that this is principally a consideration of debt allocation (ascribing some of the holdco debt to the utility or not), but with just ~$2/sh out of $100+/sh stock (<2% of total value), we sense overly focused Street on very limited side of biz.

- **Key Drivers:** Primary drivers include weather which is an 8 cent drag from normalizing 2019 results and a further 17 cent drag given heating degree days (HDD) 16% below normal. Q1 2017 saw a weather impact of similar magnitude with corresponding drag of $13m at the electric utility. We likewise assume weather-related drag of 10 cents at the gas utility given that the HDD deviation from normal was -16% in 2020 vs. +5% in 2019. We additionally assume 1 cent drag at both the electric and gas utilities stemming from demand impact of Covid – this impact is expected to be modest given the timing of shut down orders in late March. We continue to incorporate the impact of new electric rates which went into effect in May 2019 along with correspondingly higher D&A and interest expense. While DTE mgmt. has flagged its previous expectation to utilize financial contingency to mitigate impacts of weather on its utility results, we expect a partial offset to weather impact (and none to Covid impact) in Q1 due to timing.

- **Unknown:** Precise weather-related impacts are difficult to estimate although we see Q1 2017 as a comparable period (albeit with fewer storm expenses). Covid-related demand shifts in late March are expected to show an increase in residential load and a larger (in % terms) decrease across both commercial and industrial (C&I). The Energy Trading business is difficult to forecast owing to the opaque nature of its operations – given significant volatility across most asset classes in the quarter there is potential for an above/below normal quarter, although we do not incorporate this into our estimates.

Table 24: DTE Q1 earnings walk

DTE Energy 1Q20 Earnings Walk	EPS
Adjusted EPS 1Q19	$2.05
Utility	($0.16)
Electric	
Weather - return to normal	($0.03)
Weather - 1Q20	($0.07)
2019 GRC - $273mn effective 5/9/2019	$0.29
D&A, Interest, Other expenses	($0.13)
O&M savings vs. last year	$0.04
Sales impact	($0.01)
OID benefit from investment earnings - 17m gain	($0.09)
Gas	
Weather - return to normal	($0.05)
Weather - 1Q20	($0.10)
D&A, Interest, Other expenses	($0.02)
O&M	$0.02
Sales impact	($0.01)
Tax timing true up from Q1 2019	($0.05)

Table 24: DTE Q1 earnings walk

DTE Energy 1Q20 Earnings Walk	EPS
Non-utility business	($0.03)
GSP	$0.02
P&IP	$0.01
ET	$0.00
Corp & Other	($0.06)
Dilution	($0.06)
1Q20E Adjusted EPS	$1.80
1Q20E Consensus	1.98
2020E BofAe EPS	$6.56
2020E Consensus	6.60
2020 Guidance Midpoint	6.61
Shares Outstanding 1Q19	183
Shares Outstanding 1Q20	188

Source: BofA Global Research Estimates, company report, Bloomberg

Milder weather compounding Covid slowdown in Q1

Q1 2020 was substantially warmer in DTE's service territory than normal, with heating degree days (HDDs) 16% below average levels. The last time the service area experienced conditions with the same order of magnitude deviation from normal was Q1 of 2017 when HDDs 14% above normal created a $13m drag at the electric utility. We also assume that the weather-related drag on the gas business was 10 cents in Q1 2020, as compared to a 5 cent benefit in 2019. The effects of milder weather in 2020 are compounded by the fact that 2019's positive weather result of 5 cents gas and 3 cents electric is being reversed. We expect that DTE mgmt. should be able to utilize its financial contingency to offset a significant portion of weather-related impact in 2020 *throughout the course of the year*, though given timing of warmer months in Q1 we expect a partial offset of weather drag in the quarter, with further mitigation likely in Qs 2-4 through management of timing of O&M expenditures being the primary lever. We note that Q2 is typically a shoulder quarter with relatively low weather impact, while Covid-related slowdown is expected to affect demand in the quarter disproportionately – see more below.

Covid impact on load – Q2 seen most affected

DTE's latest disclosures include earnings sensitivity for all customer classes to a 1% swing in demand. As with most public utilities, residential sales provide the highest margin at $15m annual impact, followed by commercial ($6m), industrial ($1m), and other ($2m). These sensitivities assume a flat 1% impact to demand over the course of a full calendar year. Though DTE has not provided March demand impact by customer class, initial commentary from peer utilities suggests a trend of residential growth in the mid-single digits serving as a partial offset to commercial and industrial sales that decline by 10-15%. Assuming that DTE Electric sees a gain of 5% residential demand and a drop of 15% across the other customer classes through the entirety of Q2, we estimate an earnings impact of -$15m, or 1.2% of DTE's 2020 earnings guidance at the midpoint ($1,270m). Note this is an illustrative case and DTE has not provided demand estimates, and actual demand will vary depending on when Covid stay-at-home restrictions are lifted.

Table 25: DTE electric demand impact

Flat 1% annual impact

Customer type	Sensitivity (%)	Annual earnings impact ($m)
Residential	-1.0%	15
Commercial	-1.0%	6
Industrial	-1.0%	1
Other	-1.0%	2
Total		24
2020 guide midpoint		1,270
Decline impact		-1.9%

Q2 demand shock illustrative

Customer type	Sensitivity (%)	Annual earnings impact ($m)
Residential	5.0%	19
Commercial	-15.0%	(23)
Industrial	-15.0%	(4)
Other	-15.0%	(8)
Total		(15)
2020 guide midpoint		1,270
Decline impact		-1.2%

Source: BofA Global Research Estimates, company report, Bloomberg

We note that DTE's utilities entered 2020 well-positioned with mgmt. touting significant financial contingency that would enable the company to "nail it" in both the electric and gas business – in fact the company reiterated 2020 guidance in March as the Covid pandemic shock was spreading. We expect that mild Q1 weather combined with Covid impact will weigh on earned ROEs in 2020, with the impact partially but not completely offset via O&M management by utilizing the financial contingency built up in 2019. We therefore reduce our forecast for earned ROEs in 2020 at both the electric and gas utilities to 9.9% from 10.0%; note that we had previously reduced our authorized and earned ROE forecast at both the electric and gas utilities for 2021+ to reflect risk around authorized ROEs from the persistent low interest rate environment. With our reduced estimates, we still see the electric and gas businesses achieving results near the low end of mgmt.'s reaffirmed guidance range – with a protracted demand impact related to Covid as the most pressing near-term risk.

Table 26: Utility ROEs incrementally lower in 2020 on weather/Covid

ROEs							
Authorized	2018A	2019A	2020E	2021E	2022E	2023E	2024E
DTE Electric	10.0%	10.0%	10.0%	9.9%	9.9%	9.9%	9.9%
DTE Gas	10.0%	10.0%	10.0%	9.9%	9.9%	9.9%	9.9%
Earned							
DTE Electric	9.8%	10.0%	9.9%	9.9%	9.9%	9.9%	9.9%
DTE Gas	9.5%	10.5%	9.8%	9.9%	9.9%	9.9%	9.9%

Source: BofA Global Research Estimates, company report

Table 27: Utilities still expected to hit guidance range in short + long term: we could readily see upside still

Net Income ($Mn)							
Utility segment	2018A	2019A	2020E	2021E	2022E	2023E	2024E
DTE Electric	669	716	761	830	901	951	1,002
Guidance		*703-717*	*759-773*				
Growth	8%	7%	6%	9%	9%	6%	5%
Guidance CAGR '20-'24		*7-8%*					
BofAe CAGR '20-'24		7.1%					
DTE Gas	159	181	188	206	230	251	265
Guidance		*175-183*	*185-193*				
Growth	7%	14%	4%	9%	12%	9%	6%
Guidance CAGR '20-'24		*9.0%*					
BofAe CAGR '20-'24		8.8%					

Source: BofA Global Research Estimates, company report

Electric rate case decision expected by early May

Under Michigan state law, the commission is required to issue a final decision in the pending rate case within 10 months of the filing, by May 8. The commission has not yet indicated whether it may extend the timeline due to the Covid emergency and staff resources likely focused on ensuring that gas and electric service continues uninterrupted. DTE Electric filed a request for a $343m increase premised on a 10.5% ROE and $18.2B rate base. Staff countered with a recommendation for an increase of $195m, a 9.8% ROE, and $18.1B rate base. Recently, the administrative law judge (ALJ) handling the case issued a recommendation for a rate increase of $99.8m based on an ROE of 9.8% and rate base of $17.1B. At issue in the ALJ recommendation which supports the position of intervener the Association of Businesses Advocating Tariff Equity (ABATE) which claims that DTE's prepaid pension asset of ~$800m be excluded from the working capital portion of rate base as DTE did not establish that the pension asset was fully funded by investor capital or that it provides benefits to ratepayers. This is an area where the ALJ disagrees with commission staff, which approved the inclusion of the asset in rate base in the previous rate case (U-20162) but directed DTE to provide additional evidence that the asset should be included in working capital including the source of the funding of the prepaid pension asset in the current filing. DTE's testimony

asserts that the pension asset is 1) reasonable and prudent as it reduces ongoing pension costs and 2) it contributes to an increased deferred tax component in DTE Electric's weighted average cost of capital, reducing overall cost. The ALJ concludes its argument stating that DTE made "no effort whatsoever" to demonstrate that the entirety of the prepaid pension asset was supplied by investors rather than ratepayers.

Below we include a summary of the rate base impact from the ALJ proposal as compared to both DTE's request and commission staff proposal. Staff's recommendation for approved rate base was generally in line with the company's request, which stands to further highlight the degree to which the ALJ recommendation stands out in proposing to exclude the pension asset.

Table 28: Rate base recommendations

DTE projected rate base ($m)

	DTE	ALJ	Delta	Staff
Net plant	16,775	16,514	(261)	
Working capital	1,392	582	(810)	
Total rate base	18,167	17,096	(1,071)	18,120

Source: MPSC docket #U-20561

Based on intervener, staff, and the ALJ's filings, three outcomes are possible with respect to the pension asset:

- **Accept ALJ recommendation without modification.** In the event that the commission were to accept the ALJ/ABATE position, DTE Electric's revenue requirement would be reduced by $56.8m according to company filings.
- **Accept ALJ recommendation with the modification that pension expense be adjusted which results in higher recovery through rates.** DTE's rebuttal filing claims that to exclude the pension asset without considering the impact on expense is unfairly punitive. The company claims that if the pension asset were excluded from rate base, the pension expense should be increased correspondingly (by $58m per DTE calculation) which would subsequently be recovered in rates, resulting in a largely revenue-neutral outcome.
- **Reject ALJ recommendation – status quo outcome.** This option would not affect the treatment of the pension asset on working capital and DTE would continue to recover. Notably this position is supported by commission staff in docketed reply to exceptions.

Midstream: will gas price recovery de-risk prospects post contracts?

We maintain our forecast in DTE's midstream business, seeing ~9% earnings growth through 2024 from the midpoint of 2020 guidance which already bakes in a ~30% increase over 2019, driven mainly by the full-year contribution of the Momentum midstream assets purchased in Q4 of 2019. Post 2020 growth in the segment is driven primarily by the placing in service of a gathering pipeline at Momentum (late 2020 in-service) as well as continued investment in compression and other organic growth initiatives at NEXUS, Link, and other "legacy" midstream assets.

We likewise maintain a balanced view on DTE's exposure to Indigo Natural Resources, its primary counterparty in the Haynesville basin. Indigo maintains relatively low leverage for its sector (~1.0x EBITDA post-transaction). *Critically, we see the potential for gas price appreciation into the future as offsetting our otherwise concerns embedded on volume related concerns in coming years. For now we see volume-related concerns and broader midstream concerns raised by many investors as simply less relevant given where shares are priced.*

The company is largely hedged forward for its projected 2020 production, with some 2021 volumes hedged as well - while commodity price risk exists given ongoing supply-demand imbalance in US basins, we note Indigo mgmt. appears to be prudently hedging its forward exposure amid an uncertain price environment. We note DTE maintains minimum volume commitments (MVCs) with Indigo covering 90% of its expected volume from the Haynesville basin through 2020, with volume growth covering the remaining 10% of company forecast revenue - note forward sales by Indigo suggest performing under the MVCs should be an achievable goal in the near term.

Bottom line: the market has discounted DTE shares to the point where they trade with little implied value in the midstream business. We stress that investor attention here is disproportionate given healthy utility earnings visibility through the forecast despite near term risks.

EPS Estimates

We previously updated our 2020 estimates to reflect lower earned ROEs of 9.9% at the Electric and Gas utilities (10.0% previously). Our new consolidated 2020 estimate of $6.56 is below the midpoint of the $6.47-6.75 range recently reiterated by mgmt. We continue to see the long-term outlook as largely intact, having previously reduced our earned ROE assumption at the Electric and Gas utilities to 9.9% to reflect rate case risk in a low rate environment. Our updated 2020 estimate is several cents below Street though we stress downside to consensus estimates as the effects of Covid become more fully integrated in forecasts. We also highlight that earnings from the Energy Trading business may exhibit more volatility in the short term, though we continue to forecast a growth trajectory in line with previous mgmt. guidance given the opaque nature of the segment.

Table 29: EPS estimates

Earnings Contribution	2018A	2019A	2020E	2021E	2022E	2023E	2024E
DTE Electric	3.70	3.87	3.96	4.28	4.56	4.57	4.80
DTE Gas	0.88	0.98	0.98	1.06	1.17	1.21	1.27
Total utility	4.57	4.85	4.94	5.34	5.73	5.77	6.07
Non-utility segment							
Gas Storage & Pipeline	1.29	1.15	1.46	1.63	1.81	1.84	1.94
Power & Ind. Products	0.90	0.72	0.72	0.79	0.45	0.53	0.63
Energy Trading	0.22	0.16	0.11	0.13	0.15	0.16	0.16
Corp & Eliminations	(0.67)	(0.58)	(0.65)	(0.71)	(0.72)	(0.67)	(0.64)
% of total	*-11%*	*-9%*	*-10%*	*-10%*	*-10%*	*-9%*	*-8%*
Total non-utility	1.73	1.45	1.64	1.85	1.69	1.87	2.09
DTE Consolidated	6.30	6.31	6.56	7.17	7.40	7.63	8.14
Guidance	*0.00*	*6.02-6.38*	*6.47-6.75*				
Prior Estimates		*6.31*	*6.65*	*7.21*	*7.44*	*7.68*	*8.20*
Consensus		6.24	6.60	7.07	7.48	7.82	
			4.0%				
DTE Guidance 6% CAGR ('20-24)			6.61	7.01	7.43	7.87	8.34
Low End				6.94	7.29	7.65	8.03
High End				7.07	7.57	8.10	8.66
BofAe CAGR '20-'24e		5.3%					
Shares outstanding	*181*	*185*	*192*	*194*	*197*	*208*	*209*

Source: BofA Global Research Estimates, company report, Bloomberg

PO to $112; reiterate Neutral

We view risks around DTE's growth story as balanced, given the premium utility growth seen in the forecast period as balanced by less certain midstream outlook, primarily driven by single counterparty exposure at Blue Union. DTE's updated long-term guidance calls for operating EPS growth at a 5-7% CAGR from the midpoint of 2020's initial guidance of $6.61. Our updated forecast results in a 2020-2024 consolidated EPS CAGR of 5.3%, near the midpoint of mgmt's range. We apply peer group multiples of 17.6x for both the electric and gas utilities (previously, 17.9x/17.9x for electric and gas,

respectively), 8.0x midstream EBITDA multiples to the cogen/legacy coke battery and GSP businesses, a lower 6x EBITDA multiple to the Energy Trading business to reflect its lower-quality earnings profile, and an NPV valuation to the RNG development opportunity which yields an implied EBITDA multiple of 6.8x. We also tweak our valuation discount for the Momentum Midstream biz to -2.0x to reflect ongoing risk around producer activity in US shale basins. With these assumptions our resulting $112 PO reflects high single digit upside potential and we remain Neutral.

Table 30: DTE SOTP

DTE Energy Segments	2022E EPS	Premium /(Discount)	Group Multiple	Applied Multiple	Value
Utility					
Group Peer Multiple - Electric			17.6x		
Group EPS '18-'22 CAGR - Electric			5.00%		
DTE Electric (Distribution)	$4.56	1.0x	18.5x	19.5x	$88.92
Group Peer Multiple - Gas			17.6x		
Group EPS '18-'22 CAGR - Gas			5.10%		
DTE Gas	$1.17	1.0x	18.5x	19.5x	$22.73
Utility Equity Value per Share					$111.65

Non-Utility	2022E EBITDA	Premium /(Discount)	Group Multiple	Applied Multiple	
P&I					
Cogen + Legacy Coke Batteries	79	-2.0x	8.0x	6x	$477
NPV of RNG Development	$558		Implied Multiple ---->	6.8x	$558
REF Tax Credit Value (DCF), 2020-2023 @ 6%	198				$198
Energy Trading	44	0.0x	6.0x	6x	$263
Midstream (GSP)	885	-0.7x	9.0x	8x	$7,313
Allocated EBITDA	560	0.0x	9.0x	9x	$5,038
Momentum Midstream	$325	-2.0x	9.0x	7x	$2,275
Holding Company Borrowings					
Consolidated Projected B/S					20,313
(-) DTE Gas / DTE Electric Debt					(11,758)
Net Non-Utility Net Debt					8,554
Non-Utility Equity Value					$254
Shares Outstanding					197
Non-Utility Equity Value per Share					$1.29

	2022E EPS	Premium /(Discount)	Group Multiple	Applied Multiple	
Corp & Other (ex-Interest Expense)	(0.05)	0.0x	19.5x	19.5x	($0.98)
Utility Equity Value per Share					($0.98)
12 Month Price Objective					$112
Implied Consolidated P/E					17.8x
Dividend Yield NTMe					3.9%
Estimated Total Potential Return					9.7%
Shares outstanding by 2022					197

Source: BofA Global Research estimates, company report, Bloomberg

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DTE Energy: Angling for a utility-only value for one that can 'nail it'?	Julien Dumoulin-Smith	09 March 2020
DTE Energy: Poised to deliver in '20, but earnings quality concerns persist	Julien Dumoulin-Smith	07 February 2020

Edison International (EIX)

EIX shares have underperformed the broader utility index since early March (-4% vs XLU) despite decoupling and other regulatory mechanisms to offset COVID related pressures given still $800mn in pending equity needs. While we see recent moves by mgmt. to allow for delay of equity issuance into 2H, potentially allowing for the broader market to recover we remain focused on the total quantum of equity needs to right-size the balance sheet. The '20 equity addresses mgmt.'s current expectations for wildfire related liabilities and timely recovery of memo accounts ($1.09bn in aggregate); we believe clarity on these outcome remain protracted and uncertain at best. With shares trading at a 30% discount to the group (20% after adjusting for potential for additional dilution), we sense investor optimism that shares can close the gap and re-rate to some extent. Nonetheless, we remain sober on these prospects pending clearer articulation of equity from mgmt. and maintain our Neutral rating.

1Q20 EPS walk

We forecast 1Q20 EPS of $0.81 compared to 1Q19 results of $0.63 and consensus estimates of $0.77.

- **Key drivers**: Positive YoY drivers include increase FERC and CPUC core contribution (+$0.16), lower O&M expenses (+$0.04), energy efficiency benefits, and higher financing and other benefits, including lower D&A (+$0.08).
- **Unknowns**: We highlight uncertainty with O&M expenses as it continues to be somewhat challenging to handicap given the company will defer costs that are over and above the authorized limit; with $0.14 drag of O&M expected in 2020 compared to $0.25 drag in 2019, we expect a positive variance in 1Q20 and highlight that much of the accelerated covered conductor program occurred in 1H19 last year and not necessarily the same cadence this year. Another unknown item is just how much equity of the $800mn in 2020 guidance has been issued to date; we assume none given the state of equity markets with the issuance likely deferred to 2H20.

Table 31: EIX 1Q20 EPS walk

Edison Electric 1Q20 Earnings Walk	EPS
Edison Electric 1Q19 Adjusted EPS	$0.63
SCE	$0.25
FERC ROE & RB Growth	$0.01
CPUC RB Growth and 52% Equity Cap	$0.15
O&M Effect	$0.04
Depreciation	$0.00
Property Taxes	$0.00
Energy Efficiency	$0.02
Wildfire Mitigation Costs	($0.04)
Interest expense for fund contribution	($0.03)
Financial and Other benefits	$0.08
EIX Parent and Other	($0.07)
HoldCo Drag	$0.00
Dilution	($0.07)
1Q20E Adjusted EPS	$0.81
1Q20 Consensus	$0.77
2020 BofA EPS	$4.45
2020 Consensus	$4.48
2020 Guidance	4.32-4.62

Source: BofA Global Research estimates, company report, Bloomberg

Pending equity needs: waiting on more certainty

The recent $800mn term loan that EIX drew down on likely provides flexibility with the timing of EIX's pending equity issuance ($600mn of "new" equity + $200mn on ATM). While the '20 equity addresses mgmt.'s current expectations for wildfire related liabilities, timely recovery of memo accounts ($1.09bn in aggregate), and a clarity on

these outcome remain protracted and uncertain (mgmt.'s confidence remains a tad cryptic). The recent ALJ approval of the capital structure waiver is just one piece to the puzzle to gain more clarity on forward looking equity assumptions.

Capital structure waiver approved by ALJ

The Administrative Law Judge (ALJ) issued a proposed decision (PD) approving the applications of EIX for the waiver of the capital structure. The ALJ recommended: 1) approve the waiver for *two years* or until the CPUC determines cost recovery for '17/18 wildfire events, whichever comes first (we expect some migration to HoldCo debt through this period likely); 2) limit the scope of exclusions to non-cash charges and debt issuance equal to or less than the aggregate net non-cash charges stemming from the '17/18 fires; and, 3) SCE should be required to submit an advice letter stating it has returned to its authorized cap structure or a timeline/plan over which SCE will return 90 days after the CPUC determines cost recovery of '17/18 fires. The ALJ also recommended EIX should notify the CPUC if its equity ratio declines 1% or more from most recent level reported. *We perceive the terms of approval as adding pressure to provide a clear(er) view of equity needs in parallel to Street - albeit with substantial uncertainties may just provide a transition to HoldCo rather than net increase in equity to pay down OpCo debt that waiver would support for two-years.*

For EIX, the approval would represent one of three steps needed to keep $600mn of 2020 equity needs to address wildfire related costs intact. The other criteria include no movement in the wildfire liability of $4.9bn and cost recovery of $1bn in memo accounts (as well as those associated with 2020). We reiterate our uncertainty on total equity needs but see two-year transition as likely tied to a shift in debt rather than further equity (as best we read prior commentary from mgmt), but this remains unclear (as mgmt has specifically qualified equity contemplated thus far is strictly for 'core' purposes for minimal needs on ongoing basis).

Tracking the memo recovery

Mgmt. recently filed its 2019-2019 Fire Memorandum Account (FMA) update, which initiated track 2 of the 2021 General Rate Case (GRC) proceeding. The company is seeking recovery of $509mn of O&M related expenses and $302mn of capital spending. This is considered track 2 of its memo recovery request with a decision not expected until 1Q21 with the GRC. The more near-term item is from the GSRP with a decision expected in April 2020, although again these costs are not similar to the other memo accounts and is more related to capital spending rather than O&M with the latter having a bigger impact on cash flows. The other items pertain to a decision with Wildfire Memorandum Expense Account (WEMA) for higher insurance cost vs. those approved (requesting $505mn in recovery) with a decision expected in Aug. 2020 and the (Catastrophic Event Memorandum Account) CEMA with a decision in March 2021 (for $88mn request).

We stress that this does not include 2020 costs that mgmt. will file at YE w/ a decision in ’22 (potentially growing by $200-300mn incremental). Currently, mgmt. is deferring these costs, although it’s not getting any cash recovery, hence the impacts to credit metrics. We continue to see uncertainty around these items and look for more clarity in the coming months to understand the totality of equity needs as mgmt. has its own internal planning assumptions around recovery.

Bottom line, recovery clarity could still take some time and we continue to see some risks on recovery (whether with the ~$120 mn of recoveries not necessarily tied to precedence or the ~$500Mn of additional insurance expenditures tied to last year that mgmt. did not receive approval for in its last rate case).

Table 32: EIX Wildfire Memorandum Accounts

Memorandum Account	Capital Expenditure	O&M Spent	Total Request	Timeline
Wildfire Mitigation Plan	302	304		PD 1Q21
Fire Hazard Prevention		198		PD 1Q21
Fire Risk Mitigation		8		PD 1Q21
Total 2018-2019 FMA	302	510	500	
Grid Safety And Resiliency Program	419	42	NA	Apr-20
Wildfire Expense Memo Account	-	341	505	PD Aug 2020
Catastrophic Event Memo Account	57	79	88	PD March 2021
Total Other Wildfire-related Memo Accounts	476	462	593	
Grand Total	778	972	1,093	

Source: BofA Global Research estimates, company report

COVID-19 related Impacts

Mgmt. has noted that most its critical work (safety work, wildfire mitigation spend) continues with only 10-20% of work deferred and is thus far not seeing any impacts to its capex budget or permitting. Given minimal impact to capex, decoupling, and ability to delay 2020 equity issuance, we largely see 2020 EPS guidance as intact.

Decoupling limits impact due to any loss of load

EIX has a decoupling mechanism with cost recovered on an annual basis. The regulatory framework requires the California Utilities to recover authorized revenue based on estimated annual demand forecasts approved in regular proceedings before the CPUC. However, actual demand for natural gas and electricity will generally vary from CPUC-approved forecasted demand due to the impacts from weather volatility, energy efficiency programs, rooftop solar and other factors affecting consumption.

Under the General Rate Case (GRC)/California Public Utility Commission (CPUC) jurisdiction, Investor Owned Utilities (IOUs) get recovery of an uncollectible percentage of revenue based on a historical 10-year average of actual uncollectible expense. To the extent that costs are in excess of the uncollectible factor result, there would be an earnings impact. For Federal Energy Regulatory Commission (FERC) rates, the formula rate mechanism could provide for a true-up. We would expect the Emergency Customer Protections Memorandum Account (ECPMA) to track costs related to COVID-19 given the state of emergency in CA.

Managing the upcoming wildfire season will be critical

Communication with local authorities and the state is crucial given the need to focus on investments to harden the grid ahead of the upcoming wildfire season while at the same time procuring generators for its most critical customers. We see prioritization of wildfire mitigation and communication with the market as critical, especially ahead of the upcoming wildfire season. Public Safety Power Shutoffs (PSPS) efforts are likely to continue into the '20 season; and while weather conditions similar to last year would result in fewer shut-offs, mgmt. is going to continue covered conductors in the riskiest areas (1K circuit miles) and re-inspect structures in more than 50% of high-fire risk areas in order to raise the wind threshold and have an overall smaller impact on customers.

ROE concerns abated for now

Given the volatility of Moody's Baa Index and utilities waived the trigger in the '08 financial crisis (to the upside), we could see something similar happen this time around to avoid volatility in customer rates. We stress that the Moody's BAA Utility Bond index has since rebounded, placing rates within the band and abating any near-term risk to potential CPUC authorized ROEs. Meanwhile, we continue to see potential for a FERC ROE settlement regardless of base ROE policy uncertainties.

EPS Estimates

We provide our latest EPS estimates for EIX, tweaking slightly given the current share price that we assume equity is issued at. EPS estimates largely in-line with street, although above consensus in outer years given we net out equity in our SOTP rather than through dilution in EPS (stress consensus estimates are not transparent on amount of equity assumed).

Table 33: EIX EPS

EIX Mini-Model	2018A	2019A	2020E	2021E	2022E	2023E	2024E
Authorized Capital Structure							
Authorized Equity Capital %	48%	48%	52%	52%	52%	52%	52%
Authorized CPUC ROE	10.30%	10.30%	10.30%	10.30%	10.30%	10.30%	10.30%
FERC ROE Build							
FERC Base Rate	9.92%						
CAISO (RTO Participation Adder)	0.50%						
Avg Project Incentive Adder	0.78%						
Assumed Equity Capital %			47%	47%	47%	47%	47%
Authorized FERC ROE Build	11.2%	11.2%	10.3%	10.3%	10.3%	10.3%	10.3%
Ratebase Growth							
Ratebase - Including Adjustments Below (Avg)	28,601	30,913	33,694	36,114	38,062	39,948	42,069
We include mitigation spending in rate base and then net out EPS impact below							
Guidance Low ($Bn) (Ex. ~$1.6Bn of fire risk mitigation from AB 1054)				-	-	-	
Guidance Mid ($Bn) (Ex. ~$1.6Bn of fire risk mitigation from AB 1054)	28,500	30,800	33,400	35,900	38,200	41,000	
Guidance High ($Bn) (Ex. ~$1.6Bn of fire risk mitigation from AB 1054)				-	-	-	
Breakdown:							
CPUC Ratebase (Avg)	22,107	24,038	26,345	28,863	31,410	33,920	36,432
FERC Ratebase (Avg)	6,144	6,875	7,349	7,252	6,652	6,028	5,637
Ratebase Growth	9.4%	8.1%	9.0%	7.2%	5.4%	5.0%	5.3%
% FERC	23%	22%	22%	19%	16%	14%	13%
Shares (Basic)	326	342	377	379	380	382	384
Shares (Diluted)	326	340	370	380	381	383	385
Ratebase-Only EPS	4.37	4.59	4.77	5.00	5.26	5.50	5.78
Additions/Subtractions to Spend							
Storage Upside (Inlcuded in base CaEx			0.00	0.00	0.00	0.00	0.00
Transmission project - pending potential rejection (~$100 Mn capex)			-0.01	-0.01	-0.01	-0.01	-0.01
Wildfire mitigation spend (~$1.6bn excluded from earning ROE)			-0.10	-0.08			
Charge Ready II ($561Mn of Capital)			0.02	0.04	0.06	0.08	0.08
Changes to Capital Structure and ROE Adjustments							
Cost Savings (ex-Debt Cost Savings)	0.00	0.02	0.00	0.00	0.00	0.00	0.00
Debt Cost Savings	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Interest expense from Wildfire Contribution Debt (~$1.2bn)		0.00	-0.11	-0.11	-0.11	-0.11	-0.11
Energy Efficiency	0.03	0.05	0.04	0.04	0.04	0.04	0.04
AFUDC Benefits		0.24	0.25	0.25	0.25	0.25	0.25
Corp Donations and Executive Comp			-0.14	-0.25	-0.25	-0.25	-0.25
Tax benefits and Other (insurance?)	-0.08						
FERC Recovery	0.02	0.09					
Z Factor Upside (1Q19)		0.04					
Post Tax Adj	0.00						
Parent Drag & Edison Energy				*Breakeven run-rate heading into 2020*			
Edison Energy Group (EEG) --> Can it improve?	-0.04	0.00	0.00	0.00	0.00	0.00	0.00
SoCore Impairment							
Parent and Other	-0.23	-0.33	-0.26	-0.25	-0.25	-0.25	-0.25
Toal Parent & Other Drag (Incl EEG)	-0.27	-0.33	-0.26	-0.25	-0.25	-0.25	-0.25
Total EPS (Basic)	4.14	4.67	4.38	4.63	5.00	5.27	5.54
Total EPS (Diluted)	4.14	4.70	4.46	4.61	4.98	5.25	5.53
Previous estimate		4.70	4.45	4.60	4.97	5.24	5.51
Consensus		4.77	4.44	4.64	4.76	5.11	
Guidance		4.70-4.90	4.32-4.62				

Source: BofA Global Research estimates, company report, Bloomberg

Valuation: $69

We move our PO to $69 (from $61) based on peer multiples of 17.6x (from 16.2x). While we see upside in our SOTP analysis, we still see the total quantum of equity needs as uncertain and dependent on recovery of memo accounts and wildfire liabilities remaining unchanged. We admit disproportionate upside vs. peers even when including additional equity to address balance sheet but unknown around future wildfire exposures keeps us Neutral rated.

Table 34: EIX SOTP Valuation

EIX SOTP							
SCE Components	% SCE	Authorized ROE Reflected	2022E Earnings	2022E EPS	Peer Multiple	Premium/Discount	Value per Share
Group Peer Multiple - Electric					17.6x		
Group EPS '18-'22 CAGR - Electric					5.00%		
CPUC - Core	84%	10.30%	1,682	$4.41	18.5x	-3.0x	$68.28
CPUC/FERC - Further Capital	0%		-9	($0.02)	18.5x	-3.0x	($0.38)
FERC	16%	10.30%	322	$0.84	18.5x	-3.0x	$13.07
Edison Energy			0	0.00	10.0x	0.0x	$0.00
Parent/Other			-96	-0.25	18.5x	-3.0x	($3.88)
Total EPS				$4.98			
Ongoing contribution to Wildfire Fund				$Mn	EPS	Multiple	
NPV of Ongoing Wildfire Contribution ($945mn over 10yrs)				($664)			($1.74)
Total Liabilities				$Mn			
Wildfire Liabilities Assumptions							
Current Charge: 2017 Thomas, Mudslides, Woolsey Fires: Low End of Range				-4,900			
Gross Up Factor			20%	-5,880			
Insurance Receivable				2,000			
Wildfire Liability Incl Insurance Offset				-3,880			
FERC Allocation ~5%			5%	194			
Net Exposure				-3,686			
Post Tax Net Exposure			28%	-2,654			
Equity Issuance in 2020 (reflected in EPS est)				600			
Remaining Exposure				-2,054			
Equity Dilution from wildfire liability funding							
Funding of '17/18 wildfire liabilities							
Liabilities:	Equity Issued	Shares Issued	Shares O/S (pre-dilution)	New Share O/S	Equity Dilution	Equity Value - Prior dilution	Value Per Share
Wildfire Liabilities - Post-tax	*2054*						
Total	2054	34	381	415	9%	$75	
Equity Value							$69
Price Appreciation							11.2%
2020 Yield							4.1%
Total Return							15.29%
Shares- Post Dilution	*415*						

Source: BofA Global Research estimates, company report, Bloomberg

Please see our latest EIX research below:

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Edison International: Can SoCal Recover? The Total Costs Remain the Ambiguity	Julien Dumoulin-Smith	27 March 2020
Edison International: A Veritable Feast of '20 EPS Factors Plus a Splash of FFO/Debt Sobriety	Julien Dumoulin-Smith	28 February 2020
Edison International: Examining the range of equity needs built into expectations	Julien Dumoulin-Smith	31 January 2020
Edison International: Closing the discount as legacy liability uncertainty lingers	Julien Dumoulin-Smith	10 January 2020

Entergy (ETR)

Our 1Q20 EPS estimate of $1.01/sh is slightly below Street estimates at $1.08/sh. Our 2020 estimate of $5.51 was recently updated to below the midpoint of mgmt.'s range of $5.45-5.75. We see the double impact of milder weather in Q1 and potential lost sales from prolonged Covid-related shut in orders as driving downside risk in the near term. We see ETR as well-positioned for managing the difficult operating conditions in 2020 given the opportunity to rely on flexing the O&M lever as highlighted by mgmt. on our recent conference call, as well as significant visibility into industrial project pipeline in its Gulf service territory which remains intact. We continue to see the renewable angle as the principal long-term play as the company looks to replace several GW of aging fossil generation toward the back half of the decade – with the recent 250 MW solar RFP announcement the latest example. Maintain Buy.

ETR 1Q20 Earnings Walk

We forecast 1Q20 adjusted EPS of $1.01 vs. $0.82 in 1Q19 and $1.08 consensus.

- **Key Drivers:** Key positive drivers include the implementation of new rates (+$0.46sh) including ETR AR through the Formula Rate Plan (FRP), ETR LA through the AMI rider and the base rate proceeding, and a full quarter's effect of the SCPS rider and Choctaw in rates at ETR MS. We additionally see weather as being a small uplift though this is driven by normalization of temps vs. 2019 as 2020 HDDs were below normal across the service territory. Negative drivers include higher O&M spend (-$0.05), and higher D&A primarily driven by addition of new generation assets and ongoing investment in transmission and distribution rate base (-$0.14).

- **Unknowns:** Weather is expected to be a small uplift on Q1 results; however magnitude is difficult to estimate. The magnitude by which industrial load growth is affected by Covid related shut downs is a meaningful consideration though we note some latitude to manage this through O&M.

Table 35: ETR 1Q20 earnings walk

Entergy 1Q20 Earnings Walk	EPS
1Q19A	$0.82
Utilities	$0.20
Weather	
Return to normal	$0.12
Quarterly effect	($0.10)
Revenue impact	$0.46
AMI	$0.02
Non-Fuel O&M	($0.05)
Depreciation	($0.14)
Interest Expense and Interest Income	($0.08)
Income tax rate	($0.04)
Parent and Other	$0.03
Pension	($0.01)
Other	$0.04
Dilution	($0.03)
1Q20E Adjusted EPS	$1.01
1Q20 Consensus	1.08
2020 Adjusted EPS	$ 5.51
2020 Consensus	$5.57
2020 Guidance	5.45-5.75

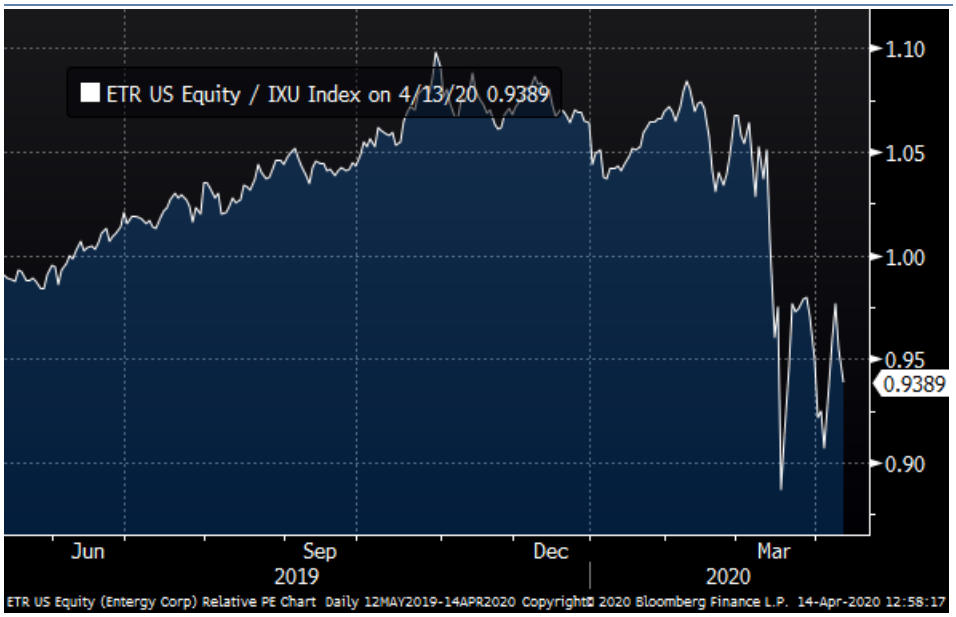
1Q19 shares outstanding	192
1Q20 shares outstanding	200

Source: BofA Global Research Estimates, company report, Bloomberg

What do we think of shares?

Shares of ETR de-rated vs. the peer group at the outset of the Covid crisis and now trade at a relative discount to the group on a forward PE basis – shares remain 1-2x turns below our electric peer group multiple for 2022 EPS since beginning their de-rating in early March. ETR's 2020 forecast included an assumption of 2% growth in weather-adjusted billed sales growth which included +5.5% growth in industrial sales with residential and commercial slightly down – with our previously-lowered estimates, we are assuming a 4-5% decline in industrial sales ($0.08-0.10 EPS impact), similar to that experienced in the 2008-09 recession, with shares continuing to screen cheap with our lower forecast. Mgmt. additionally indicated that no large customers with industrial projects in the pipeline have delayed or otherwise changed plans for new build facilities along the Gulf Coast, a signal that long-term demand growth remains intact despite near term headwinds. We maintain our confidence in ETR's long-term sustained investment profile between its entirely unscrubbed coal portfolio of ~2.2 GW and its largely steam-based gas and oil fleet which totals ~7 GW. We see investment in replacing these aging assets as the driver toward further re-rating with ETR steadily moving down the road of closing legacy nuclear plants and executing on its top quartile ratebase growth among peers and our estimated ~6% EPS CAGR through 2022. The renewable opportunity remains considerable as utility scale solar in its Mississippi and Louisiana territories and potentially wind in Arkansas are poised to replace aging fossil generation in the coming decade, supporting earnings growth over the medium to long term.

Exhibit 2: ETR relative value chart



Source: Bloomberg

Sizing the Covid impact on demand – look to '08

Mgmt.'s most recent comments regarding Covid impact on demand the company does has not seen a meaningful reduction in demand from either Residential, Commercial, or Industrial customers but acknowledges that an impact is expected as the slowdown continues. Given ETR's largely Gulf-region service area, the largest source of its demand is from Industrial customers which account for an estimated 40% of load, followed by Residential (~31%) and Commercial (~29%). Given different characteristics of each load type, mgmt. estimates that margins and corresponding EPS impact from Industrial ($0.02 EPS per 1% change in MWh sold) customers to be lowest among the three groups with Commercial ($0.05) and Residential ($0.09) following.

Table 36: ETR customer classes: we admit more load exposure to industrial, but perceive real residential offset given 9c:2c relative EPS exposure

Customer Class	% of Load	EPS impact
Industrial	40%	0.02
Residential	31%	0.09
Commercial	29%	0.05

Source: BofA Global Research Estimates, company report

During the 2008 crisis, demand from its Industrial customers declined by 4.5% in 2008 and 2009, followed by a rebound where growth averaged ~3% per annum for the decade that followed. While mgmt. expects some as-yet-unquantifiable impact on its Industrial load, thus far the impact has been limited. Mgmt expects the Gulf region to remain resilient during the economic slowdown given access to cheap natural gas feedstock, high-tech nature of industrial operations, and access to inexpensive electricity in its territory.

Managing opex is one of the key levers that mgmt. expects to utilize to offset declining load growth amid a likely slowdown. Flexing spending is a common practice for managing the effects of short term impacts such as above or below-average weather, with the ability to manage spending in the near term to partially mitigate the impact of lower growth. The other key lever being continuous improvement, which results in a more long-term bending of the opex curve – mgmt. points to last year's Q2 result where permanent cost cuts resulted in an increase in headroom for additional capex investment.

Changes in demand are an important driver as ETR has no decoupling in any of the jurisdictions where it operates – LA, AR, TX, MS, and NO. The highest sensitivity to changes in demand is residential sales with $0.09 EPS impact for a 1% change in demand, while the commercial impact of $0.05 and industrial impact of $0.02 are more tempered. While ETR does not have bad debt expense tracking across its jurisdictions, historically it has been able to achieve recovery of outsized bad debt expenses via regulatory assets. Off system sales are generally not a large driver of variability and not expected to be in the current environment. ETR has formula-based ratemaking in all jurisdictions except NO and TX, allowing for more timely recovery than under a traditional rate case structure, another lever that could potentially mitigate lost revenues due to the exogenous Covid shock.

Solar dev: Sunflower approved, 250 MW LA RFP coming

ETR MS' 100 MW Sunflower Solar facility received approval from the state's utility commission in April, clearing the way for the project to go forward. Under ETR's agreement with developer Recurrent Energy, Recurrent will construct the plant with ETR taking over upon completion. Under the proposed recovery mechanism ETR MS will add the $153m project cost to rates contemporaneous with the closing of the transfer from the developer to the utility under ETR MS' existing formula rate plan mechanism. The decision by the utility commission came in under ETR's original estimated time frame of Q2 2020 with expected project completion and transfer date by the end of 2021.

Separately ETR has announced the issuance of a new 250 MW RFP for solar generation in Louisiana. The proposals are to be structured either as build-own-transfer similar to Sunflower or self-build alternatives for up to 250 MW of generation, and/or one or more PPAs for up 100 MW. Projects are required to have a fully executed interconnection agreement with the Midcontinent Independent System Operator (MISO). Optional storage may be included with proposals as well. Draft proposals are due in April and final submissions are due in June with bidder registration to take place in July.

Grand Gulf lease complaint questions recovery

System Energy Resources Inc. (SERI) has been involved in multi-year complaints regarding its ROE and equity component as well as its sale-leaseback renewal. The sale-leaseback renewal docket (EL18-152) received a proposed administrative law judge (ALJ)

decision in April under which the ALJ found that SERI had recovered most of the cost of the original plant under its lease signed in 1988 that ran through 2015 (since renewed), and that there is no need for SERI to continue to recover its annual lease payments of 17m annually since lease renewal in 2015. ETR maintains that the lease transaction was entered prudently and has resulted in significant customer savings over the years, and that recovery should continue under the current lease. We note that the potential impact on near-term earnings would be limited to any reserve taken by SERI in order to account for a potential adverse ruling. While no formal timeframe has been set out for a final ruling by the Federal Energy Regulatory Commission (FERC), past precedent suggests that a final ruling would not be likely until 2021 or later.

EPS estimates

We previously reduced our 2020 estimates reflecting likely near-term impacts from lower industrial demand driven by fallout from the COVID crisis. Similar to the 2008-09 crisis, we adjusted our 2020 estimates to reflect a 4-5% decline in industrial sales (approx. $0.08-0.10 EPS impact per ETR sensitivities), though the key in our view is to what extent mgmt. is able to offset the impacts of lower industrial output with opex reductions. Meanwhile we stress that different from 2008-2009, ongoing industrialization projects do not appear poised to end and its critical to watch how these trend in coming months with regards to '20 industrial sales (there could very well be more of a lag effect stretching into '21 given both 12-month trialing C&I peak demand charges along with the ongoing growth of projects already in construction in petrochem, etc). We remain toward the low end of mgmt's guidance range in 2020 when we expect the most impact from Covid to hit, with a consolidated EPS trajectory within mgmt's long term 5-7% range in the latter years of the forecast period.

Table 37: ETR estimates

EPS by Business							
Subsidiary	2019A	2020E	2021E	2022E	2023E	2024E	2025E
EAI	1.33	1.49	1.61	1.73	1.84	1.93	2.04
ELL	3.51	3.43	3.63	3.96	4.21	4.47	4.75
EMI	0.61	0.71	0.75	0.80	0.85	0.89	0.94
ENOI	0.27	0.23	0.24	0.24	0.24	0.24	0.25
ETI	0.81	0.78	0.91	0.96	1.01	1.08	1.16
SERI	0.50	0.40	0.40	0.41	0.41	0.42	0.43
Other	(0.08)	0.00	(0.00)	0.00	(0.00)	(0.00)	0.00
Utilities	6.95	7.03	7.54	8.08	8.57	9.04	9.57
Parent & Other	(1.55)	(1.53)	(1.58)	(1.69)	(1.69)	(1.70)	(1.72)
Utility Parent & Other (UP&O) - BofAe	5.40	5.51	5.96	6.39	6.88	7.34	7.85
Special Items							
Adjusted UP&O	5.40	5.51	5.96	6.39	6.88	7.34	7.85
Guidance	5.25-5.45	5.45-5.75	5.80-6.10	6.15-6.45			
Midpoint of Guidance	5.35	5.60	5.95	6.30			
CAGR off 2019 Adjusted EPS Guide Mid (5-7% LT Growth)		2.95%	5.52%	6.12%	6.48%	6.53%	6.60%
Competitive Business (EWC)							
Consolidated Estimates	5.40	5.51	5.96	6.39	6.88	7.34	7.85
Prior Consolidated Estimates							
Guidance	5.25-5.45	5.45-5.75	5.80-6.10	6.15-6.45			
Consensus	5.37	5.57	5.87	6.36	6.69		
Dividend	*3.66*	*3.72*	*3.84*	*4.07*	*4.31*	*4.57*	*4.85*
Div Payout 65-75% of UP&O	67.8%	67.5%	64.5%	63.7%	62.7%	62.3%	61.7%
Overall ROE	10.5%	9.6%	9.6%	9.6%	9.5%	9.5%	9.5%

Source: Bank of America estimates, company report, Bloomberg

Valuation: PO $122, maintain Buy

Our PO moves to $122/sh applying our electric utility sum of the parts multiple of 17.6x to each of ETR's utilities and grossing the multiple up for capital appreciation by 5%. We reduce 2.0x valuation premiums at EAI, ELL, EMI and 1.0x premiums at ENOI and ETI to reflect downside risk associated with lost sales. On our estimates, ETR's total return prospects remain compelling at current valuations, particularly as shares have de-rated

vs the peer group of late. Reiterate Buy. *We see ETR as among the most compelling opportunities in our utility coverage given implied concerns on load and Oil & Gas exposure. We emphasize while there could indeed some further load risk, embedded Formula Rate Plans (FRPs) should enable resiliency. These FRP mechanisms are frequently under-appreciated relative to filters screening for decoupling by investors.*

Table 38: ETR SOTP

Entergy: Sum of the Parts Valuation

Group Peer Multiple - Electric			17.6x					
Group EPS '18-'22 CAGR - Electric			5.00%					
Core Regulated Electric Utilities	2022E EPS		Peer Multiple			Equity Value ($/Sh)		
			18.5x					
		Low	Base	High	Premium/Discount	Low	Base	High
Entergy Arkansas (EAI)	$1.73	18.5x	19.5x	20.5x	1.0x	$31.92	$33.65	$35.38
Entergy Louisiana (ELL)	$3.96	18.5x	19.5x	20.5x	1.0x	$73.14	$77.10	$81.05
Entergy Mississippi (EMI)	$0.80	18.5x	19.5x	20.5x	1.0x	$14.72	$15.52	$16.31
Entergy New Orleans (ENOI)	$0.24	17.5x	18.5x	19.5x	0.0x	$4.16	$4.40	$4.64
Entergy Texas (ETI)	$0.96	17.5x	18.5x	19.5x	0.0x	$16.70	$17.66	$18.61
Total Regulated	$7.68	18.3x	19.3x	20.3x		$140.65	$148.32	$156.00
Parent Preferred Income (ELL)	($0.62)		18.5x		0.0x		($11.37)	
Total Utility Value	$7.06	18.3x	19.4x	20.5x		$129.27	$136.95	$144.63

Parent Adjustments	$Mn	Weight	Weighted Value ($Mn)	
HoldCo Senior Notes	1,850	50%	925	($2.24)

	2022E EPS	Implied Interest Rate	Weight	P/E Multiple		
HoldCo Interest Expense - 50% Weighting	($0.72)	9.6%	50%	18.5x	0.0x	($6.69)
Corporate SG&A	($0.35)			18.5x	0.0x	($6.47)
Total Parent & Other						($15.40)

Merchant / Nuclear	Cumulative FCF	NPV @ 10%		
Merchant FCF: NPV Through 2022	$214	$177		$0.86
Total Merchant				$0.86

Total Equity Value Per Share	$115.00	$122.00	$130.00
Price Return	13.6%	20.5%	28.4%
NTM DPS		*$3.72*	
Dividend Yield		*3.7%*	
Total Return	17.2%	24.1%	32.0%
Implied Multiple Today		17.0x	
PO Implied Multiple			

Source: BofA Global Research estimates, company report, Bloomberg

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BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Entergy: Just So Many Ways to Win: Why We We're Still So Constructive: Reiterate Buy	Julien Dumoulin-Smith	25 March 2020
Entergy: The next re-rating angle gets a tad closer: reiterate Buy	Julien Dumoulin-Smith	21 February 2020
Entergy: Specifying the opportunity of the aging fleet: reaffirm our Buy thesis	Julien Dumoulin-Smith	03 December 2019

Essential Utilities (WTRG)

We see WTRG's execution on their capital plans as largely intact outside of a modest $30Mn delay related to temporary work stoppage in PA (which will likely be trued up within the calendar year). We would anticipate some further tailwinds from acceleration in muni deals during a recovery period and await looming equity likely later this year to finance the pending DELCORA acquisition. Meanwhile, we further continue to await developments around the catch up component of repairs tax implementation as additional upside to the recently rolled out guidance with a filing this quarter. We reiterate our Neutral rating on shares of WTRG, seeing risk/reward as fairly balanced at the current valuation.

WTRG 1Q20 Earnings Walk

We forecast 1Q20 adjusted EPS of $0.61 compared to 1Q19 adjusted results of $0.28 and consensus of $0.58. We see consensus as not fully appreciating the adjusted numbers reflecting weather-normalized load on the gas business.

- **Key Drivers:** The primary positive drivers y/y are new rates for the legacy water business and gas contribution following the Peoples Gas acquisition offset by higher O&M and dilution.

Table 39: WTRG 1Q20 Walk

WTRG 1Q20 Earnings Walk		EPS
WTRG 1Q19 EPS	$	0.28
Aqua		0.03
Peoples Gas		0.38
Dilution		-0.08
1Q20 BofAe Adjusted EPS	$	0.61
Consensus		$0.58
WTRG Guidance		$1.53-$1.58
2020 Consensus		$1.56
1Q20 Adjusted Shares Outstanding		254
1Q19 Adjusted Shares Outstanding		178

Source: BofA Global Research, Bloomberg

Contemplating the COVID IMPACT

Latest discussions with management have stressed the capital forecast (and recent EPS guidance) as largely intact outside of a $30Mn delay related to a two week work stoppage in PA when 500 contractors were out of work. We stress this as modest amid the $950Mn to be deployed with an expectation for this to be made up by the end of the calendar year, and see no material issues other than some small timing nuances.

While the company does not have decoupling mechanisms in a sizable way (despite PA companies privy to such mechanisms, the mechanism is only utilized in IL), industrial load is only ~3% of the overall mix for the water biz and less than 1% for gas (gas shoulder season should further limit any NT impact). During the recession in 08-09, the company did not see a large reduction on load, but we stress bill collection as more critical to watch given the moratorium on shutoffs this time. Initial discussions thus far haven't indicated any signs of trouble (typical run rate is about 50bp and 200bps for Aqua and Peoples, respectively. With TX already announcing a provision to track COVID-related expenses, we further await any add'l announcements in their ten state jurisdictions given what we expect to be a clear focus for regulators.

The remaining jurisdictions haven't seen an impact outside PA with regulatory or construction delays and muni conversations ongoing, albeit developments remain fluid: while WTRG doesn't have a particularly busy reg agenda, we could see a slight delay in the DELCORA acquisition (seemingly early next year vs. late this year/early next year) but would nonetheless anticipate equity for the transaction to be raised towards the back half of 2020. Latest conversations suggest ~$300Mn. While any infrastructure/federal

stimulus for water remains a wildcard, we see recovery out of COVID as likely another tailwind for industry consolidation.

Contemplating Repairs & LT Prospects

At their Analyst Day in February, mgmt. noted plans to invest $950Mn in 2020 for the year with visibility to ~$2.8Bn through '22, translating to rate base CAGRs of 6-7% for the water biz and 8-10% for gas (This excludes any acquisitions despite what we increasingly view as a bullish landscape for further muni acquisition acceleration – and reflecting DELCORA alone into rate base would already provide another few hundred bps of growth). Overall, we expect enabling legislation & emerging contaminants – in addition to COVID recovery tailwinds – to drive further consolidation prospects for water longer term.

Meanwhile, we await potential upside from any clarity around commission treatment of the Repairs Tax catch up component. Recall the election of tax repair for People's largest Pennsylvania sub, Peoples Natural Gas, which we perceive to be ~90% of the gas business. The company expects the election to directly contribute ~$0.08-$0.12 in 2020 – and we perceive this as a good run rate going forward. We expect the company to file something this quarter around a catch up component, with potential clarity around any construct later in the year (to determine flow through benefit to shareholders which remains less clear cut and excluded from the latest guidance.

EPS Estimates

The exhibit below reflects our current EPS estimates ahead of the upcoming quarter, with NT numbers coming down slightly. We continue to model to the high end of their LT CAGR guidance.

Table 40: EPS Estimates

EPS Estimates	2020E	2021E	2022E
PA	$0.73	$0.80	$0.86
OH	$0.07	$0.07	$0.08
IL	$0.07	$0.08	$0.08
TX	$0.06	$0.07	$0.07
NC	$0.04	$0.04	$0.05
Other States	$0.07	$0.07	$0.08
Water Utility	1.04	1.13	1.21
Peoples Gas	0.62	0.67	0.72
Parent & Other	*-0.10*	*-0.11*	*-0.14*
EPS	1.56	1.69	1.80
YoY Growth	*6%*	*9%*	*6%*
Guidance	1.53-1.58		
Fully Diluted Shares O/S	*254*	*254*	*254*
Previous EPS	*$1.58*	*$1.69*	*$1.80*
CAGR Guidance: 5-7% through '22 off 2019 Adjusted EPS			
Low End: 5%	1.54	1.62	1.70
Midpoint	1.56	1.65	1.75
High End: 7%	1.57	1.68	1.80
Consensus	1.56	1.65	1.79
DPS	0.99	1.06	1.13
Payout Ratio	*63%*	*62%*	*63%*

Source: BofA Global Research, Bloomberg

Valuation

The exhibit below reflects our latest SOTP after applying the current peer multiples to our valuation: 26.3x for water and 17.6x for gas (vs. 28.2x for water and 18.3x for gas previously). Our PO shifts to $47 and we maintain our Neutral rating seeing risk/reward as balanced at the current valuation.

Table 41: WTRG SOTP

Water Utilities	2022E EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*26.3x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		28.5x							
Water Utilities									
States	2022E EPS	ROE embedded							
PA	$0.86	10.0%	2.0x	29.5x	30.5x	31.5x	$25	$26	$27
OH	$0.08	9.4%	2.0x	29.5x	30.5x	31.5x	$2	$2	$2
IL	$0.08	9.1%	3.0x	30.5x	31.5x	32.5x	$3	$3	$3
TX	$0.07	10.0%	0.0x	27.5x	28.5x	29.5x	$2	$2	$2
NC	$0.05	9.2%	1.0x	28.5x	29.5x	30.5x	$1	$1	$1
Other (including acquisitions)	$0.08	9.2%	0.0x	27.5x	28.5x	29.5x	$2	$2	$2
Water utilities total (ex-Peoples)	$1.21			*29.3x*	*30.3x*	*31.3x*	$36	$37	$38
Gas Utilities									
Peer Gas P/E		*17.6x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		18.6x							
	2022E EPS	ROE embedded							
Peoples Gas	$0.72	12.1%	2.0x	19.6x	20.6x	21.6x	$14	$15	$16
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			-1165	50%			($582)	($582)	($582)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($537)	($497)	($582)
50/50 Weighted Drag from HoldCo Drag							($1,119)	($1,079)	($1,164)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							$45.00	$47.00	$49.00
Current Price								$43.36	
Dividend Yield								2.3%	
Total Return								10.67%	

Source: BofA Global Research, Bloomberg

See our other recent reports on WTRG:

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Essential Utilities: Peoples Set to Close Imminently, but can the People deliver? Dropping Ests	Julien Dumoulin-Smith	09 March 2020
Aqua America: Overflowing Interest: Downgrading to Neutral	Julien Dumoulin-Smith	21 January 2020
Aqua America: Snorkeling in the Deep End: A Closer Look at the Repairs Tax Benefit	Julien Dumoulin-Smith	21 August 2019
Aqua America: Pool Party continues but waiting on the Gas	Julien Dumoulin-Smith	08 August 2019
Aqua America: Diving In: See Opportunity in a Gas & Water Utility Hybrid	Julien Dumoulin-Smith	15 July 2019

Evergy Inc (EVRG)

EVRG 1Q20 Earnings Walk

We forecast 1Q20 adjusted EPS of $0.40 vs. consensus of $0.49 (we note downside risk to Street estimates as Covid effects become more fully reflected over time) and pro-forma 1Q19 results of $0.44. Our full-year forecast for EVRG of $3.06/sh is updated from $3.15 previously as we expect some Covid-related slowdowns to materialize in reduced demand. We remain concerned on load trends for EVRG but given no '20 guidance, this limits near-term revision risk. Given ongoing strategic questions what will mgmt's ability/comfort with articulating cost cuts be to mitigate this outcome. *Management states they will attempt to cut cost however did not provide any further specifics; mgmt. also said it was also difficult to see load impacts given how much later KS was to implement Covid-related stay-at-home orders suggesting negligible impact on 1Q and even early impacts on 2Q.*

- **Key Drivers:** Weather is expected to be a drag of $0.13/sh as we normalize for the positive effects of 1Q19 (5 cents) and account for milder weather in 1Q20 that reduced the number of Heating Degree Days (HDDs) in EVRG's service area. O&M savings including merger synergies are expected to provide an uplift of 6 cents as the company continues to look for ways to cut costs in order to realize full merger synergies, offset Sibley and Jeffery rulings from 2019, and offset potential Covid-related drag on demand. We additionally see 5 cents of accretion from a lower share count in Q1 2020 following EVRG's share buyback program, but note that as this program has been suspended following the Elliott agreement this effect will abate in future quarters.

- **Unknowns:** Weather was noticeably milder in Q1 2020 than normal, with HDDs 15-16% below normal throughout much of EVRG's service territory. We note that weather impact on utility results is driven not just by the aggregate number of HDDs but also in the timing of deviations from norm (Jan HDDs worth more than March), and as such the precise weather impact is difficult to gauge. The Covid effect will likely be modest in Q1 as shut-in rules in EVRG's service territory were implemented in a staggered approach at the end of the quarter – we estimate 1 cent drag. The additional question looking ahead is to what extent, if any, EVRG is able to offset the effects of reduced demand by commercial and industrial (C&I) customers with further cost cuts in the short term.

Table 42: EVRG Q1 walk: a bit weaker too vs Street on mild weather

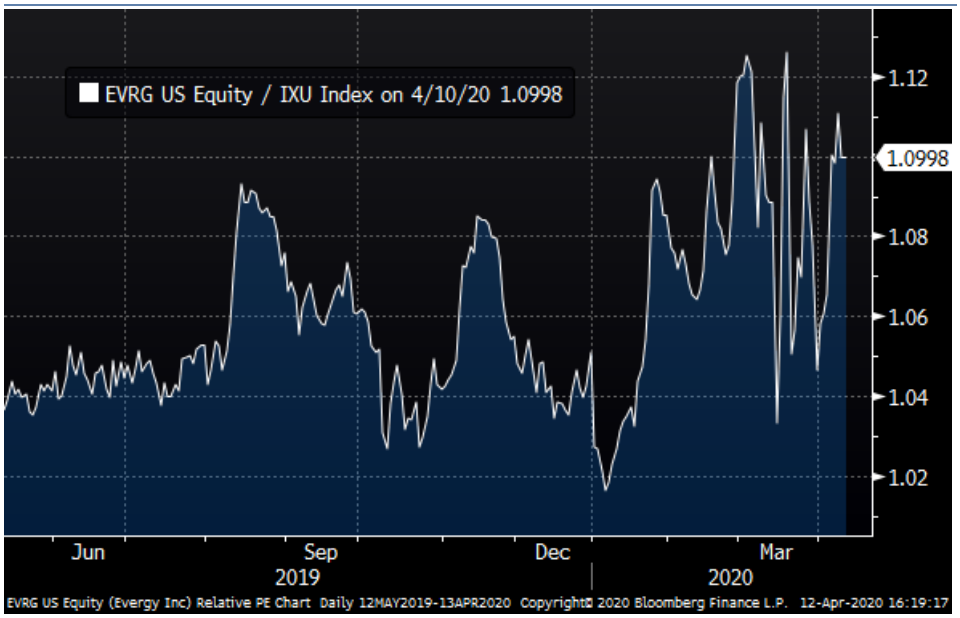
Earnings Walk	Notes	EPS
1Q19 EPS		0.44
Weather normal	Reverse favorable effect in Q1 2019	(0.05)
Weather 1Q20	15-16% HDDs below normal in KS and MO	(0.08)
Other	Effect of COVID on load	(0.01)
1Q20 drivers:		
O&M	Cost savings, includes merger synergies	0.06
D&A expense		(0.01)
Interest expense		(0.01)
COLI	Based on 2020 guidance	0.02
Accretion		0.05
1Q20E BofAe EPS		$0.40
1Q20 Consensus		$0.49
2020E BofAe EPS		$3.06
2020 Consensus		$3.11
1Q19 Share count		253
1Q20 Share count		227

Source: BofA Global Research Estimates, company report, Bloomberg

Shares reflect Covid, but strategic angle is still there

Shares of EVRG have bounced back amid substantial volatility in mid March. We note shares have outperformed the peer group since our upgrade to Buy following EVRG's Q1 results and announcement of agreement with Elliott: Evergy, Inc: Upgrade to Buy on activist engagement, cost controls, capex, & strategic angles too 03 March 2020.

Exhibit 3: EVRG relative chart



Source: Bloomberg

- **We see some short-term impact stemming from Covid.** Both the KS and MO utilities have bad debt recovery imputed in their current rates based on historical test years - recall that EVRG's rate stay outs are until 2022 and 2023 in Missouri and Kansas, respectively. The utilities do not have trackers for recovery of bad debt expense in between rate cases. Likewise the EVRG utilities do not have decoupling in either KS or MO although they have some energy efficiency mechanisms such as Missouri Energy Efficiency Investment Act (MEEIA). Off system sales are generally not a significant driver historically - the last major impact from wholesale pricing was related to the polar vortex in 2014. Estimated EPS impact from a 1% swing in demand is $0.10 ($0.05 from residential, $0.04 from commercial, $0.01 from industrial), *among the highest EPS sensitivity across our coverage universe making shares more at risk of Covid related demand destruction. That said early indications from OG&E of a very modest load impact appear to de-risk EVRG shares, and also notable is the lack of '20 EPS guidance range, forcing more of a long-term focus rather than near-term impacts of Covid in '20 (different vs peers). The real question is to what extent management can source yet further cost cuts during its stay out to offset more ongoing pressures from lower Covid-related load. We also continue to assume recovery of bad debt expenses, a consistent assumption across most jurisdictions, just could be a while before cash recovery is enabled.*
- **Cost-cutting already a big part of the strategy.** The key short-term question for EVRG (and most utilities that are not decoupled) is to what extent mgmt. can flex O&M controls to mitigate the impact of lost sales stemming from shut-in orders. EVRG has been implementing merger synergies from its last transaction and had already included an incremental ~$30m in its 2020 forecast from continuing realization of these savings – for example combining all back office systems across all utilities under one customer management system. In addition, 2019 rulings in the Jeffrey and Sibley matters put additional pressure on mgmt. to realize *further cost cuts* in order to preserve ROEs at the Kansas and Missouri utilities, respectively. To what extent mgmt. can wring out additional cuts to offset mild Q1 weather and lost

sales remains the key question – we lowered out 2020 ests. by 9 cents across the consolidated franchise to account for this additional pressure on ROEs.

Strategic review: timeline and accretion scenario

EVRG's Strategic Review & Operations Committee (SROC) created in EVRG's agreement with Elliott outlines specific dates by which proposals must be submitted, voted on, and presented publicly. Two of the four members of the SROC are the new directors selected by Elliott - industry vets Paul Keglevic and Kirk Andrews - giving the activist manager even representation with incumbent directors. Unsurprisingly, given intense focus by utility mgmt. teams and state utility regulators (not limited to EVRG) on maintaining ongoing service amid the Covid emergency, the SROC issued an updated time frame pushing back its most significant deliverables further into the year. We view the revised timeframe below as merely reflecting the practical realities of evaluating a complex transaction amid work-from-home restrictions and market volatility and remain constructive on the overall direction of the review.

- **SROC recommendation to Board due Jul 30.** The original timeline called for the committee to present to the Board its recommendation of a transaction or standalone strategy by May 30 – note that the specific recommendation will also determine the level of public disclosure, as we detailed previously.
- **Board announcement by August 17.** Previously June 17, giving the Board the same number of days to evaluate as under the previous timeframe.
- **Modified standalone plan by Oct 14 if selected.** Originally the deadline was Sep 4, so the time frame for a presentation of a potential standalone plan has been pushed back by six weeks. We continue to view this as the less likely option given specific wording of the SROC agreement and note that logistics around presenting such a plan may require rethinking in the wake of Covid.

Analyzing accretion from a potential NEE deal: running the math

Below we provide an alternative version of our previous illustrative accretion/dilution analysis on NEE's prospective acquisition of EVRG. For this scenario, we assume no debt addition at parent level, essentially keeping the FFO/Debt unchanged at NEE. The scenario yields $0.15 or 1.5% accretion ex-synergies for 2021E; we view synergies as necessary to sustain accretion through longer-term. We anticipate some degree of financial re-leveraging of NEE nonetheless with upwards of 3%+ accretion to NEE in this instance.

Table 43: Illustrative accretion - NEE acquisition of EVRG

	2020E	2021E	2022E	2023E	2024E
Legacy NEE					
Pre-Transaction NEE Net Income ($Mn)	4,500	4,847	5,402	5,722	5,972
Pre-Transaction NEE Shares Out. (Mn)	491.0	491.0	493.3	500.0	505.0
Pre-Transaction NEE EPS	$9.16	$9.87	$10.95	$11.44	$11.83
Consensus	$9.06	$9.85	$10.62	$11.24	$11.87
EVRG					
Pre-Transaction EVRG Net Income ($Mn)	715	746	774	790	797
Combined Entity					
Combined Net Income ($Mn)	5,214	5,593	6,176	6,512	6,769
Incremental Interest Expense (Tax-Adjusted at 21%)	0	0	0	0	0
Synergies ($Mn)	0	0	0	0	0
Pro Forma Net Income ($Mn)	5,214	5,593	6,176	6,512	6,769
Incremental NEE Shares Issued for Santee (Mn)	67.1	67.1	67.1	67.1	67.1
Pro-Forma NEE Shares Out. (Mn)	558.1	558.1	560.3	567.1	572.1
Pro-Forma EPS	$9.34	$10.02	$11.02	$11.48	$11.83

Table 43: Illustrative accretion - NEE acquisition of EVRG

	2020E	2021E	2022E	2023E	2024E
Accretion (Dilution)	$0.18	$0.15	$0.07	$0.04	$0.01
Accretion (Dilution)	2.0%	1.5%	0.6%	0.3%	0.1%

Source: BofA Global Research Estimates, company report, Bloomberg

Estimates

Our estimates reflect near-term 9 cents consolidated earnings drag related to Covid in 2020, as we see limited oppty for mitigation of lost sales given EVRG's lack of a decoupling mechanism and ongoing efforts to cut costs across the franchise already underway given merger synergies and Sibley/Jeffrey offset requirements. Our estimates are below Street in 2020 though we perceive downside here as consensus forecasts are updated to more fully reflect Covid impacts. We expect Covid to not be a driver of downside risks past 2020 and our estimates in future years remain largely unchanged as we see EVRG as largely able to achieve authorized ROEs in this period.

Table 44: EVRG estimates

Evergy, Inc. Dashboard

EPS Estimates by Subsidiary	2018A	2019A	2020E	2021E	2022E	2023E	2024E
Evergy Metro	$0.76	$1.06	$1.07	$1.13	$1.17	$1.20	$1.22
Evergy Missouri West	$0.35	$0.37	$0.44	$0.47	$0.49	$0.51	$0.52
Kansas Central	$1.58	$1.43	$1.67	$1.78	$1.87	$1.90	$1.91
Parent/Other	($0.19)	($0.08)	($0.11)	($0.11)	($0.13)	($0.14)	($0.14)
GAAP EPS	$2.50	$2.79	$3.06	$3.27	$3.40	$3.47	$3.50
Y/Y EPS Growth %		*11.6%*	*9.7%*	*6.8%*	*3.9%*	*2.0%*	*0.9%*
Prior estimates	$2.50	$2.89	$3.15	$3.29	$3.42	$3.48	$3.52
Consensus (BBG)		$2.92	$3.11	$3.23	$3.39	$3.58	nm
DPS	$1.84	$1.95	$2.07	$2.19	$2.30	$2.42	$2.54
Dividend Payout (60-70%)	73.5%	69.8%	67.5%	67.0%	67.7%	69.7%	72.5%

Source: BofA Global Research Estimates, company report, Bloomberg

Valuation

We updated our PO to $69 reflecting an updated electric utility peer group multiple of 17.6x (17.9x previously). Our valuation is largely unaffected by the near-term drag on our estimates related to milder weather and Covid as both are expected to normalize by 2022. Shares have re-rated vs the peer group since our upgrade to Buy though we still perceive upside to the current share price amid ongoing strategic review.

We perceive many investors as cautious into 1Q updates given exposure to Covid despite backdrop around strategic actions possible.

Table 45: EVRG SOTP

Evergy Sum-of-the-Parts Valuation	2022E EPS	P/E Multiple					Equity Value/Sh		
		Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric			17.6x						
Group EPS '18-'22 CAGR - Electric			5.00%						
			18.5x						
Evergy Metro	$1.17	19.5x		2.00x	20.5x	21.5x	$22.72	$23.88	$25.05
Evergy Missouri West	$0.49	19.5x		2.00x	20.5x	21.5x	$9.58	$10.07	$10.57
Evergy Kansas Central	$1.87	19.5x		2.00x	20.5x	21.5x	$36.42	$38.29	$40.16
Parent & Other	-$0.13	19.5x		2.00x	20.5x	21.5x	-$2.54	-$2.67	-$2.80
EVRG consolidated '22 EPS	$3.40				*20.6x*		$66.00	$70.00	$73.00
	After-tax amount $m		$/sh	Probability					
Deferral of Sibley return + D&A	23		-$0.10	50%			-$2.04	-$1.02	$0.00
Shares outstanding (Average 2022)	227								
Shares outstanding (Y/E 2022)	227								
EVRG Price Objective							$64.00	$69.00	$73.00
EVRG Current Share Price								$60.98	
Implied Return								13.15%	
EVRG Standalone NTM Dividend Yield								3.59%	
Total Return								16.75%	

Source: BofA Global Research Estimates, company report, Bloomberg

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Title: Subtitle	Primary Author	Date Published
Evergy, Inc: The Covid Risks & Prelim Possible NEE Accretion Stats: Reiterate Buy	Julien Dumoulin-Smith	13 April 2020
Evergy, Inc: Timeline & just why is the Elliott deal so constructive?	Julien Dumoulin-Smith	10 March 2020
Evergy, Inc: Upgrade to Buy on activist engagement, cost controls, capex, & strategic angles too	Julien Dumoulin-Smith	03 March 2020
Evergy, Inc: Cost Cutting, PPAs, and Kansas Prospects: Where to focus?	Julien Dumoulin-Smith	14 February 2020

Eversource (ES)

We point to Eversource as one of the more protected names from COVID given its mostly decoupled status and capex upside around grid mod and AMI (incl. EV infra/storage spend) in CT and MA. We expect the call to be relatively muted as many updates are coming later this year. Offshore wind awaits BOEM's (the Bureau of Ocean Energy Mgmt's) cumulative impact study before ES can comment on the timeline of its first project (the small South Fork project to commission in 2022 – before others). Further, approval for AMI / grid mod upside remain protracted with CT's filing potentially being looked at this July, still indicating that the earliest spend could be implemented is '21. Finally, we note that the Columbia Gas of Massachusetts is expected to close in 3Q, with filings expected (including the key one with Mass Department of Public Utilities) in the next month or so. We continue to expect ES maintains its 5-7% LT EPS growth CAGR, estimating that the CAGR remains towards the mid-point even when factoring in upside capex opportunities and the meaningful EPS uplift into '24 associated with offshore wind. We maintain our Underperform rating on shares given pricey nature relative to peers; seeing limited near-term upside capex catalysts ahead. As for the quarter, we expect a $1.02/sh – the same as Consensus.

1Q20 ES EPS Walk

Below we forecast a $1.02/sh quarter for 1Q20, the same as Consensus. This is compared to a $0.97/sh 1Q19 EPS.

- **Drivers**: We find about +12c YoY for the quarter thanks to rate case increases that increased at the beginning of this year (e.g. CLP, NSTAR & WMECO Phase II rates) or were effective over the last year (e.g. interim rate increase for PSNH July 2019).
- **Other**: Adding up the pieces of parent, D&A, interest, property taxes, and other, we find about a -4c hurt this quarter. We highlight that O&M is flat YoY, which indicates the company could 'bend the curve' and save more if needed depending on COVID impacts.
- **Wildcard**: We factor in -2c of weather to reflect PSNH – the only subsidiary not decoupled. Note that weather was very mild in 1Q, but PSNH represents only 6% of ratebase.

Table 46: ES 1Q20 EPS Walk

ES Energy Earnings Walk	EPS
Adjusted EPS 1Q19	$0.97
Utility	
Weather	
Return to normal	$0.00
Current quarter: Really mild, only PSNH not decoupled	($0.02)
Transmission & Distribution	
Ratebase transmission earnings	$0.03
NSTAR Electric & WMECO rates Phase II Jan 1, 2020	$0.02
Aquarion contribution	$0.00
CLP Phase II rates effective May 1, 2019	$0.02
Loss of generation	$0.00
Yankee Gas rates effective Jan 1, 2020	$0.02
Interim rate increase PSNH effective July 1, 2019	$0.03
Other	
Parent, D&A, Interest, Property taxes, Other expenses	($0.04)
O&M	$0.00
Parent	$0.00
One-time: Merger recovery in 4Q18	$0.00
One-time: Loss of NPT AFUDC Earnings	($0.01)
Dilution	($0.00)
1Q20E Adjusted EPS	$1.02
1Q20 BofA Model	$1.02
1Q20E Consensus	$1.02

Table 46: ES 1Q20 EPS Walk

ES Energy Earnings Walk	EPS
2020E BofA EPS	$3.65
2020E Consensus	$3.64
2020 Guidance	3.40-3.50
Shares Outstanding 1Q19	318
Shares Outstanding 1Q20	331

Source: BofA Global Research estimates, company report, Bloomberg

Key points for 1Q

- **COVID**: ES has full revenue decoupling for all of its utilities with the exception of PSNH, which is currently in a pending ratecase. As such, ES revenues are decoupled from load reduction impact at the rest of its utility subsidiaries aside from PSNH. Decoupling base lines rise with base rate increases as well. ES has a bad debt expense rider but only for medical and low-income customers. We see this as common amongst names that do have trackers (typically usually at the gas subs or at specific customer classes).

- **Financing activity strong in 1Q**: We expect ES to discuss its financing over the last few months, including $350mn of parent notes in Jan, $400mn of NSTAR Electric green bonds in March, and closing out the forward by the end of March.

- **Capex upside**: While ES provided a five-year capex roll-forward through 2020 on the last call, the company still has upside spend related to grid mod in CT and NH, AMI in MA and CT ($1bn), and natural gas distribution spend in MA (perhaps related to the NiSource subsidiary acquisition). We still await a more firm timeline associated with these opportunities as they aren't factored into guidance yet. We focus moreso on AMI in CT given activity is starting to pick up on the opportunity that could result in a proceeding starting this July.

- **Offshore wind**: The South Fork project is the first and smallest at (just 90MW + a 40MW upgrade) of ES's offshore wind projects expected to come online with a commissioning date of 2022. We point out that ES is still awaiting a cumulative impact study coming from BOEM, which could impact its online date. We point out that given ES plans to monetize the investment tax credit (ITC), we see less pressure for the project to *have* to commission within a four-year build window to qualify for the credit (it could instead prove continuous efforts towards completion). The more concerning issue would be re-negotiating the power purchase agreement (PPA) with Long Island. We stay tuned here, but we expect ES to wait to provide clarity around South Fork once BOEM's cumulative impact study timeline is certain.

- **NSTAR Gas rate case**: On Nov 8, ES subsidiary, NSTAR Gas filed its expected gas rate request with the MA DPU for a $38mn rate increase at a 10.45% ROE and 54.85% equity ratio. The filing includes a proposed performance based rate (PBR) mechanism including inflation and a 1.3% adder and would support a meaningful 5-year rate stayout. The filing includes a long-term plan to fund safety and reliability improvements following the Merrimack Valley incident with NI subsidiary Columbia Gas, which we expect to support express incremental distribution capex likely to be reflected in the 4Q capex update. Proposed rates would be effective Oct 1st 2020.

- **PSNH**: We also look for updates on the Public Service of New Hampshire (PSNH) rate case (Docket DE 19-057). Recall, the NH PUC Staff recommended a $24.4mn rate increase at a 8.5% ROE, 50% equity ratio, ~$1.15Bn year-end ratebase, denial of proposed multi-year rate plan, and proposal for a Grid Transformation and Enablement Program (GTEP). ES originally requested a $69.3mn increase in permanent rates at a 10.4% ROE, 54.85% equity layer, and ~$1.215Bn ratebase. The NH PUC has already approved a $28mn interim rate increase for PSNH, slightly

lower than the $33mn requested by ES, effective Aug 1st (benefiting 2H19 earnings). A final PUC decision is expected May 20, 2020 barring a settlement.

Estimates

We largely leave estimates untouched owing to Eversource's resilient decoupling mechanisms in all subsidiaries outside PSNH.

Table 47: ES EPS Estimates

EPS by Business	2016A	2017A	2018E	2019E	2020E	2021E	2022E	2023E	2024E
CL&P	1.03	1.17	1.19	1.30	1.32	1.37	1.42	1.44	1.46
PSNH	0.41	0.43	0.36	0.38	0.43	0.45	0.46	0.48	0.51
WMECO + NSTAR	1.10	1.17	1.20	1.39	1.39	1.52	1.65	1.81	1.92
NSTAR Gas	0.10	0.10	0.13	0.12	0.15	0.20	0.23	0.26	0.30
Yankee Gas	0.14	0.12	0.18	0.18	0.19	0.21	0.23	0.24	0.25
Parent (ex-ITCs/Offshore/Aquarion/etc)	0.15	0.11	0.10	0.07	0.06	0.04	0.02	(0.01)	(0.03)
Offshore Wind (PPA NI)								0.02	0.14
Offshore Wind (ITCs)								0.02	0.11
Aquarion			0.10	0.10	0.11	0.11	0.12	0.13	0.15
Consolidated	2.96	3.11	3.25	3.45	3.65	3.90	4.14	4.40	4.81
Guidance			3.20-3.30	3.40-3.50	3.60-3.70				
Consensus		3.12	3.28	3.45	3.64	3.89	4.13	4.38	4.84
Mgmt EPS CAGR: 5-7% off 2018A	2.98	3.11	3.25	3.45	3.65	3.87	4.10	4.35	4.61
Low End				3.41	3.58	3.76	3.95	4.15	4.36
High End				3.48	3.72	3.98	4.26	4.56	4.88
Core Utility EPS (excl. Offshore)	2.96	3.11	3.25	3.45	3.65	3.90	4.14	4.36	4.56
BofAe Utility CAGR '19-'XXE								6.0%	5.7%
BofAe CAGR '19-'24E				6.9%					

Source: BofA Global Research estimates, company report, Bloomberg

Valuation

We MtM the peer multiple to 17.6x and increase premiums to 2x for CL&P, WMECO & NSTAR to reflect decoupling mechanisms (vs 1x for PSNH),1x for gas names, and 3x for Aquarion. Even so, this results in only an $83/sh PO and we reiterate our Underperform rating.

Table 48: ES SOTP Valuation

2022E SotP Analysis - BofAe

All figures in USD millions except per share

Regulated Utilities	2022E NI	EPS	P/E Multiple					Equity Value	
			Peer	Prem/ Discount	Base	Bull	Bear	Base	Bull
Relative Utility Group P/E Multiple									
Group Peer Multiple - Electric			17.6x						
Group EPS '18-'22 CAGR - Electric			5.00%						
Electric Utilities			18.5x						
CL&P	$483	$1.42	18.5x	2.0x	20.5x	21.5x	$27.71	$29.13	$30.55
PSNH	$155	$0.46	18.5x	1.0x	19.5x	20.5x	$8.42	$8.88	$9.33
WMECO & NSTAR Electric	$561	$1.65	18.5x	2.0x	20.5x	21.5x	$32.18	$33.83	$35.48
Group Peer Multiple - Gas			17.6x						
Group EPS '18-'22 CAGR - Gas			5.10%						
Gas Utilities			18.5x						
NSTAR Gas	$79	$0.23	18.5x	1.0x	19.5x	20.5x	$4.32	$4.56	$4.79
Yankee Gas	$78	$0.23	18.5x	1.0x	19.5x	20.5x	$4.24	$4.47	$4.70
Other Segments									
Aquarion - Water Utility	$42	$0.12	18.5x	3.0x	21.5x	22.5x	$2.54	$2.66	$2.79
						NPV			
Add NPV of 1.7GW Offshore Wind						$518	$1.52	$1.52	$1.52
@ 6% Operating Discount Rate @ 50% Ownership w/ 8% Construction Risk Discount Rate									
Parent - Small Investments, etc	$6	$0.02	18.5x	0.0x	18.5x	20.5x	$0.35	$0.35	$0.38
HoldCo Debt Adjustments (50/50 Weighted to P/E and netting out debt)									
Add: Parent Interest Expense @ 50%	$69	$0.20	18.5x	1.0x	19.5x	0.0x	$1.97	$1.97	$1.97
Parent Debt @ 50%	$3,200							-$4.71	
Total	$1,406	$4.14					$78.53	$82.65	$86.80
Shares outstanding (projected avg)								*340*	
Total Equity Value Per Share							$79.00	$83.00	$87.00
Price as of close 04/20/2020								91.56	
FY20 Dividend								2.27	
Dividend Yield								2.5%	
Total Return Projected								-6.9%	

Source: BofA Global Research estimates, company report, Bloomberg

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Eversource Energy: Raising to the midpoint of range; can the offshore clouds part?	Julien Dumoulin-Smith	21 February 2020
Eversource Energy: Fairly muted 4Q update ahead, near-term capex revisions limited; Underperform	Julien Dumoulin-Smith	09 January 2020
Eversource Energy: Focus on CT AMI and grid mod as timeline in focus: Underperform	Julien Dumoulin-Smith	07 November 2019
Eversource Energy: Sunrise-ing on offshore wind: Latest NY contract details released	Julien Dumoulin-Smith	24 October 2019

FirstEnergy (FE)

We reiterate our Buy rating on FE (following our recent upgrade here) with a quiet first quarter call approaching. We expect to see the Street focus on New Jersey given it's the only regulatory rate case the company is in right now (note we see a strength in the stay-out trend in other subs). Here, interim rates already took effect, but a ruling on its 10.8% ROE request is outstanding. We note the company is somewhat shielded from COVID impacts given it recently was awarded decoupling in Ohio making it a third less sensitive to load than before; also important to note is the low portion of revenue industrial sales contribute (7%) and that just 10% of industrial revenue is volumetric-based Further, FE recovers uncollectible expenses in OH / NJ through a rider and in PA / WV / MD through base rates. As for other updates, we continue to look for commentary around extension of the Electric Security Plan (ESP) given the commission removed the requirement for rate case filing in '24; note it still may be too early on this front, though. Finally, we continue to see the company steadily moving forward with its $3bn per year of capex trajectory. We forecast a 1Q20 estimate of $0.62/sh – just 1c lower than Consensus.

1Q20 EPS Walk

Below, we present our EPS forecast for 1Q20. We are roughly in line with Consensus (BofA $0.62/sh vs. Consensus of $0.63/sh). This stems from a $0.67/sh 1Q19.

- **Drivers**: Drivers for the quarter include -4c from mild weather in 1Q20 (not as impactful as peers noting decoupling in Ohio), +4c from Ohio decoupling true up, -6c from Ohio DMR stopping.
- **Other**: We expect flat distribution sales growth, and some impact from Maryland rates and other states' riders.
- **Wildcard**: We highlight COVID impacts are a wildcard, as well as the full extent of weather.

Table 49: FE 1Q20 EPS Walk

FirstEnergy 1Q20 Earnings Walk	EPS
1Q19E Adjusted EPS	0.67
Regulated Distribution	-0.04
Weather Vs normal in 1Q19	0.00
Weather Vs normal in 1Q20	-0.04
OH decoupling	0.04
Distribution sales growth	0.00
MD: $13mn annual impact	0.01
Riders: Including Ohio Grid Mod and PA DSIC	0.02
OH: DCR Rider June 1st 2019 (+$22Mn YoY)	0.01
OH: DMR (stopped recognizing earnings benefit)	-0.06
FE Tomorrow	0.00
O&M: Pension & OPEB	0.01
D&A and taxes	-0.02
Debt maturities	0.00
4Q 2018 we had higher O&M	0.00
Regulated Transmission	0.01
Revenues (net of D&A and taxes): higher ratebase	0.01
Parent and Other	-0.02
Tax rate benefit	-0.02
1Q20E Adjusted EPS	0.62
1Q20E BofAe EPS	0.62
1Q20 Consensus	0.63
1Q Guidance	0.60-0.70
2020 BofAe EPS	2.50
2020 Consensus	2.49
2020 Guidance	2.40-2.60

Source: BofA Global Research estimates, company report, Bloomberg

Items to track

COVID: Decoupling in Ohio makes less sensitive; PA is the real focus

The company's (new) decoupling in Ohio for 2020 makes FE 1/3rd less sensitive to loan than it was beforehand; decoupling or weather normalization is not present in other jurisdictions but FE does have energy efficiency riders (incl. demand response) except in WV. For a -1% decline in load, retail is impacted by -$0.02/sh, commercial by -$0.006/sh, and industrial by -$0.005/sh. Further, FE derives most (i.e. 65%) of its revenue from residential (meaning just 28% from commercial and 7% from industrial). Finally, for industrial customers, only 10% of revenue is volumetric-based while the rest is fixed. As for bad debt, FE recovers uncollectible expenses in OH / NJ through a rider and in PA / WV / MD through base rates. Finally, there's no risk around off-system sales / wholesale revenues given WV is only jurisdiction w/ generation and FE has an ENEC rider there (reconciled annually).

Pennsylvania is what to watch

While Pennsylvania has attracted limited attention this remains *our* focus at present among the numerous Covid exposures given its lack of any contemplated base rate cases and lack of decoupling. That said, margin remains biased towards resi mix, but still an underlying risk on earned ROE trends. We've already moderated our ROEs a bit in this state albeit still assume healthy returns overall in our last EPS est update.

New Jersey: The only rate case activity this year so far

FE filed a JCP&L transmission and distribution rate cases, with formula rates having gone into effect January 1st (subject to refund); a FERC decision on these transmission rates is anticipated in 1H20. The value of the formula rate would be for future years (i.e. there is a minimal anticipated impact on 2020). There is concern given the 10.8% filed but recent models indicating FERC base rates could fall within 8-10% depending on when data is selected.

Also important to note is that FE has a limited regulatory calendar compared to other utilities; this limits risk of downward shifts in authorized ROEs that other names are likely to face this year due to lower Treasuries (leading regulators to suspect lower costs of capital to build infrastructure). Limiting authorized ROE revision risk is increasingly a key theme in the sector after our latest conference and we perceive FirstEnergy as among the quietest large-cap companies from a regulatory perspective through its entire forecast period. While this limits upside capex and further positive revisions, we view its steady EPS growth as enabling its current outlook.

Ohio: Doubt legislation for '20 but perhaps in the future

While we doubt it's possible to pass in 2020 given COVID's situation, we expect the next legislative session to at least consider bills similar to proposed HB 247, 246, and 13. These could provide key investment opportunities (particularly for neighbor AEP) around industrial customers, broadband, and utility-regulator relations, although FE has not shared how exactly this could impact EPS growth for the company. These could also indicate a potential ESP (electric security plan) resolution that extends the current plan from '24 to '30.

Capex likely to be consistent

We continue to anticipate that FE will look to largely stay around the $3bn/ yr capex range in the years to come. We sense regulatory recovery and stable cash flows, balance sheet considerations drive this spend (and as such see less of a risk from Covid) beyond the operational challenges that may exist this year in executing.

Credit discussions with S&P

While FE has more holdco leverage than peers, we anticipate that FE may consider starting to discuss its credit metrics with rating agencies soon, with potential positive news to come from S&P on its FE outlook considering the agency lowered its FFO/debt

threshold to 12%. Note Moody's upgrade threshold is 14% and our reconciliation is mid-12%'s. Recall that issuing $2bn of equity equates to roughly only a 1% increase in FFO/debt, and that the company plans for incremental equity '22 (after which mgmt. has noted could be up to $600mn/yr). With its FES business disposition resolved, we perceive few angles to meaningfully shift its balance sheet outlook.

Estimates

We keep estimates largely the same given decoupling as well as our expectation that there is a more modest pace of consistent growth given ratebase is driven largely outside of any meaningful rate cases.

Table 50: FE EPS Estimates

EPS	2016A	2017A	2018A	2019E	2020E	2021E	2022E	2023E	2024E	2025E
Ohio Utilities	0.50	1.03	1.23	0.92	0.82	0.85	0.86	0.88	0.91	0.95
Ohio Edison (Inc PennPower)	0.35	0.59	0.64	0.50	0.48	0.50	0.52	0.53	0.56	0.58
CEI	0.09	0.27	0.39	0.26	0.20	0.20	0.20	0.21	0.21	0.21
TE	0.06	0.17	0.20	0.15	0.14	0.14	0.14	0.14	0.15	0.15
West Virginia										
MonPower	0.15	0.16	0.25	0.21	0.21	0.22	0.23	0.23	0.23	0.23
Maryland										
Potomac	0.14	0.10	0.10	0.10	0.12	0.14	0.16	0.18	0.19	0.21
New Jersey										
JCP&L	0.19	0.26	0.32	0.32	0.33	0.35	0.35	0.37	0.38	0.41
Pennsylvania	0.73	0.76	0.93	0.92	0.93	0.94	0.94	0.95	0.99	1.02
PennPower (already included in OE)	0.05	0.07	0.07	0.08	0.08	0.08	0.08	0.08	0.08	0.09
Penelec	0.21	0.22	0.32	0.29	0.30	0.31	0.31	0.31	0.32	0.33
WPP	0.27	0.25	0.23	0.24	0.24	0.23	0.23	0.24	0.25	0.26
MetEd	0.21	0.22	0.31	0.31	0.32	0.33	0.32	0.32	0.33	0.34
Regulated Utilities (Inc Transmission)	*1.66*	*2.23*	*2.75*	*2.40*	*2.34*	*2.43*	*2.46*	*2.52*	*2.62*	*2.73*
Regulated Distribution	-0.55	2.32	2.31	2.26	2.16	2.23	2.23	2.26	2.33	2.41
Guidance	2.60-2.70	2.27-2.31	2.34-2.40 w/ adj	2.20-2.26	2.13-2.27					
FET	0.45	0.62	0.58	0.66	0.69	0.74	0.81	0.87	0.94	1.00
Intrastate	0.28	0.13	0.21	0.16	0.18	0.20	0.22	0.26	0.29	0.32
Transmission	0.73	0.83	0.74	0.83	0.87	0.94	1.03	1.13	1.22	1.32
Guidance		.82-.84	.74-.76	.83-.84	.85-.89					
Competitive Energy Svcs.	0.60	0.46	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Guidance		0.42-0.46								
Corporate (reduced by pref)	-0.55	-0.53	-0.56	-0.51	-0.55	-0.55	-0.56	-0.54	-0.53	-0.52
Guidance		-0.51	(.58)-(.56)	(.53)-(.50)	(.58)-(.56)					
Eliminations		0.16	0.13	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Consolidated EPS	2.61	3.07	2.59	2.58	2.50	2.61	2.71	2.86	3.03	3.19
Previous EPS		3.07	2.59	2.58	2.48	2.61	2.69	2.86	3.02	3.17
Guidance		3.00-3.10	2.50-2.60	2.50-2.60	2.40-2.60					
Consensus EPS		3.05	2.54	2.53	2.49	2.64	2.77	3.03		
EPS CAGR off 2.15 (2018)					7.93%	6.72%	5.95%	5.84%	5.87%	5.79%
EPS CAGR off 2.43 ('19 2.55 Midpt less 0.12 DMR)					3.06%	3.70%	3.69%	4.12%	4.49%	4.63%
Y/Y Growth					-2.77%	4.34%	3.67%	5.41%	6.02%	5.31%
EPS CAGR off 2020						4.34%	4.00%	4.47%	4.85%	4.95%
EPS CAGR off 2021							3.67%	4.53%	5.03%	5.10%
Ex CES EPS	2.02	2.61	2.59	2.58	2.50	2.61	2.71	2.86	3.03	3.19
YoY Growth Rate Excl CEC EPS				0%	-3%	4%	4%	5%	6%	5%
Guidance: 5-7% CAGR '18 thru '23										
Bottom - 5%			2.15	2.26	2.37	2.49	2.61	2.74	2.88	3.03
Top - 7%				2.30	2.46	2.63	2.82	3.02	3.23	3.45
Shares	429	444	538	539	541	541	547	559	570	581

Source: BofA Global Research estimates, company report, Bloomberg

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
FirstEnergy: A Reformulated Company: Upgrade to Buy on de-risked strictly regulated profile	Julien Dumoulin-Smith	10 March 2020
FirstEnergy: Holding firm on Neutral after good 4Q	Julien Dumoulin-Smith	10 February 2020
FirstEnergy: Extending the EPS CAGR to '23 at 5-7%: We're right there already too	Julien Dumoulin-Smith	08 November 2019
FirstEnergy: Making sense of 2020 guidance & ratebase comp, shifting down est's slightly	Julien Dumoulin-Smith	05 November 2019

Pinnacle West (PNW)

We expect Q1 Operating EPS of $0.15/sh as compared to $0.16/sh Street estimates. Q1 is as seasonally slow quarter for PNW as its Arizona service territory generates most of its electric demand in the warmer months, particularly Q3. We expect that Covid reduced demand slightly at the end of the quarter as shut down orders spread in the state though the greater impact is likely to come in Q2 or later. They key lever for PNW to offset lost earnings from commercial and industrial customers is control of O&M - in fact mgmt's 2020 guidance already incorporates O&M savings into the forecast and it remains to be seen whether costs can be flexed even more to offset lost revenues. We flag additional possible risk of the rate case slipping further into 2021 as the commission's attention is likely occupied with service reliability issues during the health emergency. We further note that PNW had increased its bad debt expense target for 2020 given last year's disconnect moratorium, suggesting it may be better able to withstand an increase in delinquent accounts than peers – though note the likelihood of regulatory action to address increases in bad debt expense.

1Q20 Walk

We forecast 1Q20 adjusted EPS of $0.15 vs. $0.16 in 1Q19 and $0.16 consensus.

- **Key Drivers:** Weather will be a slight negative driver as 6 cents of benefit from Q1 2019 is normalized and an additional 4 cent uplift from slightly colder than normal conditions in the most recent quarter. We expect $0.03/sh in savings from ongoing O&M initiatives and highlight that the degree to which mgmt. can flex short term costs will drive the ability to offset lost sales (1 cent impact in Q1). We expect higher D&A driven by growing rate base to be an 11 cent drag.

- **Unknowns:** Weather is difficult to estimate given Q1 months have different weightings toward cooling and heating degree days, with January heating playing the biggest role.

Table 51: PNW Q1 walk

PNW 1Q20 Earnings Walk	EPS
1Q19 Adjusted EPS	$0.16
Weather return to normal	($0.06)
Weather effect vs norm	$0.04
Sales volume effect	($0.01)
Gross margin	$0.12
O&M	$0.03
D&A	($0.11)
Property tax deferral	($0.01)
Interest Expense	($0.01)
TEAM	$0.00
Other Opex	$0.00
Dilution	($0.00)
1Q20E Adjusted EPS	$0.15
1Q20 Consensus	$0.16
2020E Adjusted EPS	$4.83
2020 Consensus	$4.82
2020 Guidance	4.75-4.95

1Q19 Shares Outstanding	113
1Q20 Shares Outstanding	113

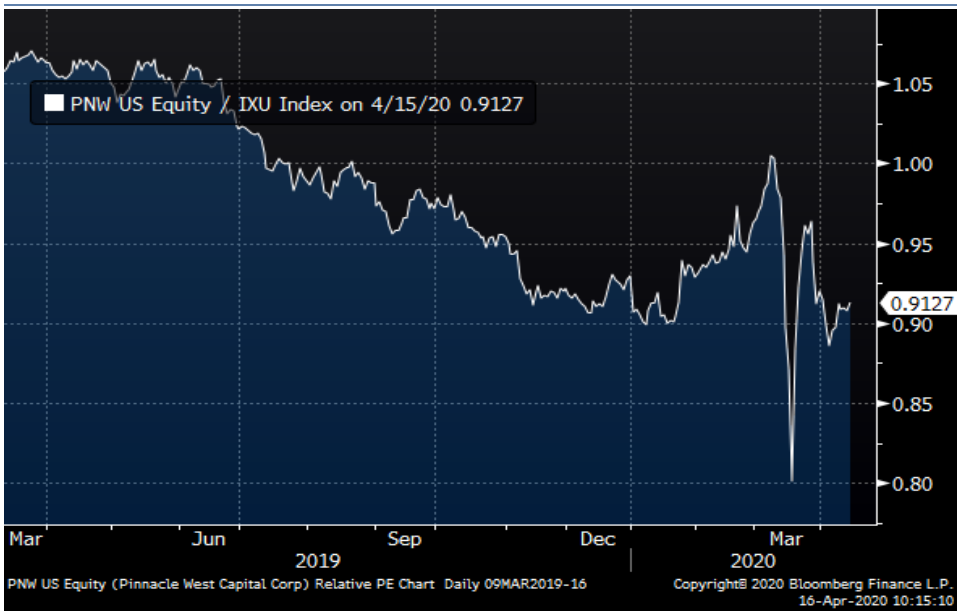
Source: BofA Global Research Estimates, company report, Bloomberg

Stock trading dynamics

Shares of PNW have de-rated slightly following the late March Covid-driven market volatility, and now trade at a relative 2-year PE to the IXU Index near the lows achieved at the end of Q4. PNW's service territory remains largely weighted toward residential

customers at over 50% of total demand, which should insulate its revenues somewhat from an expected decline in sales from commercial and industrial (C&I) customers – note that PNW has single-digit exposure to industrials with the balance being commercial exposure. The primary Covid-related risk on the regulatory front is further delay of the ongoing Arizona Public Service (APS) rate case, with the Arizona Corporation Commission (ACC) already pushing the proposed time frame of the rate case into 2021 (75-day delay) with possibility of additional delays depending on the duration of Covid shut down orders. Electoral concerns make the situation potentially more opaque given potential for turnover at the commission following Nov elections.

Exhibit 4: PNW shares relative value vs. IXU



Source: Bloomberg

Quantifying the impact of Covid shutdowns

APS does not have a separate bad debt expense recovery mechanism in its rates with expense rolled into customer rates based on a historical test year. While APS does not have traditional decoupling, it utilizes the Lost Fixed Cost Recovery (LCFR) mechanism that recovers lost fixed costs related to EE and Distributed Generation. The company estimates a 16-20 cent EPS impact from a 1% reduction in load, with the effect weighted toward residential customers who make up 51% of total load.

PNW proactively released March demand numbers indicating that through the 12th of the month residential sales were flat y/y while commercial and industrial (C&I) grew by 2-3%. For the remainder of the month as the Covid situation unfolded residential sales increased 7% y/y while C&I declined by 12-13%. PNW's annualized EPS sensitivities to a 1% move in demand for resi/comm/industrial are $0.09/$0.07/$0.01. Given PNW's disclosures, we estimate that Q1 EPS impact from Covid-related demand shifts was -$0.01, as an increase in higher-margin residential load mostly offset the larger declines in C&I.

Table 52: March EPS impact – resi mutes the C&I impacts to a large extent– are they the first of many to indicate this substantial offset in sales trends?

	EPS impact per 1% chg in annual sales	% of total load	Mar 1-12 change y/y	Mar 1-12 impact	Mar 13-31 change y/y	Mar 13-31 impact	March cumulative
Residential	0.09	51%	0%	-	7%	0.031	0.031
Commercial	0.07	38%	2-3%	0.006	(12)-(13)%	(0.043)	(0.037)
Industrial	0.01	11%	2-3%	0.001	(12)-(13)%	(0.006)	(0.005)
Total	0.16-0.20	100%	2-3%	0.007	(5)-(6)%	(0.018)	(0.012)

Source: BofA Global Research Estimates, company report

We acknowledge the limits of this disclosure given that it is only for the month of March with only half the month impacted by Covid, while demand in Jan-Feb was likely unaffected by the virus. PNW additionally included a disclosure of a potential $0.06 EPS impact if residential demand were to grow by 6% and commercial and industrial were to each decline by 10% - we note that since these are y/y comparisons they take into account the growth in residential load linked to air conditioning in the warmer Q2 months. PNW additionally disclosed that its pension plan hedges 100% of its interest rate exposure via Treasury futures, suggesting its plan's funding gap has declined YTD by less than the 11% estimated by our mtm analysis (and likely rebounded since our report with the broader market).

Rate case developments and top issues

The ACC issued a procedural order on March 18 that pushed back the timeframe of the pending rate case. By pushing out key milestones including staff and intervener testimony (originally scheduled for May, now due in August) the commission essentially assured that the case will not reach a resolution in 2020. While this assures that at a minimum commission Chair Bob Burns will not rule on the case as he is termed out at the end of the year, there remains uncertainty about the makeup of the commission in 2021 given 3 Republican-held seats are up for election, and the potential impact this would have on the outcome of the case. Below we present the updated rate case timeline while noting that the updated timeline was issued in mid-March as the Covid situation was still unfolding, and there remains the possibility of further delays.

Table 53: APS rate case amended timeline

Event / Item Due	Original	Updated
Application	10/31/2019	
Deadline for Motions to Intervene	2/11/2020	
Staff & Intervenor Testimony w/o Rate Schedules	5/20/2020	8/3/2020
Staff & Intervenor Testimony w/ Rate Schedules	5/27/2020	8/10/2020
APS Rebuttal Testimony	6/18/2020	9/1/2020
Prehearing Conference	7/13/2020	9/26/2020
Hearing Begins	7/17/2020	9/30/2020
Hearing Ends (30 day)	8/31/2020	11/11/2020
Transcripts Filed	9/11/2020	tbd
Briefs Due w/ Final Schedules	9/16/2020	tbd
Response Briefs Due	9/25/2020	tbd
Recommended Opinion and Order	11/25/2020	tbd
Exception Period Ends	12/16/2020	tbd
Open Meeting	12/17/2020	tbd
Deadline for Final Decision (AZ rule)	2/21/2021	tbd

Source: BofA Global Research estimates, ACC

Rate cases unlikely to be settled, potentially decided by different commissions

Both FTS and PNW have electric rate cases pending in front of the ACC. Stakeholders see potential for settlement as unlikely in either rate case given prior ACC utility staff statements, despite the heavy workload placed on staff of late with multiple rate cases pending. Given timing of each case, with FTS having been filed several months prior to PNW, it is increasingly likely that the commission that decides the FTS case will be different by at least one member from the one that decides PNW - recall that 3 of 5 seats are up for election this year including the one held by Chair Burns who is termed out. Bottom line: while Covid-related shutdowns are placing additional strain on an already-overburdened utility staff at the commission, we see a fully litigated path as the most likely resolution for APS's case.

Four Corners scrubbers remain key issue

The scrubbers installed at Four Corners are a meaningful portion of the total revenue ask of $73m - relative to the $184m total revenue increase requested. The recovery of the scrubbers was included in the last PNW rate case and the utility received a favorable administrative law judge (ALJ) recommendation to receive a step-up in rates mid-year in 2018. With the step-up having not been brought forward by the ACC the item now represents a significant discrete ask as part of the current case. Other notable items are

renewable generation / rooftop solar as well as rate making issues including a formula rate proposal and a pilot subscription rate program.

Renewables in focus with new resource filing in June

PNW capex outlook relies heavily on investment in renewable generation, accelerating spend in the near term such that the plan sees rate base growing by ~8% through 2022 vs. a long-term goal of 6-7%. Recall the recent announcement of a 2050 decarbonization goal with intermediate 2030 goal of 65% clean energy by 2030 with 45% renewables. The clean gen plan calls for the addition of 850 MW of battery storage as well as 100 MW of solar generation by 2025 - note storage technology has been developing rapidly with several qualified developers capable of delivering utility-scale solutions today. The storage plan will include a mix of standalone facilities as well as batteries added to existing PNW solar assets. PNW intends to file its new Integrated Resource Plan (IRP) in June, its first since the announcement of the ambitious new green generation goals. Given the focus around its decarbonization agenda we would expect the IRP to include an updated timeline for retiring of coal plants in line with the long-term plans laid out earlier in Q1 along with further renewable generation options.

The APS' recent approval of the 500-kV Ten West Link transmission project from California to APS' Delaney Substation located 60 miles outside of Phoenix should also boost the opportunity for renewable development and procurement. As the proposed line will cross from Arizona into California, it will allow APS to procure excess renewable energy from California during peak generation times. Further, the project has already reported 5,000 MW of interconnection requests from Arizona-based renewable developers which could further boost renewable development. Recall that under a recent ACC ruling, APS and other state utilities are required to sign contracts of 18 years or longer with operators of Qualified Facilities (QFs) under the Public Utility Regulatory Policies Act (PURPA) – APS had initially proposed a 2 year minimum contract tenor but the commission increased it to 18 in its final decision last December.

Lost fixed cost rate finalized

APS received a decision in its most recent Lost Fixed Cost Recovery (LCFR) mechanism filing related to lost energy sales revenues from customers related to energy efficiency initiatives, principally those utilizing distributed generation. The new rate will be $0.372/kW per month for customers on a demand rate and $0.00125/kWh per month for customers on an energy-only rate, with an estimated revenue recovery of $26.6m in 2020, down from $36.2m in 2019. Recall the LCFR is an annual filing under which APS seeks to recover fixed costs related to revenues lost by customers who are electing for distributed generation.

EPS estimates

We tweak our 2020 estimates lower to account for the likelihood of lost revenues due to Covid shutdown orders in place. Our new consolidated estimate of $4.78 is toward the low end of mgmt.'t guidance range and reflects essentially flat EPS growth y/y. We are slightly below Street consensus for 2020 on our updated estimates though we perceive downside to consensus forecasts as Covid-related lost revenues are factored in. As the ACC has not yet flagged a *further* deterioration in the rate case time frame, we do not adjust our estimates for 2021+ which currently assume the existing rate case schedule with a fully litigated resolution in mid-Q1.

Table 54: PNW estimates

PNW EPS Estimates	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E	2025E
EPS From Continuing Operations	$4.55	$4.71	$4.95	$4.96	$5.32	$5.39	$5.79	$6.32	$6.34
Net Income (Loss) Attributable to Noncontrolling Interests	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17
Income From Discontinued Operations	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
Accounting Changes/Non Operating Adjustments	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
Linked to model - EPS	$4.37	$4.54	$4.77	$4.78	$5.15	$5.23	$5.62	$6.15	$6.18
APS - EPS From Continuing Operations	$4.66	$5.24	$5.19	$5.20	$5.58	$5.72	$6.16	$6.69	$6.72
Parent - EPS From Continuing Operations	($0.11)	($0.53)	($0.24)	($0.24)	($0.26)	($0.33)	($0.37)	($0.38)	($0.38)
Net Income (Loss) Attributable to Noncontrolling Interests	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)
EPS From Cont Ops Attributable to Common Shareholders	$4.37	$4.54	$4.77	$4.78	$5.15	$5.23	$5.62	$6.15	$6.18

Table 54: PNW estimates

PNW EPS Estimates	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E	2025E
Previous Estimates	*$4.37*	*$4.54*	*$4.77*	*$4.83*	*$5.14*	*$5.24*	*$5.63*	*$6.16*	*$6.19*
Guidance	4.15-4.30	4.35-4.55	4.75-4.95	4.75-4.95					
Consensus	$4.27	$4.48	$4.70	$4.82	$5.10	$5.34			
Delta vs Consensus			$0.07	($0.04)	$0.05	($0.12)			
EPS CAGR off 2019A				0.3%	3.9%	3.1%	4.2%	5.2%	4.4%
Street CAGR			3.5%	3.1%	4.0%	4.2%			

Source: BofA Global Research Estimates, company report, Bloomberg

Valuation: PO to $84, maintain Neutral

We maintain our Neutral rating on PNW as we see the current share price as adequately reflecting near-term risks around rate case outcomes, including the uncertain rate case recovery of SCR step up associated with Four Corners along with recovery related to Ocotillo. We reduce the valuation discount applied to PNW's peer group electric utility multiple of 17.6x to -2.5x from -1.5x in order to more adequately reflect ongoing rate case risk – with an uncertain timeline potentially pushing the implementation of new rates further out and lingering uncertainty around the outcome of commission elections in the fall. We reiterate our Neutral rating.

Table 55: PNW SOTP

Price Objective $84	
PNW Valuation: P/E Based on 2022E EPS	
	Price Objective
2022E EPS	$5.23
Group Peer Multiple - Electric	17.6x
Group EPS '18-'22 CAGR - Electric	5.00%
P/E Multiple - Utility Average	18.5x
Premium	-2.5x
Price Objective	$84
2020E Dividend	$3.16
Dividend Yield	4.0%
Total Return (%)	9.1%

Source: BofA Global Research Estimates, company report, Bloomberg

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BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Pinnacle West: Positive capex surprise, equity coming post-2020	Julien Dumoulin-Smith	24 February 2020
Pinnacle West: Equity needs lower than perceived? Ests still have sizable uncertainty	Julien Dumoulin-Smith	19 November 2019
Pinnacle West: Framing the wide Street EPS miss & more to come: Downgrade to Neutral, $90 PO	Julien Dumoulin-Smith	08 November 2019
Pinnacle West: Disconnect Meeting: Few Revelations, Maintain Buy	Julien Dumoulin-Smith	05 September 2019

PPL Corporation (PPL)

We remain Neutral rated on shares of PPL into the quarter. While shares have meaningfully underperformed this year, FX remains volatile with current forwards already at the low end of mgmt.'s (recently lowered) assumptions and we see load degradation as particularly concerning for the company. While the UK is decoupled, volumes are only trued up on a two year basis while US utilities are fully exposed outside of some fixed billing components (sensitivities suggest a 1% change in load is a penny impact in each jurisdiction). *We remain focused on the KY footprint as to sales impacts, particularly as a rate case this year seems unlikely given the latest ROE backdrop. Bottom line, we ultimately see risk/reward as balanced at the current valuation.*

PPL 1Q20 Earnings Walk

We forecast 1Q20 adjusted EPS of $0.73 compared to $0.70 1Q19 & $0.72 consensus.

- **Key Drivers:** We expect gross margin growth across the portfolio and currency tailwinds y/y given hedging position in the UK partially offset by dilution and higher expenses.

Table 56: 1Q20 Walk

PPL 1Q20 Earnings Walk	EPS
1Q19 EPS	$0.70
WPD	$0.02
Kentucky	$0.02
PPL PA	$0.01
Corp & Other	($0.02)
1Q20 BofAe Adjusted EPS	$0.73
1Q20 Consensus	$0.72
BofAe 2020E EPS	$2.50
2020 Consensus	$2.47
2020 Guidance	$2.40-2.60
1Q19 Shares outstanding	730
1Q20 Shares outstanding	756

Source: BofA Global Research, Bloomberg

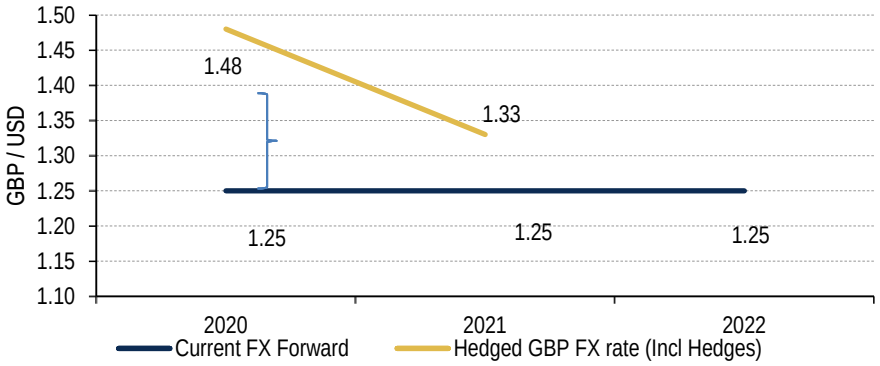
Contemplating COVID Implications

We see PPL as particularly exposed to load degradation amid the ongoing COVID pandemic. While the UK is decoupled, volumes are only trued-up on a two-year basis. While the US has some demand components, we note no decoupling in PA or KY and remain focused on the KY footprint specifically, particularly as any near term rate relief seems less likely on the margin given the latest rate paradigm. For domestic utilities, a 1% change in load is a penny impact in each jurisdiction and the company has some off system sales exposure but no bad debt expense trackers.

FX Outlook: Forwards Imply Low End of Revised Guide

Mgmt lowered expectations with its latest update given current FX rates and forecasts. While the company is 90% hedged for 2020 at an average rate of $1.48, it is only 5% hedged in 2021 at $1.33 and completely exposed in outer years. We note that on an open basis, every 1c in the exchange rate equates to about $0.01/sh of EPS for the company.

Chart 8: Budgeted vs. FX Forwards



Source: BofA Global Research, Bloomberg

WPD RIIO-ED2 Mini Model: OFGEM Prospects

The exhibit below reflects our latest UK mini model for the WPD (Western Power Distribution) business. Recall that Ofgem formally kicked off its RIIO-ED2 process in August 2019 with the publishing of an open letter consultation. A framework was laid out in Mid-December setting the blueprint, confirming the expectation that most design features would follow the earlier RIIO-2 reviews for Transmission and Gas Distribution (being finalised in 2020): a 5 year duration, retaining debt cost indexation, strengthening output incentives, and a move from RPI to CPI inflation indexation (which could ultimately help cash flows). Additional specifics and final decisions for ED (Electric Distribution) will start to shake out over the next couple of years (RIIO-ED1 price control is set to end at the end of March '23).

We therefore expect investors to continue to look for potential read-throughs as Ofgem works through the gas/transmission specific methodology – albeit likely with some delays given the on-going crisis. Developments thus far on the ED2 process have principally reflected those of its earlier counterpart including lower base returns and potentially a similar level to those proposed for transmission and gas. We continue to assume a -3% drop in ROEs under new rates, which we view as a sober set of assumptions *(anywhere in the low 5% to even 7% range on nominal basis appears reasonable in our view given lack of clarity on process).*

We ultimately expect nuances between ED2 and the gas/transmission framework given different risk profiles. However, we see a clear desire from Ofgem to maintain incentives and give the best performing companies an ability to overearn, particularly as distribution networks will be a key enabler of the net-zero carbon target. Any developments out of the COVID crisis will also be critical in terms of nuances around their thought process for UK utilities longer term.

Table 57: RIIO Mini Model

PPL WPD RIIO TABLE	2020E	2021E	2022E	2023E
Nominal RAV (WPD Financials) £Mn	7,996	8,415	8,917	9,449
Equity ratio	35%	35%	35%	35%
Current Allowed ROE	6.40%	6.40%	6.40%	6.40%
ROE Cut	0.00%	0.00%	0.00%	-2.25%
Adjusted ROE	6.40%	6.40%	6.40%	4.15%
UK Net Income (£Mn)	179	189	200	137
US Net Income ($Mn)	261	236	250	172
Hedge Price ($/£)	1.48	1.33	1.33	1.33
% Hedge	90%	5%	0%	0%
Hedge Value	$37.08	$0.75	$0.00	$0.00
Inflation				
Implied RAV Inflation	5.10%	5.24%	5.96%	5.96%
US Net Income Adjusted for Hedges	261	236	250	172

Table 57: RIIO Mini Model

PPL WPD RIIO TABLE	2020E	2021E	2022E	2023E
Depreciation/Pension	729	691	631	611
US GAAP vs UK Reporting	729	691	631	611
Incentives (USD)	2020	2021	2022	2023
Fast Track Award	32	28	28	29
Performance	114	98	106	125
Total Incentives	146	125	134	154
*Implied ROE (Incentives + UK NI / Nominal RAV * 35%)*	*9.26%*	*9.12%*	*9.14%*	*7.13%*
Earned ROE vs. Base ROE (+/-300bps in RIIO)	*2.9%*	*2.7%*	*2.7%*	*3.0%*
Less HoldCo Int	-68	-68	-68	-68
Adjusted US Net Income ($Mn)	1,068	985	946	868
Adjusted EPS	$1.41	$1.30	$1.24	$1.13

Source: BofA Global Research, Bloomberg

EPS Estimates

The table below reflects our latest EPS estimates after reflecting the latest currency forwards and on-going developments, and we continue to stress limited growth ahead given pension headwinds and questions around longer term UK returns, particularly without meaningful FX improvement.

Table 58: PPL Estimates

PPL EPS Estimates	2020E	2021E	2022E	2023E
Regulated Utilities				
International Regulated	$1.41	$1.30	$1.24	$1.13
Pennsylvania Regulated	$0.63	$0.66	$0.69	$0.72
Kentucky Regulated	$0.59	$0.65	$0.69	$0.72
Domestic Utilities	*$1.22*	*$1.31*	*$1.38*	*$1.45*
Parent/Other	($0.13)	($0.13)	($0.12)	($0.12)
Consolidated EPS	$2.50	$2.47	$2.50	$2.46
Prior Estimates	*$2.51*	*$2.48*	*$2.59*	*$2.59*
Consolidated Growth CAGR off 2018 ($2.30 midpoint)	4.31%	2.44%	2.07%	1.39%
Consensus	$2.47	$2.46	$2.56	$2.80
Guidance	$2.40-2.60	$2.40-2.60		
DPS	1.66	1.68	1.69	1.71
DPS Growth (%)	*0.61%*	*1.00%*	*1.00%*	*1.00%*
DPS Payout	66.34%	67.82%	67.84%	69.42%
FFO (CFO pre-W/C) / Total Debt	15.11%	15.18%	15.33%	15.29%

Source: BofA Global Research, Bloomberg

Valuation:

The table below reflects our latest valuation. As shown, we apply the latest peer multiple of 17.6x (vs. 20.6x previously) to our utility estimates for both PPL Electric and PPL Kentucky. We use a 30% premium to RAV for the UK business. Our price objective ultimately shifts to $29. We remain Neutral rated on shares seeing risk/reward as balanced.

Table 59: PPL SOTP

PPL Sum-of-the-Parts							Equity Value		
	EPS	Lower	Peer	Prem/ Disc.	Base	High	Low	Base	High
RAV Approach	C2021 RAV								
WPD RAV	11,058	0.8x	1.0x	0.30x	1.3x	1.8x	$8,846	$14,375	$19,904
Less: WPD leverage (80% Gearing)							($8,846)	($8,846)	($8,846)
							$0	$5,529	$11,058
UK Equity Value							$0	$5,529	$11,058
Implied Valuation / Share							*0.00*	*7.25*	*14.50*
Domestic: Regulated Utilities			2022 P/E Multiples						
Group Peer Multiple - Electric			17.6x						
Group EPS '18-'22 CAGR - Electric			5.00%						
	-	Base Multiple	18.5x						
PPL Electric Utilities	$0.69	17.5x		0.0x	18.5x	19.5x	$9,179	$9,705	$10,230
PPL Kentucky (KU/LG&A)	$0.69	17.5x		0.0x	18.5x	19.5x	$9,218	$9,746	$10,273
Parent/Int Expense	($0.12)	17.5x		0.0x	18.5x	19.5x	($1,661)	($1,757)	($1,852)
			50% Weighting						
PPL Cap Funding Debt	4,530		2,265				-2,265	-2,265	-2,265
Parent Interest Expense (Tax effected @ 21%)	145		73				1,270	1,342	1,415
--> Add back 50% of EPS drag above							-995	-923	-850
PPL Equity Value ($/Sh) Unrounded							$20.64	$29.24	$37.84
Shares Outstanding	2022E EPS						763	763	763
Total PPL Equity Value Per Share	$2.50						$21.00	$29.00	$38.00
Implied P/E							8.4x	11.6x	15.2x
Total Return Calculation									
Current Stock Price								$25.70	
Price Objective								$29.00	
Upside/Downside (%)								12.86%	
Dividend								$1.66	
Dividend Yield								6.46%	
Total Return								19.32%	

Source: BofA Global Research, Bloomberg

See below for our previous research on PPL:

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
PPL Corporation: Have shares round-tripped from their European tryst?	Julien Dumoulin-Smith	18 February 2020
PPL Corporation: Mum on M&A but US prospects need to be back in focus to add to deal confidence	Julien Dumoulin-Smith	06 November 2019
PPL Corporation: Upgrading to Neutral as Ofgem reaffirms the same, known, downside again	Julien Dumoulin-Smith	07 August 2019
PPL Corporation: Solving for 2021: UK overshadows the value proposition	Julien Dumoulin-Smith	19 February 2019

WEC Energy (WEC)

We expect WEC to hit the low end of its guidance range for the quarter despite the weather headwind given ability to flex O&M down as we expect demand impact from Covid to be limited in Q1 and largely weighted toward Q2. WEC is able to utilize its fuel recovery mechanism as a means of partially offsetting lower demand which had been forecast by the company to decline by ~1% in 2020. Accordingly, we maintain our Underperform rating.

WEC 1Q20 Earnings Walk

We forecast 1Q20 adjusted EPS of $1.32 compared to 1Q19 results of $1.33, consensus estimates of $1.33, and guidance of $1.32-1.34.

- **Key Drivers:** Positive YoY drivers include infrastructure investments from the Upstream, Bishop Hill, and Coyote Ridge wind farms (+$0.01), sales growth at the gas utility (+$0.01), reduced O&M expenses (+$0.01). Offsetting results includes the impact of weather which is estimated at 7 cents including a 2 cent drag from normalizing the impact of 1Q19 and incorporating the impact of 2020 milder weather which is estimated at 12% warmer than normal and 16% warmer than 2019.

- **Unknowns**: While Heating Degree Days (HDDs) were 16% above the prior year's level in WI, the exact magnitude of the benefit is difficult to estimate. Recall, WEC is decoupled in IL and at MN gas. Another unknown is the extent to which load growth was affected by Covid-related slowdowns as shut-in orders were generally implemented at the end of the quarter.

Table 60: WEC 1Q20 walk

WEC 1Q20 Earnings Walk	EPS
1Q19 Adjusted EPS	$1.33
Weather - 1Q19 normalized	($0.02)
Weather - 2Q20	($0.05)
Utility sales growth	
Electric	$0.01
Gas	$0.01
Rate Relief	$0.00
Fuel Recovery Mechanisms	$0.02
Interest Expense - re-financing	$0.00
D&A	($0.01)
O&M	$0.01
Storm expense	$0.00
ATC	$0.02
Infrastructure	$0.01
Dilution	($0.00)
1Q20 Adjusted EPS	$1.32
1Q20 Consensus	$1.33
1Q20 Guidance	$1.32-1.34
2019 BofASe	$3.72
2019 Consensus	$3.73
2020 Guidance	$3.71 -$3.75
Share Count	
1Q19	317
1Q20	317

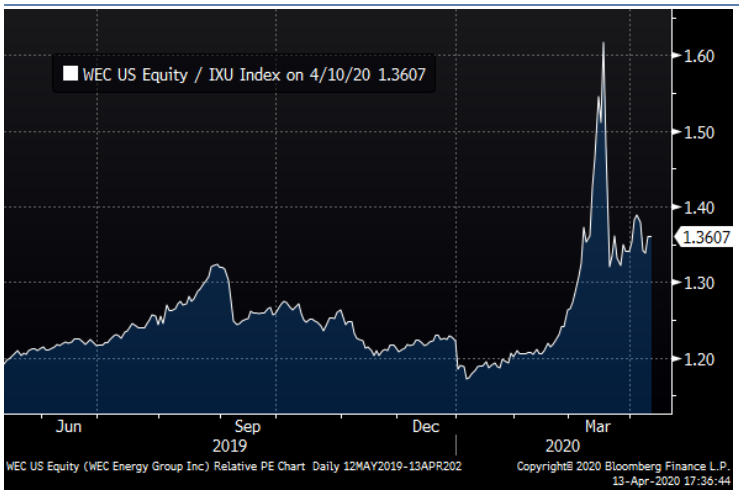
Source: BofA Global Research Estimates, company report, Bloomberg

Stock trading implications

Shares of WEC have performed well vs. the peer group of late reflecting the company's defensive nature amid significant market volatility and investor concerns about the effects on demand from Covid-related shut downs. After re-rating for much of the month of March, WEC trades at roughly 22x forward earnings ('22), a meaningful premium vs. our electric utility peer multiple of ~17x. While shares have consistently traded at a premium to the peer group since 2019, WEC now trades at over 1.3x

premium to the IXU on a 2 year forward PE relative basis, the highest such level in the past 12 months with the exception of the extreme market volatility seen in March. Accordingly we remain Underperform on shares of WEC as the shares remain priced richly relative to the peer group.

Exhibit 5: WEC relative PE chart



Source: Bloomberg

Partial decoupling and a debt tracker to mitigate impact

Most of WEC's jurisdictions do not have a bad debt rider with the exception of IL Gas. Additionally Wisconsin Gas and Wisconsin Electric have bad debt escrow accounting mechanisms. WEC's Illinois Gas and Minnesota Gas businesses have decoupling while the other jurisdictions of Michigan and Wisconsin do not - at both the electric and gas utilities. WEC's electric utilities do not have material exposure to losses from wholesale volumes and accordingly off-system sales are not expected to be a significant source of downside risk. In terms of margin breakdown, 62% of total margin comes from the Electric business with the balance coming from Gas. Residential is relatively heavily weighted among electric demand at 47%, with industrial accounting for 17% and commercial for the balance. 2020 EPS is expected to be impacted by approximately 2-3 cents from a 1% decline in demand and by 0.5 cents from a 1% decline in industrial sales, according to the company. We also highlight that pension funding is less of an issue for WEC than for many utility peers, as the company was fully funded in its *qualified* defined benefit plans at the end of 2019 and over 90% funded on a GAAP basis across all of its pension plans.

Commission latest: new appointee, addressing Covid

Back in March, Wisconsin Governor Tony Evers appointed Tyler Huebner to fill the seat vacated by the retirement of Mike Huebsch on the three-person Public Service Commission of Wisconsin (PSCW). Huebner has been the Executive Director of RENEW Wisconsin since 2013, where he led the organization's efforts to expand and promote the use of renewable energy in the state. He will serve out the remainder of Huebsch's term that expires on Mar 1, 2021. Huebner joins PSCW chair Rebecca Valcq as an appointee of Democrat Gov. Evers, while the third commissioner (Ellen Nowak) was appointed by Republican Scott Walker. We expect that the PSCW will continue to (and perhaps accelerate) its support for renewables investment in the state following this appointment. We expect incumbent utilities WEC and LNT to benefit from increased support for renewables and potentially an increased push for accelerated coal retirements - WEC's Columbia, South Oak Creek, and Weston units being potential candidates. As with other jurisdictions, the issue of undepreciated plant remains a hurdle for possible accelerated retirement, particularly given recent investment in scrubber technology at Columbia.

The PSCW was one of the first utility commissions in the US to act in response to Covid shut downs, suspending late fees and power disconnections for affected customers across the state on Mar 24 and opening a docket to evaluate recovery by utilities of extraordinary expenses incurred in an effort to keep power on for all customers during the declared health emergency. The PSC is working with utilities to identify specific expenses and foregone revenues that have been and are expected to be incurred due to the Covid emergency and is evaluating methods for recovery. Though it remains early days we see this as a constructive and proactive move by the PSC which should at least partially offset WEC's lack of bad debt trackers in Wisconsin.

EPS estimates

We update our 2020 EPS estimate for WEC to reflect headwinds from both lost demand resulting from Covid as well as mild Q1 weather, though the latter point may abate later in the year particularly if warm weather persists into the cooling season and residential load may be boosted by extended stay-in orders. Accordingly we reduce our 2020 estimate to $3.72 from $3.75, toward the low end of mgmt.'s $3.71-3.75 guidance range. Estimates are slightly below Street consensus in 2020-21 and a penny ahead in 2022. The degree to which mgmt. can flex O&M spending in order to offset the effects of Covid related shutdowns remains a key question as stay at home orders persist through Q2 and potentially longer.

Table 61: WEC estimates

WEC EPS Estimates	2018A	2019A	2020E	2021E	2022E	2023E	2024E
WI Electric	$1.13	$1.15	$1.25	$1.27	$1.31	$1.35	$1.38
WPS	$0.55	$0.59	$0.56	$0.59	$0.64	$0.68	$0.71
WI Gas	$0.24	$0.26	$0.39	$0.48	$0.58	$0.67	$0.75
Peoples Gas	$0.42	$0.50	$0.44	$0.49	$0.55	$0.60	$0.65
North Shore Gas	$0.05	$0.05	$0.05	$0.05	$0.06	$0.06	$0.06
ATC	$0.36	$0.39	$0.42	$0.44	$0.47	$0.49	$0.51
We Power (PTF) + Non utility infrastructure	$0.70	$0.76	$0.84	$0.89	$0.92	$0.95	$0.99
MERC/MGU	$0.14	$0.15	$0.13	$0.14	$0.15	$0.15	$0.16
Parent & Int Expense	(0.23)	(0.24)	(0.36)	(0.38)	(0.40)	(0.41)	(0.42)
BofA Estimate	$3.34	$3.60	$3.72	$3.97	$4.27	$4.53	$4.78
Company Guidance			$3.71 -$3.75				
Prior Estimates		*$3.60*	*$3.75*	*$4.00*	*$4.30*	*$4.56*	*$4.81*
BofA CAGR (off 2019 estimate of $3.50)			*6.15%*	*6.50%*	*6.86%*	*6.68%*	*6.43%*
Consensus	$3.33	$3.53	$3.73	$3.99	$4.26	$4.57	
Consensus CAGR			*6.6%*	*6.8%*	*6.8%*	*6.9%*	
Mgmt. Guidance 5-7% off $3.50 in 2019							
Low		$3.48	$3.71	$3.86	$4.05	$4.25	$4.47
Mid		$3.50	$3.73	$3.93	$4.17	$4.42	$4.69
High		$3.52	$3.75	$4.01	$4.29	$4.59	$4.91

Source: BofA Global Research Estimates, company report, Bloomberg

Valuation

We move our PO to $85 after refreshing for updated peer group electric (17.6x) and gas (17.6x) multiples and continue to stress very limited upside with shares trading above our valuation. We update our relative peer group premium for the Wisconsin electric utilities to 3.0x from 2.0x given positive regulatory backdrop in the state including prospects for bad debt recovery and decoupling. We also reduce the premium applied to We Power (PTF) from 2.0x to 1.0x. Bottom line, WEC shares continue to trade at a premium valuation and despite accounting for Wisconsin's positive regulatory backdrop in our SOTP the shares remain expensive, and accordingly we maintain our Underperform rating on WEC.

Table 62: WEC SOTP

Regulated Utilities	2022E EPS	2022E Net Income	P/E Multiple					Equity Value		
			Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric				17.6x						
Group EPS '18-'22 CAGR - Electric				5.00%						
Group Peer Multiple - Gas				17.6x						
Group EPS '18-'22 CAGR - Gas				5.10%						
Applied Multiple				Electric 18.5x Gas 18.5x						
WI Electric	$1.31	416	20.5x		3.0x	21.5x	22.5x	$8,528	$8,944	$9,361
WPS	$0.64	202	20.5x		3.0x	21.5x	22.5x	$4,141	$4,343	$4,545
WI Gas	$0.58	184	18.0x		0.5x	19.0x	20.0x	$3,306	$3,489	$3,673
Peoples Gas	$0.55	173	18.0x		0.5x	19.0x	20.0x	$3,120	$3,293	$3,466
North Shore Gas	$0.06	18	18.0x		0.5x	19.0x	20.0x	$317	$335	$352
ATC	$0.47	148	19.5x		2.0x	20.5x	21.5x	$2,876	$3,023	$3,171
We Power (PTF)	$0.61	193	18.5x		1.0x	19.5x	20.5x	$3,569	$3,762	$3,955
MERC/MGU	$0.15	46	18.0x		0.5x	19.0x	20.0x	$835	$882	$928
Parent & Int Expense	-$0.40	(126)	17.5x		0.0x	18.5x	19.5x	($2,201)	($2,327)	($2,453)
Total Implied Utilities	$3.96	1,254				20.5x		$24,490	$25,744	$26,998
Non Utility Energy Infrastructure	$0.31	98	15.5x		-2.0x	16.5x	17.5x	$1,521	$1,619	$1,717
Implied Valuation Multiple					19.9x					
HoldCo Debt Adjustment										
Add Back: 50% of Interest Expense	$0.11	35	19.5x		0.0x	20.5x	21.5x	$679	$713	$748
Subtract: HoldCo Debt (Net out 50%)	2,200	(1,100)						($1,100)	($1,100)	($1,100)
Total Equity Value								$25,589	$26,976	$28,364
Valuation								$81.00	$85.00	$90.00
Shares Outstanding										317
Rounded 12 Month Target Price										
Stock Price									$97.59	
Upside/Downside									-12.9%	
NTM Div Yield									2.5%	
Total Return									-10.4%	

Source: BofA Global Research Estimates, company report, Bloomberg

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BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
WEC Energy Group Inc: Watch the Cost Trajectory; Accelerating Infra Piece: but this is the debate	Julien Dumoulin-Smith	03 February 2020
WEC Energy Group Inc: Rolling out an ever higher capex plan	Julien Dumoulin-Smith	08 November 2019
WEC Energy Group Inc: Settlement terms more constructive than expected	Julien Dumoulin-Smith	26 August 2019

Xcel Energy (XEL)

After resolving much of the regulatory calendar from filing rate cases in 2019 (even recently announcing a settlement w/o details in TX), XEL is still working to file in 2020 in many states and exploring ability to push off some of the rate cases. We see two states of focus here: MN (using 2015 legislation that allows XEL to recover advanced grid spend through the transmission rider) and CO (depending on in the advanced grid initiative can be recovered via rider). Both depend on regulators, and we saw value in XEL being able to stay out of MN's last year. XEL isn't as exposed to COVID demand impacts as other names given its decoupling mechanisms in CO & MN (accounts for 45% of retail electric sales) and given its impact in prior events (i.e. '08 crisis and low oil prices of '16). Finally, we note our ests reflect XEL now selling Mankato to keep the utility fully regulated (we see viewed positively); while we had factored in 4c/yr for the non-reg asset before the sale, XEL was only expecting 1-2c/yr in early years. With our expectation of LT earnings squarely in the 5-7% trajectory, good FFO/debt metrics, and a consistent earnings growth story, we expect the name to be strong during recovery. Finally, given orig O&M '20 guidance, we expect there's room for savings that counterbalance some impacts from COVID & mild winter overall. As for 1Q, we forecast $0.53/sh vs. $0.62/sh likely un-updated Consensus. Reiterate Neutral.

1Q20 Walk

We expect a $0.53/sh 1Q20 estimate, versus a Consensus of $0.62/sh and a prior year's 1Q19 est of $0.61/sh. We expect Consensus has not been adjusted for weak weather and COVID impacts on demand.

- **Drivers**: With a number of rate cases filed in 2019, XEL has new rates starting in 2020 for MN, CO, NM, and TX (although some taking effect later this year). Impacting 1Q include Minnesota's interim sales true up and nuclear decommissioning (Jan 1, 2020), Colorado's electric rates (Feb 25, 2020), and last year's $4.5mn SPS incremental rate increase (March 11, 2019); these contribute to +5c for the walk. The capital rider revenue and AFUDC contribute another +3c.

- **Other**: We evenly distribute XEL's annual '20 guide between quarters for interest expense, O&M, and property taxes (-5c). We only include -5c of D&A as this will likely be a little more back-end loaded. Finally, we expect -2c of demand impact from COVID since most businesses were shut down for the last 2 weeks in March and some folks were working from home for the last 3 weeks.

- **Wildcard**: We expect XEL to be negatively impacted by the wild winter, likely a few pennies worth (1-3c); note 45% of the electric sales (in CO & MN) are decoupled.

Table 63: XEL 1Q20 Walk

Xcel Energy 1Q20 Earnings Walk	EPS
Ongoing EPS 1Q19	$0.61
Weather	
Return to normal	($0.03)
Current quarter	($0.02)
Rate Changes	
NSPM Minnesota Electric Interim sales true up & Nuke decommissioning ($122mn, Jan 2020)	$0.04
PSCo Colorado Electric rates ($35mn, Feb 25 2020)	$0.01
SPS New Mexico Electric rates ($31mn, 2Q20)	$0.00
SPS Texas Electric rates (requested $136mn, 3Q20)	$0.00
SPS Electric rates ($4.5mn March 2019)	$0.00
Capital rider revenue	$0.02
AFUDC	$0.01
Other	
Interest Expense increase	($0.02)
Increase in D&A expense	($0.05)
O&M (1-2% increase)	($0.01)

Table 63: XEL 1Q20 Walk

Xcel Energy 1Q20 Earnings Walk	EPS
Property taxes	($0.01)
COVID 1Q demand impact (-) and leap year pick-up (+)	($0.01)
Dilution (settled)	($0.00)
1Q20E Adjusted EPS	$0.53
1Q20E BofA Estimate	0.53
1Q20 Consensus	0.62
2020E BofA EPS	$2.72
2020 Consensus	2.76
2020 Guidance	2.73-2.83
Shares Outstanding 1Q19	516
Shares Outstanding 2Q20	525
Tax rate	25%

Source: BofA Global Research estimates, company report, Bloomberg

Key 1Q20 Topics

- **O&M**: XEL's original 2020 guidance includes a 1-2% O&M increase; we could see the company look to bend the curve if it needs from COVID impacts. We see this as a key differentiating strength compared to peers.

- **2019 Rate cases**: XEL is resolving many of its rate cases, having a settlement in principal for its TX case (we expect somewhat slowed down from working remote); we expect cap structure avoids concerns peers recently saw since XEL is integrated in TX and interveners all proposed 51% layers or higher. CO gas just received a schedule from an administrative law judge (would allow rates to be implemented in Nov) and NM is waiting for the commission to decide on the settlement.

- **2020 Rate cases**: As for next cases to be filed, we look for commentary on whether XEL can pursue transmission trackers to recovery other expenses in MN (given 2015 legislation allowed XEL to recover advanced grid spend) and CO (perhaps recovering the advanced grid initiative through a rider). We see rate case stayouts as a key strategy in avoiding ROE risk, and have confidence in XEL's ability. If filed, timelines would be later this summer for CO and in Nov for MN.

- **Mankato sold**: After purchasing Mankato as a non-regulated instead of regulated (which was accretive 3-4c vs 1-2c in the near-term, respectively), mgmt. absorbed feedback on being fully regulated and viewed a purchase as resulting in a better valuation for the company. We removed from our estimates any more PPA buyouts we thus expect to be regulated or not pursued.

- **COVID**: XEL has decoupling mechanisms in both Minnesota (fully) and Colorado (partially) representing 45% of retail electric sales: In MN, sales are trued-up for all electric classes, and in CO, decoupling is for resi and SC&I non-demand classes. XEL doesn't have bad debt recovery but we would expect the company to request deferred accounting if expenses significantly increase. As for looking at historic responses, we note that in 2016 when oil prices were in the $30 range, SPS YTD 2016 sales through 2Q16 declined by 1.1% (resi declined 3.2% and C&I only 0.6%). Meanwhile during the '08/09 crisis, XEL saw weather-adjusted sales down 1.8%. Finally in terms of sensitivity, we highlight the company anticipates a 100bps change in electric equates to a $25mn pre-tax impact (if the full change in sales was for C&I, the impact would be less but it's not separately broken out); we calculate this to be a 3-4c impact using a 21% tax rate.

Estimates

Our estimates remove the non-regulatory Mankato asset (given its sale in '20) and reflect our expectation that lower demand from COVID, mild winter, and oil price are somewhat balanced by more cost cutting. We await O&M announcements on the call.

Table 64: XEL EPS estimates

Subsidiary	2016A	2017A	2018A	2019E	2020E	2021E	2022E	2023E	2024E
Northern States Power Minnesota (NSPM)	0.96	1.01	0.96	1.05	1.11	1.29	1.44	1.53	1.63
Southwestern Public Service (SPS)	0.30	0.30	0.42	0.51	0.59	0.60	0.60	0.61	0.62
Public Service Colorado (PSCo)	0.91	0.94	1.08	1.11	1.06	1.05	1.07	1.14	1.19
Northern States Power Wisconsin (NSPW)	0.14	0.16	0.19	0.15	0.16	0.18	0.20	0.21	0.23
Parent (Excl Mankato)	(0.10)	(0.12)	(0.18)	(0.17)	(0.15)	(0.17)	(0.19)	(0.21)	(0.22)
Consolidated	2.21	2.29	2.47	2.64	2.76	2.94	3.12	3.28	3.44
EPS Growth (%)			*8%*	*7%*	*4%*	*7%*	*6%*	*5%*	*5%*
Prior Estimates			*2.47*	*2.64*	*2.83*	*2.99*	*3.14*	*3.31*	*3.46*
Guidance (Excl Mankato)	2.17-2.22	2.25-2.35	2.45-2.49	2.60-2.65	2.73-2.83				
Consensus			2.46	2.62	2.76	2.96	3.14	3.31	#N/A N/A
Mgmt EPS CAGR: 5-7% off 2018 base ($2.43)	2.21	2.29	2.47	2.60	2.78	2.95	3.12	3.31	3.51
		low	*2.43*	*2.55*	*2.73*	*2.87*	*3.01*	*3.16*	*3.32*
		high	*2.43*	*2.65*	*2.83*	*3.03*	*3.24*	*3.47*	*3.71*
BofAe CAGR '18-'23e (off $2.43)	6.2%								
BofAe CAGR '18-'24e (off $2.43)	5.9%								
Target FFO/Debt			17%	18%	17%	17%	17%		
BofAe FFO/Debt		22%	19%	19%	17%	18%	17%	17%	

Consolidating				2.64	2.76	2.94	3.12	3.28	3.44
Guidance				2.60	2.78				
Difference				*0.04*	*(0.02)*				

Source: BofA Global Research estimates, company report, Bloomberg

Valuation

We MtM the peer multiple (now 17.6x) and derive a $66/sh PO with the same 3x premium awarded for the quality mgmt., decoupling, and opportunity for more O&M. Reiterate Neutral.

Table 65: XEL SOTP Valuation

Regulated Utilities	2022E Net Income	EPS	P/E Multiple					Equity Value		
			Bear	Peer	Prem/ Discount	Base	Bull	Bear	Base	Bull
Group Peer Multiple - Electric				17.6x						-
Group EPS '18-'22 CAGR - Electric				5.00%						-
										-
Relative Utility Group P/E Multiple				18.5x						
Northern States Power Minnesota (NSPM)	$773	$1.44	20.5x	18.5x	3.0x	21.5x	22.5x	$29.49	$30.93	$32.37
Southwestern Public Service (SPS)	$325	$0.60	20.5x	18.5x	3.0x	21.5x	22.5x	$12.38	$12.98	$13.58
Northern States Power Wisconsin (NSPW)	$106	$0.20	20.5x	18.5x	3.0x	21.5x	22.5x	$4.04	$4.24	$4.43
Public Service Colorado (PSCo)	$575	$1.07	20.5x	18.5x	3.0x	21.5x	24.5x	$21.93	$23.00	$26.21
Total/Average Utility Earnings (excl Mankato)	$1,779	$3.31			3.0x					
Parent/Unallocated (excl Mankato)	-$103	-$0.19	20.5x	18.5x	3.0x	21.5x	22.5x	-$3.93	-$4.13	-$4.32
		NPV								
Add NPV of Mankato Non-Ratebase Acquisition		$308						$0.57	$0.57	$0.57
Add back 50% of HoldCo interest	$74	$0.14	20.5x	18.5x	3.0x	21.5x	22.5x	$2.80	$2.94	$3.08
Less: 50% of HoldCo Debt	-$2,524							-$4.70	-$4.70	-$4.70
Total	$1,675	$3.12						$62.57	$65.83	$71.23
Shares Outstanding (2022e)									*537*	
Total Equity Value Per Share								$63.00	$66.00	$71.00
Price as of close 04/20/20									$67.15	
Dividend FY20									1.72	
Dividend Yield									2.6%	
Total Potential Return Projected								-4%	1%	8%

Source: BofA Global Research estimates, company report, Bloomberg

Table 66: BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Xcel Energy Inc: Upgrade to Neutral: Rate Case Risks Poised to be Resolved	Julien Dumoulin-Smith	31 January 2020
Xcel Energy Inc: Rate case clarity in time for more in 2020	Julien Dumoulin-Smith	09 January 2020
Xcel Energy Inc: Rolling in Mankato as a Contracted Plant; Waiting on Deals in Key States	Julien Dumoulin-Smith	25 October 2019

Source: BofA Global Research

Table 67: Stocks Mentioned

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
LNT	LNT US	Alliant Energy Corp	US$ 49.99	A-1-7
AEE	AEE US	Ameren Corp	US$ 73.24	A-1-7
AEP	AEP US	American Elec Power	US$ 82.91	A-1-7
AWK	AWK US	American Water	US$ 126.46	A-3-7
ED	ED US	Consolidated Edison	US$ 85.47	A-2-7
DTE	DTE US	DTE Energy	US$ 100.76	A-2-7
DUK	DUK US	Duke Energy	US$ 86.65	A-2-7
EIX	EIX US	Edison Intl	US$ 60.01	B-2-8
ETR	ETR US	Entergy Corp.	US$ 96.45	A-1-7
WTRG	WTRG US	Essential Utilities	US$ 42.24	A-2-7
EVRG	EVRG US	Evergy	US$ 59.12	A-1-7
ES	ES US	Eversource Energy	US$ 87.77	A-3-7
FE	FE US	FirstEnergy	US$ 44.49	A-1-7
PNW	PNW US	Pinnacle West Capit	US$ 76.60	A-2-7
PPL	PPL US	PPL Corp.	US$ 25.25	B-2-8
WEC	WEC US	WEC Energy Group Inc	US$ 95.88	A-3-7
XEL	XEL US	Xcel Energy	US$ 64.35	A-2-7

Source: BofA Global Research, Bloomberg

Price objective basis & risk

Alliant Energy Corporation (LNT)

Our $56 PO is based on a sum of the parts analysis employing relative premium and discounts to the large cap regulated peer multiple of 17.6x 2022E P/E. While our PO is on a 1 year basis we note the 2022 P/E multiple reflects a discount back to 2019. We note that electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector.

We apply a 2.0x P/E premium on IPL as we see the ratecase overhang being resolved. We apply a 3.0x P/E premium on Eastern Wisconsin Electric Company reflecting 1) low risk investment nature of the state, 2) above average ROEs, 3) higher than average growth runway for investments, and 4) bad debt deferral. At ATC, we reflect a 2.0 x P/E premium on LNT's 16% share in the transmission company. Growth expectations for this segment are high, paired with above average ROEs that we believe face less downward pressure vs. regulated state distribution ROEs. We apply an in line multiple at the parent to account for the blend of numerous businesses some which benefit from long term stable PPAs via intercompany generation.

Risks to our price objective are: 1) adverse rate case outcomes, 2) further equity dilution beyond our estimates, 3) interest rate risk, 4) natural disasters, and 5) lower allowed ROE's

Ameren Corporation (AEE)

Our $85 price objective is predicated on a P/E based sum of the parts, valuing each business subsidiary relative to the 2022E ratebase weighted peer multiple of 17.6x for electric. We apply a 3.0x premium to peers at AEE Missouri to account for the improving

prospects of capital spend, supplemented by a regulatory jurisdiction becoming more favorable. We apply a 3.0x premium to peers at AEE Illinois to account for decoupling on the distribution business which aids in earnings predictability. The overall business is expected to grow at a more meaningful clip than that of peers - we see a 10% EPS CAGR at IL 2020-2024. At ATXI, we apply a 0x premium to peers to reflect the latest potential step down in FERC ROEs. At the Parent, we assume an in line multiple given the healthy debt metrics with FFO/Debt at 17%+. Electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector.

The upside (downside) risks to our price objective are the utilities earning their allowed returns or better (worse), a significant increase (decrease) in 30-year U.S. Treasury bond yields, and positive (adverse) regulatory outcomes that could impact mgmt's ability to earn its allowed return

American Electric Power (AEP)
Our price objective of $93 is based on SOTP analysis. We ascribe a peer forward P/E multiple (17.6x) with a 0x premium for its transmission-only Utilities segments as well as Kentucky Power, a 1x premium for its T&D utilities, and a 0x premium for regulated utilities. We ascribe limited value to the nascent renewables business & SRE Renewables deal ($0.03/sh), based on a in-line peer P/E multiple given uncertainty. We note that electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. We assume 100% likelihood of the North Central wind project and assign it a 0x premium under the reg utes as well.

Downside risks to our price objective are 1) regulatory outcomes are less favorable than expected, which could result in reduced ROE, 2) large capital intensive are subject to delays or cost overruns, which can change the return profile, 3) natural disasters or catastrophic events can affect system reliability and are subject to regulatory cost recovery risk, 4) utilities are subject to interest rate risk to fund their business, which affects cost of capital, 5) commodity risk affects the generation business margins and indirectly affects the regulated business as a pass through cost, 6) consumer advocates are focused on bill inflation, which can affect regulatory outcomes, 7) non-regulated businesses are inherently more risky and subject to execution risk and commodity variation.

American Water Works (AWK)
Our PO for American Water Works is $133. We apply the sector average 26.3x P/E multiple to American Waters 2022E earnings based on the water peer multiple and a 8.3% group EPS CAGR for '18-'22E. We think this multiple is justified as in our view AWK largely drives the peer multiple as the largest publicly traded water utility. We ascribe a 3x premium for NJ, PA, and IL, and a -3x discount to the military biz. Meanwhile, we ascribe a 12x multiple to the non-regulated Retail biz. Also a -1x P/E for Cali utility. no prem/discount for 'Other' segment with smaller state exposures.

Risks to the downside are increase in market interest rates, potential impact of tax reform on utilities, operational errors, changes in valuation levels for water utilities. Risks to the upside are accelerating muni acquisitions, multiple expansion, and constructive legislation in regulatory jurisdictions.

Consolidated Edison (ED)
Our $93 PO is based on a sum-of-the-parts analysis applying premiums and discounts to the regulated group multiples (17.6x/17.6x for electric/gas respectively) with a 1.0x premium to reflect defensive nature of the stock. We note that both electric and gas peer P/E multiples are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We applied inline peer regulated multiple at CECONY despite its rate certainty for conservatism as our higher capex expectations are reflected in our EPS outlook. We apply a discounted PE for infrastructure projects given the lack

of clarity around the capital structure. We further apply an EV/EBITDA approach on 2022E EBITDA to the CEB business using a 10.0x multiple for both the legacy portfolio and the renewables portfolio seeing it as having higher quality returns.

Downside risks: ED, like all utility stocks, is also sensitive to changes in the market level of interest rates. Utilities historically underperform if bond yields rise, and outperform when they fall. Further downside risks are the inability to recontract storage, adverse regulatory outcomes, a deteriorating regulatory environment, or unforeseen disasters such as the Harlem gas explosion, the SRE transaction not being completed. Customer inflation is also a downside risk. PCG related counterparty exposure is among the nearest exposures to watch.

DTE Energy (DTE)

We value DTE Energy at $112 using a SOTP approach.
We value the utility segment on a 2022E forward P/E multiple basis and the non-utility seg. on a 2022E forward EV/EBITDA mult. basis. For the utility segment we apply a 1x premium to our both reg. electric and gas utility peer mult. of 17.6x. Both electric and gas peer P/E mult. are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We subtract out Corp & Other expense excl. interest rate. For GSP we use a midstream peer group multiple of 9x, with a -0.5x discount for Momentum. P&I, we apply a 8x EV/EBITDA mult, despite the lower equality of these earnings and opaque disclosures, as mgmt has been able to execute on new project origination. We value the reduced emissions fuel (REF) tax credits separately using a DCF methodology at 6%
discount rate.
Upside risks to our PO are capex expansions, higher authorized ROEs, and strong performance in the ET segment. Downside risks are interest rate hikes, execution risk on organic growth initiatives at the nonregulated business, and less favorable regulatory environment.

Duke Energy (DUK)

Our $93 PO is derived from a sum-of-the-parts valuation. We value the Electric and Gas utilities using peer 2022E P/E multiples. We apply a 1.0x multiple premium to Duke's operations in Florida to reflect more favorable regulatory environments. We apply an in-line multiple to the Carolinas given risk ahead. We value the other regulated electric utilities and the gas utilities at peer group multiples of 17.9x 2022E P/E, respectively. Both electric and gas peer P/E multiples are grossed up by 5% for the groups CAGR to reflect capital appreciation across the sector. The commercial midstream, and transmission are valued on a 2022E EV/EBITDA basis. We use a 11.0x multiple for midstream and transmission segment, although we assume a 50% weighting for ACP given risks to completion. We add the net present value of renewable segment using an 8% discount rate. We subtract out the impact of commercial debt, and add back for the renewable debt.

Upside risks: constructive rate case results, higher capital expenditure additions vs our assumptions, ACP ahead of schedule, lower interest rates. Downside risks: poor rate case results, operating errors, and negative changes in the regulatory environment, ACP delays. Macro risks: Increases in interest rates and decreases in equity market valuations.

Edison International (EIX)

Our $69 PO is based on SOTP, applying a 3x disc to the FERC and CPUC jurisdictional subsidiaries, and the parent/other segment 17.6x on 2022E (grossed up by 5% to reflect capital appreciation across the sector). The disc reflects CA ongoing wildfire risk despite the improved construct through AB1054. We apply 10x 2022E P/E to the Edison Energy segment to reflect uncertainty in the nascent biz. We net out ongoing contribution to the fund on an NPV basis. Lastly, we assume equity financing to fund '17/18 wildfire claims.

Downside risks: 1) Regulatory outcomes less favorable than expected. 2) Natural disasters or catastrophic events can affect system reliability and are subject to regulatory cost recovery risk. 3) Interest rate risk. 4) Non-reg businesses are inherently more risky and subject to both execution risk and commodity variation. 5) CA has specific risks given the differentiated regulatory regime. 6) CA wildfires.
Upside risks: rate case outcome above what's embedded in companies' guidance and BofA estimates, lower interest rates, more constructive regulatory / legislative outcomes to address wildfire risk

Entergy (ETR)
Our $122 PO is SOTP based. We assign P/E multiples (peer multiple of 17.6x) for 2022E on most segments, in line with peer multiples (and grossed up by 5% to reflect capital appreciation across the group) due to similar growth, and strip out 50% of the holdco senior notes. The Merchant business is also added as a DCF (10% discount rate, no terminal value). Both electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector.

Downside risks: 1) Regulatory outcomes or earned ROE's could worsen, 2) Rate making mechanisms could change in the future, 3) Failure to get trackers or ROE adjustment mechanisms could hurt realized ROE, 4) weather can affect operations and earnings, 5) Interest rate risk affects cost of capital, 6) Consumer advocates or utility staff may focus more on issues that challenge the company ROE, 7) ETR has had safety issues in the past, which have affected regulatory relationships and company liabilities, 8) Exit from the competitive business could present unforeseen challenges.

Essential Utilities (WTRG)
Our price objective is $47 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 2.0x premium to Peoples Gas given the organic growth opportunities.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Risks to the upside include upward revisions to street estimates and further accretion from implementation of the Repairs Tax Benefit.

Evergy, Inc (EVRG)
Our $69 price objective for EVRG shares is based on sum of the parts valuation, applying an in-line utility peer 2022E P/E of 17.6x. Electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We further apply a +2.0x turn discount across all jurisdictions based on our perception of improving regulatory relationships and possibility of further stakeholder engagement.

Downside risks to our price objective are adverse regulatory outcomes in rate cases, higher interest rate environments, adverse and unexpected risks associated with operating a nuclear facility, the possibility that the strategic review committee does not result in a transaction recommendation and that a modified standalone plan disappoints in rate base and earnings growth when presented later in 2020.

Upside risks to our price objective are favorable regulatory outcomes in rate cases, lower interest rate environments, higher than anticipated O&M benefits and merger synergies, ability to recover capital tied to retired coal plant.

Eversource Energy (ES)
Our sum of the parts based price objective of $83 uses P/E multiples on 2022E earnings. For electric utilities, we attribute a 2x premium NSTAR and 1x for CL&P, reflecting future potential positive revisions to capex and earnings, while maintaining an in line multiple of 17.6x P/E for PSNH. For gas, we apply an in-line to the peer 17.6x multiple, given recently compressed spread relative to electric peers. Both electric and gas peer

P/E multiples are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We value Aquarion at a 22.6x multiple to reflect the premium water utilities are currently trading at. We reflect ES' 50% ownership in Revolution and South Fork offshore wind sites on NPV basis. We take out 50% of parent debt, and 50% of interest to accurately reflect parent leverage.

Upside risks to our price objective are additional capex announcements on the T&D side, as well as success in offshore wind RFPs or other larger projects such as Northern Pass.

Downside risks are reduction in authorized ROEs, inability to meet earned ROE expectations, as well as failure to receive permitting on incremental capex opportunities

FirstEnergy (FE)
Our PO of $47 is based on a SOTP: Multiples are driven by relative P/E premiums/discounts to the 2022 regulated peer multiple of 18.5x. Electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. For NJ, we apply an in line multiple to account for slightly higher ROEs vs. the national average and a generally constructive commission. In PA, we apply a -1x disc to reflect O&G royalties (albeit limited). In OH, we apply a -4x P/E discount multiple and a -2x discount to others. We argue this accounts for overearning risk. Finally, we apply a 0x P/E premium to peers 2022E multiple to the Transmission business given some limited ability to invest and FERC ROE difficulties. We removed impact of DMR payments. We subtract out the holding co debt given the high parent lev. We net out potential liabilities from a potential FES bankruptcy by assuming all known 'extra' potential liabilities.

Downside risks: 1) Reg outcomes may improve/deteriorate, 2) legislative solutions may materialize for challenged parts of biz or FE could lose/fail to gain legislative support in key states, 3) int rates positively/negatively affect cost of cap, 4) reg staff or cons advocates may focus on issues beneficial/detrimental to ROEs, 5) exit from comp power biz may or may not have substantive liabilities accrued to equity holders.

Pinnacle West (PNW)
Our price objective of $84 is based on a peer utility 2022E P/E multiple of 17.6x with a -2.5x discount to account for PNW's risk around its pending rate case as well as headline risk related to disconnect policy review. Electric and gas peer P/E mult is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We ascribe an in-line premium despite clear renewable capex backdrop given ongoing regulatory risk associated with the company's upcoming rate filing and 2020 election risk.

Upside risks: 1) Regulatory relationships/outcomes could improve, including changes at the elected commission 2) load growth in territory above expectations 3) Riders and capital trackers could help achieve ROE 4) positive weather helps earnings 5) interest rate risk changes cost of capital - lower rates could improve 6) Consumer advocates or utility staff could become focused on issues that improve ROE

Downside risks: 1) Regulatory relationships/outcomes could decline, including changes at the elected commission 2) load growth in territory below expectations 3) Riders and capital trackers could hurt ROE 4) negative weather hurts earnings 5) interest rate risk changes cost of capital - higher rates could worsen 6) Consumer advocates or utility staff could become focused on issues that hurt ROE 7) Solar advocates in the state have engaged in public confrontations with the utility, which could change public relations in the future.

PPL Corporation (PPL)
Our $29 price objective is based on a sum of the parts methodology applying respective premium/discounts to the 2022E peer group multiple of 17.6x. Electric peer P/E multiple is grossed up by 5% to reflect capital appreciation across the sector. We apply a 1.3x

RAV multiple in our base case for our Western Power Distribution (WPD) RAV approach, seeing the higher ROEs relative to other distribution networks commanding a premium valuation.

Downside risk to our price objective is exposure to FX rates. Since the UK segment represents a significant portion of PPL's earnings, a Federal Reserve decision to raise interest rates could produce a fall in the GBP/USD currency rate that would adversely affect our estimates and valuation for PPL. Also, like all utility stocks, PPL has historically underperformed if bond yields rise. Upside risks are a rising $/pound (GBP) price, positive regulatory outcomes, and decreasing treasury yields.

WEC Energy Group Inc (WEC)
Our $85 PO is based on a 2022E SoTP analysis, based on the large cap electric group multiple of 17.6x and the gas regulated multiple of 17.6x. Both electric and gas peer P/E multiples are grossed up for a year to reflect capital appreciation across the sector.

We apply a 3.0x premium to WEC's electric subs to compensate for surety in earnings growth for the next two years following the Commissions affirmation of the recent settlement on above average ROE's of 10%+. We apply a 0.5x premium to the gas utilities, including Peoples Gas and North Shore Gas with the Gas System Modernization Program (GSMP) and capex forecasts de-risked following the ICC order. We ascribe a 2x premium vs. the group at ATC to account for the steady nature of earnings growth as well as above average ROE's that are set at a federal level by FERC. We give Power the Future (PTF) a 2.0x premium multiple given the ROE is set indefinitely on historical and new investments. We ascribe an in line multiple for the parent accounting for the interest expense which finances overall utility operations. For the HoldCo adjustment to debt, we net out 50% of HoldCo debt from equity valuation and adjust to add back the parent drag on interest expense.

Upside Risks to achieving our price objective include 1) stronger than expected execution 2) accelerating capital opportunities and 3) favorable ratecase outcomes

Xcel Energy Inc (XEL)
Our PO is $66. We value Xcel Energy using a sum of the parts (SOTP) approach. Given the difference in geography, earnings strength, growth opportunity and risk profile, we divide the segments by subsidiary.

We use 2022E forward P/E multiples to derive a value for the different business segments, including the parent segment. We use on a peer multiple of 17.6x . Electric peer P/E multiple is then grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We apply a 2x premium to subsidiaries. We see this multiple as appropriate as the company has growth opportunities, resolving regulatory drag and resolving uncertainty around rate cases. We include Mankato as a non-reg asset in our SOTP. We also net back 50% of the parent interest expense and instead subtract out 50% of parent debt to more accurately reflect HoldCo leverage.

Downside risks are interest rate increases, regulatory risk such as lower authorized ROEs or less favorable riders/trackers for renewables and transmission, interest rate risk, execution delays, and weather anomalies.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
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	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Utilities Group (as of 31 Mar 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	72	50.35%	Buy	51	70.83%
Hold	38	26.57%	Hold	28	73.68%
Sell	33	23.08%	Sell	24	72.73%

Equity Investment Rating Distribution: Global Group (as of 31 Mar 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1602	52.15%	Buy	1005	62.73%
Hold	713	23.21%	Hold	463	64.94%
Sell	757	24.64%	Sell	382	50.46%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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North American Utilities & IPPs

AGA Digital Takeaways: What We Learned on Day 1

Industry Overview

Holding the line on ’21 remains the focal point

We hosted meetings on Day 1 of the online version of the AGA conference with AEE, AGR, CNP, ED, DUK, WTRG, MDU, NWE, SRE, SO, and WEC. Much of the discussion remains focused on holding the line on both costs and rate case strategy heading into ’21 for most companies. We stress an implicit pivot on how costs are managed into ’21 to ensure their sustainability, with several companies increasingly contemplating labor-related savings annualizing into ’21 based on headcount freezes enacted (as well as forthcoming voluntary headcount reductions/early retirement options increasingly considered should Covid impacts last beyond ’20 too). That said, the most critical considerations remain how to *establish a test year* based on current year (inclusive of updated load growth & updated/suppressed cost inputs) while similarly facing pressures on authorized ROEs. We suspect companies will *continue* to attempt to delay any future rate increases on customers beyond 2021, suggesting another year of cost cutting necessary to keep EPS intact. By contrast, 2022 could prove substantially more active on rate activity as ’21 should provide a ‘normalized’ set of assumptions and the palatability of rate cases proves more intact among regulators. We could see this accentuate all the more the differences between companies benefitting from automated structures such as decoupling and formula rates, in contrast to those companies without any such mechanisms. We also see a need to remain vigilant on costs. We anticipate another wave of modestly cautious updates by 2Q and definitely by the 3Q as discussions around next year begin to frame up (cost cutting once more should feature prominently in these updates we think). While 1Q ended up proving more intact than anticipated, largely due to affirmations on outlook on ’20 to cost reductions the question remains just if companies can sustain reductions & still execute on contemplated growth: increasingly tricky backdrop albeit risks to sector EPS remain quite limited to downside (1-2% order of magnitude).

What companies stood out from our meetings?

We see AEE’s strong affirmation on its outlook as quite notable, seeing sizable latitude between its recently concluded MO rate case and ongoing costs to ensure continued earning close to its authorized level. Following earlier fears permeating in the marketplace we perceive shares as substantially intact with mgmt. notably confident on its outlook despite its volumetric exposure in Missouri. In fact, we continue to see latitude to execute against its plan if not *more* on the back of its forthcoming IRP this fall. We could see a net increase in capex, bolstering doubts that seem to be emerging around shares. Related we also saw SO’s confidence in ongoing pivot at Vogtle as worthwhile given pivot on employee execution. SRE appeared quite confident on its CA outlook again, but note emerging risk of capex deferrals in Mexico is likely under-appreciated among investors and could partially offset in its outlook. We maintain our Underperform on CNP as we maintain our concerns on prospects for execution at levels contemplated. We see DUK’s Sept update on its IRP as likely understated & explaining its recent pos re-rating relative alongside greater confidence in cost cuts. Rate case risks loom here otherwise.

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Thematic Prospects

1. Execution intact; bill arrears remain quite early

We note few incremental comments in recent days on load trends, with most of the focus increasingly focused on the ramp in bill arrears from customers. With April bills just becoming due now, preliminary data does not necessarily show the full ramp. While residential customers are typically eligible for non-disconnect and avoidance of late feeds, we also note discussion among many companies of the benefits provided from the CARES act in allowing funds disbursed to small businesses to qualify towards paying utility bills (in addition to employee labor expenses, etc) such that this class of customers is likely to remain more intact than otherwise expected.

2. Renewable delays, but not really an issue

We stress that few investors really appreciate the potential *benefits* of forthcoming PTC guidance latitude from IRS. We could actually see this add to the net NPV of projects (seeing currently '21 contemplated projects) partially qualify for the full 100% PTC. This would appear the most constructive to NEE of companies covered.

3. Capex upsides still quite real

We perceive investors need to appreciate that companies could very well see capex increases altogether as they move forward with a wider array of coal plant retirements on an accelerated basis including AEE, ETR, and DUK among others. We see this all likely forthcoming in 2H despite a related backdrop & fear of capex *slippage from 2020 into future years* to limit pressure on balance sheet metrics. This remains a key potential variable as companies seek to hold the line on the outlook in '20 as virus could very well imperil guidance more than otherwise perceived/reflected in sales guidance presently with greater corresponding impacts to balance sheets than appreciated as well.

Ameren (AEE)

Standing by the main points from the 1Q call: *quite confident*

Mgmt. reiterated much of what was discussed on its earnings call last week (as discussed in our last note), including its affirmation of 2020 guidance $3.40-3.60/sh under adjusted assumptions including the constructive Missouri (MO) rate case outcome, O&M savings, and a YoY sales decrease expectation of -2.5% (a -$0.10 item). There's still lack of clarity around how much of an O&M swing AEE is factoring in (recall mgmt. stated on the 1Q call original guidance had a YoY increase in expenses, changed to a YoY decrease). We hope for further clarity as peers have provided a sense of how much is factored in – important in tracking impacts if stay-at home orders last a little longer than anticipated. Either way, as we previously calculate a 1% change in O&M is equivalent to roughly $0.10/sh, we still expect AEE has room left for other O&M savings if need be to keep '20 in its guide. We maintain Buy given this, that also see growth opps, and the company's strong FFO/debt metrics that are better than those of peers.

Capex and growth rate

AEE affirmed its 6-8% EPS CAGR from '20-'24, emphasizing its $36bn 10-year capex plan (as well as its $16bn 5-year plan). Mgmt. pointed out that the plan's capex is largely focused on grid modernization as well as projects that enhance reliability, resiliency, and security. AEE doesn't have big generation growth other than the $1.2bn invested in wind, which is still expected to commission mostly this year (perhaps just $100mn rolls into 2021 due to COVID-related supply chain delays). We see further opps for gen-related growth, but it's too soon for the company to firmly fold upside into guidance; this includes the IL downstate legislation & associated renewable and electrification of transportation proposals, as well as potential generation trajectories proposed this fall through Missouri's integrated resource plan (IRP).

Missouri rate case settlement: When's the next one?

Mgmt. reiterated its constructive rate review outcome including having the commission affirm its 95% / 5% sharing as well as a decrease in revenues by -$32mn, fuel cost expenses by -$115mn, and other costs by -$50mn. This results in a net +$133mn pre-taximpact, with rates taking effect April 1st. We calculate the annual impact of this

result is $0.40/sh annually, i.e. $0.30/sh for 2020 given it impacts nine of twelve months. Note the electric result was an ROE of 9.4-9.8% as well.

Recall prior to COVID & this rate case result, AEE had indicated it was planning to file *another* MO rate case once its wind program came online YE 2020 to reduce lag beyond what PISA (plant in-service accounting) provides in deferring 85% of depreciation. While the company had never provided an exact sense of timing, one could have assumed that AEE might have wanted to file July 2020 for a true up by year end that would have included the wind projects. However, we note that mgmt. again expressed it was happy with the construction result of this last recent settlement. Moreover, now with COVID, *AEE is still debating the timing of when to come in next to limit regulatory lag but be conscious on the backdrop.* In other words, we see AEE looking to balance the recent rate case result (which we believe would support a stay-out) with wanting to bring 2020 wind investments into rate base (which we believe would support an earlier case, but with some flexibility given PISA eliminates as much loss on depreciation of rate base) and then COVID impacts (which in itself has a push-pull: We'd see reason to push out given economic impact on customers but reason to pull forward to balance impacts of lower demand and bad debt expense). Nothing is on the table yet in terms of the next filing, but AEE mentioned the Commission Staff did open a workshop to look at tools around costs from COVID.

We discussed potential alternatives to a full rate case, noting that AEE chose PISA rather than decoupling. We still wonder whether the MO commission could be amenable to a stabilization filing, like LNT is pursuing in Wisconsin (i.e. keeping rates stable by using cost costs and other accounting mechanisms to balance the increase to rate base the wind would provide). We also could see AEE look to pursue accounting authority orders (AAOs) related to COVID-specific costs in MO.

Coal update: Still waiting on this fall

AEE did not provide a glimpse into any future potential accelerated coal retirements. It noted its unique situation since it has not made as many investments in scrubbing equipment as peers have, resulting with coal representing just 12% of rate base now, expected to drop to 8% in 2024 without facing stranded costs. Plants outside of Meramec (which is set to retire in '22) are still operating at 70% capacity factors, and the state has historically appreciated the ownership aspect of generation.

While not discussed, we still see accelerated unscrubbed coal retirements as untapped potential not only as a catalyst in which to pursue more rate based renewables (which could be discussed this fall as the IRP is due), but also as a way to pursue better ESG metrics as well (see our recent ESG flows note here, which suggested flows have continued strong this year, but utilities as a whole are underutilized even with some of the largest clean energy rate of changes proposed – we could see an opp'y here). We think that if not this fall, AEE could also be waiting for the result of the 8th Circuit environmental issue around Rush Island (with oral arguments likely later this year) and/or securitization legislation in MO to be pushed forward.

Illinois: Downstate bill isn't off the table yet

While impacted by 30-year Treasury rates, AEE's Illinois formula rates in the electric segment result in no regulatory lag. The company continued to discuss the Downstate legislation including extension of formula rates with the 100bps adder – in addition to plans for more renewables and electrifying the transportation sector – by specifically noting that the legislation is based on a strong foundation that has driven investment, jobs, and reliability in the past. We interpreted the company still sees palpable backing by environmental & labor group, in addition to geographically and politically diverse legislators. While investors appear quite worried about sustaining status quo; we note the program officially expires in coming years (and would otherwise seemingly result in a more traditional litigated rate case). While timing could yet get shifted out we perceive a clear bias towards an extension, likely in oru vie won more favorable ROE terms given the wide discrepancy from other 'normal' returns for companies. This backdrop makes us more constructive on shares despite the more acute recent arguments suggesting risks to their LT EPS CAGR carrying forward current EPS CAGR outlook.

Avangrid (AGR)

New England Clean Energy Connect (NECEC) saga continues

As we noted here, AGA recently filed a lawsuit in Maine at the Superior Court level regarding the state's referendum to derail the NECEC transmission project through this November's election. The suit is based on AGR's view that (1) the referendum exceeds the power of the law as it's not a rule for all (focused on just one project) and it's retroactive, and that (2) there is a separation of powers issue that is allowing the legislative branch to exert power over the judicial and executive branches. The outcome is needed before the item would go on the ballot this November. AGR did not address impacts to capex deployment yet, noting it continues to first focus on receiving the remaining permits as well as ensuring the referendum is challenges and voters have all the information to make an educated decision. We point out that construction is now not expected to start until the end of August; the ME DEP permitted the project recently so the only two outstanding permits are the Army Corps expected in August (which is necessary to start US construction) and then the Presidential permits 60 days later (which is necessary to cross the Border into Canada). The silver lining in the delays faced by AGR is that a concurrent non-appealable order in Massachusetts (which was appealed by NextEra) won't be ruled on until this June. As such, AGR has gained flexibility on when exactly the project contractually needs to be in service; the company is still anticipating a '22 in-service date as of now, but can bleed into '23 if difficulties cause further delay (i.e. giving AGR a risk mitigating factor of more time and latitude if it is delayed more). Bottom line: AGR pulled its long-term guidance on the 1Q call and by the time we expect an update (at the Analyst Day likely in line with Iberdrola's), AGR will have referendum clarity on whether this project will go forward.

Note also in ME, AGR recently teamed up with two wind generators (EDPR and Clearway) to propose wind farms (~325MW) for the state's request for proposal (RFP) due last week. AGR would be responsible for transmission gen-ties – and the projects represent significant distances. Stay tuned here, with the RFP announcement likely this December. *These transmission interconnects would be modest upside to the plan.*

ROEs: Company expecting largely around authorized once all said and done

AGR anticipates it will finalize its New York rate case settlement with interveners this month such that it is able to file a joint proposal with the Commission soon. As noted in our recent upgrade to Neutral from Underperform (here), AGR anticipates the final order to be approved this fall, with rates taking effect in September but being made-whole as of April 17th. We point out two key discussions in our eyes: First whether the commission will allow recovery of some bad debt expenses, and second the ability to earn at the authorized ROE. AGR noted in 2009 the commission put in place a methodology for recovery after a generic hearing. It expects something similar – we'd expect more likely a generic proceeding but if need be through the settlement. Note CT and ME already opened dockets recovered to bad debt, and AGR seemed confident some sort of recovery would be possible in NY due to past precedent.

As for earning as close to the allowed as possible, the outcome on minor storm recovery particularly with staging costs is key. NY had limitations on how many staging costs it could recovery, and would allow just 3 events at NYSEG and 2 at RGE. AGR is seeking more events and more dollars to recover. It also is looking to deploy incremental dollars for maintenance, equipment failures, and enhancing the system (due to age or quality). In other words, AGR is looking for capital, O&M, head count, and storm recovery – mostly at NYSEG. Once rates are in place, mgmt. expects to earn around the allowed ROE. This would indicate the first year of limited lag for NY Is 2021.

As for ME, the company expects to earn around the allowed ROE as well – although likely closer to having 2020 as the first full normal year. Note the company is facing 1x items in 2020 that will prohibit earning at the authorized return, and until September 2021 at

the earliest the company faces a -100bps penalty on its authorized ROE. This penalty will be lifted if AGR proves its customer standards metrics.

Question of capex and resolution on bad debt unlikely in JP

We perceive a generally cautious attitude on storm related capex & opex coming out of the NY rate case resolution. While already an ambitious plan articulated in its capex projection, we perceive a potential for modestly reducing expectations. Meanwhile resolution in the joint proposal of bad debt recovery appears increasingly unlikely in our view and would likely be joined together with other utilities including ConEd. We stress recovery appears to be dimming in a separate Covid docket in sharp contrast to many other regions nationally.

Offshore wind update: Waiting on BOEM with study all focused on distance

AGR indicated that the Bureau of Ocean Energy Management (BOEM) communicated last that it is still on target to issue its cumulative impact study this June 12th. The company expects it will be an all-encompassing finding on project density – i.e. how far apart turbines must be in the New England area. Note that the industry up to this point has largely agreed upon a one-nautical mile spacing in all directions (N/S/E/W) and that the Coast Guard has indicated it is in line with this spacing; most fishermen negotiations were reflecting of this as well. We point out that AGR is still waiting to comment officially on how Vineyard Wind will be included its updated EPS CAGR (i.e. to commission in 2023 or 2024?). Due to the delay from the original online-date of '21-'22, AGR has a silver lining of being able to explore larger turbines with more capacity, improving its density of its total offshore wind lease area (having originally looked to 9.5MW turbines, but now looking at turbines 12MW+).

On track '20 and succession

Finally, the company indicated its '20 projects are on track and that it is not seeing a COVID-related slow-down. We expect AGR is one of the more shielded companies from lower demand and other impacts due to its decoupling at Networks. We stay tuned for succession plans, likely to be announced by Jim Torgerson's departure at the end of June.

Centerpoint Energy (CNP)

While CNP remains a highly debated name, we remain cautious on the overall outlook and see downside to shares given both ambitious 5-7% growth targets that are difficult to achieve as best we can tell (w/ inclusion of mandatory converted shares offset by interest expense savings) with upside case principally centered around the strategic review process, which has yet to be clearly articulated. With Change of Control at a sector-record at ~$10Mn for the chair, we believe the question remains whether this could potentially evolve further with additional incentives, a dynamic we've seen elsewhere among companies evaluating strategic actions, although still no timeline on this process. Meanwhile, there are some signs of progress on the new CEO search although still no definitive timeline. At the end of the day, we continue to see a challenged outlook and maintain our Underperform rating.

Succession planning: Still no definitive timeline although making progress

During our call, mgmt. highlighted that several candidates have been identified for a new CEO appointment, and is in the process of narrowing down the list and working to prepare arrangements. That said, mgmt. was unable to put a more specific timeline on the process. Given wider governance concerns around the structure & compensation of the board, we see this as critical to re-establishing confidence in the strategic direction of the company. While an astute CEO appointment would be the most obvious upside angle, especially if it were to come from in-state peer, we could see the process be more drawn out.

What about the strategic preview process? CoC critical to watch

While mgmt. talked down the M&A angle on its earnings call, commentary from our AGA meeting suggested that the advisory board committee would look to optimize the business by assessing all assets and the business as a whole with still plans to announce something by the Analyst Day in early 2021. Given we perceive limited independence of recently appointed board member Lesar and current Chair Milton given historic relationship, we continue to see changes around Change of Control (CoC) incentives as critical to watch. Yet there was no more specificity as to when these payments will be subject to annual review or around additional details for the process itself beyond the fact that the interim CEO/CFO will be involved in the process. With CoC at a sector-record at ~$10Mn for the chair, we believe the question remains whether this could potentially evolve further with additional incentives, a dynamic we've seen elsewhere among companies evaluating strategic actions. We note the chair has three years left prior to mandatory retirement age; we also still note the decision by CNP in past efforts around strategic actions *not* to pursue a sale. Bottom line, we remain less convinced about the motivations on this front, although recognize this is a key upside angle.

What about the dynamics in IN?

With ~$300mn/yr of IN electric capex that will need to be backfilled and largely dependent upon the Integrated Resource Plan (IRP) filing, mgmt. highlighted that it remains on track for its June filing with expectations to bring a more balanced portfolio mix of new generation to the table. While details of the plan have not been disclosed, mgmt. highlighted a much more engaged stakeholder process taking in factors from both the coal industry and the renewable energy in order to balance low cost needs with stakeholder objectives. Meanwhile, despite 80% of capex trued up on an annual basis, we remain concerned around COVID pressures and ability to earn authorized returns; see recent read-throughs from in-state peers AES and NI on load trends as also cautious given Commercial & Industrial (C&I) load declines in the mid-teens, and it remains unclear if resi trends of +10-11% can be sustainable.

Consolidated Edison (ED)

We maintain our Buy rating on ED as we continue to see the shares as largely de-risked following implementation of new rates at its CECONY (Con Ed co. of New York) subsidiary and given its decoupled electric and gas business. Nonetheless mgmt. continued to strike a sober tone on assumptions for recovery of Covid-related items including higher bad debt expense and direct expenses. Mgmt. acknowledged that the timing of a potential commission docket for Covid recovery would likely come after the state has better visibility into the length and depth of the economic downturn, particularly as it relates to unemployment. On the financing front the company reports ample liquidity following the establishment of a new $750m credit facility. No change in plans to issue $600m of equity in 2021 as the company continues to see annual equity needs, thus any delay would cause requirements to increase in future years.

'20 guidance cut driven by Covid which is seen as a current-year drag

Mgmt. sees the impact of Covid on financial results as seen in lower revenue from disconnect fees, late payment fees, no access charges, and related O&M items to largely be limited to 2020. Incentive programs built into rates are reset on an annual basis, with the expectation that the Covid impact from these will also be limited to 2020. Looking beyond 2020 the company sees its multi-year earnings CAGR guidance as intact given expected recovery in subsequent years as fee collections normalize. The reduced 2020 guidance range of $4.15-4.35 was driven in part by the negative contribution from weather in the CECONY Steam business (ED's largest non-decoupled segment). Mgmt. estimates that thee Q1 drag on Steam was approximately 80-20 due to weather and reduced consumption stemming from Covid stay at home orders in the end of March. Mgmt. did not give a forecast for the segment for the remainder for the year though noted that Steam is economically sensitive – it is unclear to what extent demand will continue to be reduced by remote working employees given that large office buildings in the city may continue to take steam even at reduced occupancy rates.

Bad debt expense largely depends on depth and duration of downturn

ED sees its bad debt expense as largely dependent on the path of economic recovery in the NY City area, in particular the length of time that unemployment rates stay elevated and to what level unemployment rises. Mgmt. provided color into the determination of bad debt expense in a rate proceeding – the beginning point is the actual bad debt expense in a historical test year with a normalization process that takes place to account for one-time or unusual events during the test year, making the final outcome difficult to forecast. At present mgmt. is using 2008-09 as a template in the absence of more detailed data – in both instances collections for delinquent accounts were suspended, though the reduction in demand has been faster in 2020 as compared to the prior recession. Mgmt. sees a potential for a generic cost recovery docket to be opened by the NY commission, though does not expect clarity in the near term as the commission remains focused on delivery of service to customers.

Equity needs remain $600m in '20, liquidity seen as adequate

ED established a line of credit in April that will allow it to draw down up to $750m to fund operations and capex in the near term. The company sees its current year equity needs as unchanged at $600m though acknowledged the possibility of drawing down the credit line *prior* to an equity issuance (by mid year) if market conditions precluded an issuance by that time frame. Looking further out mgmt. sees annual equity needs "as far as the eye can see" making pushing out the current equity needs difficult as they would accumulate in the following year. Mgmt. stressed market conditions and ensuring the best possible price as the key factor in its timing decision. *Bottom line, could see this come by mid-year depending on market conditions. With this company among the single remaining marketed issues for the year to be issued we perceive disproportionate 'overhang' and hence concerns on shares reflected today.*

Duke Energy (DUK)

Despite Duke's recently announced sizeable cost cutting plan to offset expected load declines this year, we maintain our Neutral rating on shares given lingering risks in the Carolinas with 3 untested NCUC commissioners and potential for delay at ACP with NWP12 timing. With the near-term uncertainty in the Carolina rate cases given litigated ROEs, coal ash pressures and implementation timing, Duke's execution of its cost cut initiatives will be critical for the company to maintain its +4-6% EPS growth target (reaffirmed on 1Q call). On the other hand, we see potential progress with the Clean Energy report from the NC where we see pathway for alternative rate making mechanism (MYRPs, ROE banding, securitization, riders, etc.), although specifics around a particular outcome remains premature: we see our AGA meeting as a net positive driven by growing confidence around future Carolinas spend (watch large re-write on capex outlook with the IRP) as well as focus into '21 on cost cutting. Specifically its forthcoming IRP should both add to cash flow potentially with accelerated depreciation of plants – improving balance sheet while laos providing a further uptick in capex this ~September.

Regarding ACP, we continue to perceive challenges in having all permits approved by the tree-felling window in November; in addition to potential risk that the 9th does not approve the motion to stay for the recently narrowed NWP12 order (likely hear on the stay next week). Long term, we see the upcoming NC IRP in September including a meaningful amount of incremental opportunity by way of clean energy for Duke, but risk remains around the natural gas build out due to uncertainty at ACP.

ACP needs 4 items resolved this yr to remain on schedule; NWP12 in focus

With 47% interest in the $8bn Atlantic Coast Pipeline (ACP), the project continues to be an overhang on DUK shares as there are several items that need to be resolved this year to keep the expected in service timeline of early 2022 intact. Moreover, the recent Nationwide Permit 12 (NWP12) vacature order out of the US District Court of Montana, which was narrowed last week to only new oil and gas pipelines, has become an incremental obstacle for ACP and all other new pipelines across the nation. On Friday (5/15), after declining to grant an immediate stay of the MT Court's narrowed order, the 9th Circuit US Court of Appeals established an expedited briefing schedule concluding on May 22 (this Friday) to address the defendants' motions for a stay implying the 9th's critical decision on the motions to stay for NWP12 will likely come next week (May 25-29). Duke hopes this motion to stay is granted next week allowing the project schedule to remain in line with expectations. This assumes the other three items are resolved this year, which include: 1) biological opinion from the US Fish and Wildlife Service (expected by end of 2Q20) – a pre-requisite for water crossings authorized by the NWP12, 2) a favorable SCOTUS ruling on Appalachian trail crossing (expected in next few weeks), and 3) an air permit for the Buckingham, VA Compressor station (expected by YE20). FERC likely needs all these major permits in place to approve recommencing construction and tree felling. Bottom line, we continue to see risk of a delay at ACP with a potential motion to stay for the narrowed vacature of NWP12 presenting incremental delay risk.

Upcoming IRP to be broader than DUK's typical IRPs historically

Duke's upcoming North Carolina Integrated Resource Plan (IRP) that will be filed in September is expected to be broader than the company's usual IRP as it will contain more carbon reduction initiatives, renewables, third party providers, and distributed generation. The carbon reduction initiatives will include more thoughts on the early retirement of coal plants. We expect the commission will look to find a balance between the lowest cost plan and aligning de-carbonization efforts, which Duke likely incorporates into its IRP. The company is trying to reflect a composition of assets that is less base load, but rather more on the grid and smaller generation assets. Further we perceive the NC IRP filing could create additional opportunities for DUK in terms of clean energy and coal reduction opportunities, although see risks to natural gas build considerations given still uncertainty around ACP.

Securitization as a potential tool for coal retirement in the Carolinas

For the early retirement of coal plants, we believe Duke could potentially securitize these early retirement costs such that they are not penalizing the rate payer, creating headroom. Duke has used securitization for storms in the past, and we perceive this as an attractive tool for Duke to potentially apply to coal retirements if the corresponding amendment is made to the legislation (assuming put forth in the Clean Energy study by year-end). We will continue to watch for this as another potential lever for Duke.

Multi-year rate plan legislation

Duke continues to push the Public Utilities Commission (PUC) for alternative rate mechanisms to move forward, specifically, a multi-year rate plan (MYRP). With the upcoming report due from the Governor's committee on Clean Energy, there remains potential for Duke to have a recommendation back to the legislation that would include a MYRP, ROE banding, securitization, and/or rider capability. There are a wide range of tools available, but it will take time to educate the necessary parties. All of these tools would be positive for Duke, but there are a number of steps it will take to get there as past efforts stalled/failed. With that said, we see both increased confidence from the company and corresponding stakeholder commentary as supportive for DUK's legislative prospects in the 2021 long session.

Offsetting COVID-driven load declines with cost cuts; some sustainable cuts

On the 1Q update, Duke announced targeted cost cut reductions of $350-450mn to offset annualized load decline expectations of 3-5% this year. A portion of these cost savings are savings that Duke will benefit from beyond 2020 (i.e. structural) and some are not. Recall, Duke noted hiring freezes into '21 and corporate IT reductions as a tailwind for O&M agility. The new processes Duke is putting in place will drive efficiencies and yield cost savings through the incorporation of more digital, analytics and robotics throughout the organization. These new processes likely require less people going forward, which will sustainably lower the company's overall cost structure. Duke has dedicated resources working on these efficiency gains, and we expect to get more transparency on the major cost savings buckets later this year.

Essential Utilities (WTRG)

NT COVID Implications De-Risked, with LT Recovery Prospects Emerging

With their 1Q report earlier this month, WTRG reaffirmed 2020 guidance of $1.53-$1.58 and a 5-7% EPS CAGR through '22. We stress the largely residential profile of the water biz as providing some protection against load degradation while the gas biz enters shoulder season against the pandemic backdrop for now, as we monitor duration on a go-forward basis and any second waves or further escalation. While early action was taken to maintain a more conservative amount of liquidity, bad debt has been our primary concern. That said, discussions with mgmt. stressed last week's order in PA as helping to de-risk this given their particularly large presence in the state: recall, last Wednesday, the PA PUC issued a letter directing utilities to track COVID expenses and authorized regulatory assets for incremental uncollectible expenses incurred above those embedded in rates since the PUC's March 13, 2020 Emergency Order -any regulatory asset created under the authorization contained in the Secretary's Letter will be subject to review by the PUC in future proceedings. While this won't provide immediate help to cash flow, it should help limit degradation to P&L in the nearer term.

Meanwhile, we perceive the latest economic pressures broadly as likely to further accelerate consolidation in the industry as muni budgets are further flex'd from the crisis - and stress any further resulting acquisitions would be upside to mgmt's latest reaffirmed targets. States we are watching in the near term include TX & OH following the passage of FMV legislation in the states early last year and VA passing the legislation more recently. While we perceive TX bids as likely more competitive, WTRG is currently the only large water utility in the state of OH - and we see particular opportunities as likely to emerge following the Campbell acquisition. Meanwhile, we see NC as another state to watch given the new commission dynamic, albeit muni acquisitions there seem less clear cut relative to the more challenged munis in PA and IN.

Overall, mgmt. stressed confidence in our latest discussions around both volume and magnitude of muni acquisitions, and we perceive particularly bullish prospects for further consolidation for the water industry going forward.

Latest discussions also pointed to their intact balance sheet (following the Peoples acquisition despite some add'l debt to improve liquidity) with equity only needed to finance acquisitions. While continuing to allude to $300Mn in equity for DELCORA (& some latitude for further add'l acquisitions), we see timing as either 4Q or 1Q given a likely somewhat protracted process from the COVID backdrop and the current market environment.

Watch Repairs Tax Developments for the Catch Up Component

After closing on the Peoples Gas acquisition in Mid-March, the company elected the current component of repairs tax, reducing income tax by $5.9Bn for the quarter with expectations to drive $0.08-$0.12 worth of contribution for the year. Latest discussions suggested a filing for the catch up component in June or July with the process taking six to nine months. *We see this as the critical debate driving shares.*

Under implementation for the water biz, seven years of a ten year amortization went to the shareholder while three went to the ratepayer under what we stress as a particularly constructive outcome. While it remains to be seen how the commission will rule this time around, a constructive outcome remains clear cut upside to their numbers.

We remain Neutral rated on shares of WTRG, seeing risk/reward as balanced.

MDU Resources (Not Rated)

Catching Up Post Cut on COVID & More

MDU Resources (MDU) is a $4.4Bn market cap company based out of Bismark, ND that operates in 44 states. The company is a mix of regulated electric, natural gas, pipelines, and an unregulated construction materials and services business. MDU recently narrowed its 2020 EPS guidance from $1.65 - $1.85 to $1.50 - $1.70 with a 5-8% long-term CAGR while also lowering its revenue guidance for the construction business by $100M (while pulling margin guidance) following weak 1Q weather and as they continue to navigate the COVID crisis. Despite the lower guide, the company has a record backlog of $1.3Bn for construction services and a backlog of over $900Mn in construction materials.

Despite the more uncertain backdrop, management remains committed to M&A primarily through bolt on acquisitions, noting potential for more distressed opportunities in particular going forward and financing will likely be determined on a case by case basis. Shy of acquisitions, the company doesn't anticipate any near term equity needs and FFO/Debt metrics remain north of S&P's upwardly revised target of 22% (from 15% previously). Bottom line, while organic growth remains the primary driver of mgmt's capital allocation on a go forward basis, mgmt. has clearly identified a desire and opportunities for further acquisitions.

Northwestern Energy (NWE)

Contemplating Prospects & Evolving COVID Crisis

With their latest AGA update, NWE reaffirmed their recently revised 2020 guidance of $3.30-$3.45, but didn't provide any additional color around the latest weeks of load data. As previously noted, guidance assumes flat gross margin growth through the remainder of the year at the midpoint and we continue to watch any decoupling developments after the MT commission recently denied the intervener motion for reconsideration (around the potential ROE reduction for NWE if decoupling is implemented). While decoupling for NWE was initially contemplated for July, the MT commission plans on opening another docket to explore impacts of implementation during the pandemic and latest discussions suggested postponement would be beneficial given 90% relates to resi load (which has seen an uptick as expected given latest lockdowns across the nation). As such, we perceive NWE as likely to advocate for postponing any action around the mechanism into 2021 *(a presumably more normalized baseline)* despite a clear cut desire to implement in LT (not just in a five year pilot). Nuances & timeline to implementation remain critical both in the near term and longer term in MT.

We stress another nuance to watch is bad debt in particular given management's assumption of recovery in the latest guidance - albeit we continue to perceive a constructive backdrop in both SD and MT. The company has filed a joint expense recovery filing in SD with plans to file soon in MT.

Rate Cases & LT Gen: Awaiting MT RFP Bids

While the company doesn't plan to file any rate cases this year, discussions suggested they will continue to evaluate every April - and we don't perceive any firm decisions as having been made regarding a potential filing for next year. That said, given the capital spent and investment underway in SD with the latest generation win (and known and measurable gen spend into '21), we see a SD filing as more likely than not - and ultimately view a constructive backdrop for the state. We would expect MT filings to be more challenging on the margin given the aggressive cost cuts underway in '20 - as well as the likely ROE environment (with outstanding FERC uncertainty even as potentially weighing on state returns). All that said, we perceive bias towards a MT generation filing as opposed to a full rate case if the company is able to be successful with any generation bids in the state. Following an extension of the timeline, initial RFP bids are now due in July and we perceive confidence around maintaining the schedule and turning things around in a reasonable amount of time. Preapproval of a project could help mitigate impact in pushing out a rate case to '22.

Meanwhile, the company continues to work through potential approval to acquire additional Colstrip that would reduce their generation needs in MT and are hopeful to have clarity by the end of the year if ultimately approved. The company earlier notified the MT PSC that Talen Energy has purported to exercise its right under the Colstrip Ownership and Operation agreement to acquire a portion of the transaction that was negotiated between Puget Sound Energy and NWE for the proposed sale of the 185MW of Colstrip Unit 4. If Talen purchases a portion of the Puget Unit 4 interest, NWE would acquire at least half of Puget Sound Energy's interest equating to 92.5MW with a purchase price of $0.50, with the PPA with Puget Sound shifting to 45MW (from 90 initially contemplated) for five years. With any approval and potential close expected to play out by the end of the year, we continue to see rejection of the add'l Colstrip as best case scenario as meaningful generation spend and rate base is critical to driving longer term EPS growth.

We maintain our Underperform rating, seeing NT risk to the revised '20 guide under a protracted crisis and a lack of LT growth without meaningful generation.

Sempra Energy (SRE)

We maintain our Neutral rating as we continue to see shares as fairly valued given average implied upside as well as the uncertainty in LNG development given the market backdrop and limited recent developments after 1Q call as we await ECA FID (and financing disclosures). However, we stress SRE is one of few peers to have reaffirmed '20 guide at the top-end and provided visibility into '21 in the wake of COVID with potential upside at the CA utilities with clear bias to earn at more robust historical earned ROE levels. Confidence in TX also remains notable as incremental capex depends on interconnect approvals rather than the base plan despite the oil patch woes.

While IEnova concentration continues, mgmt. stresses that majority of $1bn growth capital can be deferred while confidence in counterparty contracts given continued payment and fixed/pass-through rates. Deferal of segment capex remains a unique risk. Further, we continue to see an equity issuance as unlikely as management prioritizes shareholders over a potential credit downgrade at Moody's (currently on downgrade review). Note SRE targets 16% FFO/debt in 2020 vs the 17% Moody's downgrade threshold; see Fitch/S&Ps outlook as critical given likely foregone conclusion at Moody's. Bottom line, while we see potential upside to the utility outlook, LNG uncertainty continues to linger with both the credit outlook (sending mixed messages to LNG counterparties?) and lack of tangible data points beyond ECA phase 1.

On balance we see upside to our ests consistent with management commentary on its 1Q call. That said, we suspect investors in SRE largely under-appreciate the consternation at IENova emerging in recent months.

California returning to a premium regulatory environment?

With recent constructive rate cases, we perceive confidence in mgmt.'s ability to earn closer to its historical earned ROEs. SRE has a history of earning strong ROEs relative to its authorized rates – see our report: Sempra Energy: Focus on the Utility: Raising expectations on (adamant) continued mgmt. confidence 06 February 2020. We continue to believe our estimates could very well see an improving trend through the forecast period. Sempra continues to allocate a significant amount of capital towards safety and reliability (80%+ of 5-yr capex relates to safety and reliability), and the company got nearly everything it asked for in the last general rate case under RAMP (risk mitigation phase). Bottom line, we perceive SRE's CA jurisdiction to be the most well positioned given the healthy ROE outlook and upside to spending initiatives to further align with state policy (wildfire mitigation/de-carbonization).

Balance Sheet: equity continues to seem unlikely with Moody's action likely

We continue to see FFO/Debt achieving the 16% threshold by YE2020, which compares to Moody's 17% threshold to maintain its BBB+ rating. With the addition of ECA LNG and management's commitment to its shareholders (i.e. no equity), we believe it will be difficult for SRE to maintain its BBB+ rating at Moody's. However, we expect the other agencies to grant more latitude to SRE with the Port Arthur FID pushed to 2021 as of the 1Q call, which gives the company more time to improve its metrics. We continue to see FFO/debt at 17% in 2022. Given ECA phase 1 could still move forward with the current threshold and Port Arthur would be project financed for 2-3yrs (with equity likely needed in year 3) we see no equity needs through the forecast period. Hence, we see a downgrade at Moody's as likely inevitable given commitment to no equity and company target of 16% FFO/Debt in 2020, but not at the other agencies that will likely allow SRE more leeway.

Texas: mgmt. still feels good about current capex plan

Management was clear it remains confident regarding the current capex plan at Oncor in the face of COVID and blatant exposure to the apex of the oil downturn in West Texas. The company does not expect an update to the Oncor capex program until its annual meeting in October, where the company will refresh the 5-year capital program as it

typically does each year. While management is cognizant of the steep decline in activity in the oil patch, it noted three areas offset to this, which include 1) Dallas Ft. Worth being one of the fast growing metropolitan areas in the country with 18k hookups in 1Q alone, 2) >100 GW of renewable generation in the queue in Texas, and 3) marginal producers in the Permian demand for converting diesel generation (30c/KW) to lower cost natural gas. On top of those three areas, management sees up to $750mn of ongoing capex deployment and has 13 renewable interconnects in the queue that are not in the base plan (i.e. incremental). *Despite clear risk of renewable project delays, management appears to feel confident a future roll forward could be at least as constructive as its latest update from late 2019. This was surprising in our view.*

IEnova: deferring of growth capital but not a material concern

At IEnova, mgmt. highlighted that its counterparty contracts continue to pay with over 50% backed by government entities (PEMEX, etc) with fixed rates/past through transmission costs. Despite confidence in navigating the regulatory climate, consternation persists following recent dynamics with the President and avoidance of subsidizing private industry. That said, mgmt. acknowledged that growth capital of $1bn+ associated with fuel terminals are likely to be deferred as the company looks to align with counterparty timing (BP, Valero, etc.). While majority of contracted EBITDA comes from ECA imports and pipelines with total income from the Mexican unit roughly 10-15% of SRE consolidated, we continue to monitor developments with the government bodies as it pertains to both ECA phase 1 approval and ability to execute on growth capex. See our colleagues note on IEnova for more.

Reiterate LNG update from 1Q call

Management had no change in messaging on the LNG front during its AGA update noting confidence in the future of the LNG business. The company emphasized its discipline where it looks for LNG returns well in excess of those at the utilities to justify the investments. SRE expects a Final Investment Decision (FID) on ECA LNG phase 1 this quarter (2Q20) subject to receiving an export permit. Once the project is sanctioned, the company plans to announce the financing terms. SRE noted it is reasonable to expect some of IEnova construction capital will be deferred from 2020 to 2021due to COVID-related pressures. We perceive the delay on logistics/terminals given lower liquids makes room in capex budget for ECA related spend. We expect SRE likely sells down some of its ownership stake to counter parties, adding some latitude to the balance sheet. Recall, as of the 1Q call, SRE secured the sale of two 20-year Supply Purchase Agreements (SPA) with Total and Mitsui for a total of 2.5Mtpa from ECA LNG phase 1. Further, the Port Arthur FID is still expected in 2021 (previously expected in 3Q20 ahead of COVID). On Cameron LNG Phase 2, MOU negotiations will likely take some time to turn into Sale and Purchase Agreements (SPAs) given the uncertain market environment. Net net, we continue to be cautious on LNG growth given the current market backdrop, but see this reiterated update as a moderate positive under the current circumstances of the market.

Incremental capex upside via RNG, hydrogen, DG, and mobile home parks

Despite an already robust 5-yr capex plan ($32bn 2020-2024), Sempra identified that the company has incremental upside to capex via 1) Renewable Natural Gas (RNG), 2) hydrogen, 3) distributed generation (DG), and 4) mobile home park upgrade programs. Recall, SoCalGas committed to replacing 20% of its traditional natural gas supply with RNG by 2030. We would note Sempra continues to be very focused on distributed generation, particularly in fuel cells, which could help supplement public safety power shutoffs (PSPS) especially for more isolated communities. These initiatives all provide upside to capex at the utilities over the next five years that is not baked into guidance. While we do not currently model these several items into our capex, it could drive eventual bias to positive estimate revisions.

Southern Company (SO)

We sensed an overall confident tone from mgmt. during our meetings on ability to sustain both cost cuts into the future (potentially 2/3 of upper end of $400mn range) and execution on Voglte w/ improvements in absenteeism and focus on upcoming Cold Hydro testing in the June/July timeframe. Meanwhile, mgmt. remains confident in the ability to overcome increased arrears/bad debt expense both from an EPS and cash flow impact. Aside from ability to defer costs in GA/MS (and annual filings in AL and gas LDCs insulated), the utilization of CARES Act loans for commercial and low income customers (loans forgiven as long as utility bills are paid) should help to alleviate cash flow impact. While we still see workforce reduction transition as important to monitor as well as remaining cost contingency relative to percentage to complete (w/ utilization of contingency a good barometer to monitor in terms of execution on costs), focus on upcoming testing data points remain critical to the SO story as start of Unit 3's Cold Hydro testing and execution will indicate if SO can turn the switch on. Net-net maintain Neutral rating given critical execution ahead.

Vogtle execution: watching productivity as Cold Hydro the next key inflection

Following reaffirmation of the aggressive schedule for Unit 3 (May '21) and regulatory in-service date and costs for both units (albeit pushed the aggressive schedule for Unit 4 back to its original May '22 date), commentary during our AGA call suggested no material updates although it has seen a noticeable improvement in absenteeism after reduction in workforce (to 7k from 9k). While we still see workforce reduction transition as important and remaining cost contingency relative to percentage to complete (w/ utilization of contingency a good barometer in terms of execution on costs) as critical to monitor, execution on upcoming testing items remain the most critical inflection point to the story. To that end, we look to Unit 3 start of conducting Cold Hydro testing in the June to July 2020 timeframe, although mgmt. continues to highlight that it has headroom in its plan so that Cold Hydro doesn't need to be done until Sept. to meet the Nov. 21 deadline. *Bottom line, execution at Vogtle for the remainder of 2020 will be critical to the SO story, and we will be keen to hear an update on the next data point in June/July with regard to the start of Unit 3's Cold Hydro testing.*

Examining cost savings and sustainability through outlook

With expectations for load to be down 2-5% for FY20 ($250-400mn impact in base revenues), mgmt. has been broadly confident that focus on O&M reductions would offset the substantial majority of load declines. During our discussions, mgmt. further opined on the ability to sustain these cost reductions more indefinitely, suggesting that nearly 2/3rs of its targeted range could be sustained (hiring freeze and new work from home capabilities) while 1/3rd are likely to be a headwind in future periods as there can only be a delay in items such as vegetation mgmt. for a period of time. While we perceive ability to maintain '20 guide (at least conceptually) as a positive given pervasive concerns of EPS guidance reductions across the space through focus on cost reductions, the broader commitment to '20 rather than explicit reaffirm is similar to that of CMS and is a tad cautious. That said, mgmt. highlighted a review of headcount reductions at the end of the year if the duration of COVID latest longer than expected as the most obvious upside angle to increased cost savings; albeit we perceive this as potentially the least palatable with regulators given the importance of maintaining jobs.

Watching bad debt expense w/ COVID; CARES Act all the more relevant

SO's gas utilities already have riders and trackers in place that help recover most of their bad debt expenses, but its electric utilities do not. This leaves the electric utilities more exposed to bad debt expense due to COVID. However, similar to a number of other states, both the Georgia and Mississippi commissions have announced orders to implement regulatory assets that will allow recovery for COVID-related cost. In Alabama, there is already a bad debt recovery mechanism within the Rate Stabilization and Equalization (RSE) mechanism. Mgmt. has highlighted that it has yet to see a material increase in arrears payments, although has ample liquidity ($7bn) to withstand a 40% of

customers in arrears ($1bn impact per quarter vs 15% modeled expectations). Aside from ability to defer costs in GA/MS, the utilization of CARES Act loans for commercial and low income customers (loans forgiven as long as utility bills are paid) should help to alleviate cash flow impacts. While we believe SO will ultimately be able to recover most of its bad debt expenses associated with COVID, the timing of this recovery presents uncertainty and further negative revision risk to near-term estimates.

Southern Power: No major impacts from COVID given profile

The vast majority of growth is expected to come from the current wind assets in its portfolio and Hypothetical Liquidation at Book Value (HBVL) accounting as the company did tax equity financing on those assets to further enable growth at the 5% clip. Mgmt. highlighted that even if it stopped investing today it could maintain the 5% growth through the plan period, although remains optimistic around potential upside with $500mn/yr in investments in the outer years of the plan; mgmt. highlighted it has seen some battery opportunities in CA this year. Further, with contracts for gas plants (CTs and CCTGs) based on capacity payments and renewables on take or pay contracts; it does not expect to see any degradation in the revenue stream due to COVID.

Elsewhere, mgmt. remains committed to its Gas LDC business, although continues to see challenges with midstream given the difficulty in rectifying permits (pervasive throughout the space).

WEC Energy Group (WEC)

Our discussions with mgmt. largely focused on the outlook for 2020 in the wake of Covid, with management continuing to emphasize early stages in terms of visibility on demand for the remainder of the year while stressing confidence in its ability to manage O&M expense; long-term mgmt. stresses that the pipeline of large industrials coming to Wisconsin remains intact with a recent addition of a large ship builder to the other high-profile projects previously announced.. Renewable updates were limited other than the previously communicated update on Badger Hollow 1 which has been pushed back by several months in an effort to manage the onsite workforce. Company mgmt. acknowledged being linked to Bloomberg News reports on a possible M&A transaction but declined to comment on the story. Mgmt had earlier talked down M&A on its call seeing few opportunities to find accretive prospects that would meet its 5-7% EPS growth. We continue to maintain our Underperform rating.

Early days in state reopening, but cost cutting remains key lever

WEC mgmt. reiterated its confidence in being able to manage O&M such that higher expenses and lost sales linked with the shut down orders during the Covid pandemic are expected to be offset. Among tailwinds cited was a lower level of maintenance required by leaks in the gas distribution system given the warmer than average winter. We continue to see cost cuts over and above mgmt.'s initial guidance range of 2-3% of day to day O&M as key to achieving the 2002 EPS guidance range of $3.771-3.75. Mgmt. noted that the reopening of business in the state of Wisconsin has been moved ahead of schedule previously laid out by the governor which initially lifted the stay at home order in late May with a phased reopening of some businesses including bars and restaurants in the middle part of the month. Recall that the company provided an updated forecast for electric sales with its Q1 reporting – now assuming small C&I sales declining by 4.6% and large C&I sales declining by 10.5% - mgmt. did not indicate that the forecast has shifted following the early suspension of stay at home orders following a state court ruling in early May.

Generation updates: modest delays in renewables, additional detail on Riverside

Badger Hollow 1 remains the one renewable project with notable delays – following a recent decision to push back construction the project is now expected to be in service in Apr/May 2021 after initially targeting an in service date of year-end 2020. Mgmt. cited the need to maintain social distancing guidelines, making it difficult to mobilize a workforce of ~100+ workers in an area of the state resources for bringing in a large work crew are limited. On the non-renewables front the company is pushing forward with its LNG project which was submitted to the commission earlier in the year and is expected to come for approval later in 2020. Mgmt. provided some additional color on the option to purchase a stake from the newly operational Riverside plant – the option gives WEC the opportunity to purchase a stake in the unit over a four year period; additionally WEC and LNT have the option to co-invest in new utility-scale projects being developed by either party – mgmt. flags the second option as advantageous given the availability of locations available for siting new renewables. Overall, the company expects to maintain adequate reserve margins for the foreseeable future given its ongoing renewables buildout and the retirement of 1800 MW of coal generation assets over the past several years.

Large industrials keep plans intact, ship builder plans to build

Importantly, the *long-term industrial sales forecast is intac*t with mgmt. still expecting large-scale industrial projects from Foxconn, Amazon, Milwaukee Tools, and others to come online as currently forecast with no expectation of altered plans in the state. As a positive data point mgmt. flagged Marinette Marine as a new large-scale project coming online in the Green Bay area as an addition to the industrial pipeline. Bottom line: mgmt. indicated that given the current line of sight the capital plan remains intact as growth in the state continues to be supported by large-scale industrial projects, with an expected updated capex plan coming in the fall in line with the company's normal update schedule.

Stocks mentioned

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
AEE	AEE US	Ameren Corp	US$ 72.23	A-1-7
AGR	AGR US	Avangrid	US$ 41	A-2-7
CNP	CNP US	CenterPoint Energy	US$ 17.49	B-3-7
ED	ED US	Consolidated Edison	US$ 73.11	A-1-7
DUK	DUK US	Duke Energy	US$ 84.92	A-2-7
WTRG	WTRG US	Essential Utilities	US$ 41.23	B-2-7
SRE	SRE US	Sempra Energy	US$ 124	A-2-7
SO	SO US	Southern Company	US$ 54.42	A-2-7
WEC	WEC US	WEC Energy Group Inc	US$ 87.62	A-3-7

Source: BofA Global Research

Price objective basis & risk

Ameren Corporation (AEE)

Our $75 price objective is predicated on a P/E based sum of the parts, valuing each business subsidiary relative to the 2022E ratebase weighted peer multiple of 15.8x for electric. We apply a 2.0x premium to peers at AEE Missouri to account for the improving prospects of capital spend, supplemented by a regulatory jurisdiction becoming more favorable - but lack of decoupling. We apply a 3.0x premium to peers at AEE Illinois to account for decoupling on the distribution business which aids in earnings predictability. The overall business is expected to grow at a more meaningful clip than that of peers - we see a 10% EPS CAGR at IL 2020-2024. At ATXI, we apply a 0x premium to peers to reflect the latest potential step down in FERC ROEs. At the Parent, we assume an in line multiple given the healthy debt metrics with FFO/Debt at 17%+. Electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector.

The upside (downside) risks to our price objective are the utilities earning their allowed returns or better (worse), a significant increase (decrease) in 30-year U.S. Treasury bond yields, and positive (adverse) regulatory outcomes that could impact mgmt's ability to earn its allowed return

Avangrid (AGR)

Our PO of $47 is based on an SOTP. The utilities are valued on a 2022E with a 1x disc to the electric peer P/E of 17.2x and 17.8x on the gas, given perceived risk to earned ROEs. Both electric and gas peer P/Es are grossed up to 2020 by 5-5.1% to reflect capital appreciation across the sector. We apply a 10X 2022E EBITDA multiple on the renewables sales earnings but strip out the tax credits/hedge value and apply a DCF (8%, no terminal) and an 8x EBITDA multiple for the small thermal assets (both based on comps). We back out 50% of the non-reg debt at the parent also. We include the value of the two offshore wind awards assuming $3500/kW cost, 6% disc, and 6% construction risk disc. We use an in-line discount for CMP's NECEC transmission project, but probability weight it 40% (broken out as well).

Upside risks: 1) ROE improvement in AGR's network business 2) Improvement in wind resources net capacity factor 3) higher than expected growth from offshore wind opp's.

Downside risks: 1) Iberdrola controls over 80% of AGR, limiting liquidity and exerting control over AGR's activities 2) Reg. relationships/outcomes could deteriorate 3) Existing and likely increasing exposure to the renewables biz results in a number of PPA related risks including commodity, recontracting & tax benefit recovery risk 4) Lack of adequate capital recovery mechanisms could threaten ROE's 5) The renewables biz may not expand as fast as expected or have worse returns 6) Offshore delays.

CenterPoint Energy (CNP)
We value CenterPoint Energy at $18 using a SOTP approach: electric business on an in-line utility multiple of 16.5x on 2022E P/E. We take out any earnings attributable to the transition bonds amortization, as those are temporary and instead add back the DCF value of future payments. For CNP's gas utilities we use an in-line utility gas peer multiple of 16.5x. Both electric and gas peer P/E multiples are grossed up by 5% to reflect capital appreciation across the sector. We integrate Vectren into our model and apply a 60/40% weighting to the gas/electric multiple. For VESCO we apply a 12x P/E multiple. We subtract parent interest expenses at a weighted average multiple. Further we net out the perpetual preferred, and apply a 50/50 weighting to parent debt and add back interest expense for recapitalization. We add CNP's interest in ENBL at the market value. We net out holdco interest at the weighted average P/E.

Downside risks: execution risk, decreases in capex which could support or weaken earnings ability, lower authorized returns, interest rate increases, and lower earnings from ENBL.
Upside risks: increase in capex, higher authorized returns, interest rate increase, better performance from the midstream biz.

Consolidated Edison (ED)
Our $85 PO is based on a sum-of-the-parts analysis applying premiums and discounts to the regulated group multiples (16.0x/16.5x for electric/gas respectively) with a 1.0x premium on gas and electric to reflect decoupling, and a -1.0x discount on steam to reflect volume exposure. We note that both electric and gas peer P/E multiples are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We applied inline peer regulated multiple at CECONY despite its rate certainty for conservatism as our higher capex expectations are reflected in our EPS outlook. We apply a discounted PE for infrastructure projects given the lack of clarity around the capital structure. We further apply an EV/EBITDA approach on 2022E EBITDA to the CEB business using a 10.0x multiple for both the legacy portfolio and the renewables portfolio seeing it as having higher quality returns.

Downside risks: ED, like all utility stocks, is also sensitive to changes in the market level of interest rates. Utilities historically underperform if bond yields rise, and outperform when they fall. Further downside risks are the inability to recontract storage, adverse regulatory outcomes, a deteriorating regulatory environment, or unforeseen disasters such as the Harlem gas explosion. Customer inflation is also a downside risk. PCG related counterparty exposure has abated as a source of risk but remains worth monitoring.

Duke Energy (DUK)
Our $83 PO is derived from a sum-of-the-parts valuation. We value the Electric and Gas utilities using peer 2022E P/E multiples. We apply a 1.0x multiple premium to Duke's operations in FL/IN to reflect more favorable regulatory environments. We apply an in-line multiple to the Carolinas given risk ahead. We value the other regulated electric utilities at 15.8x and the gas utilities at peer group multiples of 16.3x 2022E P/E, respectively. Both electric and gas peer P/E multiples are grossed up by 5% for the groups CAGR to reflect capital appreciation across the sector. The commercial midstream, and transmission are valued on a 2022E EV/EBITDA basis. We use a 9.0x multiple for midstream and transmission segment, although we assume a 50% weighting for ACP given risks to completion. We add the net present value of renewable segment using an 8% discount rate. We subtract out the impact of commercial debt, and add back for the renewable debt.

Upside risks: constructive rate case results, higher capital expenditure additions vs our assumptions, ACP ahead of schedule, lower interest rates. Downside risks: poor rate case results, operating errors, and negative changes in the regulatory environment, ACP delays. Macro risks: Increases in interest rates and decreases in equity market valuations.

Essential Utilities (WTRG)
Our price objective is $47 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 2.0x premium to Peoples Gas given the organic growth opportunities.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Risks to the upside include upward revisions to street estimates and further accretion from implementation of the Repairs Tax Benefit.

Sempra Energy (SRE)
Our $127 PO is based on a SOTP valuation based on 2022E net income. We apply a 1x discounted multiple to SDG&E and no premium multiple to SoCal Gas earnings (vs peer multiples of 16.3x and 17.1x, respectively). We use an in-line multiple for TX utility business given uncertain regulatory outlook despite T&D upside. For the LatAm business we value post-tax est for both sale of Peru & Chilean utilities. We value Cameron using a DCF at a 10.0% dis using a CAPM approach off its adjusted beta. We run a DCF on other LNG development and probability weight for project execution. We value the balance of the midstream segment using an EV/EBITDA approach using a 10.0x multiple as the Cameron import pipeline EBITDA doesn't step up until 2020. We further adj. for HoldCo debt & parent drag.

Downside risks: 1) negative reg risk from CA regulatory changes & int'l govts where SRE operates 2) incremental costs associated with Aliso canyon, 3) unanticipated cost overruns or delays for the Cameron LNG & other large organic growth projects 4) Capital markets or execution risk around the proposed Oncor transaction 5) rising rates, volatile natural gas prices & FX risks for SRE's int'l businesses Upside risks: 1) positive regulatory outcomes, 2) higher capex, 3) execution on Cameron ahead of our expectations, 4) lower interest rates.

Southern Company (SO)
Our $58 PO is derived from a SOTP. We use a P/E val approach on 2023 and use peer multiples of 15.7x for electric and 16.2x for gas, respectively (with dis/prem applied per asset depending on growth/risk): we then gross this multiple by +5% to account for sectorwide EPS growth to derive a 12-month forward PO. We subtract the 50% of the 2022 parent interest expense multiple by an electric P/E peer multiple to reflect parent lev supporting the utilities. We net out total parent drag and add back the remaining parent interest expense with a 50% weighting. Both electric and gas peer P/E multiples are grossed up by 5% to reflect capital appreciation across the sector.

Upside risks are: 1) Regulatory outcomes or RO's could be better vs expectations, as exposed to multiple state jurisdictions 2) Additional riders and capital trackers can help the company achieve better than expected ROE, but failure to get riders would hurt SO 3) The nat. gas related biz are relatively new and could prove more or less able to earn an ROE in line with or different from their allowed ROE, 4) high capital forecasts and subsequent earnings streams vs our assumptions
Downside risks are: 1) Regulatory outcomes or ROE's could be worse than expectations, particularly since exposed to mult. state jurisdictions, 2) SO has exposure to Vogtle which could shift earnings, 3) Weather patterns could influence usage or natural disasters could affect system reliability 4) Utilities are subject to interest rate risk.

WEC Energy Group Inc (WEC)
Our $81 PO is based on a 2022E SoTP analysis, based on the large cap electric group multiple of 16.3x and the gas regulated multiple of 16.7x. Both electric and gas peer P/E multiples are grossed up for a year to reflect capital appreciation across the sector.

We apply a 3.0x premium to WEC's WI electric & gas subs to compensate for surety in earnings growth for the next two years following the Commissions affirmation of the recent settlement on above average ROE's of 10%+. We apply a 1x premium to the gas utilities, incl IL's Peoples Gas and North Shore Gas with the Gas System Modernization Program (GSMP) and capex forecasts de-risked following the ICC order. We ascribe a 2x premium vs. the group at ATC to account for the steady nature of earnings growth as well as above average ROE's that are set at a federal level by FERC. We give Power the Future (PTF) a 2.0x premium multiple given the ROE is set indefinitely on historical and new investments. We ascribe an in line multiple for the parent accounting for the interest expense which finances overall utility operations. For the HoldCo adjustment to debt, we net out 50% of HoldCo debt from equity valuation and adjust to add back the parent drag on interest exp.

Upside risks are stronger than expected execution and accelerating capital oppt'y.

Downside risks are inability to achieve historical track record on cost cutting and ability to cont. to scale regulated investments given growing portion from contracted renewables.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

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BofA Securities is currently acting as financial advisor to Iberdrola SA in connection with the proposed sale of 50% ownership of the Dry Lake II Wind Farm and 50% of the Copper Crossing Solar Project to Axium Infrastructure Inc, owned by its subsidiary Avangrid, which was announced on 17 September 2019.

BofA Securities is currently acting as Financial advisor to Sempra Energy in connection with its proposed sale of 100% stake in Chilquinta Energia S.A., and Tecnored S.A as well as its 50% interest in Electrans S.A. to State Grid International Development Limited, which was announced on October 14, 2019.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
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	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Utilities Group (as of 31 Mar 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	72	50.35%	Buy	51	70.83%
Hold	38	26.57%	Hold	28	73.68%
Sell	33	23.08%	Sell	24	72.73%

Equity Investment Rating Distribution: Global Group (as of 31 Mar 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1602	52.15%	Buy	1005	62.73%
Hold	713	23.21%	Hold	463	64.94%
Sell	757	24.64%	Sell	382	50.46%

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
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Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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Aqua America

Diving In: See Opportunity in a Gas & Water Utility Hybrid

Initiating Coverage: BUY | PO: 45.00 USD | Price: 41.00 USD

Bank of America Merrill Lynch

Equity | 15 July 2019

Making a Splash: The gas uplift is real for EPS growth

We are initiating coverage on WTR, the second largest publicly traded water utility, with a Buy rating and $45 price objective. While we view the water sector overall as particularly pricey, we see a unique EPS revision potential for WTR as enabling a unique opportunity: we are above Street pro-forma for the Peoples Gas transaction (even with the full share o/s uplift), with our '20 EPS indicating upwards of $1.74 vs. Street of $1.55 (albeit unclear on what basis); we remain above Street on '21 EPS too with largely flat EPS still ($1.75 vs. Street of $1.66). While proforma EPS remains opaque prior to close, opportunities around Peoples Gas around repairs tax enable a potentially strong start to the EPS profile. While less confident on a precise figure, we perceive an upward bias relative to Street EPS expectations. While shares have already meaningfully rallied off lows, we sense a further re-rating opportunity as comfort emerges around the combined outlook. The deal comes on the heels of WTR's own step-down in EPS with normalization of earned ROEs at its principal subsidiary in PA, which has enabled outsized returns vs. authorized levels for years.

Water remains a pricey, but high quality & growth niche

We see the water sub-sector as lower risk vs. utility peers, with low overall consumer bills, opportunities for municipal consolidation across both water & waste-water systems affording a long tail of opportunities at above-sector growth. Smaller capital investments & recovery mechanisms limit material exposure to discrete project approval & afford for a more consistent return profile. Gas utilities fit many of these criteria with few large discrete projects

Valuing the Combined Company: The Right Move.

We use a SOTP analysis to value the company, applying a blended multiple (26.2x for water and 21.2x for gas). The Peoples Gas acquisition comes as water utilities are trading at what we see as an unsustainable premium to adjacent sectors. The ability to add among the highest growth utility assets at a discount to its own water multiple as particularly de-risking shares & strategically opportunistic.

Estimates (Dec)

(US$)	2017A	2018A	2019E	2020E	2021E
EPS	1.36	1.41	1.22	1.74	1.75
GAAP EPS	1.36	1.41	1.22	1.74	1.75
EPS Change (YoY)	3.0%	3.7%	-13.5%	42.6%	0.6%
Consensus EPS (Bloomberg)			1.36	1.55	1.66
DPS	0.81	0.86	0.92	0.99	1.06

Valuation (Dec)

	2017A	2018A	2019E	2020E	2021E
P/E	30.1x	29.1x	33.6x	23.6x	23.4x
GAAP P/E	30.1x	29.1x	33.6x	23.6x	23.4x
Dividend Yield	2.0%	2.1%	2.2%	2.4%	2.6%
EV / EBITDA*	1.1x	8.0x	26.2x	16.4x	15.6x
Free Cash Flow Yield*	-1.1%	-1.4%	-1.9%	-1.4%	-1.0%

* For full definitions of *iQmethod*℠ measures, see page 29.

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Stock Data

Price	41.00 USD
Price Objective	45.00 USD
Date Established	15-Jul-2019
Investment Opinion	A-1-7
52-Week Range	32.09 USD - 42.14 USD
Mrkt Val (mn) / Shares Out (mn)	8,845 USD / 215.7
Average Daily Value (mn)	37.97 USD
BofAML Ticker / Exchange	WTR / NAS
Bloomberg / Reuters	WTR US / WTR.N
ROE (2019E)	8.1%
Net Dbt to Eqty (Dec-2018A)	127.1%

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Timestamp: 15 July 2019 06:00AM EDT

iQprofile℠ Aqua America

*iQ*method℠ – Bus Performance*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Return on Capital Employed	5.1%	3.9%	4.4%	5.2%	5.1%
Return on Equity	12.6%	9.7%	8.1%	8.6%	8.3%
Operating Margin	41.5%	38.7%	48.1%	70.3%	71.2%
Free Cash Flow	(97)	(127)	(170)	(120)	(87)

*iQ*method℠ – Quality of Earnings*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash Realization Ratio	1.6x	1.9x	1.7x	1.8x	1.9x
Asset Replacement Ratio	3.5x	3.4x	3.3x	2.6x	2.5x
Tax Rate	6.6%	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	108.3%	127.1%	98.1%	101.2%	103.9%
Interest Cover	3.9x	2.8x	3.4x	3.5x	3.3x

Income Statement Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Sales	805	835	902	949	966
% Change	0.6%	3.7%	8.0%	5.3%	1.7%
Gross Profit	810	838	1,044	1,596	1,657
% Change	-1.3%	3.5%	24.6%	52.9%	3.8%
EBITDA	14,226	1,941	597	954	999
% Change	-33.6%	-86.4%	-69.2%	59.7%	4.8%
Net Interest & Other Income	(88)	(99)	(132)	(196)	(211)
Net Income (Adjusted)	**240**	**192**	**272**	**413**	**416**
% Change	**2.4%**	**-19.9%**	**41.6%**	**52.1%**	**0.6%**

Free Cash Flow Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Net Income from Cont Operations (GAAP)	240	192	287	442	445
Depreciation & Amortization	137	147	191	330	356
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	14	(15)	0	0	0
Other Adjustments, Net	(9)	45	(10)	(26)	(3)
Capital Expenditure	(478)	(496)	(639)	(865)	(885)
Free Cash Flow	**-97**	**-127**	**-170**	**-120**	**-87**
% Change	**NM**	**-31.5%**	**-33.9%**	**29.7%**	**27.7%**

Balance Sheet Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash & Equivalents	4	4	3	5	5
Trade Receivables	99	101	126	193	200
Other Current Assets	28	42	46	57	58
Property, Plant & Equipment	5,400	5,930	9,103	9,638	10,168
Other Non-Current Assets	801	887	2,462	2,462	2,462
Total Assets	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**
Short-Term Debt	117	160	289	312	333
Other Current Liabilities	167	239	258	309	315
Long-Term Debt	2,008	2,398	4,330	4,664	4,980
Other Non-Current Liabilities	2,083	2,158	2,158	2,158	2,158
Total Liabilities	**4,375**	**4,955**	**7,035**	**7,442**	**7,785**
Total Equity	**1,958**	**2,009**	**4,706**	**4,913**	**5,108**
Total Equity & Liabilities	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**

* For full definitions of *iQ*method℠ measures, see page 29.

Company Sector

Water Utilities

Company Description

Aqua America is a regulated water utility providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI. In Oct 2018, The company announced acquisition of Peoples Gas, a gas utility providing distribution services to 740,000 customers in PA, WV, and KY. The acquisition is expected to be closed by mid- 2019.

Investment Rationale

We see our Buy rating as supported by meaningfully above Street EPS projections on the back of its pending Peoples Gas business and above average ratebase growth.

Stock Data

Average Daily Volume	926,118

Quarterly Earnings Estimates

	2018	2019
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NA

Bank of America Merrill Lynch

Investment Thesis

We are initiating coverage on WTR with a Buy rating and $45 price target. Our estimates are meaningfully above the street, and we see higher revisions to numbers likely providing support for shares to move yet higher even after their de-risking post equity offering, particularly as we see risk to the multiples of pure water peers with less diverse growth prospects. We see growth as largely driven from Peoples Gas moving forward, where we expect the company to capture strong earnings power from repairs tax benefits in PA. We see an 11% total return to our price objective of $45, with further potential EPS upside if particularly successful in extracting ROE benefits in its core Peoples Gas utility from repairs tax benefits.

Strong Returns with Constructive Reg Backdrop

Following the acquisition expected to close this Fall, the company will be largely located in PA (the company received regulatory approval for Peoples in KY and WV and hearings PA hearings were recently completed) - a constructive utility jurisdiction, and will have a variety of mechanisms in place across states in which it operates to help drive recovery through rates. 46% of the company's legacy business is DSIC eligible, which they can leverage to stay out of formal ratecases, with a step up to 57% of spending DSIC eligible under the combined company. We have seen WTR utilize a repairs tax benefit in their legacy business that has helped to drive earnings without rate cases, and we could see a similar development on the gas side of the business post acquisition. If implemented, this should help to drive returns meaningfully higher over the next several years before any benefit is pushed back through to customers in a ratecase. We expect this to be a big driver of near term earnings, and a large reason why our estimates are well above the street.

What Are the Right ROEs for the Water Biz?

While ROEs are somewhat nuanced across WTR's footprint given varying mechanisms and the black box nature of some ratecase ROEs such as WTR's recent PA case, we expect the company to generally earn their authorized returns across most jurisdictions. 46% of WTR's business is currently DSIC eligible, which they can leverage to stay out of ratecases longer when returns start to fall. While their latest authorized ROE in Pennsylvania - the company's largest jurisdiction - isn't known, we suspect it to be close to around 10%. However, the company should benefit more in 2019 given the forward looking nature of the test year, with returns hovering at authorized levels across their water business looking forward. We see the regulatory construct in NC as the most challenging, with the commission historically focusing on water consumption, which typically declines 1% annually. That said, we note the company's small presence in the jurisdiction (~100K customers). While not likely to be material, an acceleration in muni acquisitions can also challenge modeling ROEs and create some regulatory lag.

Why Diversify into Gas? Ensuring Organic Prospects

Why invest in a gas utility when premiums are so material for stand-alone water companies? We see this as a bit of an experiment as to how investors will value a hybrid utility company considering the strong investor appetite for water today.

We see the gas transaction as principally motivated by its desire to firm up its own EPS growth outlook with the Peoples Gas business projected to grow its ratebase by 8-10% per mgmt. guidance, notably *higher* than WTR's stand-alone prospects of 7% (this is itself slower than the 8.7% EPS CAGR we have for its closest competitor AWK). We appreciate that gas utilities have more meaningful near-term prospects, but the underlying tension that is less clear is the question of how sustainable the ratebase growth profile is for each company? We believe current Street perception is that the ratebase growth outlook for water is more sustainable than that of gas. Should the reality be that gas growth is indeed more sustainable – whether on a discrete basis for Peoples Gas or for the wider gas utility industry –the valuation premium currently ascribed to the water industry could be in question, particularly as it continues to expand.

What about having other businesses? AWK experience has been positive

Contrasting with the Peoples Gas business, American Water, its closest competitor also maintains ongoing non-regulated operations as part of its overall business mix. The company has highlighted how this will not expand beyond 15% of the overall company and is designed to provide complementary opportunities to raise cash in a manner to minimize external equity. We see this firm cap as effective in reducing Street focus on this business at large. While actually achieving EPS growth for AWK has been another story given the specific non-reg efforts pursued, investor willingness to discount the company for these less valuable businesses has been less clear.

Without a set of comparisons, it's hard to say what the 'right' water multiple (and premium vs. electric utilities should be).

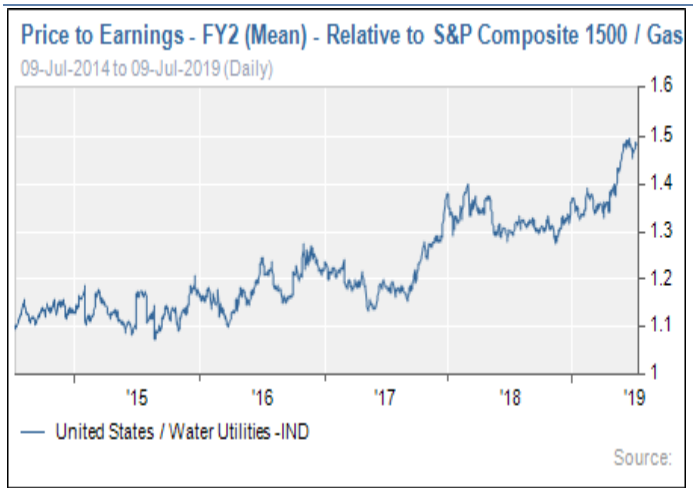
AWK's decision to pursue non-reg efforts as well as WTR's decision to pursue non-water efforts should in theory partially dilute down their exposure to pure-play water utility earnings growth. However, there is little evidence thus far this indeed the case.

We value Aqua America using a SOTP approach, ascribing an average of peer water utilities for its core water operations and ascribing a gas multiple for its gas businesses. We see upside to street estimates for WTR as supportive, particularly given the uncertainly around the water multiple more broadly. Our forward looking estimates reflect earnings on a combined basis with Peoples Gas.

Water: A Premium Product?

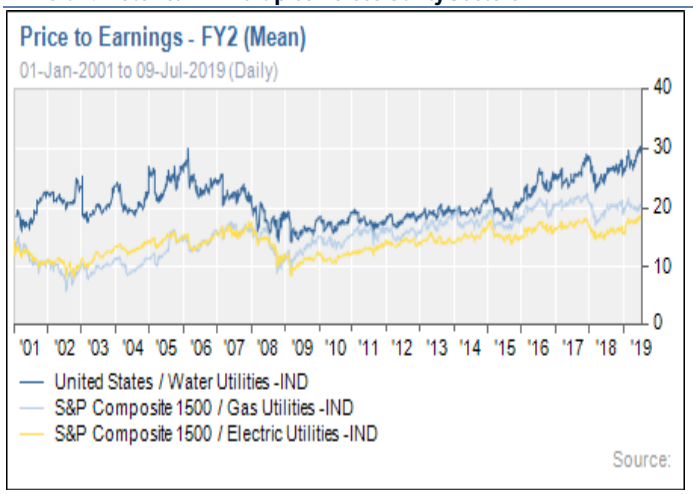
The exhibits below show the historical two year forward P/E ratio for water, gas, and electric utilities, as well as a history of water's premium over gas. While water has consistently traded at a premium to gas and electric, we note a strong acceleration in the spread more recently. We believe the historical premium is largely driven by water utilities' lower project risk associated with smaller and frequent projects, lower compliance and regulatory risk, and lower overall levels of scrutiny.

Exhibit 1: Historical Water Premium Relative to Gas



Source: BofA Merrill Lynch Global Research, FactSet

Exhibit 2: Historical PE multiples Across Utility Sectors



Source: BofA Merrill Lynch Global Research, FactSet

Water Growth Leading the Charge

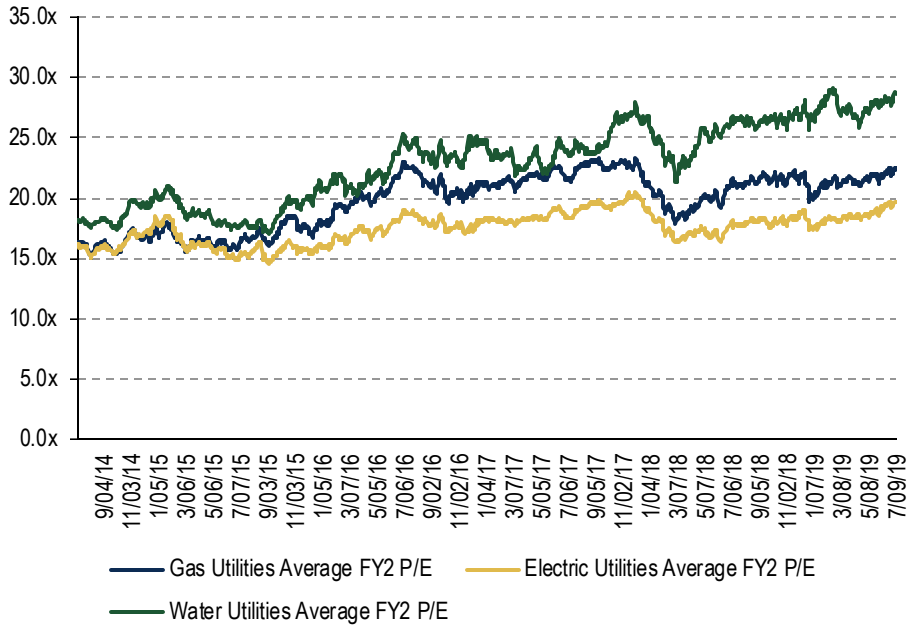
In the exhibit below, we reflect Consensus estimates for growth across the water, electric, and gas utility sectors. From 2018 through 2021, water is expected to grow at the fastest pace, at an 8% CAGR relative to 5% CAGRs for gas and electric, respectively. We also highlight the smaller variation y/y across the water space.

Table 1: Just how fast do utilities grow?

	2018	2019	2020	2021	2018-2021 CAGR
Water Utilities	4%	6%	9%	9%	8%
Gas Utilities	13%	-2%	10%	7%	5%
Electric Utilities	8%	2%	7%	6%	5%

Source: BofA Merrill Lynch Global Research, Bloomberg

Chart 1: Historical PEs Across Sectors



Source: BofA Merrill Lynch Global Research, FactSet

How did the Peoples Gas Transaction Come About?

The company is acquiring Peoples Natural Gas from SteelRiver Infrastructure Partners. SteelRiver is the successor of Babcock & Brown Infrastructure Fund North America, The current company was created through the acquisition of Peoples in February 2010, TW Phillips in May 2011, Equitable in December 2013, and Delta Gas in September 2017. Our sense is that the Steel River fund was looking to sell as it approaches maturity, presenting an opportunity for Aqua America to diversify their business.

Why does water trade at such a premium & does adding gas create a risk?

This is the second critical question for Aqua America in its bold move to acquire Peoples Gas. We believe much of the outsized premium for water utilities broadly is a direct result of a capital flows from ESG-specific funds allocating capital into the most palatable utilities. We ascribe a scarcity premium to water utilities relative to available capital. That said, we question the sustainability of the water premium broadly following the latest re-ratings, and expect gas driven earnings growth to provide relative support.

Business Overview

Aqua America is the second largest publicly traded water utility with corporate headquarters in Byrn Mawr, Pennsylvania. The company currently operates in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana and Virginia. Following the close of the acquisition of Peoples Natural Gas now expected in Fall 2019 (from mid-2019 previously), the company will also operate in West Virginia and Kentucky, with a pro forma rate base of over $7Bn (70% of combined company net income and rate base in water and wastewater).

Aqua Pennsylvania

Aqua Pennsylvania is the company's largest operating subsidiary, and accounted for ~53% of operating revenues and 71% of the regulated segment income in 2018.

Recent & Pending Acquisitions: Momentum in Muni Tuck-Ins

The acceleration of Fair Market Value Legislation in a number of jurisdictions has made muni acquisitions more palatable, and we continue to expect WTR to drive incremental rate base growth through additional tuck-ins. The company completed six muni acquisitions in 2018 for an incremental 100mn in rate base, with another 6 signed agreements pending closing. While we don't anticipate any large water acquisitions, we expect to see additional announcements over the course of the year. Mgmt has noted active pursuit in four of their existing states totaling over 400K customers, but has not disclosed the particular states they are pursuing the larger acquisitions.

Table 2: Acquisitions in 2018

Acquisitions - Closed in 2018	State	Rate Base	Customers	Ratebase Composition	Customer Concentration
Sun Valley	PA	0	81	0%	1%
Firestone Trace	OH	0	367	0%	3%
Manteno	IL	25	3,890	24%	27%
Limerick	PA	64	5,497	60%	39%
Peotone	IL	13	3,083	12%	22%
East Bradford	PA	5	1,240	5%	9%
Total		**107**	**14,158**	**100%**	**100%**

Inorganic Growth	*14,158*
Organic Growth	*8,500*

Source: Company report

The company is currently awaiting approvals for another six acquisitions YTD, largely concentrated in the state of PA (~95% on purchase price basis) with an overall purchase price consideration of $110M that would likely add another 19.4K customers (with 18k based out of PA).

Table 3: Pending Acquisitions - YTD

Pending Acquisitions	State	Purchase Price	Customers	Ratebase Composition	Customer Concentration
New garden	PA	30	2,106	27%	11%
Schuy kill	PA	4	600	3%	3%
Grant Park	IL	2	540	2%	3%
Cheltenham	PA	50	10,450	46%	54%
Sky line	IL	4	752	3%	4%
East Norriton	PA	21	4,952	19%	26%
Total		**110**	**19,400**	**100%**	**100%**

Source: Company report

Peoples Natural Gas

In 2018, WTR announced the acquisition of Peoples Natural Gas in an all-cash transaction that reflects an enterprise value of $4.3Bn (including $1.3Bn of debt). The company is headquartered in Pittsburgh, PA and provides natural gas distribution services to over 740K customers in three states (PA, KY, and WV; with KY and WV

expanding WTR's legacy geographic footprint). The company has ~15,500 miles of distribution pipeline, 1,500 miles of gathering pipeline and 250 miles of intrastate transmission pipeline. WTR has noted a 3,100 mile bare steel and cast pipe replacement opportunity at about 150 miles per year (implies 20+ years increased capex). In the near term, the company projects annual rate base growth of ~8-10% following a Pennsylvania rate case filed in January and new rates expected in the fall. Through the acquisition, WTR seeks to create a multi-platform regulated utility company, and expects the acquisition to be accretive to earnings in the first full year.

Pipeline Opportunity: Peoples has identified 3,000+ miles of bare steel and cast iron pipe to be replaced under their Long-term Infrastructure Improvement Plan (LTIIP) by 2034 in its PA service territory. The company currently has a Distribution System Improvement Charge (DSIC) in place that allows for the accelerated recovery of capital between rate cases. We see this as a key component of the company's ability to make timely recovery with minimal regulatory lag.

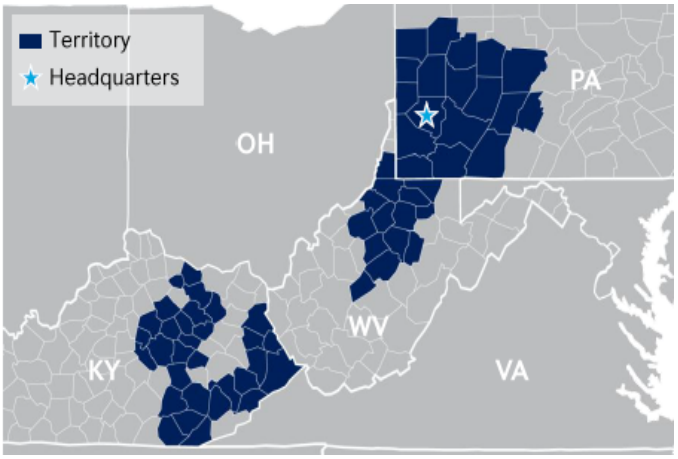
Operating Territories

Below we include the map of operating service territories of WTR and Peoples Gas on a standalone and pro forma basis. While WTR is currently present in the states of PA, OH, TX, IL, NC, NJ, and IN, Peoples Gas currently provides services in the states of KY, WV, and PA. Pennsylvania remains the only state where the footprints overlap.

Exhibit 3: Aqua America service areas– stand alone

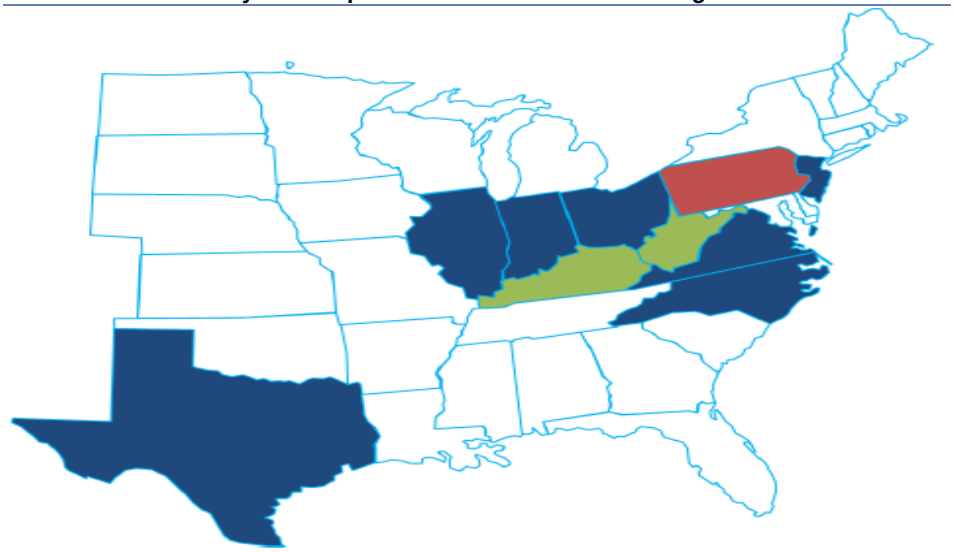
Source: Company Report

Exhibit 4: Peoples Gas service areas – stand alone



Source: Company Report

Exhibit 5: Combined Entity – Post acquisition service territories – PA being the common state



Source: Company Report

Bank of America Merrill Lynch

Rate Base: History and Beyond

Ratebase – WTR prior to Peoples Gas Transaction

We highlight that standalone ratebase for WTR as of yearend '18 stood at $4.5B for WTR with 878k water and 128K waste water connections, respectively. PA remains the single largest contributor to the company, contributing ~69% of the total ratebase; given the size of its existing operations and future growth prospects, PA is likely to remain the most critical state in WTR's service territories.

Table 4: Aqua – Standalone – Ratebase/Customer Details

States	Rate Base ($M)	Water Connections	Wastewater Connections	Total Customers	Ratebase Composition	Total Customer Concentration
PA	3,095	440,487	28,115	468,602	69%	47%
OH	317	145,938	6,878	152,816	7%	15%
IL	320	65,214	15,222	80,436	7%	8%
TX	235	64,360	17,480	81,840	5%	8%
NJ	171	53,639	6,213	59,852	4%	6%
NC	204	81,074	19,114	100,188	5%	10%
IN	83	1,226	26,979	28,205	2%	3%
VA	75	25,843	7,787	33,630	2%	3%
Total	**4,499**	**877,781**	**127,788**	**1,005,569**	**100%**	**100%**

Source: Company report

In 2018, WTR closed six acquisitions across the states of PA, OH, and IL that contribute $107M to the YE2018 ratebase, adding ~14K customers in the process (in addition to +8.5K of customer growth organically). The company has guided to 2%-3% customer growth from the legacy water business, with management noting about 70bp from new homes and the remainder from muni acquisitions.

Revenue Surcharge

Revenue surcharge is a mechanism through which regulators allow utilities to recover depreciation and capital costs associated with capital expenditures related to replacing and maintaining infrastructure systems. By permitting utilities to add a surcharge on to customer bills without a full rate case, utilities can reduce regulatory lag between completion of a capital project and the recovery of its costs through a formal rate review process. While WTR is permitted to apply a surcharge in seven states for its water utility operations, six states allow a surcharge for its wastewater operations.

Below we include the tables on rate cases/surcharges that are already approved by the respective regulatory commissions, as well as the cases pending before the commission. While completed and approved rate cases and surcharges in the states of IL, OH, and PA will add ~$5M of annual revenues, pending proceedings if approved could increase revenue requirement by another $78M. That said, settlement agreements pending approval in PA contemplate a $47Mn in revenue vs. an original request of $71Mn.

Table 5: Completed Surcharges in 2019

2019 Completed Surcharges	Revenue Increase ($M)	Type
IL	2	Surcharges
OH	1	Rate Case
OH	2	Surcharge
PA	0	Surcharges
Total	**5**	

Source: Company report

Table 6: Pending Surcharges

Pending Surcharges	Revenue Increase	Type	Docket ID
NJ	7	Rate Case (W)	WRT18121351
NC	1	Surcharge (w)	W-218, Sub 497A
NC	0	Surcharge (ww)	W-218, Sub 497A
OH	(4)	Tax Compliance Surcharge	18-1843-WW-UNC & 18-1841-ST-UNC
OH	2	Surcharge (w)	19-567-WW-SIC
PA	58	Rate Case (w)	R-2018-3003558
PA	13	Rate Case (ww)	R-2018-3003561
Total	**78**		

Source: Company report

Capex

WTR expects standalone rate base to be ~$5B at the end of 2019, and the company is projecting a CAGR of 7% through 2021. This is driven by $1.4B in investments over the next three years, with $550M earmarked for 2019. 46% of WTR's current capex is DSIC eligible.

WTR has guided to capital spending for Peoples Gas of $297Mn and $360Mn the next couple of years, largely driven by its Long-term Infrastructure Improvement Plan (LTIIP) for 3,100 miles of gas pipelines (~150 miles/year for next 20 years). 70% of Peoples capex is DSIC eligible to help reduce the regulatory lag. Under a combined entity, management expects capital spending to be 57% DSIC eligible.

Table 7: Peoples gas – Capex Plan

	2016	2017	2018E	2019E	2020E	2021E
Capex $M	140	205	280	297	360	360

Source: Company report

Could Clean Water Legislation Provide another Lever?

The Federal Safe Drinking Water Act, the Clean Water Act, and related state laws and regulations could provide further potential capital opportunities. While the US Environmental Protection Agency (EPA) has established health advisory levels at 70 parts per trillion for Perfluorooctanoic acid and Perfluorooctanesulfonic acid, states are increasingly looking to further limit such levels. Our sense from management is that installation of additional filters relating to stricter regulations could be an incremental $100Mn opportunity.

Texas the Latest to Adopt Fair Market Value Legislation

In 2016, fair market value legislation was enacted in Pennsylvania, WTR's largest jurisdiction, allowing the public utility commission to utilize fair market value to set ratemaking rate base (as opposed to the depreciated original cost of water or wastewater assets) for qualifying muni acquisitions. Under the process, independent valuation experts perform appraisals and the ratemaking base is the lower of the purchase price or average of the appraisals. The legislation ultimately provides a more accretive opportunity through these acquisitions, and we expect to see further tuck-ins across the water utility sector as the legislation gains momentum in additional jurisdictions. We highlight that six other states that WTR operates in currently have fair value legislation: Illinois, Indiana, New Jersey, North Carolina, Ohio and most recently Texas. Virginia is now the only state where Aqua operates without the legislation at the moment.

Ratebase – Peoples Gas

The table below reflects the rate base by state for Peoples Gas as of the end of 2018. Of the $2.1 total ratebase, PA represented $1.9Bn with small allocations for KY and WV. Looking forward, the company expects to grow ratebase at a 8%-10% CAGR through 2021.

Table 8: Peoples gas – Ratebase - standalone

State	Rate Base ($M)	Connections
PA	1,939	693,244
KY	108	38,701
WV	26	12,868
Total	**2,073**	**744,813**

Source: Company report

Peoples Gas filed its PA rate case earlier this year (Docket No. R-2018-3006818) for the first time since 2012. The request is for a revenue increase of $94.9m with a projected rate base of ~$2.1B for the test year ending October 2020. While rates are expected to go into effect in fall 2019, the rate case proceeding is ongoing. After rates go into effect, we expect the company to look at utilizing the repairs tax benefits to drive

material earnings growth for the gas business over the next several years. Under the treatment, the company could maintain any new revenue requirement while driving down the tax rate through expensing as opposed to capitalizing certain improvements.

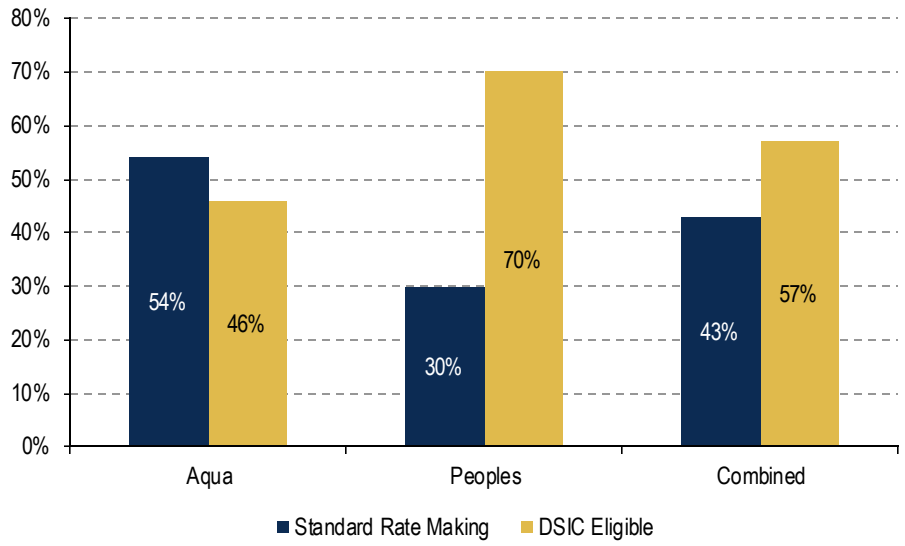
Table 9: Applicable surcharge and Mechanisms

Stae	Allowed Surcharge	Mechanism
Aqua		
IL	2.5% avg annual increase	QIPS
IN	10%	DSIC
NC	5%	WSSIC
NJ	Water - 5%	DSIC
OH	12.75% - water; 9% - wastewater	SIC
PA	7.5% - water; 5% - wastewater	DSIC
Peoples		
PA	5%	DSIC
KY	No Cap	PRP
DSIC	*Distribution System Improvement Charge*	
WSSIC	*Water and Sewer System Improvement Charge*	
QIPS	*Qualifying Infrastructure Plant Surcharge*	
PRP	*Pipeline Replacement Program*	

Source: Company report

Below, we highlight the % of planned capex from 2019 through 2021 that is eligible for DSIC and that of which is dependent on Standard Rate Making procedures. On a combined basis, management has highlighted over half of pro forma capital spending will be DSIC eligible, an incremental 11% relative to WTR's standalone mechanisms.

Chart 2: % of capex 2019-2021 recovered through DSIC



Source: Company report

Projected Combined Rate base

In the exhibit below, we reflect average rate base by company and on a pro forma basis. Management has guided to 7% for the standalone water utility with stronger growth of 8%-10% for Peoples Natural Gas. Our water utility rate base assumes just under 100Mn in annual tuck in acquisitions.

Table 10: Projected Ratebase

Average Ratebase	2019E	2020E	2021E	2022E	2023E
Water Utility	4,748	5,171	5,513	5,842	6,158
Ratebase growth		8.9%	6.6%	6.0%	5.4%
Guidance (RB CAGR 7% 19-21E, excluding acquisitions)			**7.8%**		
Peoples Gas	2,100	2,293	2,482	2,679	2,881
Ratebase growth		9.2%	8.3%	7.9%	7.6%
Guidance (RB CAGR 8-10% 19-21E)			**8.7%**		
Pro Forma	**6,848**	**7,464**	**7,996**	**8,521**	**9,039**
Ratebase growth		9.0%	7.1%	6.6%	6.1%
CAGR			**8.1%**		

Source: BofA Merrill Lynch Global Research estimates, company report

Combined Company Will Be Heavily Exposed to PA Jurisdiction

The Pennsylvania Public Utility Commission (PUC) consists of five commissioners – Gladys Brown Dutrieuille (D – Chairman), David Sweet (D – Vice Chairman), John Coleman (R), Andrew Place (D), Norman Kennard (R) – and 503 commission staff members. The commissioners are appointed to serve five years with the governor appointing a chairman. No more than three commissioners may be from the same political party.

NJ Jurisdiction

The New Jersey Board of Public Utilities (NJ BPU) consists of five commissioners – Joseph Fiordaliso (D - President), Mary-Anna Holden (R), Dianne Solomon (R), Upendra Chivukula (D), Robert Gordon (D) – and 247 staff members. The commissioners are appointed to serve six years with the governor appointing president. The NJ BPU has adopted fair market value legislation as well as a 5% DSIC mechanism for the water utility.

KY Jurisdiction

The Kentucky Public Service Commission (PSC) consists of three commissioners – Michael J. Schmitt (R – Chairman), Robert Cicero (R – Vice Chairman), Talina R. Mathews (R) – and approximately 70 staff members. The commissioners are appointed to serve 4 years with the governor appointing a chairperson.

IL Jurisdiction

The Illinois Commerce Commission (ICC) consists of five commissioners – Carrie K. Zalewski (D – Chairman), Brien Sheahan (R), Sadzi Martha Oliva (R), D. Ethan Kimbrel (D), Maria S Bocanegra (I – Acting Commissioner) – and 232 staff members. The commissioners are appointed to serve five year terms with the governor appointing the chairman.

IN Jurisdiction

The Indiana Utility Regulatory Commission (IURC) consists of five commissioners – Jim Huston (R – Chairman), Sarah Freeman (D), Stefanie Krevda (R), David Ober (R), David E. Ziegner (D) – and approximately 75 staff members. The commissioners are appointed to serve four year terms with the governor appointing a chairman to serve for four years.

NC Jurisdiction

The North Carolina Utilities Commission (NCUC) currently consists of six commissioners – Charlotte Mitchell (D – Chair), TroNola D. Brown-Bland (D), Jerry Dockham (R), James Patterson (R), Lyons Gray (R), Daniel Clodfelter (D) – and about 60 staff members. The commissioners are appointed by the governor to serve a term of six years, with the chairperson appointed to serve four year terms. With the recent resignation of Ed Finley and terms up for James Patterson and Jerry Dockham, Gov Cooper nominated three new commissioners Floyd Mckissick (D) Kimberly Duffley and Jeff Hughes, all of which are pending approval.

OH Jurisdiction

The Public Utilities Commission of Ohio (PUCO) consists of five commissioners – Sam Randazzo (I – Chair), Beth Trombold (I), Lawrence Friedeman (D), Dennis Deters (R), Daniel Conway (R) – and about 330 staff members. The commissioners are appointed by the governor to serve five year terms, with the governor electing a chairperson to serve through the duration of their tenure. The next appointment will be at the conclusion of Friedeman's term in April of 2020.

TX Jurisdiction

The Public Utilities Commission of Texas consists of three commissioners – DeAnn Walker (R – Chair), Arthur D'Andrea (R), Shelly Botkin (R) – and about 215 staff members. The commissioners are appointed by the governor to serve five year terms, with the governor electing a chairperson to serve through the duration of their tenure. The next appointment will be at the conclusion of Botkin's term later this year. The company transitioned to being regulated by the Texas PUC in 2014, and has been enjoying a 12% current authorized ROE, which we expect to fall under a PUC ratecase proceeding.

WV Jurisdiction

The Public Service Commission of West Virginia consists of three commissioners – Charlotte Lane (R – Chair), Brooks McCabe (D), Renee Larrick (R) – and about 230 staff members. The commissioners are appointed by the governor to serve six year terms, with the governor electing a chairperson to serve through the duration of their tenure.

Table 11: Commissioners by Jurisdiction

State	Commissioners	Position	Political Inclination	Took Office	Term Expires
NJ	Joseph L. Fiordaliso	President	D	2019	2025
	Mary-Anna Holden	Commissioner	R	2018	2024
	Dianne Solomon	Commissioner	R	2013	2019
	Upendra Chivukula	Commissioner	D	2014	2020
	Bob Gordon	Commissioner	D	2018	2023
PA	Gladys Brown Dutrieuille	Chairman	D	2019	2023
	David W. Sweet	Vice Chairman	D	2018	2021
	Norman J. Kennard	Commissioner	R	2017	2019
	Andrew G. Place	Commissioner	D	2015	2020
	John F. Coleman, Jr.	Commissioner	R	2017	2022
KY	Michael J. Schmitt	Chairman	R	2016	2019
	Robert Cicero	Vice Chairman	R	2016	2020
	Talina R. Mathews	Commissioner	R	2017	2021
IL	Carrie K. Zalewski	Chairman	D	2019	2024
	Brien J. Sheahan	Commissioner	R	2015	2020
	Sadzi Martha Oliva	Commissioner	R	2017	2022
	D. Ethan Kimbrel	Commissioner	D	2018	2023
	Maria S. Bocanegra	Acting Commissioner	I	2019	2023
IN	Jim Huston	Chairman	R	2014	2021
	Sarah Freeman	Commissioner	D	2016	2022
	Stefanie Krevda	Commissioner	R	2018	2022
	David Ober	Commissioner	R	2018	2020
	David E. Ziegner	Commissioner	D	1990	2023
NC	Charlotte Mitchell	Chair	D	2017	2023
	ToNola D. Brown-Bland	Commissioner	D	2017	2023
	Jerry C. Dockham	Commissioner	R	2013	2019
	James G. Patterson	Commissioner	R	2013	2019
	Lyons Gray	Commissioner	R	2016	2021
	Daniel G. Clodfelter	Commissioner	D	2017	2023
OH	Sam Randazzo	Chairman	I	2019	2024
	M. Beth Trombold	Commissioner	I	2018	2023
	Lawrence K. Friedeman	Commissioner	D	2017	2020
	Dennis P. Deters	Commissioner	R	2019	2021
	Daniel R. Conway	Commissioner	R	2017	2022
TX	DeAnn T. Walker	Chairman	R	2017	2021
	Arthur C. D'Andrea	Commissioner	R	2017	2023
	Shelly Botkin	Commissioner	R	2018	2019
WV	Charlotte Lane	Chairman	R	2019	2025
	Renee A. Larrick	Commissioner	D	2017	2023
	Brooks F. McCabe	Commissioner	R	2014	2021

Source: BofA Merrill Lynch Global Research, SNL

Merger Timeline

The exhibit below reflects the merger timeline for the Peoples Gas acquisition. Following the hearings related to the acquisition on June 11th, the company provided updated timing expectations of Fall 2019 from mid-year 2019 previously.

Table 12: Merger Timeline

Date	Proceedings
10/23/2018	*WTR announced Peoples acquisition*
11/13/2018	*WTR filed merger applications with PA/WV PUCs*
11/20/2018	*WTR filed merger applications with KY PUCs*
3/13/2019	*KY PSC approved merger*
3/27/2019	*Merger settlement filed with WV PSC*
3/29/2019	*$750M Investment from CPPIB*
4/18/2019	*Announced pricing of common stocks and tangible equity unit offerings*
4/24/2019	*Announced pricing of $900M senior notes offering*
2Q19	*WV PSC approved merger*
2Q19	*Targeted final order on PA merger proceedings*
6/11/2019	*Updated targeted closing date of merger to fall 2019*
Fall 2019	*Targeted closing date of merger*

Source: Company report

Bank of America Merrill Lynch

With the Company's updated timeframe for their expectations around the close of the Peoples Gas acquisition, we are projecting the transaction to close near the beginning of 4Q. The company has noted that they expect the transaction to be accretive to earnings in 2020 and longer term.

Comparing Aqua America with its peers

In the exhibits below, we reflect the latest WTR metrics relative to other water utilities. As the second largest publicly water utility (after AWK), the company is trading at 23.5x versus the broader water sector at 26.2x 2021 estimates on average. We see the street as largely underestimating the earnings ability for Peoples Gas in the near term, and see upside to estimates as largely supportive of valuation. The company's 2% dividend is in line with peers.

Table 13: DPS Comparison Across Water Comps

					DPS ($)			
Companies	**Ticker**	**Market Cap ($M)**	**Price ($)**	**Div Yield**	**2019**	**2020**	**2021**	**2022**
American Water	AWK	21,027	116.63	2%	1.97	2.15	2.36	2.58
SJW Group	SJW	1,791	62.87	2%	1.18	1.29	1.39	1.52
Artesian Water	ARTNA	339	36.41	3%	na	na	na	na
Connecticut Water Service	CTWS	845	69.90	2%	1.31	1.38	1.47	1.59
Middlesex Water Company	MSEX	983	59.49	2%	na	na	na	na
California Water Services	CWT	2,450	50.94	2%	0.79	0.83	0.87	na
Average				**2%**	**1.31**	**1.41**	**1.52**	**1.90**
Aqua America	**WTR**	**8,837**	**41.00**	**2%**	**0.9**	**1.0**	**1.1**	**na**

Source: BofA Merrill Lynch Global Research estimates, FactSet. Priced as of 12 July 2019.

Exhibit 6: Water Comps

						P/E Multiples					Earnings per Share					
	Ticker	**Market Cap**	**EV**	**Short Int**	**Days**	**2018A**	**2019E**	**2020E**	**2021E**	**2022E**	**2018A**	**2019E**	**2020E**	**2021E**	**2022E**	**CAGR**
Water Utilities																
American Water	AWK	21,206	27,673	2.9%	5.4	35.6x	33.0x	30.3x	27.7x	25.5x	3.30	3.56	3.88	4.24	4.61	8.7%
SJW Group	SJW	1,791	1,879	0.8%	1.2	30.0x	30.3x	27.4x	23.9x	20.5x	2.10	2.08	2.30	2.64	3.07	10.0%
Artesian Water	ARTNA	336	482	0.7%	3.0											
Connecticut Water Service	CTWS	845	1,152	1.4%	2.2	31.5x	29.6x	27.9x	25.7x		2.23	2.36	2.51	2.73		7.1%
Middlesex Water Company	MSEX	991	1,138	1.5%	2.5	30.7x	27.7x	26.9x	25.5x		1.96	2.17	2.24	2.36		6.4%
California Water Services	CWT	2,452	3,507	4.0%	5.1	40.9x	36.5x	31.6x	29.3x		1.25	1.40	1.61	1.74		11.7%
Average		**36,507**		**2.4%**	**4.4**	**33.0x**	**31.2x**	**28.4x**	**26.2x**	**23.0x**		5.6%	9.0%	9.1%	11.6%	**8.3%**
Aqua America	WTR	8,886	9,166	5.3%	11.3	29.3x	33.8x	23.7x	23.5x	22.4x	1.41	1.22	1.74	1.75	1.84	7.0%

Source: BofA Merrill Lynch Global Research, Bloomberg

What about Gas comps?

The 8-10% ratebase CAGR contemplated for Peoples Gas appears meaningfully ahead of peer gas utilities. We do not ascribe a premium to the gas utility in our valuation, however, as we believe the balance of the stand-alone gas utility sector is awarded a premium in part because of M&A expectations. We do not see WTR as a seller; rather the question is if it will continue to acquire gas utility platforms to complement its organic EPS growth outlook.

Exhibit 7: Gas Comps

	Ticker	Market Cap	EV	Short Int	Days	P/E Multiple					Earnings Per Share					
						2018A	2019E	2020E	2021E	2022E	2018A	2019E	2020E	2021E	2022E	CAGR
Gas Utilities																
Atmos Energy Corp	ATO	12,518	15,586	3.0%	4.5	27.1x	24.7x	23.4x	21.7x		3.95	4.33	4.58	4.93		7.7%
Spire Inc	SR	4,337	6,933	2.0%	4.3	23.1x	22.8x	21.9x	21.0x	19.4x	3.70	3.74	3.91	4.07	4.41	4.5%
New Jersey Resources Corp	NJR	4,462	5,646	3.5%	7.2	18.9x	25.0x	22.8x	20.9x		2.65	2.00	2.19	2.39		NM
Northwest Natural Gas Co	NWN	2,137	2,807	4.4%	6.1	31.6x	29.3x	27.8x	26.7x		2.22	2.40	2.52	2.64		5.8%
ONE Gas Inc	OGS	4,813	6,291	2.1%	4.8	28.0x	26.4x	25.3x	23.9x		3.26	3.46	3.61	3.83		5.5%
Southwest Gas Holdings Inc	SWX	4,825	na	1.3%	2.3	23.8x	23.0x	21.4x	19.8x	18.4x	3.82	3.94	4.25	4.59	4.95	6.7%
UGI Corp	UGI	9,260	14,241	4.3%	6.4	19.3x	22.1x	17.2x	16.2x		2.75	2.41	3.09	3.28		6.0%
NiSource Inc	NI	11,014	20,705	4.3%	5.1	22.7x	22.7x	21.9x	20.2x	18.8x	1.30	1.30	1.35	1.46	1.57	4.8%
South Jersey Industries Inc	SJI	3,107	5,755	7.0%	12.8	22.5x	30.4x	21.0x	19.3x		1.49	1.11	1.60	1.75		5.3%
Average		**56,472**		**3.6%**	**6.0**	**24.1x**	**25.2x**	**22.5x**	**21.2x**	**18.9x**		-1.8%	9.8%	6.7%	8.0%	**5.8%**

Source: BofA Merrill Lynch Global Research, Bloomberg

Bank of America Merrill Lynch

EPS Estimates

The exhibit below reflects our EPS estimates based on the expectation for the acquisition to close later this year. Given the tangible equity unit offering in connection with the acquisition, the company will provide EPS based on a share conversion and excluding the ongoing interest expense from the units. The equity units will convert between 1.1790 and 1.4442 shares per purchase contract depending on share price, and we assume ~16mn incremental shares based on price. That said, we expect parent drag to be mostly limited to holdco debt.

Our '21 estimates of $1.75 are well above the street at $1.66, driven primarily from an expectation of stronger earnings at Peoples Gas. Earned ROE degradation at PA, also itself a gradual process drives the relatively flat outlook for its core water utilities through the near-term as well.

Table 14: EPS Estimates

EPS Estimates	2019E	2020E	2021E	2022E	2023E
PA	$0.79	$0.80	$0.77	$0.82	$0.86
OH	$0.07	$0.07	$0.07	$0.08	$0.08
IL	$0.07	$0.07	$0.08	$0.08	$0.09
TX	$0.06	$0.06	$0.06	$0.06	$0.06
NC	$0.04	$0.04	$0.04	$0.04	$0.05
Other States	$0.08	$0.08	$0.09	$0.09	$0.10
Water Utility	**1.11**	**1.12**	**1.11**	**1.18**	**1.24**
Peoples Gas	**0.16**	**0.70**	**0.75**	**0.79**	**0.82**
Parent & Other	*-0.05*	*-0.08*	*-0.10*	*-0.12*	*-0.14*
EPS	**1.22**	**1.74**	**1.75**	**1.84**	**1.92**
YoY Growth		*43%*	*1%*	*5%*	*4%*
Shares O/S	*223*	*238*	*238*	*250*	*254*
Fully Diluted Shares O/S	*235*	*254*	*254*	*254*	*254*
Consensus	**1.36**	**1.55**	**1.66**		
Consensus '19-'21 CAGR					
BofAML CAGR 2019-2021					
DPS	**0.92**	**0.99**	**1.06**	**1.13**	**1.21**
Payout Ratio	*76%*	*57%*	*60%*	*61%*	*63%*

Source: BofA Merrill Lynch Global Research estimates, company report

Valuation

With our estimates, we set a price objective of $45 based on a SOTP analysis. We apply the water utility multiple of 26.2x to the water segment (with no discounts to reflect no over-earnings by '21 at any of the subsidiaries) and 21.2x for the gas segment (with a -1x discount to reflect risks related to both no takeout premium reflected in the balance of the sector in our judgement as well as its over-earning ROE profile particularly upfront), grossing each up for the respected growth CAGR. The question is just over what period of time can Peoples Gas navigate substantive rate increases without sacrificing a refund of merger synergy benefits fully; WTR's PA segment was able to maintain its over-earning position for upwards of 7-years. We net out 50% of holdco debt and 50% of interest expense. While we see risk to the water utility multiple premium broadly, we expect WTR to be supported from strong earnings growth and estimates moving higher.

Table 15: WTR SOTP

Water Utilities	2021 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*26.2x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		**28.4x**							
Water Utilities									
States	**2021E EPS**	**ROE**	**embedded**						
PA	$0.77	10.0%	**0.0x**	27.4x	28.4x	29.4x	$21	$22	$23
OH	$0.07	9.9%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$2
IL	$0.08	9.6%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$2
TX	$0.06	10.0%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$2
NC	$0.04	9.9%	**0.0x**	27.4x	28.4x	29.4x	$1	$1	$1
Other (including acquisitions)	$0.09	9.9%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$3
Water utilities total (ex-Peoples)	**$1.11**			*27.4x*	*28.4x*	*29.4x*	**$30**	**$32**	**$33**
Gas Utilities									
Peer Gas P/E		*21.2x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		**22.4x**							
	2021E EPS	**ROE**	**embedded**						
Peoples Gas	**$0.75**	14.1%	**-1.0x**	**20.4x**	**21.4x**	**22.4x**	**$15**	**$16**	**$17**
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			**-752**	50%			($376)	($376)	($376)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($364)	($379)	($393)
50/50 Weighted Drag from HoldCo Drag							($740)	($755)	($769)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							**$43.00**	**$45.00**	**$46.00**
Current Price								$41.00	
Dividend Yield								2%	
Total Return								**11.89%**	

Source: BofA Merrill Lynch Global Research estimates

Bank of America Merrill Lynch

Debt and Capital Structure

The exhibit below reflects our estimated debt construction across the pro-forma portfolio. We expect debt to move towards 15% at the holdco level, creating an additional parent lag. Our sense from management is that they will look to hold enough debt to finance a run rate of $100Mn in annual muni acquisitions.

Table 16: Debt Projections

Debt by Construct	2019	2020	2021	2022
Regulated - Legacy Business	2,419	2,588	2,750	2,906
Peoples Gas	1,300	1,387	1,478	1,572
Holding Company	611	689	752	822
Total Debt	**$4,330**	**$4,664**	**$4,980**	**$5,300**

Debt by Construct (%)	2019	2020	2021	2022
Regulated - Legacy Business	56%	55%	55%	55%
Peoples Gas	30%	30%	30%	30%
Holding Company	14%	15%	15%	16%

Source: BofA Merrill Lynch Global Research estimates

S&P: (Aqua Pennsylvania)

Following the announcement of the People Gas acquisition, S&P placed subsidiary utility Aqua Pennsylvania on credit watch with negative implications for the A+ issuer rating and their AA- first mortgage bond rating. S&P noted this reflects the likelihood that the transaction would result in materially weaker consolidated financial measures for the overall group. For the rating agency to keep their current investment rating, they look for consolidated FFO/Debt to be 13%-23%, with their current forecast projecting 11.5%-13% following the close of the transaction.

Moodys: Baa2 – Stable Outlook

In late April, Moody's launched on WTR with a Baa2 rating and a stable outlook issued a on the senior unsecured debt. The rating agency noted the low-risk of water and waste water operations and strong regulatory support in the primary jurisdiction of Pennsylvania and diversity across the rest of the portfolio. That said, they expect a declining financial profile due to the pending acquisition (PNG is currently rated Baa2 positive) and debt funded capex. Post close, Moodys expects holding company debt to be roughly 15% of consolidated debt on their calculation.

While Moody's Stable outlook takes into account the weaker financial profile, key ratios of FFO/net debt and retained cash flow (RCF) are expected to be maintained above 12% and 7%, respectively. We see these as the two key indicators to monitor for potential equity needs.

Table 17: Moodys Metrics

	2016	2017	2018	2019E	2020E	2021E	2022E
CFO	**412**	**396**	**384**	**614**	**745**	**798**	**846**
+/-: Working Capital Adjustments	(1)	7	17	10	26	3	4
CFO Pre-WC	**411**	**403**	**401**	**624**	**771**	**801**	**850**
+/-: Other Adjustments	(4)	3	1	1	1	1	1
FFO	**407**	**406**	**402**	**625**	**772**	**802**	**851**
Less: Dividend	131	141	151	205	234	251	282
CFO Pre-W/C - Dividends	**280**	**262**	**250**	**418**	**537**	**550**	**568**
Less: Capex (Includes Acquisitions)	395	486	644	4,939	865	885	905
FCF	**(114)**	**(231)**	**(411)**	**(4,531)**	**(354)**	**(337)**	**(341)**
Retained Cash	**277**	**267**	**251**	**419**	**538**	**551**	**569**
FFO / Debt	20.3%	18.3%	15.3%	13.3%	15.3%	14.9%	14.8%
RCF / Debt	13.8%	12.0%	9.5%	8.9%	10.6%	10.2%	9.9%

Source: BofA Merrill Lynch Global Research estimates, Moodys

Management Bios

Board of Directors

We see WTR's board as particularly qualified relative to the balance of the utility sector with numerous former corporate & business-unit level CEOs, but what is particularly remarkable are the multiple executives who have been previously involved in senior management positions within the utility industry. For instance, the experience offered from SO and DUK, two large cap utility peers, is particularly relevant in addressing strategy. The board recently voted to increase the size of their board to 8 members with the election of Francis Idehen, in line with peer AWK. Francis is a particularly relevant director given his prior role in IR at Exelon.

Christopher H. Franklin is Chairman, Chief Executive Officer and President

Christopher H. Franklin is Chairman, Chief Executive Officer and President of WTR. He was previously president and chief operating officer, regulated operations. He has held several key executive roles in public affairs, customer operations and as regional president of the company's southern and mid-western operations, and was responsible for company's corporate and public affairs federal, state and municipal legislative affairs, investor relations, and communications. He joined WTR in 1992 as director, corporate and public affairs. Prior to that, he worked at PECO Energy Company (an Exelon Company) as regional, civic and economic development officer and was responsible for the review, recommendation and promotion of economic development initiatives in the Philadelphia region. He serves as a director on the National Association of Water Companies' board of directors. Previously, he served on the board of directors of ITC Inc.

He earned his B.S. from West Chester University and his M.B.A. from Villanova University.

Elizabeth B. Amato - Director Since 2018

Ms. Amato, a director since 2018, appointed to the Executive Compensation Committee and the Corporate Governance Committee of the Board, is a human resources executive with over twenty years of leadership experience. She has been Executive Vice President and Chief Human Resources Officer of United Technologies Corp. since November 2015. Previously, she was Senior Vice President, Human Resources and Organization of UTC from August 2012 to November 2015. She joined UTC in 1985 and held a variety of the most senior human resources leadership positions across the corporation in both aerospace and commercial building systems, including UTC Climate, Controls & Security (2011-2012), Carrier (2010-2011), Pratt & Whitney (2006-2009) and Sikorsky (1997-2006).

She holds a bachelor's degree in political science from Davidson College and a law degree from the University of Connecticut. She is a recipient of the YWCA Women Achievers Award, is currently a member of the National Academy of Human Resources CHRO Board Academy, and is a member of the Board of Directors for Children's Healthcare Charity, Inc.

Nicholas DeBenedictis - Chairman Emeritus

Nicholas DeBenedictis currently serves as chairman emeritus. He recently stepped down as the non-executive chairman of the board of Aqua America. Previously, He served as Chairman and CEO of Aqua America (formerly Philadelphia Suburban Corporation) from June 1993 to July 2015. Prior to that, he served as senior vice president of corporate and public affairs for PECO Energy from 1989 to 1992 and was responsible for government relations, economic development and environmental policies, plus implementation of the utility's public policy positions. He also serves on the Board of Exelon. Before that, he worked as president of the Greater Philadelphia Chamber of Commerce from 1986 to 1989. He worked as a Secretary of the Department of Environmental Resources (1983-1986) and Director of the Office of Economic Development (1981-1983) in Pennsylvania

government's cabinet positions. Before joining the cabinet, he was associated with the U.S. Environmental Protection Agency fort eight years (1973-1981). He served in the Army Corps of Engineers between 1970 and 1973 reaching the rank of Captain. He is the current president of the Pennsylvania Society, and currently serves on the policy committee of the Pennsylvania Business Council and is a former Chairman of the Council (formerly the Pennsylvania Business Roundtable). He also serves on the Board of Directors for many regional businesses, economic and environmental organizations that include Drexel University, Exelon Corporation, PNC Bank - Southeast Pennsylvania Advisory, P.H. Glatfelter Company, and Independence Blue Cross. He is a past president of the National Association of Water Companies.

He earned his Bachelor's degree in business administration from Drexel University in 1968, and a Master's degree in environmental engineering and science from Drexel in 1969. He received an Honorary Doctorate of Science degree from Widener University, an Honorary Doctorate of Letters degree from Drexel University, and an Honorary Doctor of Humane Letters from Misericordia University.

Daniel J. Hilferty - Lead Independent Director, Director since 2017

Daniel J. Hilferty is Lead Independent Director of the company since 2017. He worked as president and chief executive officer of Independence Blue Cross. Previously, he worked as a Senior Vice President of Corporate and Government Affairs at Mercy Health Corporation in Bala Cynwyd, PA and then as President and CEO of AmeriHealth Caritas Family of Companies (formerly Amerihealth Mercy) in Philadelphia PA from 1996 to 2009.

He earned his undergraduate degree from St. Joseph's University in Philadelphia, Pennsylvania, and a master's degree in public administration from American University. He also serves on the boards of the Greater Philadelphia Chamber of Commerce, the Catholic Foundation of Greater Philadelphia, and FS Investment Corporation III and as chairman of the board of directors for the Blue Cross Blue Shield Association.

Ellen T. Ruff - Director since 2006

Ms. Ruff is director since 2006. She has over 30 years of experience with a major utility company in various management, operations, legal planning and public affairs positions. She is also a partner in the law firm of McGuire-Woods, LLP. Previously, she served as President, Office of Nuclear Development, for Duke Energy Corporation, from December 2008 until her retirement in January 2011. Prior to that, she worked as President of Duke Energy Carolinas from 2006 through 2008. She served Duke Energy organization in various capacities, including: Vice President and General Counsel of Corporate, Gas and Electric Operations; Senior Vice President and General Counsel for Duke Energy; Senior Vice President of Asset Management for Duke Power; Senior Vice President of Power Policy and Planning; and Group Vice President of Planning and External Affairs.. She is also a director of Mistras Group, Inc

Lee C. Stewart - Director Since 2018

Mr. Stewart, a director since 2018 is a private financial consultant with over 40 years of experience as an investment banker, corporate executive and professional director. He has been appointed to the Audit Committee and the Risk and Investment Policy Committee of the Board. Previously, he was Vice President at Union Carbide Corporation from 1996 to 2001, and as Chief Financial Officer of Foamex International, Inc from 2001 to 2002. After that, he served as a director of AEP Industries, Inc., a chemical company listed on the Toronto Stock Exchange from 2000 till 2011, as a director of ITC Holdings Corp. from 2005 to 2016, as well as associated with Momentive Performance Materials Inc., a specialty chemical company in silicone and advanced materials from May 2013 through its successful emergence from bankruptcy in October 2014. He has been director of P.H. Glatfelter, a global supplier of specialty papers and engineered materials, since 2002 and is also director of Mood Media, Inc.

Mr. Stewart has a bachelor's degree from the Wharton School of the University of Pennsylvania

Christopher Womack - Director Since 2019

Mr. Womack is a director of the company since 2019. He has served as President, External Affairs, Southern Company from December 2008 until the present. He has worked in various executive leadership positions at Southern Company since 1988 that includes Executive Vice President, Georgia Power Company from March 2006 to December 2008, Senior Vice President, Fossil & Hydro Power, Georgia Power Company from December 2001 to March 2006, and Senior Vice President, Human Resources from March 1998 to December 2001. He also served as a legislative aide in the U.S. House of Representatives from 1979 to 1987.

Francis Idehen – Director Since 2019

Mr. Idehen is the newest director of the company and was elected to the board at the beginning of June when the board voted to increase their size to 8. He currently serves as managing director and COO at Grosvenor Capital Management, a position he has held since 2017. In his current capacity, he is responsible for overseeing core operations functions, including fund finance, corporate finance, technology, compliance and legal. He is also a member of the firm's operations committee and labor impact fund investment committee. Previously, he has held senior roles at Exelon from 2011-2017, serving as treasurer, head of investor relations and managing director of Exelon's investment office. Prior to that, Idehen served as a Senior Portfolio Manager at Intel. Mr. Idehen has a bachelor's degree in economics from Yale University and an MBA from Harvard Business School.

Leadership Team

Rick Fox - Executive Vice President and Chief Operating Officer, Regulated Operations

Rick Fox serves as Chief Operating Officer (COO) of Aqua America since July 2015 and is responsible for the company's regulated operations, including engineering and environmental compliance.

Prior to that, he served as regional president for Aqua America since January 2012, responsible for managing utility operations in Texas, Illinois, North Carolina, Indiana and Virginia. Before that he was vice president, customer operations and responsible for all customer service operations for Aqua America's regulated operating subsidiaries, including the company's national customer call centers, national meter operations, and company-wide billing and collections. He joined Aqua America in 2002 as manager of customer service following 17 years in the chemical manufacturing industry in both operations and technical management.

He earned his B.S. in chemical engineering from Virginia Polytechnic Institute and State University, and his M.B.A from Villanova University, where he achieved Beta Gamma Sigma honors. He is a member of the American Institute of Chemical Engineers.

Christopher P. Luning - Senior Vice President, General Counsel and Secretary

Christopher P. Luning was appointed Senior Vice President, General Counsel and Secretary for Aqua America, Inc. in May 2012. He is the company's chief legal counsel and responsible for the company's legal, human resources, internal audit, and safety departments. Previously, he worked as a vice president, corporate development and was responsible for corporate development activities. He joined Aqua America in 2003 as assistant general counsel. Prior to WTR, he worked at Hovnanian Enterprises, Inc. as legal counsel.

He earned his B.S. business/political science from Albright College and his J.D. in 1993 from Villanova University. He is licensed to practice law in Pennsylvania and New Jersey.

Matt Rhodes - Executive Vice President, Strategy and Corporate Development

Matt Rhodes works as Executive Vice President, Strategy and Corporate Development for Aqua America since June 2018 and responsible for assisting the chief executive officer with developing, communicating, executing, and sustaining strategic initiatives, with an emphasis on growth. He is also responsible for overall corporate development, as well as acquisitions of regulated and market-based businesses.

Previously, he worked as Managing Director at Goldman Sachs in the Natural Resources Investment Banking Group with a focus on power and utility clients. Prior to that, he served at Bank of America and Duke Capital partners in energy finance roles.

He earned his BBA from the University of Texas at Austin and an MBA, with honors, from the Stern School of Business at New York University.

Robert A. Rubin - Senior Vice President, Chief Accounting Officer and Controller

Robert A. Rubin serves as senior vice president, controller and chief accounting officer (CAO) of Aqua America, since January 2012, and responsible for external and internal financial reporting, taxes, coordinating external audits, corporate accounting and maintaining compliance with accounting standards and principles throughout the company. Previously, he worked as chief accounting officer of the company from 2004 to 2012. Prior to that, he worked as controller for the company from 1999-2004. He joined Aqua America in 1989 as an accounting manager. Prior to that he was associated with KPMG LLP

He is a Certified Public Accountant with a B.S. in accounting from Penn State University and associated with the Pennsylvania and American Institutes of Certified Public Accountants and the National Association of Water Companies – Taxation Committee.

Dan Schuller - Executive Vice President, Chief Financial Officer

Dan Schuller is Executive Vice President and Chief Financial Officer for Aqua America, Inc. and responsible for accounting, tax, treasury, regulatory relations, planning, Sarbanes-Oxley compliance and capital spending in regards to return on investment. Previously, he served as Executive Vice President, Strategy and Corporate Development for Aqua America and was responsible for Aqua's strategic growth initiatives. Prior to Aqua America, he was associated with J.P. Morgan Asset Management – Infrastructure Investments Group as an investment principal. Prior to joining J.P. Morgan, he was a manager at Mars & Co., an international strategy/general management consulting firm and was responsible for consulting engagements related to growth and profitability for Fortune 500 companies and conducted due diligence for private equity firms.

He earned his B.S., M.S. and Ph.D. in civil engineering from Purdue University and also a member of the American Society of Civil Engineers.

Financial Statements

Income Statement

Table 18: Income Statement

	2016	2017	2018	2019E	2020E	2021E	2022E	2023E
Regulated	*800*	*805*	*835*	902	949	966	1,004	1,042
Other & Eliminations	*20*	*5*	*3*	3	3	3	3	3
Peoples Gas	*0*	*0*	*0*	139	643	687	733	770
Operating revenues	**820**	**810**	**838**	**1,044**	**1,596**	**1,657**	**1,740**	**1,815**
Operating expenses:								
Operations and maintenance	297	282	308	351	500	513	525	534
Regulated	278	282	292	336	485	498	510	519
Other & Eliminations	20	0	16	15	15	15	15	15
Depreciation	131	136	146	191	330	356	382	409
Amortization	2	0	1	-	-	-	-	-
Taxes other than income taxes	56	57	60	68	98	101	103	105
Regulated	54	55	57	66	96	98	101	103
Other & Eliminations	2	2	3	3	3	3	3	3
Total operating expenses	**487**	**476**	**515**	**610**	**928**	**969**	**1,011**	**1,049**
Operating income	**333**	**334**	**323**	**434**	**668**	**687**	**730**	**766**
Allowance for funds used during construction	-9	-15	-13	(13)	(13)	(13)	(13)	(13)
Change in fair value of interest rate swap agreements	0	0	60	-	-	-	-	-
Gain on sale of other assets	0	0	-1	-	-	-	-	-
Equity earnings in joint venture	-1	0	-2	(2)	(2)	(2)	(2)	(2)
Other	8	5	2	-	-	-	-	-
Other expense (income)	**(2)**	**(11)**	**46**	**(15)**	**(15)**	**(15)**	**(15)**	**(15)**
EBIT	**336**	**345**	**277**	**449**	**683**	**702**	**745**	**781**
Interest expense, net	81	88	99	132	196	211	226	241
Income before income taxes	**255**	**257**	**178**	**317**	**487**	**491**	**519**	**540**
Provision for income taxes (benefit)	21	17	-14	32	49	49	52	54
Net income	**234**	**240**	**192**	**285**	**439**	**442**	**467**	**486**
Adjustments	0	3	59	2	3	3	1	
Adjusted NI	**234**	**243**	**251**	**287**	**442**	**445**	**468**	**486**
EPS								
Diluted	**1.32**	**1.36**	**1.41**	**1.22**	**1.74**	**1.75**	**1.84**	**1.92**
Fully Diluted Share Count	178	178	178	235	254	254	254	254

Source: BofA Merrill Lynch Global Research estimates, company report

Bank of America Merrill Lynch

Balance Sheet

Table 19: Balance Sheet

Balance Sheet	2016	2017	2018	2019E	2020E	2021E	2022E	2023E
Assets								
Property, plant and equipment, at cost	6509	7004	7648	12,396	12,932	13,461	13,983	14,499
Less: accumulated depreciation	1508	1604	1718	1,910	2,239	2,595	2,977	3,387
Net property, plant and equipment	**5,002**	**5,400**	**5,930**	**9,103**	**9,638**	**10,168**	**10,690**	**11,206**
Current assets:								
Cash and cash equivalents	4	4	4	3	5	5	5	6
Accounts receivable and unbilled revenues, net	97	99	101	126	193	200	210	219
Inventory, materials and supplies	13	14	16	20	30	31	33	34
Prepayments and other current assets	13	13	23	23	23	23	23	23
Assets held for sale	2	2	3	3	3	3	3	3
Total current assets	**129**	**131**	**147**	**176**	**254**	**263**	**275**	**286**
Regulatory assets	949	714	788	788	788	788	788	788
Deferred charges and other assets, net	31	38	39	39	39	39	39	39
Investment in joint venture	7	7	7	7	7	7	7	7
Goodwill	42	42	53	1,628	1,628	1,628	1,628	1,628
Total assets	**6,159**	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**	**13,427**	**13,953**
Liabilities and Equity								
Aqua America stockholders' equity:								
Common stock at $.50 par value, authorized 300,000,000 shares, issued 181,151,827 and 180,700,251 in 2018 and 2017	90	90	91					
Capital in excess of par value	798	807	820					
Retained earnings	1033	1133	1174					
Treasury stock, at cost, 3,060,206 and 2,986,308 shares in 2018 and 2017	-71	-73	-76					
Accumulated other comprehensive income	1	1	0					
Total stockholders' equity	**1,850**	**1,958**	**2,009**	**4,706**	**4,913**	**5,108**	**5,293**	**5,473**
Long-term debt, excluding current portion	1760	2029	2419					
Less: debt issuance costs	22	22	21					
Long-term debt, excluding current portion, net of debt issuance costs	**1,738**	**2,008**	**2,398**	**4,330**	**4,664**	**4,980**	**5,300**	**5,619**
Current liabilities:								
Current portion of long-term debt	151	114	145	274	296	317	339	360
Loans payable	7	4	15	15	15	15	15	15
Accounts payable	47	59	77	96	147	153	161	168
Book overdraft	13	22	9	9	9	9	9	9
Accrued interest	18	21	23	23	23	23	23	23
Accrued taxes	26	24	22	22	22	22	22	22
Interest rate swap agreements	0	0	60	60	60	60	60	60
Other accrued liabilities	40	41	47	47	47	47	47	47
Total current liabilities	**302**	**284**	**399**	**547**	**620**	**647**	**676**	**705**
Deferred credits and other liabilities:								
Deferred income taxes and investment tax credits	1269	769	845	845	845	845	845	845
Customers' advances for construction	92	93	93	93	93	93	93	93
Regulatory liabilities	251	542	531	531	531	531	531	531
Other	116	107	97	97	97	97	97	97
Total deferred credits and other liabilities	**1,727**	**1,512**	**1,567**	**1,567**	**1,567**	**1,567**	**1,567**	**1,567**
Contributions in aid of construction	542	571	591	591	591	591	591	591
Total liabilities and equity	**6,159**	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**	**13,427**	**13,953**

Source: BofA Merrill Lynch Global Research estimates, company report

Cash Flow Statement

Table 20: Cash Flow Statement

Cash Flow Statement	2016	2017	2018	2019E	2020E	2021E	2022E	2023E
Cash flows from operating activities:								
Net income	234	240	192	287	442	445	468	486
Adjustments to reconcile net income to net cash flows from operating activities:								
Depreciation and amortization	133	137	147	191	330	356	382	409
Deferred income taxes	17	14	-15					
Provision for doubtful accounts	6	5	5					
Stock-based compensation	5	6	8					
Loss (gain) on sale of utility system and market-based business unit	-1	1	0					
Gain on sale of other assets	0	0	-1					
Interest rate swap agreements	0	0	60					
Net change in receivables, inventory and prepayments	-4	-6	-18	(10)	(26)	(3)	(4)	(4)
Net change in payables, accrued interest, accrued taxes and other accrued liabilities	5	-1	1					
Pension and other postretirement benefits contributions	-10	-16	-14					
Other	11	3	5					
Net cash flows from operating activities	**396**	**381**	**369**	**469**	**745**	**798**	**846**	**892**
Cash flows from investing activities:								
Property, plant and equipment additions	-383	-478	-496	(639)	(865)	(885)	(905)	(925)
Acquisitions of utility systems and other, net	-9	-6	-146					
Acquisitions				(4,300)				
Net proceeds from the sale of utility systems/other	8	1	1					
Other	1	2	1					
Net cash flows used in investing activities	**-383**	**-480**	**-640**	**-4,939**	**-865**	**-885**	**-905**	**-925**
Cash flows from financing activities:								
Customers' advances and contributions in aid of construction	7	7	7					
Repayments of customers' advances	-4	-7	-6					
Net proceeds (repayments) of short-term debt	-10	-3	12	129	22	21	21	21
Proceeds from long-term debt	504	591	1332	1,813	333	317	320	318
Proceeds from Amortizing Notes				119				
Repayments of long-term debt	-373	-359	-914					
Change in cash overdraft position	-8	9	-13					
Proceeds from issuing common stock	1	1	5	1,294				
Prepaid Stock Purchase Contracts	0	0	0	571				
Proceeds from stock Purchase agreement	0	0	0	750				
Proceeds from exercised stock options	4	3	1					
Share-based compensation windfall tax benefits	1	0	0					
Repurchase of common stock	-3	-2	-3					
Dividends paid on common stock	-131	-141	-151	(205)	(234)	(251)	(282)	(307)
Other	-1	-1	-1					
Net cash flows from (used in) financing activities	**-12**	**100**	**271**	**4,470**	**121**	**87**	**59**	**33**
Net (decrease) increase in cash and cash equivalents	1	0	-1	0	2	0	0	0
Cash and cash equivalents at beginning of year	3	4	4	4	3	5	5	5
Cash and cash equivalents at end of year	**4**	**4**	**4**	**3**	**5**	**5**	**5**	**6**

Source: BofA Merrill Lynch Global Research estimates, company report

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Price objective basis & risk

Aqua America (WTR)
Our price objective is $45 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 1.0x discount to Peoples Gas as we expect earned ROEs to be driven down over time.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Electric Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Aqua America	WTR	WTR US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	AES	AES	AES US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Pattern Energy Group	PEGI	PEGI US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Terraform Power	TERP	TERP US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

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iQmethod℠ Measures Definitions

Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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Equity Investment Rating Distribution: Utilities Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	61	44.20%	Buy	47	77.05%
Hold	42	30.43%	Hold	30	71.43%
Sell	35	25.36%	Sell	27	77.14%

Equity Investment Rating Distribution: Global Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1516	51.23%	Buy	942	62.14%
Hold	687	23.22%	Hold	431	62.74%
Sell	756	25.55%	Sell	380	50.26%

* Issuers that were investment banking clients of BofA Merrill Lynch or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Merrill Lynch Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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US Electric Utilities & IPPs

Power Points: ENBL lowers '19, WTR 2Q, AEE equity raise a bit more

Industry Overview

Bank of America Merrill Lynch

Equity | 07 August 2019

ENBL posts solid 2Q19 but points to low-end on '19

ENBL reported 2Q19 earnings of $124mn with adjusted EBITDA of $281mn, slightly ahead of expectations. The earnings contribution translates to ~$0.12/sh for CNP's 53.8% ownership and ~$0.12/sh for OGE's 25.5% ownership. Operationally, volumes continued to improve, principally at the natural gas business (90% of mix) with gathering (+4.3% YoY), processing (+9% YoY), and transportation (+14.4% YoY) all up and offsetting the decline in the oil biz. That said, ENBL mgmt. is now pointing to the low-end of guidance for 2019 net income of $435-$505mn as it doesn't expect hedging benefits that occurred in 4Q18 to follow through into 2H. We see this as cautionary for CNP in particular as concerns increase over midstream weakness given the recent decline in energy prices potentially impacting the company's 2019 and LT guidance. We reiterate our Buy rating on CNP, given confidence in mgmt's outlook and as we see a possible inflection on resolution of TX rate case settlement possible by mid-Sept. However, we look for affirmation of '19 guidance on the 2Q call. For OGE, we maintain our Neutral rating as we await potential indication of upside to capex with pending rate case nearly complete.

WTR: Expect Call to Focus on Pending Acquisition

WTR posted 2Q19 adjusted EPS of $0.37 compared to consensus at $0.36, with mgmt. reaffirming its 2019 guidance range of $1.45-$1.50 (excluding impacts related to the Peoples transaction). Management reiterated expectations for an organic rate base growth CAGR of 7% through '21(we still guide to 7.8% inclusive of acquisitions) and the closing of the Peoples transaction in the fall of 2019. The company also highlighted the recently received a letter of intent from the Delaware County Regional Water Control Authority (DELCORA) to exclusive discussions that could result in a combination with Aqua Pennsylvania Wastewater; if this occurs, we would view it as a nice potential tuck-in acquisition in a constructive jurisdiction where mgmt. could expand in the relatively niche wastewater sub-segment. Mgt is hosting a call at 11am ET, and we expect focus to largely center around the pending acquisition of Peoples and the potential to take advantage of the Repairs Tax benefit for the business; will mgmt. opt to spread this benefit thru its forecast period & how much of an initial jump will be realized? With shares valued off '21 & eventually '22 by 4Q, we stress spreading may become less relevant to valuation as longer-term ability to retain some amount of repairs benefits. We perceive upward bias to Street EPS expectations from Repairs Tax Benefit and further re-rating of shares as comfort emerges on the combined outlook; maintain Buy rating.

AEE: Prospectus for share issuance indicates slightly more

Ameren sold 7.549mn shares for $74.30/sh, indicating a total raise of $560.89mn; not all of the amount will be included in the resulting equity dilution for the company. Even so, this suggests more 2020 equity need than we include in our model to help finance the $1.2bn wind program; we model $350mn in '20. We still expect dilution in '20 even though the forward sale could be settled as late as March '21. We see clarity around the equity need as a positive for the company given some may have been anticipating the raise already. However, we reiterate it is offset by the slightly higher raise than some in the Street anticipated (we perceive up to ~$500 Mn had been in expectations). The equity raise also affirms to us mgmt. is unlikely to be more aggressive on its balance sheet; note the MO rate case is pending.

United States
Electric Utilities

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Refer to important disclosures on page 5 to 8. Analyst Certification on page 3. Price Objective Basis/Risk on page 2.

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Timestamp: 07 August 2019 06:58AM EDT

Stocks mentioned

BofAML Ticker	Ticker	Company name	Price	Rating
AEE	AEE US	Ameren Corp	US$ 75	A-2-7
WTR	WTR US	Aqua America	US$ 41.15	A-1-7
CNP	CNP US	CenterPoint Energy	US$ 28.86	B-1-7
OGE	OGE US	OGE Energy Corp	US$ 42.49	A-2-7

Source: BofA Merrill Lynch Global Research

Price objective basis & risk

Ameren Corporation (AEE)

Our $81 price objective is predicated on a P/E based sum of the parts, valuing each business subsidiary relative to the 2021E peer multiple of 19.1x. We apply a 1.0x premium to peers at AEE Missouri to account for the improving prospects of capital spend, supplemented by a regulatory jurisdiction becoming more favorable. We apply a 1.0x premium to peers at AEE Illinois to account for formulaic rates and decoupling on the distribution business which aids in earnings predictability. The overall business is expected to grow at a more meaningful clip than that of peers - we see a 9% rate base CAGR at IL nat gas through 2023 - and at ATXI, we apply a 1.5x premium to peers even when contemplating the latest potential step down in ROEs. At the Parent, we assume an in line multiple given the healthy debt metrics with FFO/Debt at 19%+. Electric peer P/E multiple is grossed up for a year to 2019 by 5% to reflect capital appreciation across the sector.

The upside (downside) risks to our price objective are the utilities earning their allowed returns or better (worse), a significant increase (decrease) in 30-year U.S. Treasury bond yields, and adverse regulatory outcomes that could affect mgmt's ability to earn its allowed return

Aqua America (WTR)

Our price objective is $45 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 1.0x discount to Peoples Gas as we expect earned ROEs to be driven down over time.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

CenterPoint Energy (CNP)

We value CenterPoint Energy at $31 using a SOTP approach: electric business on 1x premium to the utility multiple on 2021E P/E. We take out any earnings attributable to the transition bonds amortization, as those are temporary and instead add back the DCF value of future payments. For CNP's gas utilities we apply an in-line multiple to the utility gas peer multiple of 21.1x (from 21.2x). Both electric and gas peer P/E multiples are grossed up for a year to 2019 by 5% to reflect capital appreciation across the sector.We integrate Vectren intor our model and apply a 60/40% weighting to the gas/electric multiple. For VISCO/VESCO we apply a 12x P/E multiple, and an 11x P/E multiple for the announced synergies. We subtract parent interest expenses at a weighted average multiple.We value the Energy Services segment we rely on a 12x P/E. We add CNP's interest in ENBL at the market value. We take a 50/50 interest/debt approach, where we net out 50% of interest and 50% of HoldCo debt.

Downside risks: execution risk, decreases in capex which could support or weaken

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earnings ability, lower authorized returns, interest rate increases, and lower earnings from ENBL.

OGE Energy Corp (OGE)

We value OGE at $45 based on a sum of the parts, separating the utility business from the Enable stake.

For the utility business we apply the peer multiple of 19.2x on 2021E EPS and a 0.5x premium given the improving regulatory environment in OK. Electric peer P/E multiple is grossed up for a year to 2019 by 5% to reflect capital appreciation across the sector.

For the Enable Midstream Partners, LP stake we rely on the current market price of ENBL multiplied by the number of the shares owned by OGE to determine the equity value. We attribute no value to the GP shares, as we don't anticipate IDRs materializing over the next three years.

Downside risks are further declines in the regulatory environment possibly resulting in lower ROEs or other hurdles hindering OGE's ability to earn its authorized return. While not as exposed due to low parent interest, we see interest rate hikes as another potential downside risk. Finally, execution risk on existing capex schedule could put further pressure on earnings growth. Declines in value of ENBL share could also provide downside to our valuation.

Upside risks are shifts towards a more favorable Oklahoma regulatory environment, which could ease OGEs ability to earn its authorized return in the jurisdiction and possibly increase capex plan as management views prospects in the state more positively. Improvements in value of ENBL share could also provide upside to our valuation.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Electric Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Aqua America	WTR	WTR US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	AES	AES	AES US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Pattern Energy Group	PEGI	PEGI US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Terraform Power	TERP	TERP US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

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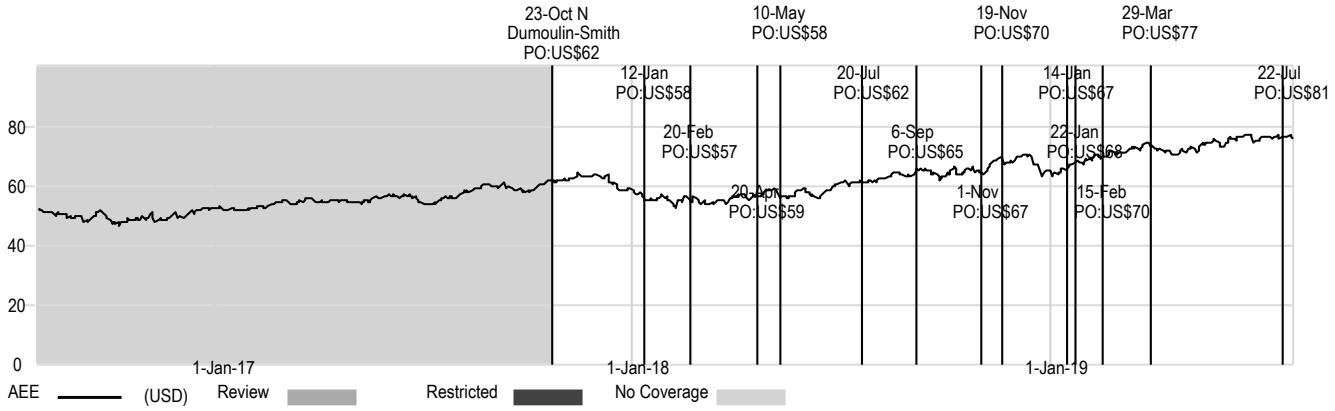
Disclosures

Important Disclosures

AEE Price Chart



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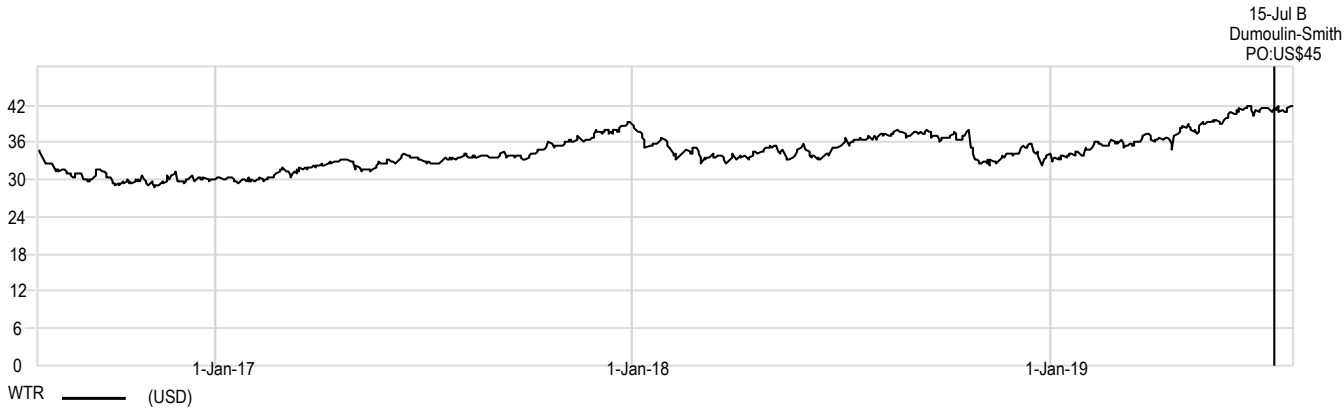
WTR Price Chart



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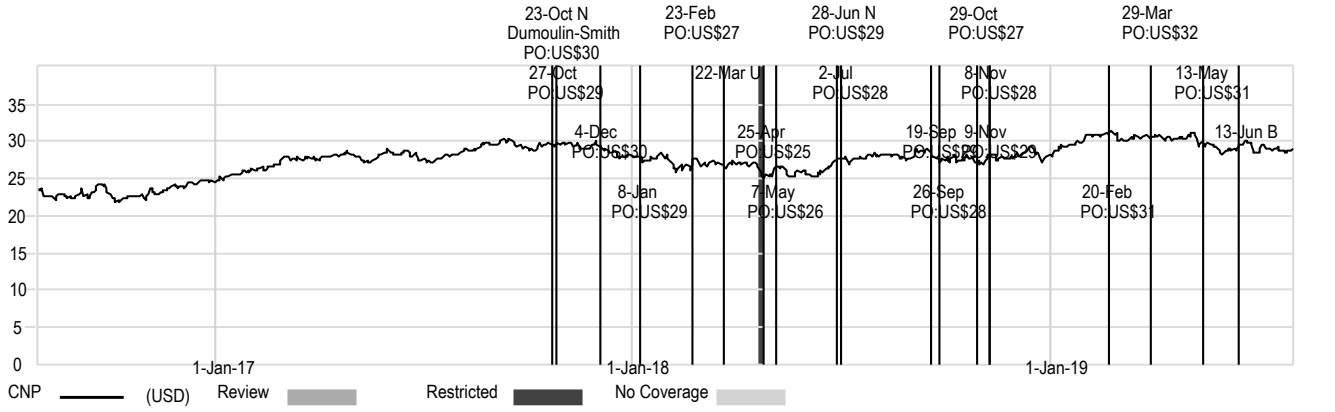
CNP Price Chart



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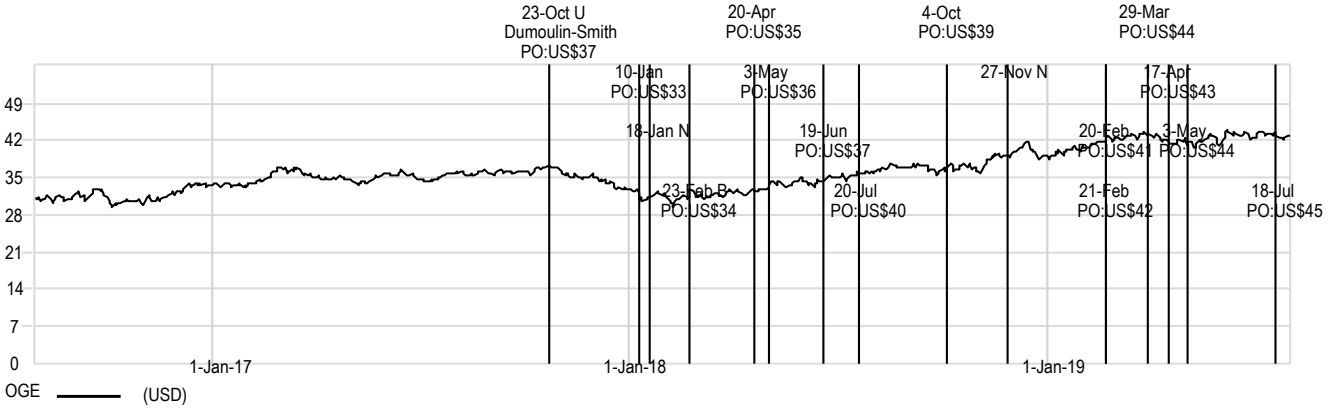
OGE Price Chart



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Equity Investment Rating Distribution: Utilities Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	61	44.20%	Buy	47	77.05%
Hold	42	30.43%	Hold	30	71.43%
Sell	35	25.36%	Sell	27	77.14%

Equity Investment Rating Distribution: Global Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1516	51.23%	Buy	942	62.14%
Hold	687	23.22%	Hold	431	62.74%
Sell	756	25.55%	Sell	380	50.26%

* Issuers that were investment banking clients of BofA Merrill Lynch or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Merrill Lynch Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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Aqua America

Pool Party continues but waiting on the Gas

Maintain Rating: BUY | PO: 45.00 USD | Price: 42.06 USD

Bank of America Merrill Lynch

Equity | 08 August 2019

Executing on Legacy Water Biz and Tuck-Ins

WTR's latest update shows further execution on the core water business and continued focus on tuck in acquisitions. Following Ohio's adoption of FMV legislation in January, the company announced a purchase agreement earlier this month to acquire a small utility in Campbell (3.2K customers) to drive the latest addition to the $100Mn in expected rate base from signed muni acquisitions. Outside of the Peoples acquisition, we expect water tucks ins to continue driving incremental growth. The Fair Market Value legislation has been passed in 7 of the 8 states the company operates in (following TX in June). Thus, we could see mgmt start to pursue a wider geographic footprint as additional states become more appealing; mgmt highlighted a path to 30K customers as critical. More materially, we highlight DELCORA's recent announcement of intent to commit to exclusive discussions with WTR for a potential acquisition. While purchase price (& thus rate base opportunity) are yet to be negotiated, FMV legislation potentially could facilitate a step up from the ~$240Mn depreciated asset base. If such a scenario materializes, it could be a meaningful driver, albeit it may come with some kind of equity issuance.

Peoples Acquisition Remains on Track: October Order?

Following earlier approvals from the KY and WV PSCs for the Peoples acquisition, the company continues to await final approval from PA after filing a non-unanimous settlement. Latest commentary from management highlighted expectations for an October order from the commission with the transaction to close shortly after. Following the close of the transaction, we would expect more guidance around any upside at the Analyst Day tentatively set for December 5th.

Valuation: Repairs Tax Upside Remains Key

With the latest developments, our estimates are unchanged. We remain above the street as we still credit the company with execution of the repairs tax benefit. Our PO ultimately remains unchanged at $45. Maintain Buy given what we perceive as meaningful upside to estimates from Repairs Tax Benefit and further potential re-rating of shares as comfort emerges on the combined outlook.

Estimates (Dec)

(US$)	2017A	2018A	2019E	2020E	2021E
EPS	1.36	1.41	1.30	1.74	1.75
GAAP EPS	1.36	1.41	1.30	1.74	1.75
EPS Change (YoY)	3.0%	3.7%	-7.8%	33.8%	0.6%
Consensus EPS (Bloomberg)			1.36	1.57	1.66
DPS	0.81	0.86	0.92	0.99	1.06

Valuation (Dec)

	2017A	2018A	2019E	2020E	2021E
P/E	30.9x	29.8x	32.4x	24.2x	24.0x
GAAP P/E	30.9x	29.8x	32.4x	24.2x	24.0x
Dividend Yield	1.9%	2.0%	2.2%	2.3%	2.5%
EV / EBITDA*	1.1x	8.1x	26.5x	16.6x	15.8x
Free Cash Flow Yield*	-1.1%	-1.4%	-1.9%	-1.3%	-1.0%

* For full definitions of *iQmethod*℠ measures, see page 8.

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Stock Data

Price	42.06 USD
Price Objective	45.00 USD
Date Established	15-Jul-2019
Investment Opinion	A-1-7
52-Week Range	32.09 USD - 42.32 USD
Mrkt Val (mn) / Shares Out (mn)	9,074 USD / 215.7
Average Daily Value (mn)	43.86 USD
BofAML Ticker / Exchange	WTR / NAS
Bloomberg / Reuters	WTR US / WTR.N
ROE (2019E)	7.5%
Net Dbt to Eqty (Dec-2018A)	127.1%

DELCORA: Delaware County Regional Water Control Authority

PSC: Public Service Commission

FMV: Fair Market Value

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Timestamp: 08 August 2019 09:32AM EDT

iQprofile℠ Aqua America

iQmethod℠ – Bus Performance*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Return on Capital Employed	5.1%	3.9%	4.4%	5.2%	5.1%
Return on Equity	12.6%	9.7%	7.5%	8.6%	8.3%
Operating Margin	41.5%	38.7%	48.1%	70.2%	71.1%
Free Cash Flow	(97)	(127)	(170)	(120)	(87)

iQmethod℠ – Quality of Earnings*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash Realization Ratio	1.6x	1.9x	1.9x	1.8x	1.9x
Asset Replacement Ratio	3.5x	3.4x	3.3x	2.6x	2.5x
Tax Rate	6.6%	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	108.3%	127.1%	97.0%	100.1%	102.8%
Interest Cover	3.9x	2.8x	3.4x	3.5x	3.3x

Income Statement Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Sales	805	835	902	949	966
% Change	0.6%	3.7%	8.0%	5.3%	1.7%
Gross Profit	810	838	1,044	1,596	1,657
% Change	-1.3%	3.5%	24.6%	52.9%	3.8%
EBITDA	14,226	1,941	597	953	998
% Change	-33.6%	-86.4%	-69.2%	59.6%	4.8%
Net Interest & Other Income	(88)	(99)	(132)	(194)	(210)
Net Income (Adjusted)	**240**	**192**	**251**	**414**	**416**
% Change	**2.4%**	**-19.9%**	**31.0%**	**64.5%**	**0.6%**

Free Cash Flow Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Net Income from Cont Operations (GAAP)	240	192	287	442	446
Depreciation & Amortization	137	147	191	330	356
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	14	(15)	0	0	0
Other Adjustments, Net	(9)	45	(10)	(26)	(3)
Capital Expenditure	(478)	(496)	(639)	(865)	(885)
Free Cash Flow	**-97**	**-127**	**-170**	**-120**	**-87**
% Change	**NM**	**-31.5%**	**-33.9%**	**29.8%**	**27.7%**

Balance Sheet Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash & Equivalents	4	4	3	5	5
Trade Receivables	99	101	126	193	200
Other Current Assets	28	42	46	57	58
Property, Plant & Equipment	5,400	5,930	9,103	9,638	10,168
Other Non-Current Assets	801	887	2,462	2,462	2,462
Total Assets	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**
Short-Term Debt	117	160	288	310	331
Other Current Liabilities	167	239	258	309	315
Long-Term Debt	2,008	2,398	4,305	4,638	4,955
Other Non-Current Liabilities	2,083	2,158	2,158	2,158	2,158
Total Liabilities	**4,375**	**4,955**	**7,008**	**7,415**	**7,758**
Total Equity	**1,958**	**2,009**	**4,733**	**4,940**	**5,135**
Total Equity & Liabilities	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**

* For full definitions of *iQmethod℠* measures, see page 8.

Company Sector

Water Utilities

Company Description

Aqua America is a regulated water utility providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI. In Oct 2018, The company announced acquisition of Peoples Gas, a gas utility providing distribution services to 740,000 customers in PA, WV, and KY. The acquisition is expected to be closed by mid- 2019.

Investment Rationale

We see our Buy rating as supported by meaningfully above Street EPS projections on the back of its pending Peoples Gas business and above average ratebase growth.

Stock Data

Average Daily Volume	1,042,678

Quarterly Earnings Estimates

	2018	2019
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NA

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Capitalizing on Fair Market Value Legislation

During 2Q, Texas became WTR's seventh state to adopt Fair Market Value Legislation when they adopted the legislation in June after Ohio adopted the legislation earlier in the year. Just this month, the company entered a purchase agreement to acquire the water system in Campbell, OH (3,200 customer connections), bringing the total signed purchase agreements for municipalities to 22.6K customers in 2019 and 2020. With WTR the only regulated water utility on size after acquiring operations from AWK, we could see more development in this state in particular following the latest move. Overall, management has noted ~$100Mn in rate base acquisition activity signed set to generate ~$5Mn of incremental earnings. While some of the transactions will close in 2020, the company remains on track to grow customers between 2-3% in 2019.

More materially than the typical tuck-ins, the board of directors of Delaware County Regional Water Control Authority (DELCORA) announced a letter of intent in July committing to exclusive discussions with Aqua Pennsylvania Wastewater that could result in a combination with DELCORA, who currently serves 500K people in 42 municipalities across Delaware and PA. While a sizable opportunity, management noted it would look to put an ATM program in place to raise some add'l equity, partially offsetting potential upside. Aside from a major acquisition, the company doesn't expect any other additional near term equity needs.

On the call, management noted a willingness to expand its footprint to additional states as Fair Market Value legislation gains momentum. We believe All expansion to additional states is increasingly likely following the successful push for passage of the legislation in 7 of the 8 states they operate in.

Peoples Acquisition: Still Guiding to Fall Close

The company received regulatory approval for the Peoples transaction from the Kentucky Public Service Commission in March and the West Virginia Public Service Commission in April after reaching unanimous settlements in the states. Following the approvals in those jurisdictions, the company filed a PA settlement agreement in June that is currently pending before the PA PUC (all but 2 intervenors to the case have entered into or chosen not to oppose the settlement agreement). With the settlement currently under review by the commission given the non-unanimous nature, the company continues to guide to a Fall decision. Specifically, management noted on the call that they expect an order from the commission on October 24th, with the transaction closing shortly after. That said, there is no statutory timeline for the commission to rule on the decision in the state.

EPS Estimates

The exhibit below reflects our EPS estimates which are largely unchanged as we await further developments on the pending acquisition. We remain above the street on '21, driven primarily from an expectation of stronger earnings at Peoples Gas. Earned ROE degradation at PA (assumed to be a gradual process) drives the relatively flat outlook for the core water utilities through the near term. *We appreciate there is substantial latitude in framing the '20 EPS & beyond based on the outlook of this acquisition around repairs tax. We emphasize the shape & form of deal approval remain critical to earnings trajectory, particularly given some mgmt commentary on smoothing its outlook. We stress some scenarios could result in EPS higher than Street consensus still though.*

Table 1: WTR SOTP

EPS Estimates	2019E	2020E	2021E	2022E	2023E
PA	$0.84	$0.80	$0.77	$0.82	$0.86
OH	$0.07	$0.07	$0.07	$0.08	$0.08
IL	$0.08	$0.07	$0.08	$0.08	$0.09
TX	$0.07	$0.06	$0.06	$0.06	$0.06
NC	$0.04	$0.04	$0.04	$0.04	$0.05
Other States	$0.08	$0.08	$0.09	$0.09	$0.10
Water Utility	**1.18**	**1.12**	**1.11**	**1.17**	**1.24**
Peoples Gas	**0.17**	**0.70**	**0.75**	**0.79**	**0.82**
Parent & Other	*-0.05*	*-0.08*	*-0.10*	*-0.12*	*-0.14*
EPS	**1.30**	**1.74**	**1.75**	**1.84**	**1.92**
YoY Growth		*34%*	*1%*	*5%*	*4%*
Shares O/S	*193*	*238*	*238*	*250*	*254*
Fully Diluted Shares O/S	*221*	*254*	*254*	*254*	*254*
Previous EPS	***$1.22***	***$1.74***	***$1.75***	***$1.84***	
Consensus	**1.36**	**1.57**	**1.66**		

Source: BofA Merrill Lynch Global Research, Bloomberg

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Valuation

On our unchanged estimates, our PO remains $45. We continue to apply a 1x discount to Peoples Gas to reflect related removal of any sector takeout premium as well as discounting the strong returns we ascribe to it in the near term.

Table 2: WTR SOTP

Water Utilities	2021 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*26.2x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		**28.4x**							
Water Utilities									
States	**2021E EPS**	**ROE**	**embedded**						
PA	$0.77	10.0%	**0.0x**	27.4x	28.4x	29.4x	$21	$22	$23
OH	$0.07	9.9%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$2
IL	$0.08	9.6%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$2
TX	$0.06	10.0%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$2
NC	$0.04	9.9%	**0.0x**	27.4x	28.4x	29.4x	$1	$1	$1
Other (including acquisitions)	$0.09	9.9%	**0.0x**	27.4x	28.4x	29.4x	$2	$2	$3
Water utilities total (ex-Peoples)	**$1.11**			*27.4x*	*28.4x*	*29.4x*	**$30**	**$31**	**$33**
Gas Utilities									
Peer Gas P/E		*21.2x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		**22.4x**							
	2021E EPS	**ROE**	**embedded**						
Peoples Gas	**$0.75**	14.1%	**-1.0x**	**20.4x**	**21.4x**	**22.4x**	**$15**	**$16**	**$17**
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			**-727**	50%			($363)	($363)	($363)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($351)	($325)	($379)
50/50 Weighted Drag from HoldCo Drag							($715)	($688)	($743)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							**$43.00**	**$45.00**	**$46.00**
Current Price								$42.06	
Dividend Yield								2%	
Total Return								**9.18%**	

Source: BofA Merrill Lynch Global Research, Bloomberg

Price objective basis & risk

Aqua America (WTR)
Our price objective is $45 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 1.0x discount to Peoples Gas as we expect earned ROEs to be driven down over time.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Specifically, we derive a value of $31 or the Water Business and $16 per share for the Gas utilities. We then deduct $688M which accounts for $2 per share, and gives us our PO of $45.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

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US - Electric Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Aqua America	WTR	WTR US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
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	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	AES	AES	AES US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Pattern Energy Group	PEGI	PEGI US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Terraform Power	TERP	TERP US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

iQmethod℠ Measures Definitions

Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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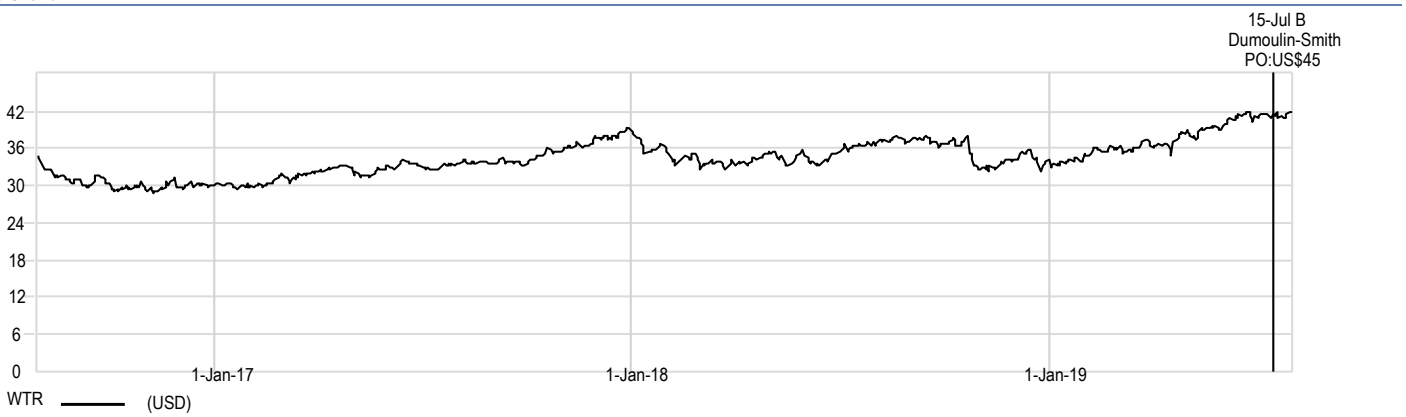
WTR Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Utilities Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	61	44.20%	Buy	47	77.05%
Hold	42	30.43%	Hold	30	71.43%
Sell	35	25.36%	Sell	27	77.14%

Equity Investment Rating Distribution: Global Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1516	51.23%	Buy	942	62.14%
Hold	687	23.22%	Hold	431	62.74%
Sell	756	25.55%	Sell	380	50.26%

* Issuers that were investment banking clients of BofA Merrill Lynch or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Merrill Lynch Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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Aqua America

Snorkeling in the Deep End: A Closer Look at the Repairs Tax Benefit

Reiterate Rating: BUY | PO: 45.00 USD | Price: 44.18 USD

Bank of America Merrill Lynch

Equity | 21 August 2019

Repairs Tax Remains Focal Point...but What Will Qualify?

As WTR continues to progress through the approval process for the pending Peoples acquisition, we provide our latest model with slight tweaks to our estimates ahead of a potential order (Management has guided towards an Oct 24th ruling but note there is no statutory timeline for an order in the state). While latest discussions with the company suggest that they continue to work through a potential settlement, we see likelihood of one materializing as limited. That said, pending what we still perceive as a likely close during 4Q, the company plans to host an Analyst Day the first week of December that should provide a broad update for the combined company. We would expect a consolidated EPS range for 2020 and some longer term growth guidance to be provided, as well as potential clarity around sizing the repairs tax benefit opportunity for the gas business. The previously employed strategy consists of two components – a current portion based on qualified capex which can be elected (with the benefit flowing through in the income statement immediately) and a catch up adjustment component to reflect prior investments that are currently capitalized and depreciated for tax purposes. While the company has clearly articulated plans to elect the *current* component, the *catch up* component remains somewhat more of a wildcard given the requirement of a commission order and potential nuances around how it could be treated. In the past, the company was able to amortize the catch-up deduction for the PA water business over a 10-year period of time to provide additional tax relief. That said, we perceive the commission is more likely to give at least some benefit back to customers if enacted now. Nonetheless, we don't see the catch up component as necessary for our base case scenario, particularly given the likelihood of a ramp in capital investments going forward. While quantifying qualified capex remains somewhat more challenging, we continue to suspect robust ability to earn in PA, which makes up around 90% of the gas business.

Valuation: Shifting +$1/sh to $46/sh on higher multiple

We shift our '20-22 estimates 1% lower as we assume more conservative ROEs for Peoples Gas. That said, we remain 3% above the Street on '21 given what we still perceive as a robust earnings profile likely to materialize as the company moves to elect the current component post transaction close. On our new estimates and after reflecting the latest mark to market of peer multiples, our price objective shifts up $1 to $46.

Estimates (Dec)

(US$)	2017A	2018A	2019E	2020E	2021E
EPS	1.36	1.41	1.30	1.74	1.75
GAAP EPS	1.36	1.41	1.30	1.74	1.75
EPS Change (YoY)	3.0%	3.7%	-7.8%	33.8%	0.6%
Consensus EPS (Bloomberg)			1.39	1.58	1.67
DPS	0.81	0.86	0.92	0.99	1.06

Valuation (Dec)

	2017A	2018A	2019E	2020E	2021E
P/E	32.5x	31.3x	34.0x	25.4x	25.2x
GAAP P/E	32.5x	31.3x	34.0x	25.4x	25.2x
Dividend Yield	1.8%	2.0%	2.1%	2.2%	2.4%
EV / EBITDA*	1.1x	8.4x	27.3x	17.1x	16.3x
Free Cash Flow Yield*	-1.0%	-1.3%	-1.8%	-1.3%	-0.9%

* For full definitions of *iQmethod℠* measures, see page 7.

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Stock Data

Price	44.18 USD
Price Objective	45.00 USD
Date Established	15-Jul-2019
Investment Opinion	A-1-7
52-Week Range	32.09 USD - 44.60 USD
Mrkt Val (mn) / Shares Out (mn)	9,531 USD / 215.7
Average Daily Value (mn)	51.25 USD
BofAML Ticker / Exchange	WTR / NAS
Bloomberg / Reuters	WTR US / WTR.N
ROE (2019E)	7.5%
Net Dbt to Eqty (Dec-2018A)	127.1%

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Refer to important disclosures on page 8 to 10. Analyst Certification on page 5. Price Objective Basis/Risk on page 5.

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Timestamp: 21 August 2019 08:49AM EDT

iQprofile℠ Aqua America

iQmethod℠ – Bus Performance*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Return on Capital Employed	5.1%	3.9%	4.4%	5.2%	5.1%
Return on Equity	12.6%	9.7%	7.5%	8.6%	8.3%
Operating Margin	41.5%	38.7%	48.1%	70.2%	71.1%
Free Cash Flow	(97)	(127)	(170)	(120)	(87)

iQmethod℠ – Quality of Earnings*

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash Realization Ratio	1.6x	1.9x	1.9x	1.8x	1.9x
Asset Replacement Ratio	3.5x	3.4x	3.3x	2.6x	2.5x
Tax Rate	6.6%	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	108.3%	127.1%	97.0%	100.1%	102.8%
Interest Cover	3.9x	2.8x	3.4x	3.5x	3.3x

Income Statement Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Sales	805	835	902	949	966
% Change	0.6%	3.7%	8.0%	5.3%	1.7%
Gross Profit	810	838	1,044	1,596	1,657
% Change	-1.3%	3.5%	24.6%	52.9%	3.8%
EBITDA	14,226	1,941	597	953	998
% Change	-33.6%	-86.4%	-69.2%	59.6%	4.8%
Net Interest & Other Income	(88)	(99)	(132)	(194)	(210)
Net Income (Adjusted)	**240**	**192**	**251**	**414**	**416**
% Change	**2.4%**	**-19.9%**	**31.0%**	**64.5%**	**0.6%**

Free Cash Flow Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Net Income from Cont Operations (GAAP)	240	192	287	442	446
Depreciation & Amortization	137	147	191	330	356
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	14	(15)	0	0	0
Other Adjustments, Net	(9)	45	(10)	(26)	(3)
Capital Expenditure	(478)	(496)	(639)	(865)	(885)
Free Cash Flow	**-97**	**-127**	**-170**	**-120**	**-87**
% Change	**NM**	**-31.5%**	**-33.9%**	**29.8%**	**27.7%**

Balance Sheet Data (Dec)

(US$ Millions)	2017A	2018A	2019E	2020E	2021E
Cash & Equivalents	4	4	3	5	5
Trade Receivables	99	101	126	193	200
Other Current Assets	28	42	46	57	58
Property, Plant & Equipment	5,400	5,930	9,103	9,638	10,168
Other Non-Current Assets	801	887	2,462	2,462	2,462
Total Assets	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**
Short-Term Debt	117	160	288	310	331
Other Current Liabilities	167	239	258	309	315
Long-Term Debt	2,008	2,398	4,305	4,638	4,955
Other Non-Current Liabilities	2,083	2,158	2,158	2,158	2,158
Total Liabilities	**4,375**	**4,955**	**7,008**	**7,415**	**7,758**
Total Equity	**1,958**	**2,009**	**4,733**	**4,940**	**5,135**
Total Equity & Liabilities	**6,332**	**6,964**	**11,741**	**12,355**	**12,893**

* For full definitions of *iQmethod℠* measures, see page 7.

Company Sector

Water Utilities

Company Description

Aqua America is a regulated water utility providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI. In Oct 2018, The company announced acquisition of Peoples Gas, a gas utility providing distribution services to 740,000 customers in PA, WV, and KY. The acquisition is expected to be closed by mid- 2019.

Investment Rationale

We see our Buy rating as supported by meaningfully above Street EPS projections on the back of its pending Peoples Gas business and above average ratebase growth.

Stock Data

Average Daily Volume	1,159,263

Quarterly Earnings Estimates

	2018	2019
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NA

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Smoothing Out the Impact: What Would it Look Like

With the election of the repairs tax benefit the company plans to pursue for 2020, earnings will see a large step up as the company expenses capital costs as opposed to depreciating them over a useful life for tax purposes. The magnitude of the initial increase will ultimately be determined by how much of the capital investment program qualifies for the treatment and whether the commission allows the company to use a catch up component for costs that are currently being depreciated. Our sense is that capital investments back to 2012 could potentially be privy to such treatment – albeit investment was likely more muted relative to the current capital plans – and we don't see management relying on such election. We perceive the commission is more inclined to give at least partial benefit of any catch up component back to customers. If management is able to reach an acquisition settlement – which we don't see as likely given the current timeline – that could include a balancing account to help drive more stable earnings growth in a similar mechanism that has been employed by NEE for storms. Alternatively, the company could look to manage capex in a way that accelerates qualified expenses y/y. We see the level of overall eligibility as the more critical question into the transaction's close and the potential Analyst Day later this year.

EPS Estimates

The exhibit below reflects our latest EPS estimates. Our '20-22 estimates shift -1% lower as we assume more conservative ROEs for the Peoples Gas business (albeit still close to 14%). We remain 3% above the street for '21 given what we still perceive as a strong earnings potential from the election of the Repairs Tax Benefit, regardless of the company's ability to capture any benefit from the catch up adjustment. Despite any additional efforts by the company to smooth the impact from the benefit, we perceive a continued upward bias to street estimates.

Table 1: EPS Estimates

EPS Estimates	2019E	2020E	2021E	2022E	2023E
PA	$0.84	$0.80	$0.77	$0.82	$0.86
OH	$0.07	$0.07	$0.07	$0.08	$0.08
IL	$0.08	$0.07	$0.08	$0.08	$0.09
TX	$0.07	$0.06	$0.06	$0.06	$0.06
NC	$0.04	$0.04	$0.04	$0.04	$0.05
Other States	$0.08	$0.08	$0.09	$0.09	$0.10
Water Utility	**1.18**	**1.12**	**1.11**	**1.17**	**1.24**
Peoples Gas	**0.17**	**0.68**	**0.72**	**0.77**	**0.81**
Parent & Other	*-0.05*	*-0.08*	*-0.10*	*-0.12*	*-0.14*
EPS	**1.30**	**1.72**	**1.73**	**1.82**	**1.90**
YoY Growth		*32%*	*1%*	*5%*	*5%*
Shares O/S	*193*	*238*	*238*	*250*	*254*
Fully Diluted Shares O/S	*221*	*254*	*254*	*254*	*254*
Previous EPS	*$1.30*	*$1.74*	*$1.75*	*$1.84*	
Consensus	**1.39**	**1.58**	**1.67**		
Consensus '19-'21 CAGR					
BofAML CAGR 2019-2021					
DPS	**0.92**	**0.99**	**1.06**	**1.13**	**1.21**
Payout Ratio	*71%*	*57%*	*61%*	*62%*	*64%*
Share Count	**193**	**238**	**238**	**250**	**254**

Source: BofA Merrill Lynch Global Research, Bloomberg

Valuation: PO Shifts to $46

The exhibit below reflects our latest SOTP on our new estimates and after marking to market for the latest peer multiples (27.9x vs. 26.2x and 20.7x vs. 21.2x for water and gas, respectively). We continue to apply a 1x discount to Peoples Gas to reflect removal of any sector takeout premium as well as discounting the strong returns we ascribe to it in the near term. Our lower gas contribution and multiple was more than offset by the sharp increase in peer water multiples. Overall, our water valuation shifts up $3, while lower gas contribution and higher corporate drag are a $2 headwind relative to our prior valuation. Net net, our PO ultimately shifts up $1 to $46.

Table 2: WTR SOTP

Water Utilities	2021 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*27.9x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		**30.2x**							
Water Utilities									
States	**2021E EPS**	**ROE**	**embedded**						
PA	$0.77	10.0%	**0.0x**	29.2x	30.2x	31.2x	$23	$23	$24
OH	$0.07	9.9%	**0.0x**	29.2x	30.2x	31.2x	$2	$2	$2
IL	$0.08	9.6%	**0.0x**	29.2x	30.2x	31.2x	$2	$2	$2
TX	$0.06	10.0%	**0.0x**	29.2x	30.2x	31.2x	$2	$2	$2
NC	$0.04	9.9%	**0.0x**	29.2x	30.2x	31.2x	$1	$1	$1
Other (including acquisitions)	$0.09	9.9%	**0.0x**	29.2x	30.2x	31.2x	$3	$3	$3
Water utilities total (ex-Peoples)	**$1.11**			*29.2x*	*30.2x*	*31.2x*	**$32**	**$34**	**$35**
Gas Utilities									
Peer Gas P/E		*20.7x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		**21.9x**							
	2021E EPS	**ROE**	**embedded**						
Peoples Gas	**$0.72**	13.7%	**-1.0x**	**19.9x**	**20.9x**	**21.9x**	**$14**	**$15**	**$16**
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			**-738**	50%			($369)	($369)	($369)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($370)	($342)	($399)
50/50 Weighted Drag from HoldCo Drag							($739)	($710)	($767)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							**$44.00**	**$46.00**	**$47.00**
Current Price								$44.42	
Dividend Yield								2%	

Source: BofA Merrill Lynch Global Research, Bloomberg

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Price objective basis & risk

Aqua America (WTR)
Our price objective is $46 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 1.0x discount to Peoples Gas as we expect earned ROEs to be driven down over time.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Specifically, we derive a value of $34 or the Water Business and $15 per share for the Gas utilities. We then deduct around $3 per share related to corp drag, which gives us our PO of $46.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Electric Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Aqua America	WTR	WTR US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	AES	AES	AES US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Pattern Energy Group	PEGI	PEGI US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Terraform Power	TERP	TERP US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

US - Electric Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Merrill Lynch ticker	Bloomberg symbol	Analyst

iQmethod℠ **Measures Definitions**

Business Performance	**Numerator**	**Denominator**
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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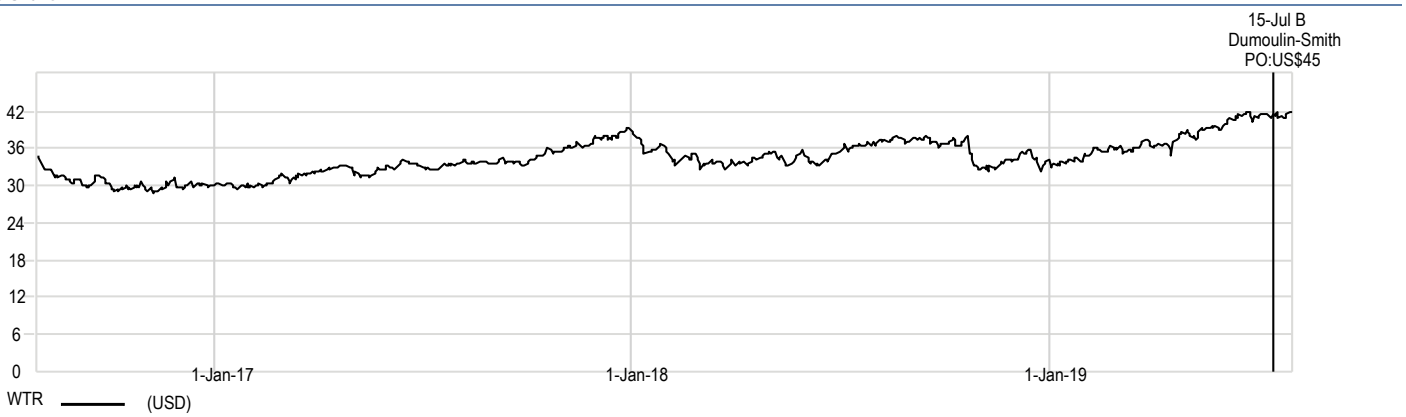
Disclosures

Important Disclosures

WTR Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of July 31, 2019 or such later date as indicated.

Equity Investment Rating Distribution: Utilities Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	61	44.20%	Buy	47	77.05%
Hold	42	30.43%	Hold	30	71.43%
Sell	35	25.36%	Sell	27	77.14%

Equity Investment Rating Distribution: Global Group (as of 30 Jun 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1516	51.23%	Buy	942	62.14%
Hold	687	23.22%	Hold	431	62.74%
Sell	756	25.55%	Sell	380	50.26%

* Issuers that were investment banking clients of BofA Merrill Lynch or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Merrill Lynch Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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North American Utilities & IPPs

Water on Wall Street: Takeaways from Our Inaugural Conference

Industry Overview

Splashing into the Water Industry

On Thursday, we hosted our Inaugural Water on Wall Street Conference in New York City with AQUA, AWK, AWR, CWT, HASI, MSEX, SJW, WTR, and YORW as well as a number of state regulators and industry experts. There were a variety of panels throughout the day with updates from company mgmt. and latest thoughts on trends and the state of the water industry. Key themes included what to make of emerging contaminates and expectations for further consolidation across the water industry against a backdrop of accelerating legislation momentum and stressed municipalities. Open the note for full takeaways.

Legislation, Infra Pressures to Drive Consolidation

Across the panels, speakers continuously emphasized the incredibly fragmented nature of the water industry. There are over 50K community water systems in the US, ~85% of which are publicly owned. This translates to a modest share for IOUs, particularly when contrasted with electric and gas (~3,000 electric utilities, the majority of which are structured as IOUs) and we increasingly view a clear cut opportunity for continued consolidation across the space. Given limited governmental funds and rising pension liabilities, we perceive a growing struggle around muni's abilities to inject the investments needed to maintain the water systems (with at least 1,200 systems deemed to be non-compliant with regards to the safe water act). Enabling legislation continues to pick up across states with FMV (FL likely to introduce next) & Single Tariff legislation gaining momentum and the Water Accountability Act starting to emerge (with IN following NJ's lead). We see this as creating a perfect backdrop to enable acquisitions - albeit not all of these states are created equal - with capital likely to flow to the most constructive jurisdictions. Meanwhile, discussions highlighted more limited participation from private equity players with underexposure to the space and a slower momentum around P3s in the US relative to other countries. Bottom line, we continue to expect an acceleration of tuck in acquisitions for the IOUs. One critical question is whether a constructive outcome with JEA in FL will drive more large acquisitions going forward.

Contemplating Emerging Contaminants

Another key focal point all day at the conference was around emerging contaminants and how they are changing the industry. Relative to the more publicized fire risks facing electric utilities, contamination is a critical – and likely still underappreciated - risk for the water industry. The EPA has currently established health advisory levels for PFAs at 70 parts per trillion, and concerns were voiced around how commissions will treat investment without a more clear cut standard. A handful of states have already started setting their own levels of stricter standards, and we perceive it as a likely driver of capital investment as awareness continues to be raised. While costs to treat will vary widely depending on technology and what contaminants are in the water, we perceive it as around $0.02-$0.10 per thousand gallons (note that AWK processes 1 billion gallons of drinking water daily). Bottom line, we would expect this to increasingly be a capital investment consideration and a potential driver for consolidation longer term as a more standard set of guidelines are adopted and municipalities are forced to comply.

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NYAW: New York American Water

JEA: Jacksonville Electric Authority

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How do we think about the sector?

Growth remains consistently robust and the merits of a premium to the electric and gas peers remains clear. We perceive the latest re-rating higher as preventing consolidation more broadly, but could very see a return to consolidation should sector valuations normalize closer to historic norms (on corporate side). That said, municipal deals will continue, albeit always on a protracted basis given the local approvals typically required. We perceive the sector as among the single highest quality within our coverage universe albeit with valuations (earnings yields) approaching that of the cost of debt, it's hard to see how re-rating improves barring significant shifts in interest rates lower. We maintain our Buy rating on WTR and Underperform on AWK.

So what do we recommend?

Despite the latest underperformance this week, we continue to stress the premium valuations ascribed to the water sector broadly, with the group still trading at 25.6x 2022 estimates (vs. electric and gas peers both trading at 18.5x). While we appreciate the scarcity element and visibility into longer term growth, we see risk as underappreciated at these levels – despite growing attention to contamination. We remain Underperform rated on shares of AWK, with estimates coming down out of their latest Analyst Day, and our concerns for convergence of sector multiples. Meanwhile we highlight our Buy rating on shares of WTR given their discrete opportunities into the expected closing of the Peoples Gas transaction; we perceive an upward bias to estimates upon implementation of the Repairs tax.

Water Universe

Table 1: Water Universe

						P/E Multiples					Earnings per Share					
	Ticker	Market Cap	EV	Short Int	Days	2018A	2019E	2020E	2021E	2022E	2018A	2019E	2020E	2021E	2022E	CAGR
Water Utilities																
American Water	AWK	21,409	31,584	2.2%	4.4	35.9x	33.3x	30.4x	27.9x	25.7x	3.30	3.56	3.89	4.25	4.61	8.7%
Aqua America	WTR	9,739	10,749	6.0%	5.2	32.0x	34.7x	26.2x	26.1x	24.8x	1.41	1.30	1.72	1.73	1.82	6.6%
SJW Group	SJW	2,005	2,092	0.8%	2.2	33.6x	39.6x	30.6x	27.0x		2.10	1.78	2.31	2.61		7.6%
Artesian Water	ARTNA	342	492	0.5%	3.4											
Connecticut Water Service																
Middlesex Water Company	MSEX	1,100	1,328	2.6%	4.5	32.2x	32.3x	31.4x	29.7x	26.4x	1.96	1.96	2.01	2.13	2.39	5.1%
California Water Services	CWT	2,423	3,479	3.9%	9.5	40.4x	35.1x	31.7x	29.2x		1.25	1.43	1.59	1.72		11.4%
The York Water Co	YORW	583	668	1.6%	6.9	44.4x	39.0x	37.7x	35.0x		1.01	1.15	1.19	1.28		8.2%
American States Water	AWR	3,178	3,789	4.6%	7.8	49.6x	42.1x	40.2x	37.8x	33.8x	1.74	2.05	2.15	2.28	2.55	10.0%
Average (ex AWR/YORW)		**37,018**		**2.6%**	**4.9**	**34.8x**	**35.0x**	**30.1x**	**28.0x**	**25.6x**		0.1%	14.8%	8.1%	8.8%	**7.9%**

Source: BofA Global Research, Bloomberg

Regulatory updates

Speakers highlighted views that surcharges including Distribution System Investment Charge (DSIC) programs are critical for return on capital that can be reinvested in future infrastructure projects. Commissions seem to be considering more innovative tools to help as well, whether DSICs, decoupling, or future test years. Commissioners also look to NJ and other states that are considering implementing water quality accountability standards – particularly to level the playing field and ensure smaller and medium-sized utilities keep in line with the same standards as IOUs. We see reducing lag for AWK in its core geographies remains a strategic priority with 59% tracked – and a return to lag in '20 thru rate cases emphasizing this need in particular. Regulatory support across key states remains clear and all the more pressing given litany of water quality issues lingering including lead, arsenic, and now proliferation of PFAS materials (principally fire retardants used that stay in environment; a particular issue on military installations).

We perceive legislation such as Fair Market Value legislation, Single Tariffs, and the Water Quality Accountability Act will all continue to gain momentum, setting up opportunities for further consolidation. We look to Texas as another evolving geography to watch for potential consolidation, especially for Aqua America.

Company Highlights

We include our latest company takeaways below:

Aqua America (WTR – Buy, A-1-7, $45.12)

WTR continues to await final approval for the pending Peoples gas acquisition, which we would expect to come over the next several weeks. Upon close, mgmt noted a path to growing the gas rate base at 8-10% for 15-20 years, a faster pace than the organic 7% that the company expects from the water biz. Nonetheless, mgmt highlighted their continued appetite for water and remains bullish on acquisition opportunities (Recall the company announced the acquisition of DELCORA following the initial Peoples transaction, which will already dilute down the 70-30 mix of water-gas that is expected upon close). We perceive less likelihood of mgmt further diversifying away from the pro-forma water & gas portfolio, with the company particularly talking down interest in anything non-regulated. Further – despite the recent move by peer AWK to optimize their portfolio and divest of NYAW and Keystone – we see more of a willingness from WTR to continue to pursue the thriving municipal market. When it comes to entering new territories, mgmt continues to suggest visibility to 30K customers in the state before jumping in. On the other hand, after previously exiting Florida operations, the company noted a lack of interest in pursuing JEA, and we don't expect the state as a likely candidate to grow the footprint (despite the pending FMV legislation). Following the close of the Peoples transaction, we expect the conversation to shift more towards Repairs Tax (and quantifying the impact given limited new details at this point), which we see as a critical driver of earnings and the reason we remain above the street. Reiterate Buy given upside to estimates.

American Water Works (AWK – Underperform, A-3-7, $118.43)

Following their Analyst Day earlier in the week, AWK highlighted their latest five-year plan of $8.8-$9.4Bn, which is $800Mn higher than the previous five-year plan. The company has also laid forward longer term visibility with a ten-year plan of $20-$22Bn for 2020-2029. With the latest guidance, mgmt. reiterated their expectations for 2019 EPS of $2.56-$3.64 while launching 2020 EPS guidance of $3.79-$3.89. Despite the recently announced pending sales of Keystone and NYAW assets, mgmt. has clearly articulated that they don't plan to sell off any additional assets, and the company should be poised to capitalize on the growing trend of M&A amid the latest momentum of legislation & compliance requirements. We further stress the recent decision to de-lever the balance sheet as providing additional flexibility to pursue acquisitions. That said, we reiterate our Underperform rating given the lofty valuation.

American States Water (AWR – Not Rated)

American States Water Company (AWR) is a consolidated low volatility water company that operates through 2 subsidiaries; 1) Golden State Water Company (GSWC) and; 2) American States Utility Services (ASUS). GSWC is a regulated water and electric utility the serves 261,000 and 24,000 customers across California, respectively. Meanwhile, ASUS is a contracted service for water/wastewater systems that serves military bases under 50-year contracts. The EPS breakdown is 76% GSWC (8% belonging to the electric utility with the other 24% coming from ASUS). The company expects to have continued military success as it won two RFP's for military bases over the past two years. Although the company operates an electric utility in California, mgmt is not overwhelmingly concerned about wildfire risk given the system does not contain any transmission lines and is also at 7,000ft of elevation (less winds). AWR emphasized that it has been able to continue to seek the benefits of forward test years.

California Water Service Group (CWT – Not Rated)

CWT mgmt. discussed the company's growth priorities, rate setting backdrop, and unique regulatory environment in the state. CWT recently filed a settlement with the CPUC in the company's general rate case which includes $609Mn of new capital spend

and $200Mn of authorized improvements spent in prior years – mgmt. notes this represents 85% of the company's ask, an improvement over the 80% established in the previous case. The company had been expecting a settlement before the end of the year but mgmt. now expects the timeline to be pushed to Q1 2020 given the ongoing PCG situation remains the top priority for the CPUC. Mgmt. flagged that the company actively works with regulators to remain in sync with state priorities, highlighting its decoupling mechanism as generally supportive of state water conservation efforts - in particular in light of the drought conditions seen during the previous decade. In terms of M&A (mgmt. has made tuck-in acquisitions in the past year in Washington state and Hawaii), the company sees systems with 1,000 – 5,000 customers as its target range. CWT plans to file its Cost of Capital with the CPUC next May, as public water utilities in the state synchronize their filings – mgmt. expects an improved cost of debt (4.5% currently vs 5.5% in the previous filing) to provide some headroom in the upcoming filing. Inverse Condemnation remains a risk for water utilities though not to the extent that it affects electric utilities. While water availability remains an issue in Western states including California, supply for residential and commercial customers is a lesser concern in mgmt's view with 80% of California demand driven by agricultural customers.

Middlesex Water (MSEX - Not Rated)

MSEX mgmt. expects to deploy $325m in capital in 2019-21 in its New Jersey and Delaware service territories. The spending will be driven by three projects including a Western Transmission Main ($50m), new treatment plant ($70m), and unlined and aging pipe replacement ($35m). The total plan is forecast by mgmt. to grow to $1.1B by YE 2021 with an approximate $800/300 split between NJ and DE. MSEX remains open to consolidating smaller municipal systems, having recently acquired a 1000-customer system in Delaware. While the company has not articulated a formal goal for EPS growth in the forecast period, mgmt. does expect its DPS payout ratio to increase from 49% in 2019 to a range of 65-70% in the coming years. MSEX is subject to a Distribution System Improvement Charge (DSIC) in both its NJ and DE jurisdictions which allows accelerated recovery of certain pre-approved investments subject to a cap. Mgmt does not anticipate approaching its 7% cap in Delaware in the near term owing to the system's relatively young age.

SJW Group (SJW – Not Rated)

SJW Group has completed transformative M&A activity – amounting up to 40 acquisitions in the last 10 years alone. The company sees these purchases as great for diversification when it comes to location (the company sits across four states), regulatory environment, weather, and availability of water; SJW Group sees diversification as a level of comfort and safety. Each geograpy provides different benefits: Silicon Valley, CA represents 60% of earnings, the Austin-to-San Antonio, TX region grew 16% last year (8% organically and the rest through M&A), and the CT and ME communities provide what SJW sees as the best in class regulatory relationships. The company has increased its payout ratio in recent years to increase its competitiveness with other companies. Finally, we note the company now has the third largest pure-play water utility ratebase in the country.

The York Water Co (YORW – Not Rated)

The York Water Company (YORW) is a water utility that serves customers ~200K across the state of Pennsylvania and is currently the oldest stock that trades on the NYSE (founded in 1819); The company currently has a 42/57% debt/equity ratio coupled with an A- credit rating from S&P. The company also has an average demand of 20Mn gallons of water per day (vs. 40Mn capacity) and is replacing 1% of its infrastructure per year (based off a 100yr rate). Of all of the publicly traded water companies YORW is the most expensive; it trades at 35x '21 earnings vs. the comp set avg of ~29x (inclusive of YORW). In addition to its water utility services, the company also owns and operates wastewater collection systems, which mgmt thinks will grow near-term given constructive legislation in the states (Act 11). The act ultimately combines water and wastewater revenue into one – meaning that the company can now buy a wastewater

system and allocate the cost over all its customers, thus preventing rate shock. Further positive legislation in the state includes Act 120 which allows the company to replace led lines at no cost to the customer. Mgmt emphasized that their presence in one state – and a constructive one at that – as a key advantage relative to larger peers.

PE investment in water infrastructure

Broadly, private equity investment in infrastructure has increased at a 16% CAGR over the last 10 years, to nearly $500bn by 2018 (incl. $312bn unrealized value, $179bn dry powder). This has resulted in upward pressure to valuations on private infra asset valuations, while fundamental valuations have not changed materially, given the tremendous amount of capital looking to be deployed. Water assets, however, have seen limited activity, averaging only 2.8% of annual infrastructure deal flow (3% water in 2018). Select opportunities do exist in certain areas including industrial water, water-as-a-service, technology deployment, and on-site residential wastewater.

We see this as driven by a number of challenges to water investment. These include:

1. **Investment size:** Few opportunities in the $200-$500mn EV range, with the market generally divided between larger publicly traded companies and municipal assets as well as many much smaller systems. Roughly 56% of systems serve less than 500 customers, representing only 1.6% of people served.
2. **Rising valuations:** Many assets reaching above 2x rate base valuations
3. **Change of control regulations:** Commissions skeptical of the PE model
4. **Limited flow of Public-Private Partnerships:** Municipalities have shown limited willingness to privatize facilities
5. **Diverse asset class:** Wide range of opportunities including IOUs (investor-owned utilities), water technologies, wastewater, water-as-a-service, etc.
6. **Political-related issues**

Storm Water Remediation

We highlight sustainable infrastructure opportunities as including stormwater remediation, environmental restoration, and water & wastewater infrastructure. Within wastewater infrastructure, the American Society of Civil Engineers estimates $271bn of needed facility upgrades in order to meet demand of an incremental 56mn users by 2032, while $1tn may be needed to update and upgrade water infrastructure.

HASI sees opportunities within storm water remediation, including $7mn investment in four projects to slow pollution runoff into downstream waterways in the Chesapeake Bay area. Waterway restoration and wetland mitigation credits are another opportunity: credits are generated through state or private restoration projects, and then banked and sold to offset environmental impact. In addition to the Chesapeake Bay and Great Lakes areas, these have some prevalence in the Gulf Coast with refineries needing to mitigate the impact on land in order to obtain permits for construction.

Public sector funding poses various limits. Federal funding includes the WIFIA (Water Infrastructure Finance and Innovation Act of 2014) program, which only funds 49% of the project cost, with a 35-year maximum duration. While state revolving funds have a low cost of capital with a 30-year maximum loan term, projects are ranked with preventative maintenance and plant expansion not considered to be a priority. Tax-exempt funding sources need voter approval and also take time to implement.

Private capital is also available for infrastructure funding purposes, with water public-private partnerships (P3) an option, although we note these can be challenging to find given a limited number of opportunities as well as municipal hesitancy. Specifically, P3s are contracts that allow a private partner to construct, upgrade, operate, and/or manage

a public service facility or system while investing capital, while the public entity remains ownership; income generated is shared between the two parties.

While HASI did not specify return criteria for their water investments, we note that their sustainable infrastructure portfolio yields 5.6% while their BTM portfolio has an 8.0% yield; their overall portfolio yield is 7.7% as of 3Q19. HASI expects water returns to increase over time given an underserved market with pressure for infrastructure investment to build in this market.

Price objective basis & risk

American Water Works (AWK)
Our PO for American Water Works is $130. We apply a 26.0x P/E multiple to American Waters 2022E earnings based on the water peer multiple and a 8.3% group EPS CAGR for '18-'22, as we see AWK largely driving the peer multiple as the largest publicly traded water utility.

Risks to the downside are increase in market interest rates, potential impact of tax reform on utilities, operational errors, changes in valuation levels for water utilities. Risks to the upside are accelerating muni acquisitions, multiple expansion, and constructive legislation in regulatory jurisdictions.

Aqua America (WTR)
Our price objective is $47 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 0.5x discount to Peoples Gas as we expect earned ROEs to be driven down over time.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Aqua America	WTR	WTR US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith
NEUTRAL				
	AES	AES	AES US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
UNDERPERFORM				
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Terraform Power	TERP	TERP US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith

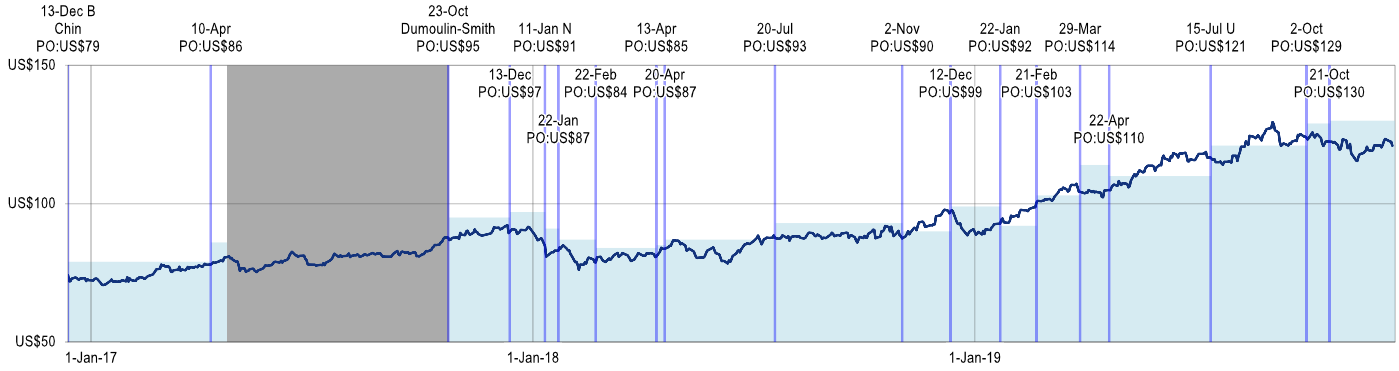
North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Pattern Energy Group	PEGI	PEGI US	Julien Dumoulin-Smith

Disclosures

Important Disclosures

American Water (AWK) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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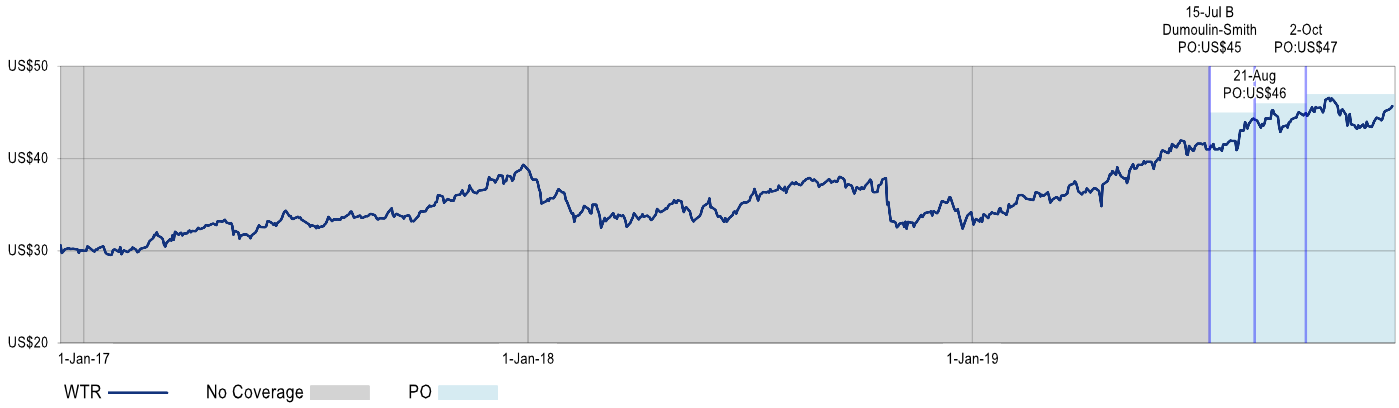
Aqua America (WTR) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Utilities Group (as of 30 Sep 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	67	47.86%	Buy	51	76.12%
Hold	36	25.71%	Hold	24	66.67%
Sell	37	26.43%	Sell	26	70.27%

Equity Investment Rating Distribution: Global Group (as of 30 Sep 2019)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1517	50.30%	Buy	964	63.55%
Hold	680	22.55%	Hold	434	63.82%
Sell	819	27.16%	Sell	408	49.82%

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Underperform	N/A	≥ 20%

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US Electric Utilities & IPPs

The Virtual Boston Conference Day 2: Who Said What?

Industry Overview

Summarizing the key events & updates

Our latest sector-wide Power, Utilities & Renewable Leaders conference concluded yesterday. While we hosted 50+ companies overall, stand out meetings yesterday included PEG, FE, ETR, and PCG. Day 2 Company write-ups included below include: AEE, ATO, BKH, CWEN, CMS, D, DTE, DUK, EIX, ETR, WTRG, ES, FE, HASI, NI, OGS, PCG, PNW, PEG, SR, RUN, VST, XEL.

On PEG, we see mgmt. as confident in addressing ongoing dockets and more critically poised to further its divestments in Power, offset dis-synergies, and ultimately seek further refinements of ZECs eventually too. Offshore appears clear too as a further avenue of interest for investors. Meanwhile, FE (Neutral) stated they believe a rate case could come sooner than '24, albeit with just -10c at risk based on regulatory capital structure derived off ratebase; this outcome could be substantially more accretive than our earlier concerns. That said, the pathway to such a rate case filing amidst numerous other pending dockets – and resolution in this favorable regard remains pending a lot of execution. As for ETR, we see mgmt. as quite firm in its expectations for an AR FRP extension to materialize by March 15th (rather than conceding the point of any eventual rate case). Further, LA settlement by late March also key. While we see capex cut risks under less bill headroom, we see affirmation of regulatory structures altogether as enabling some improvement off among widest discounts in group. Finally, PCG's ability to sidestep equity needs and pivot dialogue more constructively with CPUC continues to impress despite the continued pressure on the shares.

Financing with Preferreds continues to expand

Amidst an effort to limit dilution given wide discounts (EIX, ETR) and overall limit/delay dilution (NI), we look for equity-linked alternatives to prove a growing trend in utilities. With ~50% equity content treatment from the rating agencies and modest coupons, we perceive a sharp shift in financing alternatives. FE also affirmed its intent to evaluate such avenues (seemingly over asset sales) to fund any eventual B/S fix required. We see this as an expanding subject of focus from many companies – watch SEC filings for clues on extent of any such offerings.

Texas: Deep Freeze implications

So much of the conference was dedicated to understanding the vast array of implications. While a handful stand out as beneficiaries (SR principally; SO in part), we are looking at an array of cautious datapoints around cost recovery and rate impacts. With few datapoints from regulators yet on the 'crowding out' effect yet of higher fuel cost recovery charges we believe the discount will remain for some time (despite affirmation from many that recovery should prove forthcoming – whether through normal recovery mechanisms or discrete securitizations). We stress Gas LDC inflation in particular remains a cautious point. *We don't expect sharp recoveries post Texas.*

The Bigger Picture from the Administration

Few companies had good anecdoctes, but those that did are focused on transmission.

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Just Where is Biden Going?

While front and center issues such as Texas rate impacts dominated dialogues this week, the bigger picture question of just where and how this new administration intends to achieve its clean energy goals remains opaque. We note the EEI CEOs appear to have had an initial meeting with DOE Sec Granholm this week alongside our conference. Early datapoints would appear to indicate a clear focus on transmission, consistent with our earlier discussions with the FERC. While XEL is among the first companies to come back with an expanded transmission plan in response to the election (and its own state targets for 80% by 2030), we expect others to come back later this year with revised outlooks. This view on transmission was shared by many, but remains in part dictated by the planning processes of key RTOs such as SPP and MISO. This should come in three forms: 1) larger project planning awards; and 2) addressing interconnection queues and processes – helping to accelerate deployment; and 3) on the margin, we could see some greater authority on eminent domain granted.

Where is this transmission upside coming? We heard it across the board. AEE, FTS, WEC would be direct beneficiaries of processes in MISO (updates later this year even with latest plan release possible), while others like SO and DUK could see those opportunities arise out of yet to be finalized generation resource planning. Even if unsuccessful in garnering greater renewables for itself, DUK should benefit from added transmission spend from legislation.

What appears clear to us though is that this spending may not materialize meaningfully for some time – adding to longer-dated prospects in the 2024+ timeframe. While we've perceived an acceleration for some time, we see growing acceptance of both a renewed uptick in transmission spend in 2024-2026 as well as generation replacement in this period as well. We see further roll-forwards of updates late this year (EEI principally) inclusive of 2026 in 5-year views as particularly relevant in initially reflecting this accelerating fact pattern.

Biden & subsidies – where to go from here?

We remain sober on more subsidies directly for clean energy – seeing this as potentially protracted. Rather, we remain focused on storage benefits. This remains the arena in which a new subsidy could bolster the market immediately and seemingly offers greater margin to utilities and developers alike given the integration 'complexity' relative to thin margins on offer for solar today.

The blowback from Texas on resource planning

While we identified this in our Day 1 takes, we stress a focus on *retaining assets while still adding renewable resources*. The focus on costs remains on proving out the economics of adding additional solar & wind relative to the *variable* cost of dispatching coal assets (rather than all-in fixed cost structure - which are not trivial). Shifting towards seasonal dispatch for coal assets – principally winter – appears an over-arching trend that started in the Northeast but appears to be spreading elsewhere. On-site fuels during harsh winter weathers that challenge gas deliveries - this includes both coal but especially oil resources to backstop the grid.

Expect more discussion grid support with more renewables too. XEL's next update would appear to be a $0.5-1.0 Bn voltage support effort to pair with its transmission proposal. This remains another avenue to watch peer companies propose, particularly across vast distances in the West with ever greater renewable penetration.

Competition is pervasive

Owning the renewables directly remains a challenge for utilities – and we view a backdrop of competition as adding a greater degree of opacity around capex planning. Assumptions on the split of PPA vs owned opportunities in ratebase is key, in our view (SO, DUK, but also for other smids too: EVRG, POR, PNW).

Ameren (AEE)

Our update with Ameren mgmt. covered several key pending pieces of legislation and their relative levels of support. We note that downstate legislation picked up a key sponsor in the chair of the Utilities Committee which is an incremental positive. While AEE mgmt. expressed clear support for the downstate legislation and its modification of the ROE mechanism to use an average of national rates, it remains unclear to what extent competing legislation including the Clean Energy Jobs Act (CEJA) can garner further support or potentially be reconciled with downstate legislation. Maintain Neutral on AEE.

Renewed support for higher transmission spending

Ameren mgmt. reiterated the growing need for higher levels of investment in regional transmission. Recall that on the Q4 call the company flagged investment in "multi-value" transmission projects (MVP) across its Midcontinent Independent System Operator (MISO) footprint in order to increase the reliability of the grid and ease regional congestion, particularly in light of its own ambitious renewable buildout plan. While such investments would likely have modest upside in the current investment plan through 2025, mgmt. reiterated that it sees upside and potential for sustained rate base expansion as part of its longer-term spending plan, in particular during the 2025-29 period. Ameren's current 5-year plan includes a robust +11% transmission rate base CAGR through 2025, which mgmt. notes does not currently include multi-value projects which have largely been completed, suggesting upside beyond the current plan if a new group of projects were proposed and approved by MISO and relevant regulators.

Downstate bill garners key support

We note that the downstate energy legislation currently making its way through the state house in IL recently picked up the sponsorship of the chair of the influential Utility Committee. Among the key components included in this bill is a modification of the current formula-based ratemaking mechanism and its 580 bps adder in favor of one based on an average of authorized ROEs from the previous 12 months adjudicated nationwide. While we note the proposed methodology is necessarily backward-looking, it would certainly serve to align IL allowed ROEs more closely with national levels as average ROEs tend to drift higher or lower over time. While the current 30Y UST + 580 bps methodology was originally intended to achieve the same goals, today's low levels of interest rates have resulted in far below-average ROEs. The downstate legislation also includes a 40 bps performance-based band based on measurable metrics.

Rate case filing in MO concurrent with wind approvals

Ameren expects a busy regulatory schedule in MO with an impending base rate case filing coming later this month, as well as filing for certificates of convenience and need (CCNs) for the latest renewable generation proposed in its latest resource filing. In MO the rate case process typically lasts 11 months and the most recent wind projects received CCNs after 5-6 months, suggesting that by Q3 the contours of both processes should come into focus. Recall that MO has been a relatively constructive jurisdiction of late, in particular with Ameren's most recent case outcome achieved in Q1 of 2020 given substantial cost offsets more than made up for a top line reduction in revenues and ended up with a ~$100m post-tax annual increase. While Ameren needs to make this filing in order to add its soon-to-be-completed wind generation into rates we note that the current bias across the sector remains toward staying out of rate case filings given regulatory sensitivity around bill increases during the Covid pandemic.

Atmos Energy (ATO)

How to think about financing needs with upcoming $2.5bn bill due

With ATO one of the few gas utilities not to have short-term financing in place (despite $2.8bn in liquidity), mgmt. highlighted that it would expect to have its financing in place by the end of March when bills are due. That said, the company continues to leave open the door for some equity content (as well as ST debt, LT debt and cash on hand) to meet its obligations. We also wonder if there could be some sort of posturing as a negotiating tactic with 3rd parties given the different approach that ATO has taken. At the end of the day, mgmt. did reiterate its 2021 EPS guidance and LT EPS CAGR of 6-8%, so it should provide some confidence that there is clearly a preference for debt (as it awaits approval from regulatory bodies).

Not much new on strategy for recovery or lessons learned in policy hearings

Mgmt. highlighted that hearings last week with executives didn't provide much info given the focus on energy needs, and it still remains too early to predict its regulatory strategy for recovery. Securitization also remains an option in Texas with the session ending in May (special session in June/July if needed), although here too it remains very early in the process and could be somewhat protracted given subsequent approval required from regulators (assuming a bill is introduced and passed) and the time to get financing in place. From a regulatory standpoint, mgmt. highlighted that there is a peaking component to consider for recovery, although the base charge component is 59% of the customer bill; we perceive the peaking component could be somewhat tricky given the likely pushback from those without flowing natural gas. Given the substantial impact to customer bills and discussions from policy makers around these concerns, we see this likely an overhang on shares until more clarity evolves.

$2.5bn seems like a best estimate at this point

In terms of reducing the $2.5bn number, mgmt. highlighted it has good confidence in its estimate and it's still going through force majeure considerations (freeze offs in the West). At this point we don't necessarily see ability to further mitigate these gas purchase costs.

Black Hills Corp (BKH)

Texas Setbacks, but Confidence in Plan

Ahead of our meetings with management, BKH reaffirmed their recently issued guidance despite the latest cold weather challenges - with the company previously disclosing a ~$600Mn elevated purchased gas cost and $800Mn ST debt facility in tandem to improve liquidity. As we await firmer details around regulatory recovery across jurisdictions, we note that several of their states have issued orders requesting applications to seek deferred accounting treatment and we believe recovery is likely over the next 2-3 years (albeit with Arkansas and Kansas potentially more protracted).

Despite the latest setbacks, discussions more broadly continued to highlight confidence in the company's recently laid out five year outlook and inaugural long term trajectory of 5-7%. We further don't view the latest events as impacting equity financing timing with conversations suggesting constructive conversations with rating agencies (recall FFO thresholds are 13% and 12% for Moody's and S&P, respectively) and levers to avoid breaching these thresholds ahead of incoming cash.

Elevated Level of Spend and CO Developments on the Horizon

We perceive particular confidence to achieve at least a $600Mn run rate in annual spend to drive 5-6% growth, with potential for yet elevated levels of investment and asset-light opportunities to further boost margins. This should help offset any challenges around ROE pressures for any upcoming rate cases to help drive elevated growth. After the Colorado commission extended the comment period for the RRR, comments are now due early next week after the earlier rate case dismissal. If a constructive resolution is reached, look for the prior rate case to be reinstated on a 60 day delay from the original procedural schedule that sought new rates for this Fall. If the company has to re-file the rate case, we would look for a new filing in CO this summer. Either way, watch parallel developments around efforts to incorporate another rider for additional relief with more minimal lag.

We reiterate our Buy rating on the shares, stressing elevated rate base growth at an attractive valuation – and see the latest guide of 5-7% LT EPS growth affirming our confidence in what we view as a Best-in-Class SMID.

Clearway Energy (CWEN)

Still confident on 5-8% div growth with upper end of range for '21

Mgmt reaffirmed confidence on LT div growth of 5-8%, with the upper end anticipated for '21 even after adjusting for the the one-time $20-30mn TX storm impact. The high end is still expected (with $325mn CAFD outlook also intact for '21) given a number of significant dropdowns of late, with pro forma CAFD recently raised to $385mn, up $40mn from $345mn after including Agua Caliente (closed Feb 3rd) and the 1.6 GW CEG co-investment. Other opportunities in the pipeline include the 1.1-1.7 GW co-investment with CEG (target closings 2021-2023) which is in the works, in addition to the recently signed agreement for the 264 MW Mount Storm Wind. Notably, this project has a 10-yr contracted energy hedge; we note ~$10mn CAFD on $96mn corp capital, or a 10.3% CAFD yield, with this deal expected to close 1H21. With ~1.7 GW of wind and ~600 MW of solar in the portfolio, mgmt appears to be comfortable with this level of exposure to more volatile wind production, given the higher ~9-10% IRRs to be found vs. solar.

More color on the financing strategy for growth

Mgmt has noted that all commitments made through Nov 3rd have effectively been funded, with deals thereafter to be funded via a combination ATM issuance as well as potential block equity deals in cases where it makes sense, in addition to project debt, green bonds, and retained CAFD. We note CWEN recently issued a $925mn green bond (3.75% senior unsecured notes due 2031) to finance new projects and refi the $600mn 5.75% senior notes. Mgmt highlighted increasingly greater demand for higher-yield debt.

Addressing TX: No change to guidance, need for upgrades will be assessed

Clearway had previously estimated a direct cash impact of $20-$30mn from the recent ERCOT weather event, prior to any potential mitigation factors (although we note cost savings will likely be limited). The impact appeared to have been driven by weather-driven wind outages and contractual hedge obligations from certain facilities. The company is currently assessing potential initiatives that could improve fleet resiliency in response to the TX event. That said, given the low-probability nature of this event, we expect a cost-focused approach to this endeavor. We note that a minority (likely well below 10%) of CWEN's renewable PPAs are firm commitment contracts.

CA gas assets: Re-contracting opps vs. up for sale?

Our discussions also focused on the improving backdrop for Clearway's contracted gas assets in California (two CCGTs, one peaker), with existing PPAs set to expire in 2023. Mgmt continues to assess all options including a combination of bilateral re-contracting on its gas assets given the robust environment (with mgmt aiming for ~7-10-yr contracts for greater earnings stability) and/or divestment of some or part of its ownership. We expect that addressing this uncertainty will be a priority in 2021. We note recent multiples as high as 14x EV/EBITDA from recent comparable West coast deals. For re-contracting efforts, we estimate that RA market prices may be in the $5-6/kw-mo range, with upward movement likely since this summer's rolling blackouts (we continue to assume $6/kw-mo for El Segundo, Marsh Landing, and Walnut Creek).

CMS Energy (CMS)

IRP Focus – Accelerating coal retirements, incremental renewable oppty

Among key discussion focuses with CMS mgmt included its upcoming IRP filing in June. Mgmt continues to indicate likely focus on accelerating coal retirements with Campbell 1 and 2 scheduled for 2031 and Campbell 3 scheduled for 2039 given latest state emission targets set, which could drive incremental renewables spend. We note that Campbell units 1 and 2 account for a relatively smaller portion of overall rate base (4%) than unit 3 (5.5%) and thus we see these as the most likely candidates for a potentially *accelerated* retirement when CMS releases its next IRP proposal. Indeed our channel checks with interveners including the Sierra Club identified these units as a focus of negotiations with environmental groups, further bolstering our view. Recall, while CMS is only required to file an IRP every 5 years, mgmt expressed a preference in filing more frequently with a voluntarily submission every 3 years, given the clarity provided from tri-annual IRP filing cycles around capital spend around resource planning.

Indeed discussions with mgmt affirm focus on retiring remaining coal units with 5 remaining (2 to be retired in 2023 already under first IRP filing in 2018). In terms of replacing capacity with accelerated retirements, mgmt expressed IRP filing to focus upon incremental renewables beyond 6GW of solar through 2030 already approved in the last IRP as well as on battery energy storage deployment, and demand-side management.

ERCOT comparison – better managed wind assets/grid, more extreme conditions

With the latest cold snap and outages across TX, discussions were focused on resiliency with mgmt keen to address key differences between its own operations and ERCOT. In terms of underperformance of wind assets in ERCOT during the cold snap as blades froze, CMS mgmt emphasized that MI was substantially colder than TX (~20 degrees) during this same period without the same issues for its wind assets. To this point, CMS mgmt expressed its wind turbine generally all have lubricant and conditions for components such as the gearbox, paired with its ability to forecast icing conditions to take pre-emptive actions to prevent asset failure, all without having to reach the point of heated turbine blades mentioned in 'winterization' discussions on ERCOT. CMS emphasized its engineering team does a lot of work on loss of load expectations during extreme weather conditions and actively works with MISO around backup and reserve margins – further noting the capacity market in MISO supporting resiliency and appropriate grid planning relative to failures in ERCOT.

That said, given that CMS is already embedding loss of load situations and managing extremes effectively, with its upcoming IRP – despite likely greater scrutiny on reliability and resiliency side of the equation – mgmt does not expect a significant amount of incremental capex from this angle.

With some peer utilities expressing early discussions on shift from coal retirements to usage as a seasonal asset, CMS mgmt was firm in its view that this is neither economic nor feasible (with CEO expertise incl. having operated coal plants). Coal units require consistent management as coal can spontaneously combust when wet and coal piles freeze, making usage as a peaking unit impractical relative to investing in natural gas - in additional to lower heat rate/efficiency even when retrofitting an existing coal unit to gas. Carbon capture is also better for gas relative to coal.

How to effectively decarbonize heating – gas infra remains critical here on H2

Discussions also focused upon CMS mgmt's long-term plan to future-proof its gas pipeline infrastructure in tandem with its plans. Mgmt notes that heat pumps are generally not effective below a certain temperature range (below 30 degrees) with heat pump homes requiring natural gas as a backup still in MI. Notably, mgmt highlights that fully shifting all space heating in MI to electric (currently 75% nat gas and 25% propane – latter being more rural areas) would increase customer utility bills 3x (also needing

modification of homes to HVAC systems) and would also substantially burden the electric grid flipping CMS from a summer peaking utility (as its resources are planned for) to a winter peaking utility with 3x higher peak.

As such, CMS mgmt emphasizes its nat gas pipeline infra remains essential in the most economical way to decarbonize space heating. Near-term CMS expects to reach net-zero methane by 2030. For long-term decarbonization, green H_2 remains particularly notable for use in decarbonizing space heating, but importantly metal pipeline is faced with stress corrosion cracking at even 20% H_2 blending with nat gas. As such, CMS emphasizes a continued trend of replacing cast iron pipe with plastic with 14K miles of plastic pipe and 12K miles of metal pipe in its system currently. Its $10Bn in spend through '30 is primarily to replace 2K miles of metal pipes with plastic and to reduce methane to reach net zero methane target by 2030. Beyond pipe replacement, mgmt notes H_2 space heating would require upgrades of appliances in homes as well as likely upgrades to valves and packing at points where pipe is sealed. CMS emphasizes working closely with organizations such as EPRI on H_2. Bottom-line, decarbonizing space heating presents a substantial investment runway with long build-out process for CMS.

Additional areas to support decarbonization include energy efficiency (1% annually supports ~$10mn in earnings), bio-sequestration (tree planting), RNG, and carbon capture.

Nat gas storage potential to be used as green H2 storage for seasonal ESS

With its substantial net gas storage fields, CMS emphasizes potential to be used as storage for green H_2 produced long-term as well, where H_2 can then be used for either space heating or even for electric generation with retrofits to gas plants (CMS mainly uses GE and expects retrofitted turbines capable of handling green H_2) as seasonal long-duration storage assets.

Dominion Energy (D)

Remain comfortable w/ the VA construct: Filing suggesting no refund a positive

For the upcoming triennial review (2017-2020), mgmt. highlighted it intends to file with the State Corporation Commission (SCC) at March end, suggesting no refund required. We stress GAAP earnings, including the ~$630.7mn expense in 1Q20 that will reduce reported 2020 earnings (14+% ROE otherwise) and $247mn in 2019 for coal plant retirements. We note a key consideration for the upcoming triennial review will be treatment of the coal plant retirement amortization in which D elected to period expense these plants (upfront expense) given the discretion of the SCC. We also view ability to utilize $300-325mn in CCRO investments as a positive, and remain comfortable with potential outcome here. While the time period is expected to be relatively long, with a hearings in Aug/Sept. and a final decision in March, we view both the commission makeup (with Navarro a clean energy proponent) and the construct as assuaging concerns on this front. *We still look for updates from the SCC to see how the new composition votes as there are few datapoints subsequent to her nomination to the role.*

SC rate case pause continues: settlement discussions moving forward

The SC rate case remains on 6-month pause as the DESC agreed in the January 2021 rate proceeding. The parties are required to report monthly on settlement progress with parties currently in settlement discussions. We continue to view the core debate to be around the rate increase during a pandemic. We continue to estimate that the financial impact to be relatively minimal (~2.5c) with a delay, although see the concession from Dominion as likely garnering additional political capital in the state. We still see probable bias for a settlement, with the SC Public Service Commission (PSC) indicating a preference for a settlement vs a fully litigated case, where we estimate a 9.5% authorized ROE (vs staff rec. of 8.9% and company request of 10.25%) as a reasonable outcome. Mgmt. voiced confidence in the case that it filed noting it has not had an SC base rate case in 8 years. We note that while securitization has come up in the past and is likely to continue, mgmt. seems less concerned on the margin given similar proposals have been defeated. While storm securitization is a useful tool, we believe securitization of NND would not be beneficial to D's EPS outlook, although see this as a low probability event.

Combing through the details on capex: watch storage and solar spend

Mgmt.'s 5-yr capex ('21-'25) of $32bn reflects a 43% increase from prior 5-yr plan with 87% of the $23.8bn in spend VA rider eligible (potential for triennial rate review offsets) and base rates diluted down ~26% by 2025. This capex program yields an impressive rate base growth in VA at +13% and 9% overall. We note discussions with mgmt. indicated that there could be some variability (to the upside) with solar spend through federal procurement/policies, although the current law allows for up to 1GW per year (2/3 rate base and 1/3 PPA), coinciding with mgmt.'s current plan. On storage, mgmt. highlighted that this $2bn in spend is likely somewhat less defined given 3 pilot projects ongoing, although did highlight its pumped storage project as progressing well. Undergrounding of distribution appears to be solidified. Net-net, we continue to view the capex profile as favorably, although look for variability in storage and/or solar.

Winter weather event impacts muted

Mgmt. highlighted minimal impacts in terms of fuel purchased costs for its gas LDCs with Utah having some mitigates due to storage and the wexpro model with 50% of supply under a rate base model. No other impacts on assets in Texas were noted (small asset on Ft. Hood, but no impact).

DTE Energy (DTE)

Our update with DTE focused on company mgmt's ongoing efforts to maintain bill stability including its current electric case stayout which is aided by strong residential sales which enabled the company to push back its deferred tax item recovery until December. On the non-regulated side we see some competitive pressures on the Renewable Natural Gas (RNG) portion of the Power & Industrial (P&I) part of the business given additional entrants to the market of late and expect the Energy Trading segment to post a positive contribution in Q1 from long positions that benefitted from price spikes following last month's severe weather. Encouragingly mgmt. affirmed confidence in attaining 5-7% EPS growth on a consolidated basis (post-spin remainco) in '22 despite tax credit earning cliff pressures and share count dilution from settlement of its equity units. Maintain Buy on DTE.

Steady electric rates through '22 expected

Mgmt. provided an update on the expectations for the next electric rate case filing, given strong retail sales to start the year. Recall that the current electric stay out was partially achieved by the utilization of an accumulated deferred income tax (ADIT) asset that was scheduled to flow back beginning in April, though DTE has recently filed to push back the recovery timeframe to December, allowing for rate stability through most of 2022. Given the rate case process in the state of MI that requires cases to be concluded within a 10 month window, the company expects to file in late 2021 for rates effective the following year. The current pending gas rate filing requesting a $195m increase based on a 10.25% ROE is expected to reach a resolution by the end of the current year (current ROE is 9.9%).

Cold snap was a net positive

DTE mgmt. reported strong performance of its electric generation fleet during the extreme cold weather seen in Feb with no material outages or customer impacts – given the strong uptime of its generation fleet DTE electric was able to export 2,000 MW to the MISO grid, while this does not impact earnings it did generate a $20m credit via the company's power supply recovery mechanism which will flow back to ratepayers – an incremental positive in the company's efforts to maintain stable bills in the absence of a rate case filing. The Energy Trading business generated gains as a result of being long spot pricing at the time of market volatility in mid-Feb, though mgmt. reported that the segment remains mostly a support function and does not hold large unhedged positions, in particular on the short side where losses could potentially be unlimited. While some midstream customers, particularly in the Haynesville basin, experienced well shut-ins, the majority of contracts are demand-based and mgmt. reports no meaningful impact on Q1 results from lower levels of activity during the severe weather.

RNG contracting more competitive

The P&I segment principally operates in the RNG market and on-site cogeneration for industrial customers. Mgmt has experienced a slightly more competitive environment in bidding for RNG inputs (manure from ag operations) where contracts have multi-year tenors, though the company continues to actively source new supply and to bring on new projects despite the more competitive environment. Demand, in particular from California given the Low Carbon Fuel Standard (LCFS) remains robust and mgmt. reports being well contracted in the near term. Despite previously pushing out its renewable energy fuel (REF) tax credit earnings cliff to the end of 2021, mgmt. sees a further extension as unlikely though expects to be able to backfill lost earnings over time.

Duke Energy (DUK)

Still waiting on key updates in NC: Rep Ark commentary positive on margin

With upside to the LT plan largely predicated on the IRP/legislative process in NC where, we wonder just how much renewable ownership is possible (relative to HB589 at 30%) and whether mgmt. can hit the top-end of its capex plan in '25-29 ($65-79bn, RAB of $140-150bn in '29) without progress on the legislative front. Mgmt. highlighted that it assume 25-50% ownership, which it feels is conservative. Still with public data points likely few and far between, aside from Rep. Dean Ark (co-chair of the Committee on Energy and Public Utilities) commentary that suggested intent to pass legislation this year and cross-over date for bills in May, we continue to wait for progress on this front. Meanwhile, mgmt. confirmed that regulatory reform such as multi-year rate plans (MYRP) and ROE banding are not needed to hit the mid-point of guidance, although would indeed enhance the LT plan given it reduces regulatory lag. We note that while the Rocky Mountain Institute endorsed these items, getting it through in legislation will be critical to monitor. *We remain quite focused on the legislation- both around the pace of acceleration on carbon reduction as well as proscribed ownership %'s. We stress that much of the 'upside' coming from legislation is likely relatively protracted (2024+) – but utility rider reform could be the most near-term tangible benefit. We also stress regardless of procurement cycle, the transmission investment is a clear opportunity in this '24 time period, and particularly accelerating should the state pursue offshore wind (East-West capacity would need to be substantially expanded).*

Texas impact: 600MW impacted, Gas LDCs not significant

Mgmt. highlighted that it had 600MW of renewables that were affected from the freeze given the inability to produce output; we estimate this likely measured in $MN's. While it did have a 100MW asset that has Brazos as a counterparty, its only 1 of 3 off-takers on the asset. Separately, mgmt. highlighted minimal impact to its gas LDCs across OH, KY, TN, and NC and would expect to recover fuel costs through the typical gas clause mechanism. Bottom line, we see an overall limited impact to DUK on an absolute and percentage terms basis.

IN: could be upside to spending but expect slower transition

While DUK recently sold a ~20% interest in IN to GIC for $2bn to eliminate equity needs with a nice recycling of capital, we don't believe additional transactions are likely in the NT given key data points that await from the Integrated Resource Plan (IRP) filing that mgmt. intends to file. This transition of the fleet is indeed likely to be slower than NC, although mgmt. highlighted that it looks to utilize the least cost financing tool. To the extent the opportunity set for the coal transition accelerates, we could see further sell down to fund growth over-time. Still with IN coal lobbyist particularly strong, we stress not to get too far ahead of expectations here.

Edison International (EIX)

Preference for additional preferred equity seems likely

Following the $1.25bn preferred issuance that has a 5.375% coupon (w/ reset date based on the 5yr treasury rate – potentially something to monitor given increasing interest rates) and is expected to have 50% equity content ($625mn) treatment from the rating agencies, we believe remaining $375mn of equity content could come in the form of preferred as well. While mgmt. left the door open for ATM utilization, the company also suggested that it has the balance sheet capacity to do *more* preferred and also acknowledged PCG's issuance considerations where it could be a different market depending on the product. To that end, we see this as indicating that there is more a preference to do preferred equity than ATM for remaining $375mn.

Customer bill impact: not too many solutions aside from securitization

While the customer bill impact will be a key consideration going forward given the substantial wildfire related spend (and O&M that will be difficult to ratchet back), mgmt. did not highlight any ability to sell assets to mitigate those considerations. While it has seen generally lower rate increases vs. peers, this still remains a consideration. One potential solution could be securitization of bad debt expenses from COVID (although not likely under collections as EIX does not likely meet the requirements). We view this as a potential useful tool given the rate impact that would occur earlier in the year otherwise.

FERC ROE focus in part

Mgmt remains confident that with its fully resolved FERC ROE at 10.3% on a settled basis from its last case this could help avoid the pitfalls of the +50bp RTO adder that otherwise appears at risk in the state. We see some risk of degradation still upon future reviews.

Entergy (ETR)

We caught up with the mgmt. team at Entergy principally focusing on the prospects for outcomes in the ongoing Arkansas Formula Rate Plan (FRP) docket which may see a resolution by the middle of the month. We also discussed the latest System Energy Resources (SERI) complaint filed last week which adds a further Federal Energy Regulatory Commission (FERC) proceeding in addition to the ongoing sale-leaseback case which has been in focus since the Administrative Law Judge (ALJ) ruling came down nearly one year ago. On balance we see a uniquely large number of uncertain regulatory outcomes upcoming, though mgmt. continues to highlight its ongoing contingency planning (as well as recent reiteration of guidance) to deal with the potential for adverse outcomes. Maintain Buy on ETR which we see as deserving of a higher valuation than lower-growth peers.

Arkansas resolution could come by mid-March

Entergy mgmt. laid out several potential paths to resolutions of its FRP proceedings – both for the 2021 rate increase where the Arkansas Public Service Commission (APSC) has initially ordered a $1m annual increase and in the broader 5-year renewal docket. Recall that based on the most recent commission filings, Mar. 15 is the target date by which the commission expects to rule on both issues. In addition to ongoing discussions at the regulatory level, state lawmakers recently put forward an amendment to the APSC appropriation bill seeking to clarify the netting portion of the FRP statute which with a retroactive application would result in approval of ETR's $67m requested increase for 2021 – note that the posted agenda for AR's Joint Budget Committee meeting on Mar 4 does not include the proposed amendment, suggesting sides have not yet reached a consensus. In our meeting mgmt. did not offer new specifics on progress of stakeholder talks citing confidentiality of the process, *though we note the recent reiteration of the long-term guidance assumes the FRP is renewed for an additional five years, a confident signal despite persistent uncertainty.*

SERI gets a new challenge from AR, LA

The APSC along with its LA counterpart have submitted a rate complaint to FERC alleging that ETR has overcharged its AR, LA, New Orleans, and MS opcos via its Unit Power Sales Agreement (UPSA) with SERI. The complaint alleges $360m of costs that were not prudently incurred were passed on to ETR's customers via the UPSA, resulting in elevated bills in service areas where incomes are below national averages. The complaint further alleges that an $800m uprate project undertaken in 2012 failed to increase the plant's output, further harming customers. Given the recency of the latest filing ETR mgmt. only affirmed that it intends to respond to the complaint through the FERC forum. We note however that the SERI has already been the subject of an adverse ALJ ruling one year ago in its leaseback and FIN-48 proceeding, and this latest complaint threatens to push back de-risking of this situation for months or even years given the busy FERC calendar.

Pref proposal coming in proxy; O&M levers

Mgmt. reiterated its expectation of seeking shareholder approval for a preferred issuance in its upcoming proxy, potentially with a convertible component, though the size of the preferred issuance will not be disclosed until the proxy filing. Further mgmt. affirmed its existing levers for managing different regulatory outcomes, including pension, tax, and interest in the context of its flat O&M outlook (inclusive of normalization of 2020 one-time items). On balance we see some degree of levers around Prefs vs common equity, as well as further O&M levers; we perceive some caution to affirming level of cost opportunities that exist ahead of details on the fate of AR.

Essential Utilities (WTRG)

Robust Muni Opportunities despite DELCORA Hiccups

We hosted our latest meetings with WTRG following their earlier guidance roll forward and recent full year results – and ahead of a potential decision from the PA commission in coming weeks around their pending DELCORA transaction.

After the Delaware County Court of Common Pleas issued an order supporting the pending acquisition of DELCORA by rejecting the county's attempt to block the sale, the county appealed the decision and the ALJ recommended the PUC deny the transaction. Given that there are only four commissioners right now in the state, we could very well see a stalemate or see the commission send it back to the ALJ to reconsider add'l evidence as the company works through their concerns. The company expects the commission to address the transaction on either March 11th or March 25th – with the latter seemingly more likely. We stress that the equity doesn't need to be pulled until August if there is a slight delay in the transaction.

Discussions further highlighted potential for muni opportunities to arise out of the pandemic as budgets are further pressured. The company has already outlined $420Mn in rate base opportunities from signed APAs that should generate ~$21Mn in earnings, with announcements of further deals seemingly on the horizon. Following the adoption of Fair Market Value legislation in TX and VA, the company now has the constructive legislation in all eight states of their water footprint. While their water biz has a footprint in TX, the company has noted no material financial impact to the water biz and no financial impact to the recent cold weather events for the gas biz given the location of their operations.

We reiterate our Buy rating on shares, seeing value relative to AWK and longer term re-rating potential as management continues to perform and drive incremental growth through municipal acquisitions.

Eversource Energy (ES)

Offshore Prospects, CT Troubles, and Confidence in Plan

Latest discussions with ES echoed earlier commentary from Orsted around the improving BOEM landscape under the Biden administration – with the company optimistic around a pending schedule from the agency. Despite latest competitive pressures materializing – and particularly evident in the recent NY award with ES not winning any of the ~2500MW – ES continues to have plenty of spare capacity for additional projects and we look towards upcoming RFPs across their footprint. We could yet see further potential tailwinds arise from add'l legislative efforts, with the Clean Future Act the latest push at the Federal level: Similar to earlier developments around tax credits, any further benefits would flow through to ES/Orsted since they don't have flow backs with their customers for the currently contemplated project (contrasted to Ocean Wind with PEG). At the state level, we continue to watch climate policy in Massachusetts legislature and potential for incremental offshore wind targets: we see potential for another 1600MW RFP for offshore wind and more utility owned solar to pass in the next several weeks.

Recall with full year results, the company firmed up their capital plan and noted expectations to be in the upper half of their previously announced 5-7% core regulated CAGR longer term. Annual spend of $275Mn related to Columbia Gas exceeded our expectations and helped drive an 8% consolidated rate base CAGR through 2025 - and latest discussions continue to suggest integration of the acquisition as going well. We view additional ramp in spend at Columbia Gas as just one of the potential upside levers to the formal plan in addition to AMI and EV projects that could materialize. While we continue to await further developments of offshore awards and more granular timing, we expect the projects already awarded to take management comfortably above the current growth rate as they start to come online. While we still see challenges in CT the biggest risk, we perceive a relatively improved environment since late last year and continue to monitor ongoing dockets.

Bottom line, we see risk/reward as balanced. Maintain Neutral.

FirstEnergy (FE)

Deal on rate case appears a unique angle to watch

Mgmt appears keen to resolve its regulatory issues swiftly. What is remarkable to us is the potential to file a rate case either by '24 or even prior – but with mgmt. quite confident that the downside can be limited to just 10c (vs the much more meaningful step change we had been contemplating). It would appear the difference relate to the actual book equity of the Ohio utilities relative to use a hypothetical capital structure. Should mgmt. prove able to reset its rates (risking just -10c-ish) we see this as a uniquely constructive outcome to de-risk the backdrop for the utilities. We see potential further de-risking of shares to enable further re-rating despite the positive improvements already. The question remains just how and whether an (accelerated) rate case would be agreed to given the litany of parallel dockets underway. We view the company as still sincerely interested in pursuing further opportunities to de-risk the backdrop rapidly and come to conclusion around a range of dockets opened up in the wake of bribery investigations.

Asset sales: not so much?

On balance we do not see asset sales as much of a priority considering the tax leakage and relative size of cash needs. We suspect converts and other such structures appear preferable despite being open to sales processes. We see limiting dilution to shares at current levels as a key priority for mgmt.

Greater transparency with AG deal and further steps taken

Our discussions focused around FE's continued steps toward improving transparency and company culture. After FirstEnergy reached a deal with Ohio AG Dave Yost to forgo decoupling revenues, they took this a step further on their earnings call by also choosing to forgo LDR (Lost Distribution Revenues) benefit. Combined, this led to a -15c impact to '20 earnings. With the likely replacement of HB6 perhaps with legislation similar to HB10, we note no provision for LDR in the current pending bill. Mgmt highlighted that per its SEET filing, Ohio ROEs average at 7.6% for 2020 (10% for OH Edison, ~4-5% for CEI and Toledo), relative to 11.9% in 2019. The two main drivers for the decline include the collection of DMR revenues (excluded from '20) as well as the LDR-related charge taken in 2020. With no LDRs in '21+, mgmt would expect ROEs to be as similar ~7.6% levels going forward. Deconsolidation for the SEET threshold is still in pending legislation (passed by Senate thus far), although even Ohio Edison is still well below the SEET threshold (~17-18%) at ~10%.

Internal investigation remains ongoing, but minimal news of late appears pos

With recent 10-K disclosures of 'immaterial' transactions around improperly charging customers, mgmt noted that they have been in discussions with multiple states around addressing these issues and see minimal risk. Otherwise, we have seen minimal announcements and we view this as a positive, although the internal investigation is still underway with an ongoing DOJ investigation. FE is working to address liquidity issues with its FE Forward program potentially bringing cost reductions through O&M and capex efficiencies in addition to broader company transformation over a multi-year period. Further, equity issuance in 2022/2023 could potentially be used as a source of funds to finance a potential penalty (admittedly this longer perceived timeline brings some concerns around length of the federal investigation).

Hannon Armstrong (HASI)

A new era of growth, with further programmatic deals anticipated

With a recently announced 7-10% 3-yr EPS CAGR (up from the prior 2-6% through YE-20), discussions focused on the opportunities ahead given an expanding renewables outlook. Mgmt reiterated strong relationships with its partners Clearway and Engie, emphasizing the close collaboration as well as opportunities for further transactions, particularly given HASI's historical preference for programmatic deals. We expect that these meaningfully sized partnerships could provide Hannon with even further visibility to continue to expand its already robust pipeline That said, while 2020 was a successful year with $1.9bn originations, we expect that $1.0-$1.5bn will be a more normalized run-rate, although we could see upside to investments from an expanding $3.0+bn pipeline. We emphasize that mgmt did not reduce guidance in response to the ERCOT weather event. After assessing the situation, HASI determined that impact was likely minimal and any potential losses would principally be tied to force majeure disputes in the event that facilities were unable to operate. That said, given their preferred equity seniority, mgmt perceives a minor impact to returns over a 20-30 year life. HASI continues to be comfortable with achieving a portfolio yield in the ~7% range.

Mgmt expects leverage to stay in the 1.5-2x range for a period. Although the company's advocacy for an IG rating remains ongoing, it is not a key focus vs. other priorities (given relatively open access to capital markets). We note that mgmt recently amended its ATM equity issuance program, raising it to $500mn from the $350mn from May 2020.

Energy efficiency poses a strong opportunity

Under a Biden administration, we continue to see energy efficiency as an opportunistic growth sector for HASI (which had historically been a key component of earnings growth in the past). Notably, the ESPC program under Obama was expanded twice through executive order, and we see likelihood that Biden could take a similar approach to supporting this program, sometime this year, thus presenting a significant potential opportunity for Hannon. Additionally, we see federal procurement of renewables as another key area of growth, with currently only ~10% of the federal government's procured electricity sourced from renewables. We see the possibility of a new target set for ~35% procurement by 2030+. Finally, a carbon tax also remains on the table, although seemingly less likely than other options.

What to expect on REIT status?

An ongoing point of discussion appears to be the ability of HASI to maintain its REIT status given its increasing focus toward resi solar and other renewable equity stakes. While HASI remains confident in their REIT status over the next three years, they have stated that they see multiple paths ahead and would consider scenarios in which they are not a REIT if it were to mean additional investment opportunities. This remains a low probability event. That said, if Hannon were to go this route, we would expect them to disclose this shift well in advance, with a substantial amount of planning and discussion with agencies.

Tightening resi solar returns – in-line with SPWR commentary

In terms of the resi solar project equity financing business, mgmt expresses that its initial entry into this space was well-timed with much higher returns and particularly attractive rates given its ability to finance mezzanine debt (SunStrong JV with SPWR). That said, HASI mgmt acknowledges that its resi solar portfolio as well as resi solar industry broadly has matured, particularly with the latest economic downcycle and proven asset performance, though resi solar assets remain very much in the money with a lot of value in yield for prior deals still.

As such, HASI expresses that ability for future resi solar biz is more challenging as returns are less attractive from a yield perspective, particularly as resi solar service providers such as RUN can issue corporate capital at extremely attractive spreads rather

than needing project equity from a provider such as HASI. Nonetheless, HASI expressed that its SunStrong JV with SPWR will remain a good source of ongoing business given that it is more of a relationship than one-off project equity transactions. All-in, HASI expressed resi solar is not yet a point where this biz is not attractive at all, though acknowledging returns have definitively tightened – ultimately expect slower LT growth in resi solar (mostly ongoing basis with SPWR) for HASI but emphasis on ability to focus on other asset classes given diversified approach.

NiSource (NI)

2021 guidance has upside and affirmed with PA order

NI mgmt. reaffirmed '21 guidance today with the PUC order on Columbia Gas of PA's (NI Subsidiary) pending rate case, where the PA PUC granted a $65.2m rate increase with 9.86% ROE vs NI's original request of $100mn/10.95% ROE – in-line with previous guide and plan. We continue to think that NI appears among the few remaining utilities with material COVID latitude built into '21 guidance. That said, the company expects things to return to normal in 3Q21 with a vaccine in place. 5c is upside to this year should impacts be less than perceived and remains upside to the LT guidance range.

Financing coming soon; talking down portfolio optimization

On financing, the company plans to issue total amount of $600m to $1bn hybrid in 1H21with equity content at 50% or greater, we look to see updates in coming couple months. This will help dictate remaining equity needs in plan depending on size. On portfolio optimization, mgmt. seemed to talk down this angle given considerations on NIPSCO electric with its gas LDC. While not explicitly expressing a preference, we see somewhat less an emphasis on this for now.

ONE Gas (OGS)

OK regulatory asset order approved, but still waiting on recovery framework

Mgmt. highlighted it received the order to defer costs into a regulatory asset in OK (as well as in TX and OK). Mgmt. highlighted that hearings last week with executives didn't provide much info given the focus on outages, and did not seem to indicate any lessons learned. The company's gas cost estimate of $2.2bn remains a confident estimate. While volumes were higher than curtailments with 3-4BCF from OK and 10-12BCF from TX, we wonder around the recovery construct (mgmt. indicated a return on carrying cost with a shorter collection period vs. typical rate base asset), especially for those customers that did not receive gas (as those that did take on more volume will not necessarily have more of the burden). Given the substantial impact to customer bills and discussions from policy makers around these concerns, we see this likely an overhang on shares until more clarity evolves.

Securitization could be a path: but uncertain

Securitization also remains an option with the session ending in May in TX and OK (KS as well), although here too it remains very early in the process and could be somewhat protracted given subsequent approval required from regulators (assuming a bill is introduced and passed) and the time to get financing in place.

Not yet committing to LT growth rate

While mgmt. did not withdraw its LT guidance range, it did not necessarily commit to the 5-7% given some of the uncertainty. Securitization seems to be the key driver of this, and then otherwise the LT financing plan to help affirm its growth.

PG&E Corp (PCG)

We remain constructive on shares of late as we believe pressures on shares fail to reconcile with the improving regulatory & financing backdrop. On balance, we see an ever growing sense that the securitization outcome could well no longer involve equity at all – reducing key sensitivities around dilution. Moreover, don't expect equity should shares remain at their

current levels finding other alternatives. We don't look for any further capex updates in the near-term after a meaningful series of unveils with 4Q; also don't look for mgmt to pursue Preferreds akin to EIX given their commitments to existing capital structure between debt & equity.

Enhanced oversight enables Safety cert and improved trust

Mgmt continues to emphasize the point of further trust and coordination between the CPUC and PG&E as the enhanced oversight requires regular 90-day update on progress towards milestones. Overall we sense continued improvement among parties.

Defining equity needs and the customer rate impact

Mgmt. initiated EPS growth of 10% from 2021-2025, which embeds the equity needed to fund growth/additional spend in plan; we estimate this to be ~$200mn/yr likely though an ATM. Mgmt. confirmed 52% of the $2bn in additional spend to be a reasonable proxy. Additionally, mgmt. narrowed its 2021 equity needs to 0-$400mn (from prior $450-750mn) following recent asset sales agreement of $954mn, and highlighted potential to reduce those needs further (potentially to zero) with a successful resolution of its alternative proposal in the securitization filing. Further, the company highlighted additional asset sales that could be utilized to reduce the customer rate impact given items such as O&M on wildfire spend likely out of its control. This includes non-core asset sales such as undeveloped land (1/3 customer, 2/3 shareholder mix), developed properties (customer benefit), Hydro generation assets (although likely smaller in size given age, at least NT), and real estate (large building in Oakland, for instance). We continue to see ability to strip costs out of the business and other forms of solutions to reduce customer costs as key to gaining comfort in the capex profile and customer rate impact going forward.

PinnacleWest (PNW)

Our meeting with mgmt. of PNW focused on prospects for some form of concurrent recovery of clean generation investment, despite the company's recent capex cut. With the rate case currently in the hearing process we perceive that parties remain broadly opposed to the Advanced Energy Mechanism (AEM) rider as proposed by PNW. Given the need for a recovery mechanism we additionally touched on potential for a subsequent rate case filing including timing and equity needs. Overall we believe that PNW shares will remain under pressure until a proposed order is issued by the ALJ (the next concrete data point) and potentially beyond, given the broad perception of a cautious outlook in the current case. Maintain Underperform on PNW.

Renewable rider not likely despite lower capex

PNW's recent Q4 update included a resetting of its 3-year capex forecast including a reduced Clean Generation bucket owing to mgmt's assessment of the likelihood of inclusion of its AEM proposal. We note that during the hearing phase the bias across a majority of stakeholders appears to still oppose the proposed AEM, though staff has suggested potentially utilizing an existing renewable tracker instead. We expect this is likely an interim proposal as PNW's AEM was originally intended to provide not just for recovery of renewable investment, but also funding of the Coal Community Transition (CCT) program and consolidating several existing trackers into one mechanism (as requested by the commission). While the ultimate outcome remains unclear we believe that for the purposes of this rate case the bias remains against approval of the AEM, while longer term prospects are more constructive given state decarbonization priorities. Recall that PNW also increased its targeted level of transmission and distribution capex in the near term in order to accommodate its projected customer growth – we expect that the near-term capex shifts have shifted a greater portion of clean generation spend into future periods (including the second half of the decade).

Reliability will drive generation additions, coal shut downs

Despite its service territory being near both CA and TX, jurisdictions which have dealt with significant electric reliability issues in recent months, PNW mgmt. reiterated the company's commitment to retire the last of its coal burning fleet by 2031. Recall that on Day 1 of our conference we heard from several management teams who alluded to the possibility for keeping some coal assets operating in a peaking or seasonal capacity in order to ensure reliability – this does not to be a strategy contemplated by PNW beyond its current 2031 targeted date for exiting coal.

Commission legislation not likely to have near term impact

Pending state legislation intended to give lawmakers the authority to regulate generation resources has proceeded through party line votes – PNW mgmt. indicates it sees a likelihood of the legislation being signed in to law by the governor. Mgmt reaffirmed its commitment to the company's long-run decarbonization plan and maintains that other than clarifications on the bill's language regarding the procurement of lowest-cost resources, the bill as written should not have a near term impact or alter plans to reduce CO_2 emissions over the long run. Importantly under the legislation the authority to set electric utility rates is not addressed and remains under the sole discretion of the ACC.

Public Service Enterprise Group (PEG)

Scarcity value from T&D-only biz remains the key to upside

With PEG's non-nuclear asset sales progressing and initial interest received for both the solar and the fossil portfolios, we increasingly stress the scarcity value to be obtained from a standalone T&D (admittedly with offshore stake). With NRG's East/West asset sales attracting a 4.3x EV/EBITDA multiple, we perceive some investor concern on merchant gen multiples, even after considerations of fleet quality. That said, we continue to see an ESG premium warranted from a standalone utility biz. Our discussions indicate that PEG is likely still on track to complete sales by its targeted '21 timeline. What appears clear is that the cost dis-synergies contemplated by mgmt. appear to be on track to be offset by this transaction.

What to do with the nuclear portfolio? Changes to ZEC structure & spin/sale too

With nuclear to be the remaining assets in Power (aside from offshore wind, with much longer '24/'25 timeline), mgmt discussed a three-step plan for its approach to these assets. The ZEC (zero emissions certificate) 3-yr extension application is ongoing, and we largely expect the existing $10/MWh economics to be extended given the backdrop of falling power prices. That said, PSE&G continues to see a 3-yr timeline as insufficient with regard to making decisions about its nuclear fleet.

The next step post-ZEC decision (still expected late April) will be to secure the long-term economic viability of the nukes, most likely via special-purpose legislation in NJ (as opposed to less likely options such as federal action or state FRR election, which may ultimately be too cumbersome). *On balance, the 3-year review cycle putting ZECs at risk appears ill aligned with long-lived nature of assets.*

Finally, PEG would be open to selling these assets given the perceived investor benefit of divesting of generation assets. We stress a spin or sale of these assets would truly unlock its embedded scarcity value as a pure-play listed electric & gas LDC with no generation.

LIPA: yes, scrutiny again – but what will happen?

We stress that ongoing challenges in New York cloud the fate of its service agreement to operate LIPA. While the agreement remains for a further six years, we see some potential for reducing the scope of its involvement over time should the state deem its operations as inadequate from last year.

Utility biz strength with largely unchanged rate base CAGR

As the focus increasingly turns to utilities (with ~90% of earnings to come from PSE&G post-asset sales), we highlight PEG's recently updated rate base growth of 6.5-8% off a new 2020 base of $22Mn is relatively in line the prior 7-8% on a pre-rolled forward basis. PSE&G also recently updated its 5-yr capex forecast to $14-$16Bn for '21-25, with confidence by '25 on CEF-EE and GSMP extensions at least at current levels.

With NJ BPU transmission ROE negotiations ongoing, mgmt provided minimal update on negotiations (with transmission ROE change not factored into 1Q21 guidance at a minimum, giving some expectation of timeline for resolution) but we perceive the recent JCP&L settlement at a 10.2% stated ROE (incl. adder) as a positive sign that should guide resolution with others including PSE&G. As a positive, the company plans to finance its capex plan and planned offshore wind investments without the need to issue any equity. LIPA impact in aggregate is estimated to be minimal at roughly -5c/sh.

Further offshore wind opportunities

With PEG's recently confirmed agreement with Orsted to acquire a 25% equity interest in the 1.1GW Ocean Wind project, we still highlight limited contribution on an NPV basis to our SOTP at < $1/sh (no buy-in disclosed), although EPS profile could be upfront-biased. Mgmt noted clear interest in evaluating further opportunities in NJ as well as MD. Recall that Orsted has submitted a bid through Ocean Wind 2 for NJ's second

offshore wind solicitation of up to 2400 MW. While PEG has not directly entered into the bidding process with Orsted, we see it as likely that Orsted could offer to PEG at a later point a JV agreement akin to the one at present.

Spire (SR)

Spire represents the silver lining to gas LDCs relative to Texas events having invested in gas storage assets in the Southeast earlier, when they proved quite out of favor.

Gas LDC biz impact minimal; Gas marketing and off system sales big positive
Mgmt. highlighted that it would expect to use its typical Purchase Gas Account mechanism to recovery the fuel cost from the Texas winter event (with it mostly isolated to W. MO). While it did not specifically quantify the impact, we estimate this in the $200-400mn range; we view this as a clear positive given peers that experienced costs in the multi-billion dollar range and does NOT need securitization/amortization of regulatory asset with the latter that would impact customer bills more meaningfully. In terms of the impact on the gas marketing side, mgmt. is still working through the details although was clearly a beneficiary given the physical flow of gas on its storage assets in the MidCon, Texas, and Gulf. While difficult to quantify the impact, mgmt. highlighted that at a minimum it should reduce future equity needs (currently $100-150mn/yr). The company was also able to benefit on the gas utility side through off system gas sales, which should be a benefit to its gas customers. At the end of the day, we see SR as having a constructive set-up and would expect upside to both '21 guidance and the LT EPS trajectory.

Sunrun (RUN)

Strategic thoughts – but remaining focused on VSLR integration near-term
In light of continued strategic developments across resi solar sector, including peer NOVA (with SunStreet) and ENPH (software tuck-in acquisitions), RUN mgmt provided its perspective on strategic thoughts, emphasizing that it will look at companies that can add significant value to what RUN does in particular in being able to add meaningful capabilities from the acquisition of a leader in the space (as with the VSLR acquisition). Indeed RUN highlighted its past acquisitions having provided it with its Direct Biz capabilities, value for channel partners, proprietary racking technology, and digital lead generation. Specifically, mgmt expressed that RUN will evaluate any potential opportunity that provide bolt-on capabilities. While peer NOVA has expressed that it will remain tech hardware agnostic, RUN expressed that if there were a company that was also a product hardware OEM that mgmt perceived to be strategically important – it would be considered, noting that RUN has acquired a resi solar racking company in the past. Nonetheless, RUN mgmt emphasized focus on organic growth as well as continued integration of VSLR (post acquisition in FY20) – but continues to monitor M&A opportunities.

With the significant attention on cleantech from SPACs of late driving heightened public market activity of late, RUN mgmt expressed its view that sellers would perceive it as a desirable buyer in being able to further value by integrating with the leading resi solar and storage company (no SPAC 'finder's fee' either), though acquisitions are case by case in most suitable buyer (in going public via SPAC vs. strategic acquisition).

Storage inflection through '21 with >100% y/y growth guide
With its latest 4Q20 update, RUN notably guided >100% y/y increase in new storage deployments (~12-14K by our estimates) relative to its cumulative base of 16K storage systems, emphasizing that it is less impacted by higher storage cycle times (relative to solar) vs. long-tail installers given its acute focus on training installers for years within its Direct Biz. Mgmt expressed that FY21 storage guide is constrained by supply still given substantial consumer demand. That said, mgmt expressed being multi-sourced (TSLA and LG) helps with additional supply support from products from high quality

manufacturers near-term in the pipeline (for qualification to approved vendors list, expect ENPH and SEDG given existing relationship on inverters)

Mgmt highlighted significant demand from TX with latest cold snap outages, particularly as its solar+storage customers have been able to stay online with power through this period. RUN expressed it was already in the process of expanding in TX (San Antonio in particular) prior to event driven outages and expects strong traction here. In other markets, RUN expects continued geographic expansion growth organically, which includes working with channel partners/dealers.

Policy-wise, mgmt expects a stand-alone storage ITC as likely given case for meaningful value to the grid from a resiliency perspective for incremental storage assets.

Grid services – potential to expand/partner and further add to network effect

For grid services, RUN mgmt expressed that it would consider expanding beyond PPA/lease assets it owns on B/S to customers that purchase solar+storage via RUN or channel partners (where RUN still provides warranty and servicing) through cash/loan, with enrollment bringing more assets to its partnerships to deliver against its growing grid service contracts (12 awarded already currently). Additionally, mgmt acknowledged that it could potentially partner with product OEMs – here ENPH expressed it could provide customers with ENPH systems that use its app an opt-in option where it could then work with a partner to manage the grid services (such as RUN among others) This would still add $2K NPV per customer on grid service margin even if not a RUN originated or owned system.

Shift towards whole home energy – multi step approach in adding value

Beyond expansion from solar into storage, RUN mgmt expects trends to continue towards whole home energy/power – a focus are for its JV with SK. RUN mgmt expressed a multi-step approach - first electrifying more of the home, for instance electric appliances that have advanced significantly (smart water heaters, electric cooktops, etc) as well as EV additions. This creates more home electric load supporting greater sizing for home solar and storage, with saving potentially paying for much of the improvements. Smart devices such as thermostats (CFO experience as prior CFO of Nest) to support coordination of home DERs as well.

From a grid services perspective, solar+storage is the easiest to dispatch though RUN CFO emphasized experience doing this with thermostats at Nest. Key to consider here is finding the right balance between capacity for grid relative to home owner experience in properly coordinating between loads in home.

Vistra Energy (VST)

We see shares back at among their cheapest levels in the shares history – and at implied multiples that appear akin to the lows since 2008 despite the wider market backdrop. We reiterate our expectation for some degree of reform to materialize. We're surprised by continued fade in shares despite clear market focus on 'reform' and mitigating the supply impacts from recent impacts once more.

Presenting the upside case for market reform

Our discussion principally centered on market reform opportunities following the latest ERCOT severe weather event. With VST and NRG both presenting options to the TX legislature, we see VST as advocating a number of key changes. First, mgmt sees a need to address current market design, with a more defined reliability standard e.g. resource adequacy with potential for higher reserve margins, whether for dispatchable assets or all assets, or with potential changes in the ORDC curve. The question will be whether it makes sense to reduce the $9,000 price cap currently in place. While power forwards have been up of late, it is unclear how much of this can be attribute to likelihood of ERCOT market reform. Other options discussed have been improved coordination

between constituents such as natgas, power/retailers, and TDUs. A re-pricing scenario is also a point of discussion, although we see this as a lower likelihood option.

Nuances to watch in the market reform discussion: Not all reserves are created equal; look for discussion of dispatchable and un-dispatchable resreves each; also look for changes to the ORDC curve of late too. On balance, we stress how quickly ERCOT moved through its reserves was a key point of focus coming out of the events. However we do not see a capacity market as still in the cards. Rather, energy market reforms are the focus.

How much of the $900mn-$1.3bn impact can be mitigated?
With VST's plants largely winterized, mgmt emphasized their resilient business model over the long term with minimal changes necessary despite this one-time event. Notably, as VST had stated previously, the key driver of the $900mn-$1.3bn in estimated losses stemmed from gas suppliers declaring force majeure (*all of them appear to have done so).* While VST emphasized that they feel comfortable on being able to stay within this range on ultimate expected losses, the key question will be how much upside could be achieved in reducing this figure by disputing suppliers' force majeure claims. Separately, we see exposure to ERCOT default allocations as minimal given VST's 6-7% market participant share, in addition to $2.5mn monthly maximum allocations instituted by ERCOT for payments (with an event of this magnitude not previously considered, changes may need to be made).

Still see resilient integrated biz, despite it all
We continue to see a resilient integrated business model with a solid retail book backing the existing generation assets, and reduced earnings volatility aside from the latest event. It will be critical for mgmt to prove out guidance for long-term ~2% EBITDA growth. While VST mgmt made it clear that retail customers would not bear the impact of the February event, we stress that we continue to see a long-term trajectory of improving margins for the company, driven from a variety of angles including ability to capture some benefits from hedging strategies as well as cross-selling and add-on products and services. While questions had arisen of potential retail consolidation with the exit of smaller players, it now appears that this is less likely given the load curtailments seen during the TX Feb event.

What does winterization look like? Costly
Seems principally tied to coal handling systems at coal plants – costing upwards of $50-100 Mn. The question is whether this mandate for winterization will be funded in any explicit way in coming weeks. We suspect investing this level of capital back into coal assets is likely quite challenging to justify under any range of contexts. On balance we perceive few companies as poised to act substantively on winterization of their assets.

Xcel Energy (XEL)

Our update with XEL mgmt. focused on the recent announcement of transmission expansion projects in CO, with $700m of upside to the current plan through 2025, an additional $400m through 2027, and a further $1B of potential incremental investment, among the more ambitious transmission expansions recently seen across our coverage. As expected mgmt. reported that the CO ALJ recommended against the adoption of the wildfire rider while otherwise affirming recovery of wildfire mitigation spending through a reg asset. The proposed CO clean generation plan represents upside beyond the current plan through 2025 though includes a meaningful runway of generation investment. Maintain Neutral on XEL.

$2B transmission upside in CO; resource spend in '25+

The proposed transmission expansion plan calls for $1.3B of investment in 560 miles of 345 kW lines and several new and expanded substations in XEL's CO territory, supporting the buildout of over 5 GW of mostly renewable generation capacity (~4 GW rate base wind and solar, 1.3 GW distributed) as proposed in the recently filed resource plan for the state. While the investment in new generation build is targeted for beyond

2025, the supporting infrastructure buildout represents $700m of upside in XEL's current capex plan through 2025, as well as an additional $400m in the 2026-27 timeframe. A further $0.5-1.0B of incremental opportunities including network upgrades and interconnection work has been flagged but will depend on the ultimate mix and location of resources deployed. While the topic of expanding investment in transmission is not new in our coverage (and indeed has been gaining traction given expectations for infrastructure legislation at the federal level) XEL's update represents one of the more meaningful upticks in transmission investment of late. We note that as this proposal is entirely within Colorado, filings and approvals are at the state level, further reducing the regulatory burden. *On balance look for a constructive 1Q update.*

Rate case looking more likely following wildfire rec

The CO administrative law judge (ALJ) issued an order opposing XEL's proposed wildfire recovery rider which would have allowed for concurrent recovery of wildfire mitigation investment in the state through 2025 as drafted. While rejecting the rider, the ALJ recommended adoption of the investment plan ($325m) through 2025 with a proposed deferral of prudently-incurred spend for recovery in a future rate case. While mgmt. had previously indicated that the wildfire rider outcome is not in itself a driver of whether the company will elect to file a rate case in CO, XEL now expects to make a filing around mid-year.

Fuel cost impacts subject to recovery

XEL mgmt. estimates its incremental fuel costs stemming from severe weather across the country at $1.2B driven by spiking spot gas prices over a several day period. Mgmt. expressed confidence in achieving full recovery and expects an extended recovery period in order to mitigate the impact on customer bills. Based on preliminary calculations, XEL sees a per-customer impact of $250-300 across most of its jurisdictions, suggesting a $10/month or higher individual bill impact assuming recovery is spread over 2-3 years. Mgmt. maintains that its internal hedging policies were followed across all of its jurisdictions and does not expect any incremental impact on future rate case filings given what will likely be meaningful rate pressures in the near term.

Exhibit 1: Stocks mentioned
Prices and ratings for stocks mentioned in this report

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
AEE	AEE US	Ameren Corp	US$ 72.52	A-2-7
ATO	ATO US	Atmos Energy	US$ 90.87	A-1-7
BKH	BKH US	Black Hills	US$ 60.73	B-1-7
CWEN	CWEN US	Clearway Energy	US$ 27.94	B-1-7
CWENA	CWEN/A US	Clearway Energy	US$ 26.09	B-1-7
CMS	CMS US	CMS Energy	US$ 54.91	B-1-7
D	D US	Dominion Energy	US$ 69.53	A-1-8
DTE	DTE US	DTE Energy	US$ 120.65	B-1-7
DUK	DUK US	Duke Energy	US$ 88.61	B-2-7
EIX	EIX US	Edison Intl	US$ 56.27	B-1-8
ETR	ETR US	Entergy Corp.	US$ 87.95	B-1-7
WTRG	WTRG US	Essential Utilities	US$ 41.95	B-1-7
ES	ES US	Eversource Energy	US$ 79.15	B-2-7
FE	FE US	FirstEnergy	US$ 33.45	B-2-8
HASI	HASI US	HASI	US$ 53.95	B-2-7
NI	NI US	NiSource Inc	US$ 21.81	B-1-7
OGS	OGS US	ONE Gas, Inc.	US$ 70.60	A-2-7
PCG	PCG US	PG&E Corp.	US$ 10.75	C-1-9
PNW	PNW US	Pinnacle West Capit	US$ 75.02	B-3-7
PEG	PEG US	Public Service	US$ 55.10	B-1-7
SR	SR US	Spire	US$ 68.56	A-1-7
RUN	RUN US	SunRun	US$ 53.82	C-1-9
VST	VST US	Vistra Energy	US$ 17.08	B-1-7
XEL	XEL US	Xcel Energy	US$ 59.34	B-2-7

Source: BofA Global Research

BofA GLOBAL RESEARCH

Price objective basis & risk

Ameren Corporation (AEE)
Our $76 price objective is predicated on a P/E based sum of the parts, valuing each business subsidiary relative to the 2023E ratebase weighted peer multiple of 15.9x for electric. We apply a 1.0x premium to peers at AEE Missouri to account for the improving prospects of capital spend, supplemented by a regulatory jurisdiction becoming more favorable - but lack of decoupling. We apply a 1.0x premium to peers at AEE Illinois to account for decoupling on the distribution business which aids in earnings predictability. The overall business is expected to grow at a more meaningful clip than that of peers - we see a 10% EPS CAGR at IL 2020-2024. At ATXI, we apply a 1x premium to peers to reflect the FERC ROEs. At the Parent, we assume 1x multiple premium reflecting average of the subs and given the healthy debt metrics with FFO/Debt at 17%+. Electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. The upside (downside) risks to our price objective are the utilities earning their allowed returns or better (worse), a significant increase (decrease) in 30-year U.S. Treasury bond yields, and positive (adverse) regulatory outcomes that could impact mgmt's ability to earn its allowed return

Atmos Energy Corporation (ATO)
Our $99 PO is based on our 2023E sum-of-the-parts (SOTP) analysis, based on the gas LDC peer group multiple of 14.1x. Our gas peer P/E multiple is grossed up to reflect the group's 5% CAGR to reflect capital appreciation across the sector. We then apply a 3x premium to the base gas LDC multiple to reflect the high-quality nature of the assets given a sustainable runway for capex/EPS underpinned by constructive regulatory mechanisms and jurisdictions. For the Pipeline & Storage segment we apply an 8x EV/EBITDA multiple as a base to our '23E EBITDA. We then apply a 2x premium to the assets given their fully regulated nature and unique ability for APT to benefit from the spread differentials.

Upside risks: 1) improving regulatory relationships, 2) decrease in interest rates, 3) incremental capital spending, 4) constructive rate case outcomes, 5) less equity needs.

Downside risks: 1) deteriorating regulatory relationship, 2) increase in interest rates, 3) less or deferred capital spending, 4) poor rate case outcomes, 5) more equity needs.

Black Hills Corporation (BKH)
Our $68 PO is based on a SoTP valuation. Gas Utilities: We apply the 14.7x peer P/E multiple on 2023E EPS. Electric Utilities: We apply the 16.2x peer P/E multiple on 2023E EPS. Both electric and gas peer P/E multiples are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. Coal Mine: We apply an 8x peer EV/EBITDA multiple, which is in line with other PRB coal producers. Based on our view of the strength/maintainability of different coal plant output contracts, we apply a discount/prem multiple to that portion of the mine. IPP Assets: We use the recent sale price and '23/EVEBITDA multiple for Pueblo Airport and Wygen I assets, respectively. Parent Expense, Debt, and Eliminations: We apply an average regulatory P/E multiple to this segments income. This captures some Interco revenues that are double counted as well as parent SG&A drag and debt.

Downside risks: operational errors, increasing interest rates, and difficult regulatory environments.
Upside risks: favorable weather, favorable regulatory outcomes, higher capex deployment

Clearway Energy (CWENA / CWEN)

Our $38/sh PO is based on 75/25 weighted Growth/DCF methodologies. Our Growth value is $42 and our DCF value is $27.

In our DCF, we discount the current portfolio's expected cash flows. Main assumptions include:
- Our cost of equity applies a 1.50% yieldco premium to the 1.87% 30-yr Treasury
- Outstanding corporate debt is refinanced at maturity with amortizing debt with an eight-year term

Main assumptions under our drop-down approach are:
- 1,200 MW of assets are dropped down
- A target payout ratio of 80%
- A 3.8% required yield based on the 2021E dividend yield for the YieldCo peer set.
- A 0.25% premium for CWEN to the yieldco peer yield in our base case as prospects strengthen around the validity of the PPAs which are tied to PG&E

Risks are 1) misalignment between the new sponsor and the company's growth strategy, 2) the inability to purchase high-quality assets at accretive multiples, 3) the failure to successfully develop projects, and 4) the inability to access capital markets at attractive terms 5) PCG related counterparty exposure is among the nearest exposures to watch.

CMS Energy (CMS)
Our PO of $65 is based on a SotP relying on 2023E forward P/E multiples for the utility and banking business and a 2023E forward EV/EBITDA multiple for CMS' IPP assets. For the utility seg we apply a 4.0x prem to the avg regulated multiple P/E of 16.2x for the electric seg and of 14.6x for the gas seg, with the 10-yr capex update providing clear sight on ratebase growth and further upside, as well as cont'd favorable regulatory environment, and finally historically proven ability to consistently perform at the high end of guidance range. Both electric and gas peer P/E multiples are grossed up to 2020 by 5% to reflect capital appreciation across the sector. For CMS' merchant business we apply a 8x EV/EBITDA multiple, in line with current market value of CMS power plants (specifically DIG), moreover DIG has relatively favorable contracts for the near future which strengthen plant earnings. Finally, we apply a 15.5x P/E multiple on CMS' consumer lending subsidiary Enerbank, in line with forward P/Es other smaller regional banks with similar growth profile.

Risks are: 1) earned ROEs declining which reduce CMS utility earnings 2) execution risk on capex and cost cutting which would primarily affect the utility earnings, 3) negatives changes to market energy prices which could affect the DIG plant's ability to re-contract at the assumed prices.

Dominion Energy (D)
We use SOTP to derive our $78/sh PO. Utilities: We value VEPCO at 4x prem multiple to elec. peers of 16.1x '23 P/E and 14.1x w/ 3x prem on our '23E P/E to D's portfolio of gas LDCs (East Ohio, Hope Gas (WVa), and Questar (UT)). Mults are grossed up to by 5% to reflect capital appreciation. We value Wexpro at 10x disc to gas utility peers for declining rate base/ROEs and reg. risks. We ascribe a 3x premium multiple for SCANA legacy utility assets, and a 2x disc. for the NND asset. We also net out NPV of ongoing bill credits. Merchant: We apply an 8x FCF multiple for Millstone and separately apply a 100% wt to our NPV est of the ZCP cash flows. We include the full EBITDA from the contracted renewables with a 11x '23 EV/EBITDA multi w/ 3x prem in line with peers. Cove Point: We apply an NPV approach with to our DCF adjusted for the 50% sell-down in the facility. For remaining debt beyond that allocated to state utilities, we incl a 50% wt towards a str netting of leverage, with the remaining 50% using a P/E multiple on associated interest expense, in line with the methodology employed for more highly levered diversified utilities.

Downside risks: increase in rates, capex below assumptions, unconstructive regulatory outcomes, delays and/or cancellation of key projects vs our expectation.

DTE Energy (DTE)

We value DTE Energy at $133 using an SOTP approach.
We value the utility segment on a 2023E forward P/E multiple basis and the non-utility seg. on a 2023E forward EV/EBITDA multiple basis. For the utility segment we apply a 5x premium to both our reg. electric and gas utility peer multiples (of 16.3x and 13.5x, respectively). Both electric and gas peer P/E multiples are grossed up for a year to 2021 by 5% to reflect capital appreciation across the sector. We subtract out Corp & Other expense excl. interest rate.
For GSP we use a midstream peer group multiple of 9x. P&I, we apply an 8x EV/EBITDA multiple, despite the lower quality of these earnings and opaque disclosures, as mgmt has been able to execute on new project origination. We value the reduced emissions fuel (REF) tax credits separately using a DCF methodology at 6% discount rate.

Upside risks to our PO are capex expansions, higher authorized ROEs, and strong performance in the ET segment. Downside risks are interest rate hikes, execution risk on organic growth initiatives at the nonregulated business, and less favorable regulatory environment.

Duke Energy (DUK)

Our $94 PO is derived from a sum-of-the-parts valuation. We value the Electric and Gas utilities using peer 2023E P/E multiples. We apply a 3.0x multiple premium to Duke's operations in FL and 2x in IN to reflect more favorable regulatory environments (and recent sale valuation marker). We apply a 3x multiple to the Carolinas given upside to spending in improving regulatory construct combined with latest IRP & wider legislative reforms into 2021. We value the other regulated electric utilities at 16.2x and the gas utilities at peer group multiples of 14.7x 2022E P/E, respectively. Both electric and gas peer P/E multiples are grossed up by 5% for the groups CAGR to reflect capital appreciation across the sector. The commercial midstream, and transmission are valued on a 2023E EV/EBITDA basis. We use a 9.0x multiple for midstream and transmission segment. We add the net present value of renewable segment using an 8% discount rate. We subtract out the impact of commercial debt, and add back for the renewable debt.

Upside risks: constructive rate case results, higher capital expenditure additions vs our assumptions, lower interest rates. Downside risks: poor rate case results, operating errors, and negative changes in the regulatory environment, Macro risks: Increases in interest rates and decreases in equity market valuations.

Edison International (EIX)

Our $68 PO is based on SOTP, applying a 4x disc to the FERC and CPUC jurisdictional subsidiaries, and the parent/other segment 16.9x on 2023E (grossed up by 5% to reflect capital appreciation across the sector). The disc reflects CA ongoing wildfire risk despite the improved construct through AB1054. We apply 10x 2023E P/E to the Edison Energy segment to reflect uncertainty in the nascent biz. We net out ongoing contribution to the fund on an NPV basis. We also assume an additional $625mn of equity that we net out of our SOTP at the current share price given uncertainty over timing.

Downside risks: 1) Regulatory outcomes less favorable than expected. 2) Natural disasters or catastrophic events can affect system reliability and are subject to regulatory cost recovery risk. 3) Interest rate risk. 4) Non-reg businesses are inherently more risky and subject to both execution risk and commodity variation. 5) CA has specific risks given the differentiated regulatory regime. 6) CA wildfires.
Upside risks: rate case outcome above what's embedded in companies' guidance and

BofA estimates, lower interest rates, more constructive regulatory / legislative outcomes to address wildfire risk

Entergy (ETR)
Our $107 PO is SOTP based. We assign P/E multiples (peer multiple of 15.9x) for 2023E on most segments, in line with peer multiples (and grossed up by 5% to reflect capital appreciation across the group) due to similar growth, and strip out 50% of the holdco senior notes. The Merchant business is also added as a DCF (10% discount rate, no terminal value). Both electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector.

Downside risks: 1) Regulatory outcomes or earned ROE's could worsen, 2) Rate making mechanisms could change in the future, 3) Failure to get trackers or ROE adjustment mechanisms could hurt realized ROE, 4) weather can affect operations and earnings, 5) Interest rate risk affects cost of capital, 6) Consumer advocates or utility staff may focus more on issues that challenge the company ROE, 7) ETR has had safety issues in the past, which have affected regulatory relationships and company liabilities, 8) Exit from the competitive business could present unforeseen challenges.

Essential Utilities (WTRG)
Our price objective is $49 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. These peer multiples are 25.4x and 14.9x. We apply a 3.0x premium to Peoples Gas given the organic growth opportunities, while applying a variety of premiums to its water (2x previously) subsidiaries: +4x to PA, +3x to IL, +2x to OH, +2x for TX, +2x for OH, and no premium for balance of biz. We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Eversource Energy (ES)
Our sum of the parts based price objective of $89 uses P/E multiples on 2023E earnings. For electric utilities, we attribute a 3x premium NSTAR, 3x premium to PSNH, and in line CL&P to peer 15.9x multiple, reflecting future potential positive revisions to capex and earnings. For gas, we apply a 3x premium to the peer 14.9x multiple, given capex upside particularly in MA and a 2x for Columbia Gas. Both electric and gas peer P/E multiples are grossed up by 5% to reflect capital appreciation across the sector. We value Aquarion at a 1x premium to the 27.9x water multiple. We reflect ES's 50% ownership in Revolution and South Fork offshore wind sites on an NPV basis. We further reflect a devco value with an assumption of an additional 3GW through 2031. We take out 50% of parent debt, and 50% of interest to accurately reflect parent leverage.
Upside risks to our price objective are additional capex announcements on the T&D side, as well as success in offshore wind RFPs.
Downside risks are reduction in authorized ROEs, inability to meet earned ROE expectations, as well as failure to receive permitting on incremental capex opportunities.

FirstEnergy (FE)
Our PO of $32 is based on an SOTP: Multiples are driven by relative P/E premiums/discounts to the 2023E regulated peer multiple of 16.0x. Electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. As for premiums/discounts, we view NJ as at a slight discount -1x given a generally constructive commission despite overhang, PA at -2x as we view our more punitive ests already account for industrial load sensitivity incl O&G royalties, and others as in line. In OH, we apply a -2x P/E discount multiple to account for rate review risk. Finally, we apply a 0x P/E premium to peers 2023E multiple to the Transmission business given some limited ability to invest and FERC ROE difficulties. We removed impact of DMR

payments. We subtract out the holding co debt given the high parent lev. We net out potential liabilities from a potential FES bankruptcy by assuming all known 'extra' potential liabilities.

Downside risks: 1) Reg outcomes may improve/deteriorate, 2) legislative solutions may materialize for challenged parts of biz or FE could lose/fail to gain legislative support in key states, 3) int rates positively/negatively affect cost of cap, 4) reg staff or cons advocates may focus on issues beneficial/detrimental to ROEs, 5) exit from comp power biz may or may not have substantive liabilities accrued to equity holders, 6) negative outcome from any investigations and litigation including the HB6 lawsuit.

Hannon Armstrong (HASI)
Our valuation with a $63/sh price objective using a 75/25 DDM/DCF methodology, with $68 DDM valuation and $48 DCF valuation. For the DCF we apply a cost of equity of 3.0% to value the stream of cash flows from the existing portfolio as well as the growth prospects of the proprietary origination business. We assume a 11.1x P/E multiple on a peer group, with a 5x premium given strong growth prospects vs. peers, including commercial mortgage REITs and business development companies (BDCs).
Our assumptions for 7.7% yield and 3.8% cost of debt arise from analysis of historical and projected portfolio composition (and associated yields by asset class) and expectations for fixed vs. floating rate debt composition.

Upside risks: 1) Origination growth above expectations 2) Acceleration in securitization transactions 3) Dividend growth faster than expected 4) SG&A costs below expectations 5) Faster than expected yield expansion.

Downside risks: 1) Origination growth below expectations 2) Slowdown in securitization transactions 3) Shift towards greater proportion of BTM vs. GC assets may result in drag on portfolio's yield 4) Potential for rapid rise in interest rates 5) Slowing dividend growth may impact relative valuation vs. peers.

NiSource Inc (NI)
Our $26 PO is based on a sum of the parts valuation. We value each gas and electric utility separately using 2023 forward P/E multiples of 15.1 for gas utilities and 15.9x for electric utilities with a 2.0x premium for the electric utility's strong growth rates and incremental renewable buildout with capex beginning in '22, but acknowledge industrial risk. Also, we assign a 3x M&A premium to the VA, KY and MD gas utilities to account for their M&A premium. We note that electric / gas peer P/E multiples are grossed up by 5% to reflect capital appreciation across the sector. We subtract the value of excess holding company debt at the parent not supporting the utility opcos. We believe NI's 5-7% EPS/dividend growth outlook, attractive regulated earnings profile and constructive legislation across NI's service territories are under-estimated given its discounted multiple versus peers.

Downside risks to our PO are a sustained period of economic weakness pressuring customer growth, interest rate increases, high natural gas prices, financing plan updates, unforeseen costs associated with the MA incident, and challenging steel production economics in Indiana.

ONE Gas, Inc. (OGS)
We use a sum-of-the-parts analysis to calculate our $75 for OGS, applying a 23E Gas LDC peer multiple of 14.3x (grossed up by 5% to reflect capital appreciation across the space) with a 1.0x premium to the company's regulated Kansas assets due to upside on earned ROE, and a 2.0x and 3.0x premium for Oklahoma and Texas businesses, respectively, given their location and de-risked nature.

Upside risks: lower interest rates, constructive regulatory outcomes, increased capital

expenditure opportunities.
Downside risks: higher interest rates, unconstructive regulatory outcomes, decreased capex spending, ban on fracking, decarbonization efforts.

PG&E Corporation (PCG)
Our PO of $14 reflects an Electric peer P/E group multiple of 15.5x and gas group P/E multiple of 14.6x (w/ both grossed up by 5% to reflect capital appreciation across the sector) based on 2023E. We reflect a discount on both Electric and Gas group P/E multiple of -5x to PCG shares to reflect a larger fire-prone service territory, lack of dividend payment for 3yr period, and operational risks. Further, we net out the NPV of the ongoing wildfire contribution from valuation. Lastly, we net out 50% weighting of HoldCo debt and add back 50% weighting of interest expense to derive our $14 PO.

Upside risk: Better terms on equity raise or mandatory convert, incremental capex, favorable rate case outcomes, and lower interest rates.

Downside risk: Less favorable terms on further equity raises, selling pressure from unnatural owners including victims, lower capex, triggering the max liability cap for wildfires, unfavorable rate case outcomes, and higher interest rates.

Pinnacle West (PNW)
Our price objective of $74 is based on a peer utility 2023E P/E multiple of 15.8x with a -2.5x discount to account for PNW's risk around its pending rate case as well as headline risk related to disconnect policy review. Electric and gas peer P/E mult is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We ascribe an in-line premium despite clear renewable capex backdrop given ongoing regulatory risk associated with the company's upcoming rate filing and 2020 election risk.

Upside risks: 1) Regulatory relationships/outcomes could improve, including changes at the elected commission 2) load growth in territory above expectations 3) Riders and capital trackers could help achieve ROE 4) positive weather helps earnings 5) interest rate risk changes cost of capital - lower rates could improve 6) Consumer advocates or utility staff could become focused on issues that improve ROE

Downside risks: 1) Regulatory relationships/outcomes could decline, including changes at the elected commission 2) load growth in territory below expectations 3) Riders and capital trackers could hurt ROE 4) negative weather hurts earnings 5) interest rate risk changes cost of capital - higher rates could worsen 6) Consumer advocates or utility staff could become focused on issues that hurt ROE 7) Solar advocates in the state have engaged in public confrontations with the utility, which could change public relations in the future.

Public Service Enterprise Group (PEG)
Our $63 PO is derived from our SOTP valuation. For the electric utility we use a 3x premium to the 15.4x '23E group multiple to value the regulated and parent side of the business. Electric peer P/E multiple is grossed up by 5% to reflect capital appreciation across the sector. For the gas utility we use a 3x prem to the 13.7x '23E peer group multiple. PSE&G has meaningful growth capex planned, and while pressure on earned ROEs exists, the regulatory environment is favorable.
Downside risks to PO 1) interest rate increases, 2) unfavorable regulatory outcome, and 3) weather, all of which could lower PEG's earnings ability, 4) we caution dilutive asset sales, capacity auction uncertainty, and overall power headwinds as potential overhangs on the stock 5) BPU approvals.

Spire (SR)
Our $66 PO for SR is based on a sum-of-the-parts analysis, applying a Gas LDC multiple of 14.3x on '23E with in-line multiple for Missouri, and 2x premium for the

Mississippi/Gulf and 2x for AL assets given their location and de-risked nature (although COVID concerns remain). For the midstream assets, we use a base 8x EV/EBITDA multiple with a 1x premium for the STL pipeline given it is the one of the only new greenfield pipes in-service, a 4x discount for storage given uncertainty, and a 4x discount for marketing due to volatility.

Upside risks: 1) improving regulatory relationships, 2) decrease in interest rates, 3) incremental capital spending, 4) constructive rate case outcomes, 5) less equity needs.

Downside risks: 1) deteriorating regulatory relationship, 2) increase in interest rates, 3) less or deferred capital spending, 4) poor rate case outcomes, 5) more equity needs.

SunRun (RUN)
We arrive at our $95/share price objective as follows. We value the PowerCo portion of the company by taking NPV equal to Net Earnings Assets, equivalent to discounting cash flows from the existing asset by an unlevered 3.5% discount rate (roughly equivalent to 5% levered discount rate). We value the installed assets through 2025 on a DCF basis with cash flows discounted by 5% with an additional 8% discount rate on the NPV given future execution risk. We further include value from solar renewable energy credits beyond the four year contracting window also on a DCF basis at a 12% discount rate. With ITC extension prospects, we value installed assets through 2026 and include a 8x terminal value multiple on 2029 NPV given scale advantages for future growth prospects as a consolidated entity, we weigh '26+ DevCo value at 60%. We lower DevCo value created by annual R&D and non-cash SBC expenses not captured within creation costs and increase value by incremental NPV from storage and grid service contracts. We add value of operational synergies, existing grid service contracts, and upsell opportunities. We attribute credit for 50% of estimated renewal value to reflect incremental customer value.

Downside risks: We see downside risks associated with the ability to meet cost reduction expectations, MW deployment guidance, Net Energy Metering (NEM), debt capital markets given the highly leveraged strategy employed, as well as if the ITC is not extended beyond the current schedule.

Vistra Energy (VST)
Our $20/sh Price Objective is based on a 2021E SOTP valuation. We assign a discount/premium to the peer group EV/FCF multiple of 7.0x for each fuel within each geography, depending on our specific views for the asset type and market: We include the full $275mn of margin-enhancing initiatives as well as $200mn optimization benefits and the $275mn of synergies related to the DYN acquisition. We further capitalize our estimated income tax for the combined entity to reflect the higher tax burden than peers, and we include a $50mn NPV of TRA payments. We reflect accretion from the Moss Landing storage project as well.

Downside risks: 1) declining wholesale power & capacity prices, 2) competitive & regulatory change to retail businesses, principally in Texas, 3) operational issues pertaining to running power assets including Nuclear asset in Texas.

Upside risks: 1) VST may improve its retail margins and retain customers, 2) VST may beat its margin enhancements initiatives, 3) VST may see a decrease in the price of key inputs such as natural gas and coal, and 4) VST may see an increase in wholesale power prices.

Xcel Energy Inc (XEL)
Our PO is $63. We value Xcel Energy using a sum of the parts (SOTP) approach. Given the difference in geography, earnings strength, growth opportunity and risk profile, we divide the segments by subsidiary.

We use 2023E forward P/E multiples to derive a value for the different business segments, including the parent segment. We use a peer multiple of 16.1x . Electric peer P/E multiple is then grossed up for a year to 2021 by 5% to reflect capital appreciation across the sector. We apply a 2x premium to most subsidiaries except in MN where we apply a 3.0x due to additional stimulus upside. We see this multiple as appropriate as the company has growth opportunities, resolving regulatory drag and resolving uncertainty around rate cases. We stripped Mankato as a non-reg asset in our SOTP due to the sale. We also net back 50% of the parent interest expense and instead subtract out 50% of parent debt to more accurately reflect HoldCo leverage.

Downside risks are interest rate increases, regulatory risk such as lower authorized ROEs or less favorable riders/trackers for renewables and transmission, interest rate risk, execution delays, and weather anomalies.

Analyst Certification

We, Julien Dumoulin-Smith and Richard Ciciarelli, CFA, hereby certify that the views each of us has expressed in this research report accurately reflect each of our respective personal views about the subject securities and issuers. We also certify that no part of our respective compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

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North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Enphase Energy	ENPH	ENPH US	Aric Li
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Ormat Technologies	ORA	ORA US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
NEUTRAL				
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Atlantica Sustainable Infrastructure	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	TransAlta Renewables Inc.	YRNW	RNW CN	Julien Dumoulin-Smith
	UGI Corp.	UGI	UGI US	Richard Ciciarelli, CFA
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	Southwest Gas Holdings	SWX	SWX US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	AES	AES	AES US	Julien Dumoulin-Smith

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Alternative Energy Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	5	50.00%	Buy	3	60.00%
Hold	3	30.00%	Hold	3	100.00%
Sell	2	20.00%	Sell	1	50.00%

Equity Investment Rating Distribution: Energy Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	90	57.69%	Buy	69	76.67%
Hold	37	23.72%	Hold	24	64.86%
Sell	29	18.59%	Sell	15	51.72%

Equity Investment Rating Distribution: Utilities Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	80	51.61%	Buy	58	72.50%
Hold	37	23.87%	Hold	28	75.68%
Sell	38	24.52%	Sell	22	57.89%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1863	56.90%	Buy	1185	63.61%
Hold	686	20.95%	Hold	426	62.10%
Sell	725	22.14%	Sell	358	49.38%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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Essential Utilities

Moving Past the Tax: Ever Clearer 5-year Growth View

Reiterate Rating: BUY | PO: 49.00 USD | Price: 43.25 USD

Contemplating the Latest Developments

WTRG reported full year adjusted EPS of $1.58, a penny above our estimate and at the top end of management's guidance. After the earlier roll forward in January, there were limited financial updates with affirmation of 2021 EPS guidance of $1.64-$1.69 and their LT 5-7% EPS CAGR through 2023 – and while their water biz has a footprint in TX, commentary suggested no material financial impact from the recent cold weather events. After previously announcing plans to file a rate case at Aqua PA this year keeping with their three year rate case cadence for their water biz, a verbal settlement has been reached around the catch up component of Repairs tax accounting for the gas biz with plans to give **all** of the tax benefits back to customers over a five year period. While we view the decision to settle the catch up with the full benefit to the rate payers as an incremental drag on our estimates in '23, we expect rate relief in '24 to reaccelerate earnings for the gas segment and **stress their 5-7% CAGR as intact** (w/further upside support from the midpoint still given the robust muni pipeline). Meanwhile, after the ALJ recommended the PUC deny the DELCORA transaction, the commission is expected to make a decision next month: Given that there are only four commissioners right now in the state, we could very well see a stalemate or see the commission send it back to the ALJ to reconsider add'l evidence as the company works through their concerns. While we see some challenges on the margin, we stress the equity doesn't need to be pulled until August if there is a slight delay of the transaction and the robust muni opp's abound.

Valuation: PO to $49; tax noise is over; reiterate Buy

We tweak our model to reflect lower ROEs at Peoples Gas in '23 given commentary around the verbal settlement and the need to file a formal rate case for rate relief - but see '24 as intact when we would expect new rates to go into effect. We update our valuation to ascribe the current utility peer multiples of 25.4x and 14.9x for water & gas, respectively (vs. 27.4x and 14.2x previously). We reduce our premium for Peoples Gas from 3x to 1x given the need for a rate case in 2023 while our water premiums remain unchanged and continue to reflect confidence in ability to consistently deliver, strong muni acquisition prospects, and an underappreciated ESG angle. Our PO ultimately shifts to $49 (from $54 previously). Reiterate Buy given deep discount and muni upside.

Estimates (Dec) (US$)	2019A	2020A	2021E	2022E	2023E
EPS	1.47	1.58	1.67	1.80	1.87
GAAP EPS	1.47	1.58	1.67	1.80	1.87
EPS Change (YoY)	4.3%	7.5%	5.7%	7.8%	3.9%
Consensus EPS (Bloomberg)			1.54	1.67	1.79
DPS	0.92	0.99	1.06	1.13	1.21
Valuation (Dec)					
P/E	29.4x	27.4x	25.9x	24.0x	23.1x
GAAP P/E	29.4x	27.4x	25.9x	24.0x	23.1x
Dividend Yield	2.1%	2.3%	2.4%	2.6%	2.8%
EV / EBITDA*	35.4x	21.5x	17.8x	16.6x	15.3x
Free Cash Flow Yield*	-2.0%	-4.7%	-3.6%	-2.8%	-1.6%

* For full definitions of *iQmethod℠* measures, see page 8.

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26 February 2021

Equity

Key Changes

(US$)	Previous	Current
Price Obj.	54.00	49.00

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Stock Data

Price	43.25 USD
Price Objective	49.00 USD
Date Established	25-Feb-2021
Investment Opinion	B-1-7
52-Week Range	30.40 USD - 51.22 USD
Mrkt Val (mn) / Shares Out (mn)	10,608 USD / 245.3
Average Daily Value (mn)	48.23 USD
BofA Ticker / Exchange	WTRG / NYS
Bloomberg / Reuters	WTRG US / WTRG.N
ROE (2021E)	8.6%
Net Dbt to Eqty (Dec-2020A)	100.4%

ESG: Environmental Social Governance

DELCORA: Delaware County Regional Water Authority

PUC: Public Utilities Commission

ALJ: Administrative Law Judge

iQprofile℠ Essential Utilities

iQmethod℠ **– Bus Performance***

(US$ Millions)	2019A	2020A	2021E	2022E	2023E
Return on Capital Employed	3.5%	3.9%	5.1%	5.1%	5.2%
Return on Equity	8.9%	9.3%	8.6%	8.8%	8.9%
Operating Margin	38.4%	-15.6%	66.8%	66.8%	68.9%
Free Cash Flow	(212)	(498)	(379)	(300)	(169)

iQmethod℠ **– Quality of Earnings***

(US$ Millions)	2019A	2020A	2021E	2022E	2023E
Cash Realization Ratio	1.3x	1.4x	1.7x	1.7x	1.9x
Asset Replacement Ratio	3.5x	4.2x	2.9x	2.7x	2.5x
Tax Rate	NM	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	31.1%	100.4%	97.9%	105.7%	111.1%
Interest Cover	3.1x	2.4x	3.3x	3.5x	3.2x

Income Statement Data (Dec)

(US$ Millions)	2019A	2020A	2021E	2022E	2023E
Sales	886	886	1,006	1,077	1,126
% Change	6.2%	0%	13.4%	7.1%	4.5%
Gross Profit	890	890	1,661	1,785	1,865
% Change	6.2%	0%	86.7%	7.5%	4.5%
EBITDA	504	831	1,000	1,077	1,164
% Change	-74.1%	64.9%	20.4%	7.6%	8.2%
Net Interest & Other Income	(100)	(183)	(205)	(207)	(242)
Net Income (Adjusted)	**263**	**402**	**430**	**470**	**489**
% Change	**36.9%**	**53.1%**	**7.0%**	**9.2%**	**4.1%**

Free Cash Flow Data (Dec)

(US$ Millions)	2019A	2020A	2021E	2022E	2023E
Net Income from Cont Operations (GAAP)	225	403	431	470	489
Depreciation & Amortization	156	257	376	412	446
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	(10)	(75)	(75)	(75)	0
Other Adjustments, Net	(32)	(33)	(11)	(6)	(5)
Capital Expenditure	(550)	(1,050)	(1,100)	(1,100)	(1,100)
Free Cash Flow	**-212**	**-498**	**-379**	**-300**	**-169**
% Change	**-66.5%**	**-135.1%**	**23.9%**	**20.9%**	**43.4%**

Balance Sheet Data (Dec)

(US$ Millions)	2019A	2020A	2021E	2022E	2023E
Cash & Equivalents	1,869	6	6	7	7
Trade Receivables	108	177	201	216	226
Other Current Assets	36	48	52	55	56
Property, Plant & Equipment	6,346	10,739	11,462	12,150	12,805
Other Non-Current Assets	1,003	1,003	1,003	1,003	1,003
Total Assets	**9,362**	**11,973**	**12,725**	**13,431**	**14,097**
Short-Term Debt	131	129	138	154	167
Other Current Liabilities	188	236	253	263	270
Long-Term Debt	2,943	4,681	5,013	5,592	6,064
Other Non-Current Liabilities	2,219	2,144	2,069	1,994	1,994
Total Liabilities	**5,481**	**7,190**	**7,472**	**8,003**	**8,494**
Total Equity	**3,881**	**4,783**	**5,253**	**5,429**	**5,603**
Total Equity & Liabilities	**9,362**	**11,973**	**12,725**	**13,431**	**14,097**

* For full definitions of ***iQ***method℠ measures, see page 8.

Company Sector

Water Utilities

Company Description

Essential Utilities is a regulated water/gas providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI - along with a natural gas presence through the recently acquired Peoples Gas providing distribution services to 740,000 customers in PA, WV, and KY.

Investment Rationale

We are Buy rated on shares of WTRG, seeing shares as poised to re-rate higher given consistent execution, acquisition upside, and increasing conviction around the premium story.

Stock Data

Average Daily Volume	1,108,464

Quarterly Earnings Estimates

	2020	2021
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NA

LT Story Intact with Muni Acquisitions Abound

After rolling forward the outlook earlier this year, formal financial updates were relatively quiet for WTRG this quarter. Full year adjusted EPS of $1.58 was a penny above our estimate and at the top end of management's guidance, while the company reaffirmed 2021 EPS guidance of $1.64-$1.69 and their LT 5-7% EPS CAGR through 2023. While their water biz has a footprint in TX, they noted no material financial impact to the water biz and no financial impact to the recent cold weather events for the gas biz given the location of their operations.

After previously announcing plans to file a rate case at Aqua PA this year keeping with their three year rate case cadence for their water sub, management noted on the call that a verbal settlement has been reached around the catch up component of Repairs tax accounting for the gas biz – with plans to file the written agreement on March 11th that would give all of the tax benefits back to customers over a five year period. While we view the decision to settle the catch up with the full benefit to the rate payers as an incremental drag on our estimates in '23, we stress the $420Mn in rate base opportunities from signed APAs should generate ~$21Mn in earnings with further muni opportunities still to materialize – and we see opportunities abound to further accelerate water tucks ins. Following the adoption of Fair Market Value legislation in TX and VA, the company now has the constructive legislation in all eight states of their water footprint. We expect this to help further accelerate consolidation in the industry as muni budgets are further flex'd from the crisis.

Dissecting the DELCORA hiccups

After the Delaware County Court of Common Pleas issued an order supporting the pending acquisition of DELCORA by rejecting the county's attempt to block the sale, the county appealed the decision and the ALJ recommended the PUC deny the transaction. Given that there are only four commissioners right now in the state, we could very well see a stalemate or see the commission send it back to the ALJ to reconsider add'l evidence as the company works through their concerns. The commission is expected to issue a decision in March, and we stress the equity doesn't need to be pulled until August if there is a slight delay of the transaction.

We reiterate our Buy rating on shares, seeing value relative to AWK (B-2-7, $145.64) and longer term re-rating potential as management continues to perform and drive incremental growth through municipal acquisitions.

EPS Estimates

The exhibit below reflects our latest EPS Estimates. Our 2023 estimates shift down slightly to reflect a reduction in earned ROEs given the latest developments around the settlement related to the Repairs Tax Deduction. That said, we continue to stress longer dated estimates intact despite just a three year view - and see a long trajectory of tailwinds from an acceleration in muni acquisition opportunities: we continue to model to their 5-7% CAGR longer term.

Considering the tax deal we perceive this as de-risking eventual '23 rate case and positioning co well on track to execution backdrop in '24+. We see latest NI de-risking of its PA rate case as clearly improving backdrop too. Decisive reiteration of our Buy.

Exhibit 1: EPS Estimates
Lowering '23 on repairs tax developments: Still see LT outlook intact with new rates in 2024

EPS Estimates	2019A	2020A	2021E	2022E	2023E	2024E	2025E
PA	$1.05	$0.75	$0.76	$0.88	$0.94	$1.00	$1.05
OH	$0.09	$0.07	$0.07	$0.07	$0.08	$0.08	$0.09
IL	$0.10	$0.07	$0.08	$0.08	$0.09	$0.09	$0.10
TX	$0.09	$0.06	$0.07	$0.07	$0.07	$0.08	$0.08
NC	$0.05	$0.04	$0.04	$0.05	$0.05	$0.05	$0.05
Other States	$0.10	$0.07	$0.07	$0.08	$0.08	$0.09	$0.09
Water Utility	**1.47**	**1.06**	**1.09**	**1.23**	**1.31**	**1.39**	**1.46**
Peoples Gas		**0.62**	**0.67**	**0.71**	**0.71**	**0.81**	**0.86**
Parent & Other		*-0.09*	*-0.09*	*-0.13*	*-0.15*	*-0.17*	*-0.20*
EPS	**1.47**	**1.58**	**1.67**	**1.80**	**1.87**	**2.03**	**2.13**
YoY Growth		*8%*	*6%*	*8%*	*4%*	*8%*	*5%*
Guidance	**1.45-1.50**	**1.53-1.58**	**1.64-1.69**				
Three Year CAGR (off $1.56 in 2020)					***6%***		
Guidance					**5-7%**		
Fully Diluted Shares O/S	*178*	*254*	*258*	*261*	*261*	*261*	*261*
Previous EPS		***$1.57***	***$1.67***	***$1.80***	***$1.92***		
Consensus	**1.48**	**1.54**	**1.67**	**1.79**	**1.89**		
DPS	**0.92**	**0.99**	**1.06**	**1.13**	**1.21**	**1.29**	**1.38**
Payout Ratio	*63%*	*62%*	*63%*	*63%*	*64%*	*64%*	*65%*
Guidance			***60-65%***				
Share Count	**179**	**255**	**258**	**261**	**261**	**261**	**261**

Source: BofA Global Research, Bloomberg

BofA GLOBAL RESEARCH

Valuation: PO Shifts to $49

The exhibit below reflects our latest SOTP. We update our valuation to apply the current peer multiples to our latest estimates: 25.4x for water and 14.9x for gas (vs. 27.4x and 14.2x previously). We reduce our premium for Peoples Gas from 3x to 1x given the need for a rate case in 2023 while our water premiums remain unchanged and continue to reflect confidence in ability to consistently deliver, strong muni acquisition prospects, and an underappreciated ESG angle. Our PO ultimately shifts to $49 (from $54 previously). Reiterate Buy given deep discount and upside catalysts.

Exhibit 2: SOTP
PO Shifts to $49 on Lower Multiples and Gas Premium

Water Utilities	**2023 EPS**		**P/E Multiple**				**Equity Value**		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*25.4x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		27.5x							
Water Utilities									
States	2023E EPS	ROE embedded							
PA	$0.94	10.0%	4.0x	30.5x	31.5x	32.5x	$29	$30	$31
OH	$0.08	9.2%	2.0x	28.5x	29.5x	30.5x	$2	$2	$2
IL	$0.09	9.1%	3.0x	29.5x	30.5x	31.5x	$3	$3	$3
TX	$0.07	10.0%	2.0x	28.5x	29.5x	30.5x	$2	$2	$2
NC	$0.05	9.2%	2.0x	28.5x	29.5x	30.5x	$1	$1	$1
Other (including acquisitions)	$0.08	9.2%	0.0x	26.5x	27.5x	28.5x	$2	$2	$2
Water utilities total (ex-Peoples)	$1.31			*29.9x*	*30.9x*	*31.9x*	$39	$40	$42
Gas Utilities									
Peer Gas P/E		*14.9x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		15.8x							
	2023E EPS	ROE embedded							
Peoples Gas	$0.71	11.9%	1.0x	15.8x	16.8x	17.8x	$11	$12	$13
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			-1099	50%			($550)	($550)	($550)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($475)	($441)	($517)
50/50 Weighted Drag from HoldCo Drag							($1,024)	($990)	($1,067)
Fully Diluted Shares Outstanding							*261*	*261*	*261*
PO							$47.00	$49.00	$51.00
Current Price								$43.31	
Dividend Yield								2.4%	
Total Expected Return								15.57%	

Source: BofA Global Research, Bloomberg

BofA GLOBAL RESEARCH

Price objective basis & risk

American Water Works (AWK)
Our PO for American Water Works is $162. We apply the sector average 28.4x to American Water's 2023E earnings based on the water peer multiple and a 8.1% group EPS CAGR for '18-'23E. We think this multiple is justified as in our view AWK largely drives the peer multiple as the largest publicly traded water utility. We ascribe a 3x premium for NJ, PA, IL & Other given scope of acquisition opportunities. Also a -1x P/E for Cali utility.

Risks to the downside are increase in market interest rates, potential impact of tax reform on utilities, operational errors, changes in valuation levels for water utilities. Risks to the upside are accelerating muni acquisitions, multiple expansion, and constructive legislation in regulatory jurisdictions.

Essential Utilities (WTRG)
Our price objective is $49 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. These peer multiples are 25.4x and 14.9x. We apply a 3.0x premium to Peoples Gas given the organic growth opportunities, while applying a variety of premiums to its water (2x previously) subsidiaries: +4x to PA, +3x to IL, +2x to OH, +2x for TX, +2x for OH, and no premium for balance of biz. We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

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North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AES	AES	AES US	Julien Dumoulin-Smith
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Enphase Energy	ENPH	ENPH US	Aric Li
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Ormat Technologies	ORA	ORA US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
NEUTRAL				
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Atlantica Sustainable Infrastructure	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	TransAlta Renewables Inc.	YRNW	RNW CN	Julien Dumoulin-Smith
	UGI Corp.	UGI	UGI US	Richard Ciciarelli, CFA
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	Southwest Gas Holdings	SWX	SWX US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith

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Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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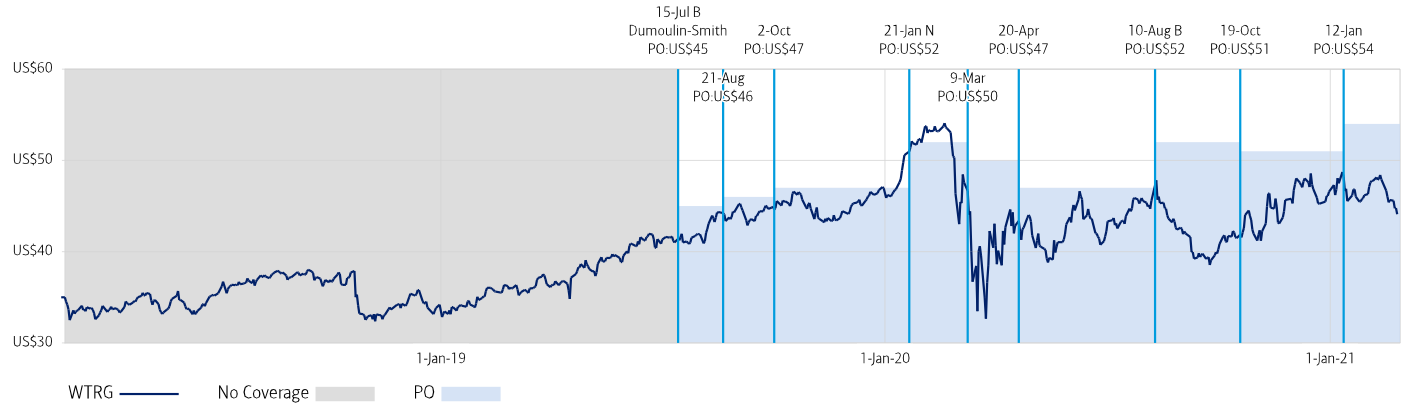
Essential Utilities (WTRG) Price Chart



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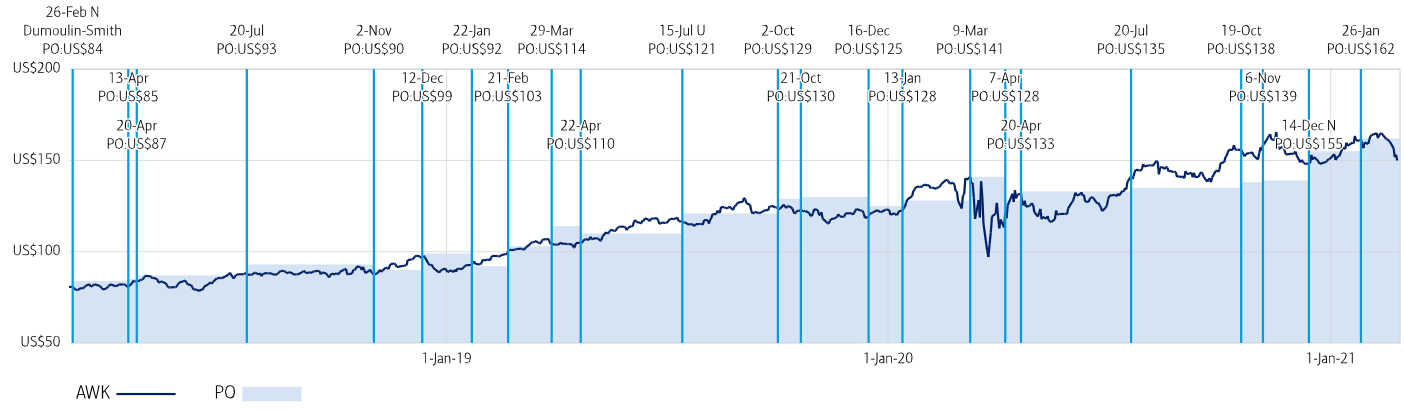
American Water (AWK) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Utilities Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	80	51.61%	Buy	58	72.50%
Hold	37	23.87%	Hold	28	75.68%
Sell	38	24.52%	Sell	22	57.89%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1863	56.90%	Buy	1185	63.61%
Hold	686	20.95%	Hold	426	62.10%
Sell	725	22.14%	Sell	358	49.38%

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
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Underperform	N/A	≥ 20%

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BARCLAYS

Equity Research
18 November 2020

North America Power & Utilities
Rolling Valuations to 2023

We have initiated 2023 estimates for our coverage and updated all price targets based on 2023 estimates. This update combined with EEI updates and relative price moves has resulted in the following ratings changes:

- Upgrading AEE to Equal Weight, from Underweight, on underperformance and higher projected earnings.
- Upgrading NI to Overweight, from Equal Weight, on higher earnings growth from the increased electric capex in Indiana.
- Downgrading NWE to Equal Weight, from Overweight, on outperformance and lower projected earnings.
- Downgrading PNM to Underweight, from Equal Weight, on low projected return given pending acquisition, along with view that and increased bid is unlikely near term.

With election results and multiple positive COVID-19 vaccine trials, risk appetite appears to be alive and well. In utilities, much like in other sectors, risk has outperformed momentum in recent weeks. This has manifested in a long awaited contraction in the PE disparity in the sector. We believe this trend will continue as investors seek risk and value over defense and momentum. We continue to see names with idiosyncratic risks expecting near term resolution along with utilities possessing higher energy exposure to be in favor given this dynamic. This aligns well with our Overweight ratings on SRE, PCG, SO and PNW and Underweight ratings on ED and WEC.

Based on EEI, Q3 and recent meetings with management, we highlight updates to stock investment theses, where our ratings remain unchanged. COVID-19 load impacts into 2021, rate case expectations, guidance updates, capex updates, corporate actions and more have been discussed recently. We highlight by stock where these changes cause a shift in our investment thesis.

RATING CHANGE

North America Power & Utilities
POSITIVE
Unchanged

For a full list of our ratings, price target and earnings changes in this report, please see table on page 2.

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PLEASE SEE ANALYST CERTIFICATION(S) AND IMPORTANT DISCLOSURES BEGINNING ON PAGE 42.

Summary of our Ratings, Price Targets and Earnings Changes in this Report (all changes are shown in bold)

Company	Rating		Price	Price Target			EPS FY1 (E)			EPS FY2 (E)		
	Old	New	17-Nov-20	Old	New	%Chg	Old	New	%Chg	Old	New	%Chg
North America Power & Utilities	Pos	Pos										
Alliant Energy Corporation (LNT)	EW	EW	54.73	56.00	**65.00**	16	2.40	**2.46**	3	2.58	**2.52**	-2
Ameren Corp. (AEE)	UW	**EW**	80.60	79.00	**95.00**	20	3.41	**3.38**	-1	3.71	**3.73**	1
American Electric Power Company, Inc. (AEP)	OW	OW	86.73	93.00	**107.00**	15	4.33	**4.35**	0	4.65	**4.62**	-1
American Water Works Company, Inc. (AWK)	EW	EW	159.29	138.00	**173.00**	25	3.86	**3.89**	1	4.22	**4.25**	1
CenterPoint Energy, Inc. (CNP)	EW	EW	25.17	21.00	**27.00**	29	1.27	1.27	-	1.36	1.36	-
CMS Energy Corporation (CMS)	EW	EW	63.83	65.00	**75.00**	15	2.67	2.67	-	2.86	**2.84**	-1
Consolidated Edison, Inc. (ED)	UW	UW	79.25	74.00	**83.00**	12	4.24	**4.25**	0	4.52	**4.47**	-1
Duke Energy Corporation (DUK)	EW	EW	92.92	87.00	**102.00**	17	5.08	**5.14**	1	5.18	**5.24**	1
Edison International (EIX)	EW	EW	65.60	57.00	**69.00**	21	4.43	4.43	-	4.58	4.58	-
Essential Utilities, Inc. (WTRG)	EW	EW	44.88	45.00	**50.00**	11	1.56	1.56	-	1.67	**1.62**	-3
Eversource Energy (ES)	EW	EW	91.75	88.00	**100.00**	14	3.70	**3.62**	-2	3.94	**3.89**	-1
FirstEnergy Corp. (FE)	EW	EW	28.74	32.00	**33.00**	3	2.50	2.50	-	2.63	2.63	-
NextEra Energy, Inc. (NEE)	EW	EW	76.61	301.00	**87.00**	-71	9.04	**2.28**	-75	9.87	**2.45**	-75
NiSource, Inc. (NI)	EW	**OW**	24.75	25.00	**29.00**	16	1.33	1.33	-	1.33	**1.38**	4
NorthWestern Corporation (NWE)	OW	**EW**	60.38	59.00	**63.00**	7	3.37	3.37	-	3.62	**3.51**	-3
OGE Energy Corp. (OGE)	EW	EW	34.21	33.00	**36.00**	9	2.14	**2.15**	0	2.20	**2.26**	3
PG&E Corporation (PCG)	OW	OW	11.72	13.00	**14.00**	8	1.62	1.62	-	1.00	1.00	-
Pinnacle West Capital Corporation (PNW)	OW	OW	86.78	89.00	**103.00**	16	4.90	**5.06**	3	4.92	**5.09**	3
PNM Resources, Inc. (PNM)	EW	**UW**	48.90	50.00	50.00	-	2.11	**2.28**	8	2.29	**2.37**	3
Public Service Enterprise Group (PEG)	EW	EW	59.05	59.00	**65.00**	10	3.41	**3.43**	1	3.43	**3.40**	-1
Sempra Energy (SRE)	OW	OW	134.06	146.00	**159.00**	9	7.57	7.57	-	7.99	7.99	-
The Southern Company (SO)	OW	OW	62.36	61.00	**73.00**	20	3.18	3.18	-	3.34	**3.27**	-2
WEC Energy Group, Inc. (WEC)	UW	UW	100.18	94.00	**107.00**	14	3.75	**3.77**	1	3.97	**4.02**	1
Xcel Energy Inc. (XEL)	EW	EW	72.63	70.00	**82.00**	17	2.73	**2.77**	1	2.97	**3.01**	1

Source: Barclays Research. Share prices and target prices are shown in the primary listing currency and EPS estimates are shown in the reporting currency.
FY1(E): Current fiscal year estimates by Barclays Research. FY2(E): Next fiscal year estimates by Barclays Research.
Stock Rating: OW: Overweight; EW: Equal Weight; UW: Underweight; RS: Rating Suspended
Industry View: Pos: Positive; Neu: Neutral; Neg: Negative

FIGURE 1
2023 Barclays EPS Estimates

Ticker	2023 EPS
LNT	$2.94
AEE	$4.28
AEP	$5.28
AWK	$5.01
CNP	$1.38
CMS	$3.25
ED	$4.94
DUK	$5.81
EIX	$5.12
WTRG	$1.82
ES	$4.34
FE	$2.86
NEE	$2.84
NI	$1.55
NWE	$3.79
OGE	$2.46
PCG	$1.25
PNW	$5.56
PNM	$2.68
PEG	$3.58
SRE	$9.05
SO	$3.92
WEC	$4.45
XEL	$3.40

Source: Barclays Research

Ratings Changes

Upgrades

AEE

We upgrade AEE to Equal Weight, as we believe recent underperformance has accounted for risks to future growth weighing on the stock, including energy rules modification in IL and the ability to execute on the preferred MO IRP scenario. At Q3, management narrowed guidance to $3.40-$3.55 (from $3.40-$3.60) and said updates to the 5-year capital plan and 2021 EPS guidance are planned for the Q4 call. We see the potential for incremental spending opportunities from the MO IRP (AEE has 950 MW of renewables opportunities before 2024 not included in current plans) as well as from regional transmission projects, though regulatory approval on a project-by-project basis and the ability to increase regulated capital plans while avoiding significant increases in customer bills will be areas of focus. Management notes the IL legislature's weak appetite for comprehensive energy legislation at this time, though Gov. Pritzker's eight-principled energy reform plan could influence regulatory policy in the future. We now view the risk/reward outlook for the stock as balanced given the uncertainty of the regulatory construct in IL offset by incremental

spending opportunities that could accelerate rate base growth. Our updated price target is $95, which is premised on a 20% premium to the 2023 regulated group average multiple of 18.5x applied to our 2023 EPS estimate of $4.28

NI

After the investor day, we used a 5% premium to the group average to reflect expectations of above-average growth driven by the $1.8-$2.0 bn in renewables investments related to RM Schahfer replacement power. By rolling our valuation forward to 2023, we are able to capture some of the earnings related to this spend via new rates from the anticipated 2022 rate case (rates expected effective mid-2023). We believe the level of cost savings necessary to achieve management's growth guidance is achievable. Additionally, although we do not believe concerns regarding the future of natural gas operations should be materially priced into the stock, we feel the need to reflect the overhang that may weigh on the stock until investors can gain more clarity into the future value of natural gas LDCs. Particularly for those companies operating colder climates, the threat posed by electrification of heating is limited by economic and technological constraints. Thus, for these reasons, we eliminate our premium to the group average, yet we still believe there is enough upside to the current valuation to merit an upgrade to Overweight.

Risks include a higher-than-anticipated skew towards PPAs from procurement results (though management remains on track as of EEI), as well as the ability to control costs and achieve savings from the NI Next initiative in 2021 and beyond. COVID-19 impacts on gas usage during winter months are a source of uncertainty, though most residential gas rate structures have decoupling mechanisms (management estimates that changes in gas usage will comprise a majority of the ($0.05) COVID-19 headwind in 2021). Considering these risks, the current risk/reward backdrop leaves opportunity for upside to the current valuation, in our view. Our updated price target is $29, which is premised on the 2023 regulated group average multiple of 18.5x applied to our 2023 EPS estimate of $1.55.

Downgrades

NWE

At EEI, NEW initiated 2021 guidance of $3.40-$3.60 (below consensus). The wider than normal range was used based on COVID-19 uncertainties and will be narrowed to a $0.15 range on the Q4 call. With the reiteration of a 3-6% growth range and rolling the starting point to a lower than expected 2021 guidance, our 2021 and 2022 numbers have come down and our updated valuation on 2023 combined with the recent outperformance, while providing upside no longer supports an Overweight rating.

We continue to view NWE as a well-managed company with limited growth opportunities compared to peers. The updated capital plan does show a $300M increase as compared to the previous 5-year plan. The updated plan includes $100m of incremental investment for SD generation from the results of a recent competitive solicitation. The Montana generation opportunity is still outstanding, but could add $200M to the capital plan over the next five years. Management had provided commentary previously that $400M/year of capex (new plan is at or above $400M in all years) would allow for growth at the midpoint of the earnings CAGR. While we see longer term opportunity and ability to grow earnings closer to 5% assuming a win in MT capacity RFPs, near term needs to manage O&M between rate cases will drive growth closer to 4% in the near term. We expect a Montana rate case filing in 2022 for new rates in 2023 and expect multiple cases in SD to coincide with commercial operation of the capacity resources to be owned by NWE selected in the competitive solicitation processes.

The current risk/reward feels balanced given the lower current relative growth, recent relative price performance, mixed recent regulatory results in MT and potential for future capex and earnings growth associated with winning MT capacity RFPs. Our updated price target is $63, which is premised on a 10% discount to the 2023 regulated group average multiple of 18.5x applied to our 2023 EPS estimate of $3.79.

PNM

We downgrade PNM to Underweight to reflect the limited upside in the stock given Avangrid's take-out offer of $50.30/share. The acquisition is expected to close in 2H21. We characterize prospects for a superior bid as unlikely given few competitors with the balance sheet capacity for such an acquisition, and none with the strategic alignment or likelihood for regulatory approval as AGR. While regulatory approval of any transaction can never be predicted with absolute certainty, we do not see any significant impediments to approval at this time. Given New Mexico is a net benefit state, AGR's commitment to maintain the PNM workforce and likely willingness to compromise on other factors (HQ location, customer credit, charitable giving, etc.) strengthen the likelihood of transaction approval. Our updated price target is $50, which is premised on the 2023 regulated group average multiple of 18.5x applied to our 2023 EPS estimate of $2.68.

Investment Thesis Updates

AEP

The 5-7% growth rate is maintained and the inclusion of North Central Wind pushes growth above the midpoint for 2022 and 2023, with expected equity to support NCW at 65% financing to be issued commensurate with commercial operation of each of the wind farms. AEP has highlighted a 5 year, $37B capital plan driving 7.4% rate base CAGR which supports the 5-7% EPS CAGR (regulatory lag, holding company debt and equity drive the difference). 2021 guidance was initiated at $3.51-$3.71.

AWK

AWK's resolution of key Pennsylvania and New Jersey rate cases is a strong step forward and should reinforce the market's confidence in AWK's ability to execute. Execution was particularly evident in 2020 as AWK was able to claw back to its original guidance range amidst Covid-19 and the ongoing uncertainty from the two material rate cases in PA and NJ. We see the upcoming 2021 and 2022 fiscal years as de-risked given the rate agreements and expect market focus to turn toward timing of equity in the forecast period, O&M management, and FMVL M&A given the lack of clear challenges ahead. AWK's multiple remains elevated, but near five-year spread averages relative to both the S&P 500 and the broader utility group P/E multiple. Following the rate case conclusions and the clear runway leaves little indication that the multiple will contract in the near term.

CNP

Management's reiteration of the prior 5-7% utility-level EPS CAGR is incrementally positive given our perception that the guidance range contemplates some type of strategic midstream corporate action. The ability to maintain the prior CAGR is viewed favorably as it seemingly overcomes headwinds from a re-allocation of corporate interest previously allocated to the midstream segment and contemplates a roll off of recovery bond equity earnings. We also note that the decision to sell at least one gas LDC business has received a positive reception as it avoids re-levering the holdco after significant debt maturities to come over the next three years. We are also more sanguine on the name following management's inclusion of IN capex in its formal guidance. The IN RFP process is ongoing, but we see the update building confidence that initial stakeholder feedback was positive enough to indicate that CNP wins more renewable build than originally expected. We

continue to model a 'status quo' forecast, but anticipate additional details to come from the December analyst day.

CMS

Management maintained the 6-8% growth rates for EPS and dividend and provided 2021 EPS guidance of $2.84-$2.86. The CMS Gas settlement includes a stay-out provision to avoid a rate case in 2021. CMS has filed for securitization of Karn 1&2 ($703m) and expects to file a new IRP mid-2021. CMS has had marked success at managing costs and work crews to offset any COVID-related headwinds. We expect CMS to refresh capital and financing plans at Q4.

DUK

The 4-6% growth rate is maintained with a bias towards the high end. DUK will provide 2021 guidance on the Q4 call, but has pointed towards expectations at or above $5.15 even with a "Dominion" coal ash outcome in North Carolina. The recent Carolina IRP provides a path to increasing rate base growth from the expected 6.5% CAGR through 2024 to 7% CAGR from 2024 through 2029. We expect earnings growth in the top half of the 4-6% range through 2023 off of a 2021 base.

ED

Management narrowed 2020 EPS guidance to $4.15-$4.30 (from $4.15-$4.35) to reflect COVID-19 impacts. ETRN pushed the expected in-service date for MVP to 2H21 due to pending legal challenges. Management accelerated some clean energy capex from 2021 to 2020 in order to create contingency against deliverables deadlines in planning for a potential second wave (5.5% rate base CAGR through 2022). In 2021 we anticipate more concrete planning regarding onshore and offshore transmission investment opportunities related to offshore wind. Strong execution on cost savings opportunities in 2021 and beyond will be critical to meeting allowed ROEs. We expect an update to financing and capex plans at Q4.

EIX

Focus remains on EIX's ability to settle remaining individual wildfire claims from the 2017 and 2018 seasons and the related equity issuance timing and magnitude. We see the $1bn figure as a helpful marker and should belay overstated credit rating agency concerns about the amount of debt issuance to occur under EIX's capital structure waiver. We still anticipate the individual victim settlement process to be a longer road than most current expectations, but delayed equity issuance and slower ultimate cash outflows could be a silver lining. We think the current discount may subside to some extent as we progress into the latter stages of wildfire season, but note that large fires in EIX's service territory as late as January.

ES

The 5-7% long-term EPS CAGR is maintained, with an expectation of the middle of the range. The CAGR does not reflect the CGMA acquisition, offshore wind, CT/NH grid modernization, or AMI in MA. Management expects to provide EPS commentary on the incremental opportunity from offshore wind at Q4. Management shifted the anticipated commercial operation dates for the three offshore wind projects back by roughly a year, dependant on BOEM review schedules expected to be released in early 2021. The Ørsted/ES partnership has submitted bids into the NY RFP (awards anticipated by EOY). Awards in the MD, NJ and RI RFPs are anticipated mid-2021. Penalties in CT related to Isaias are anticipated mid-2021. ES may be required to file a CT rate case, but otherwise has no plans for rate reviews in 2021.

FE

FE's recent management changes and discussions around financial contingencies to increases flexibility have encouraged us that the Board is moving quickly and taking the

federal investigation seriously. However, the moves could indicate management culpability, or at the least, indelicate ethical violations that could impact FE's ESG perception for the foreseeable future. We expect the FBI investigation to result in negative headlines for some time, but take recent management commentary around potential settlements or announcements in early 2021 at their merit. We look to the 4Q20 call and any investigation announcements for more clarity into financial impacts going forward and continue to monitor regulatory processes for potential impacts. We incorporate the potential for up to $2bn in penalties and fines based on historical precedent. However, with limited balance sheet capacity and our belief that public information regarding the investigation remains in the early stages, we see no reason to expect a re-rating near term.

LNT

LNT's roll forward incorporated some anticipated windfalls from the Iowa Clean Energy Blueprint and reinforced out perception in the achievability of the 5-7% EPS CAGR guidance off the back of strong rate base growth. We believe the capital investment need to hit state targets for renewables and broader sustainability efforts (including electric vehicles) actually affords LNT the ability to grow rate base and earnings at a faster clip, but believe management has concluded that 5-7% is the sweet spot because it allows for palatable customer bill increases under various load scenarios and avoids significant external funding requirements. We continue to value LNT at a 20% premium to the group on LNT's 2023E P/E, reflecting regional peers' valuations that remain above LNT.

NEE

Management expects to achieve 6-8% EPS growth through 2023 off of new adj 2021 guidance, with an assumption of the top of the range, and anticipates 10% dividend growth through at least 2022. NEE increased 2021 guidance due to strength in the renewables pipeline (~1.5 GW added since Q2). Management expects a $60bn 2019-2022 capital plan, an increase of $7.5bn from the previous midpoint.

OGE

The ability to receive approval for a grid modernization rider in OK is a positive step and provides evidence of an improving regulatory climate following years of environmentally-mandated capital. We also maintain a more positive outlook for OGE's ability to consider strategic alternatives to its ENBL stake given its strong balance sheet and ability to weather the loss of cash flows from a sale or other transaction. However, OGE's below-peer rate base and utilities EPS growth rate command a 10% discount P/E to the group average.

PCG

We believe near-term noise around PCG's safety certificate is unlikely to amount to a loss of coverage under the AB 1054 wildfire fund provision, though the proceeding merits close attention as long as there is no ruling beyond the statutory deadline. We also expect heavy investor focus on the securitization process and management appointments. Related to the securitization process, equity issuance timing and magnitude will likely gain increased clarity as we progress toward a May 2021 CPUC decision, per the procedural schedule (earlier with settlement). We see PCG as increasingly attractive as wildfire season nears an end in early 2021. We move PCG's discount to the group average 2023E P/E multiple to 35% to reflect the near-term headwinds and an active wildfire season. We believe the discount embedded in our valuation framework is an easy hurdle given regional peers and would expect PCG to re-rate higher in a risk on environment and see a further tailwind if we move through wildfire season with no additional large-liability fires.

PEG

The near-term focus will continue to be on potential participation in Ørsted's Ocean Wind, offshore wind project, a potential settlement with the NJ BPU on transmission ROE, updates

on the announced intention to divest non-nuclear generation, the NJ BPU report on resource adequacy expected in Q1 2021(will address fixed resource requirement), and a BPU ruling on non-energy efficiency aspects of the clean energy plan. The utility rate base and earnings growth are above average and the utility capital plan does not require equity, nor cashflow from the genco.

PNW

A focus going into 2021, alongside the APS rate case and AZ energy rulemaking, will be the new commissioners joining the AZCC. Commissioner Marquez Peterson (R), Jim O'Connor (R), and Anna Tovar (D), will join Commissioners Kennedy (D) and Olson (R). Though O'Connor was not initially planning on running, Commissioner Olson convinced him to run. We anticipate the two will have similar policy goals, and we look for any early alignment of rhetoric or voting between Commissioners Olson and O'Connor. A new commission chair will be voted on at the first open meeting of 2021, and, if precedent stands, Cmr. Olson would be chair as the most senior majority party member. If Cmrs. Olson and O'Connor have similar philosophies, Commissioner Marquez Peterson may be the deciding vote on contentious issues such as AZ energy rules and retail competition. For more information on the newly elected commissioners, see our note "*Last Bunch of EEI Meetings*," 11/12/20. Management does not plan to initiate FY21 guidance until the current rate case concludes.

SO

Vogtle continues to be the focus. We continue to expect and have modelled regulatory in-service dates for Unit 3 and Unit 4 of 11/21 and 11/22 respectively. Georgia Power will file an integrated resource plan (IRP) in January of 2022, the findings of which will likely be included in a mid-year 2022 rate case filing for new rates (to include Vogtle and the associated fuel savings) in 2023. We believe that the additional free cash flow from Vogtle will drive annual capex increases of $1B, which should increase the EPS CAGR from 4-6% to 5-7%. The dividend payout is expected to drop below 70% in 2023 when Vogtle is on line, providing the opportunity for dividend growth to accelerate from $0.08/share annually to a rate more in line with earnings growth.

SRE

We expect the recent FID decision at ECA to have a limited impact to SRE near term, given the low equity contribution from the SRE balance sheet, but continue to closely monitor the LNG segment as management mulls strategic options for financing future LNG export opportunities and maximize shareholder value as utility companies across the sector opt for pure-play, renewable-driven stories. We think the 'conglomerate discount' currently being ascribed to SRE is too severe and expect a re-rating to occur over the next twelve months as investors gain confidence around the energy outlook for Mexico and Ienova's role in the infrastructure buildout and management continues to seek ways to highlight value for the LNG business and reiterate our Overweight rating.

WEC

Management increased the 5-year capital plan 7.3% to $16.1 bn over 2021-2025 and firmly maintains expectations for 7% rate base growth and 5-7% EPS growth in the long term. Management sees significant bill offsets from O&M and fuel cost savings as legacy generation comes offline in 2023 and 2024 that would keep bill increases at or below the inflation rate. Management estimates legacy generation assets will amount to ~2% of company-estimated total 2025 rate base of $32 billion. Storage has become economic over peaking capacity, and for the first time WEC is adding 600 MW of battery storage to resource plans.

WTRG

WTRG continues to lag the valuation expansion experienced by AWK and other pure-play water peers. One of the drivers, in our view, is a perception of risk around the DELCORA acquisition and we keep a specific focus on the legal proceeding following local election results that flipped party affiliation of the City Council. We also believe WTRG will trade with some correlation to national gas LDC utilities, though we ascribe a 10% premium to the regulated utility group multiple to reflect our perception of People's gas as a higher-quality business mix than most. Finally, we continue to monitor WTRG's catch-up component of the repairs tax election, but remain confident that WTRG will receive an outcome that allows it to maintain its current growth and authorized ROE levels while extending the rate case need out through 2025.

XEL

The 5-7% long-term growth target is maintained. Management initiated 2021 EPS guidance of $2.90-$3.00, consistent with 5-7% long-term growth objective. Electric sales and O&M are both expected to increase 1% while gas sales are expected to remain flat in FY21 relative to FY20. The $22.6bn 2021-2025 capital plan has $1.4bn in upside from incremental renewables investments (mostly from MN Relief and Recovery spending on wind repowering and solar, which would be funded at 50% equity). Average annual capex from 2021-2024 was increased by ~$140 annually over the previous plan. The implied rate base CAGR from 2021-2025 is 6.3% (6.9% including the incremental renewables spending). XEL has requested a MPUC decision on wind repowering by EOY and expects a decision on solar investments in Q2 or Q3 of 2021. PSCo's AGIS rider filing was dismissed on procedural grounds. PSCo can still defer ~80% of AGIS-related costs for future recovery and does not believe there is any read-through to the wildfire rider filing. The MN PUC must decide whether to implement interim rates or approve the stay-out request by EOY (regardless, capital plans will not be impacted).

Relative Group Valuation and PE Disparity

P/E Disparity Starting to Show Signs of Life for Value

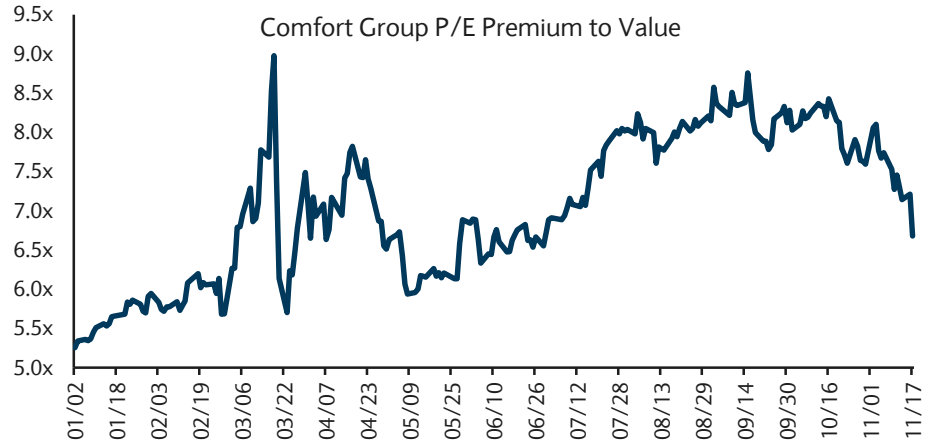
Between the lack of a "blue wave" and positive news on the COVID-19 vaccine front value or 'risk on' names have begun to show evidence of revaluing higher toward 'comfort' names premiums that had increased throughout the year. This contraction has been long-awaited by the market given the historically high spreads and a belief that the spread was unsustainable. We highlight that there is still room to go for the value trade, but are encouraged by signs that fundamentals are beginning to matter as flows move in the direction of more realistic valuation of idiosyncratic risks.

The constituent stocks for our discounted 'value' and high-premium 'comfort' groups displayed in the graphic is broken out below.

Comfort: AEE, CMS, NEE, LNT, ES, WEC, XEL,

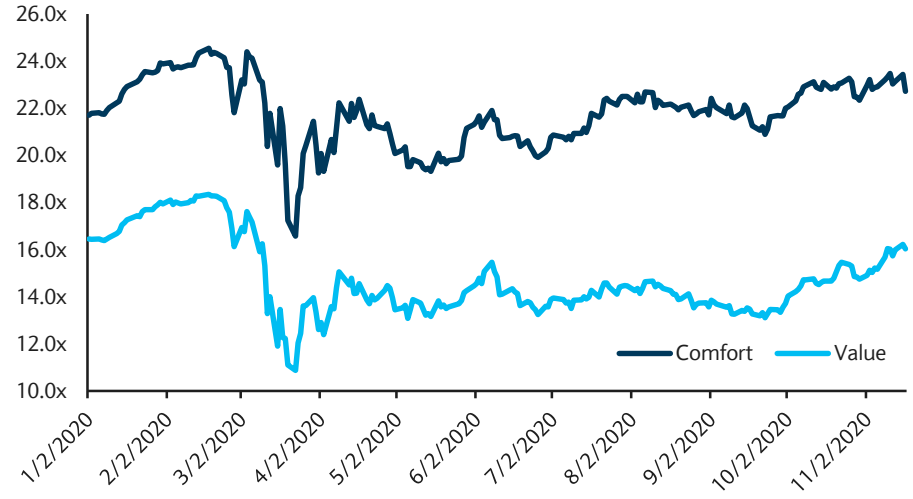
Value: CNP, DUK, EIX, NWE, PCG, PNM, PNW, SO, SRE

FIGURE 2
Spread between Value and Comfort Groups (2yr Blended Fwd P/E)



Source: Bloomberg, Barclays Research

FIGURE 3
Comfort and Value Group P/E (2yr Blended Fwd P/E)



Source: Bloomberg, Barclays Research

Valuation Methodology

We have updated our valuation methodology to use relative premiums and discounts to the 2023 regulated group average PE multiple applied to our 2023 EPS estimates combined with any sum of the parts valuation aspects updated to 2023 expectations.

Our previous valuation methodology used relative premiums and discounts to the 2022 regulated group average PE multiple applied to our 2022 EPS estimates combined with any sum of the parts valuation aspects based on 2022 expectations.

AEE

Our current $95 price target is premised upon a 20% premium applied to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS of $4.28.

Our previous $79 price target was premised upon a 20% premium applied to the 2022 utility group average PE multiple of 17x applied to the prior Barclays 2022E EPS of $3.90.

AEP

Our current $107 price target is premised upon a 10% premium applied to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS of $5.28.

Our previous $93 price target was premised upon a 10% premium applied to the 2022 utility group average PE multiple of 17x applied to the Barclays prior 2022E EPS of $4.97.

AWK

To derive our $173 price target, we utilize a group average water P/E multiple for 2023 earnings and apply a 15% premium to AWK's consolidated 2023 EPS estimate of $5.01. The premium reflects strong management, constructive regulatory exposure, and top-tier growth visibility following key rate case outcomes.

Our previous $138 price target was premised on a 15% premium to the previous 2022 group average water multiple of 27x for AWK applied to our previous 2022 EPS estimate of $4.46

CMS

Our current $75 price target is premised upon a 25% premium applied to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS of $3.25.

Our previous $65 price target was premised upon a 25% premium applied to the 2022 utility group average PE multiple of 17x applied to the Barclays 2022E EPS of $3.09 estimate.

CNP

Our current $27 price target is premised upon a 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E utility EPS estimate of $1.38 after allocating parent debt and operating expenses. We use the current ENBL price of $5 adjusted for CNP's ownership, adjusted for allocated debt – leaving $2 of ENBL value to CNP on a consolidated basis.

Our previous price target of $21 used a group average utility multiple of 17x applied to 2022E prior utility EPS of $1.46 and the prior ENBL share price of $4.

DUK

Our current $102 price target is premised upon a 5% discount applied to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS of $5.81.

Our previous $87 price target was premised upon a 5% discount applied to the 2022 utility group average PE multiple of 17x applied to the Barclays prior 2022E EPS of $5.39.

ES

Our current $100 price target is premised upon a 25% premium to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS of $4.34.

Our previous $88 price target was premised upon a 25% premium to the 2022 utility group average PE multiple of 17x applied to the Barclays prior 2022E EPS of $4.15.

EIX

Our $69 price target is based on a 20% discount to the 2023 group average multiple of 18.5x applied to an adjusted, post wildfire liability and additional funding, Barclays 2023 EPS estimate of $5.12. The 20% discount is based upon perceived wildfire risk absent a test of AB 1054 cost recovery standards and remaining uncertainty on 2017 and 2018 wildfire liabilities.

Our previous $57 price target was premised upon a 25% discount applied to the 2022 utility group average PE multiple of 17x applied to the Barclays prior 2022E EPS of $4.65.

ED

Our current $83 price target is premised upon a 10% discount to the 2023 group average P/E multiple of 18.5x applied to our 2023 EPS estimate of $4.94.

Our prior price target of $74 was premised upon a 10% discount to the 2022 group average P/E multiple of 17x applied to our prior 2022 EPS estimate of $4.73.

FE

Our $33 price target for FE is based on a 30% discount to the group average 2023 multiple of 18.5x applied to our pro forma FY23 EPS estimate, adjusted for an assumed $2bn equity issuance to reflect balance sheet repair following fines or penalties. The 30% discount is based on our expectation that the ongoing Ohio corruption investigation serves as an overhang to the stock valuation regardless of the financial impact.

Our previous $32 price target was premised upon a 30% discount applied to the 2022 utility group average PE multiple of 17x applied to our unchanged 2022E EPS estimate of $2.73.

LNT

Our LNT price target is $65. We utilize a relative target P/E multiple to value LNT shares. We apply a 20% premium to the 18.5x group average 2023 P/E multiple using EPS of $2.94 to reflect LNT's strong track record for execution, visible earnings growth, attractive rate base growth opportunities driven by renewable generation that limit customer bill inflation, and constructive regulatory oversight.

Our previous $56 price target was premised upon a 20% premium to the 2022 group average multiple applied to our prior 2022 EPS estimate of $2.73.

NEE

Our new price target of $87 is premised upon a SOTP with a 20% premium to the 2023 group average PE multiple of 18.5x applied to our 2023 EPS estimate of $1.74, a 17.5x 23E EV/EBITDA for the NEER business – comparable to valuations of renewables developers such as Ørsted. We then add $3 for NEP as we take the Barclays $67 NEP price target and flow it through to represent NEE's ownership.

Our previous price target of $301 was premised upon a SOTP with a 20% premium to the 2022 group average PE multiple of 17x applied to our 2022 EPS estimate of $6.43, a 16x 22E EV/EBITDA for the NEER business – comparable to valuations of renewables developers such as Ørsted. We then add $13 for NEP as we take the Barclays $61 NEP price target and flow it through to represent NEE's ownership.

NI

Our current $29 price target is premised upon the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS estimate of $1.55.

Our prior $25 price target was premised upon a 5% premium to the 2022 regulated utility group average P/E applied to our prior 2022 EPS estimate of $1.42.

NWE

Our current $63 price target is premised upon a 10% discount applied to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS of $3.79.

Our previous $59 price target was premised upon a 10% discount applied to the 2022 utility group average PE multiple of 17x applied to the Barclays prior 2022E EPS of $3.83.

OGE

We derive our $36 price target by applying a 10% discount to the group average multiple of 18.5x applied to our 2023 utility earnings estimate combined with the current ENBL price $5 applied to the 111 units that OGE owns. Our 10% discount reflects below average earnings CAGR compared to the group.

Our previous $33 price target utilized a group average P/E multiple of 17x reflecting our view that earnings growth could expand following the approval of certain regulatory riders and grid modernization opportunities.

PEG

Our current $65 price target is premised upon a 5% premium to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023 utility net parent EPS estimate, resulting in a $62 valuation for the utility. We then use a 5x EV/EBITDA multiple on 2023 generation EBITDA applied to the Barclays 2023 generation EBITDA estimate resulting in $3.25 valuation for PEG Power. Combining the utility $62 valuation and the $3.25 PEG Power valuation yields our $65 price target.

Our previous $59 price target was premised upon a 10% premium to the 2022 utility group average PE multiple of 17x applied to the Barclays 2022 utility net parent EPS estimate, resulting in a $55 valuation for the utility. We then used a 5x EV/EBITDA multiple on 2022 generation EBITDA applied to the Barclays 2022 generation EBITDA estimate resulting in $3.70 valuation for PEG Power. Combining the utility $55 valuation and the $3.70 PEG Power valuation yielded our $59 price target.

PCG

We move PCG's discount to the group average 23E P/E multiple to 35% to reflect the near-term headwinds and an active wildfire season. We believe the discount embedded in our valuation framework is an easy hurdle given regional peers and would expect PCG to re-rate higher in a risk on environment and see a further tailwind if we move through wildfire season with no additional large-liability fires. The P/E multiple is applied to our 2023 EPS estimate of $1.25, which gives a price target of $14.

Our previous $13 price target was premised on a 25% discount to the 2022 utility group average PE of 17x applied to the prior Barclays 2022E EPS of $1.08.

PNM

Our current $50 price target is premised upon the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS estimate of $2.68. Our price target remains consistent with the terms of the AGR acquisition offer.

Our previous $50 price target was premised upon the terms of the AGR acquisition offer.

PNW

Our current $103 price target is premised upon the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS estimate of $5.56.

Our previous $89 price target was premised upon the 2022 utility group average PE multiple of 17x applied to the Barclays 2022E EPS estimate of $5.22.

SO

Our $73 price target is premised on the 2023 group average PE multiple of 18.5x applied to our 2023 earnings estimate of $3.92. The group average multiple is based on a discount for the risk of Vogtle construction offsetting the premium valuation SO deserves based on fundamentals post commercial operation of Vogtle.

Our previous $61 price target was premised on a 5% discount to the 2022 group average PE multiple of 17x applied to our prior 2022 earnings estimate of $3.60 and then add the NPV of the Vogtle earnings uplift of $0.20 and apply 5% discount to the group average 2022.

SRE

We utilize a sum of the parts valuation framework for our $159 price target for SRE. We apply a relative P/E multiple premium / discount to the North American utility businesses a base group average (10% premium for Texas, 15% for SoCalGas, group average for SDG&E). We utilize the Barclays' Ienova price target and adjust for SRE ownership and spot USDMXN for Peso translation. We utilize a probability-weighted DCF approach for the LNG business depending on where each facility is on securing contracting for export capacity.

Our previous $146 price target was derived using the same methodology, but prior 2022 EPS of $8.49 and 2022E P/E multiple of 17x for the group.

WTRG

Our $50 price target is arrived at using our methodology where we value WTRG's water business using a 5% premium to the 2023 water group average P/E multiple. The 5% premium reflects strong regulatory exposure and public M&A opportunities, balanced by growth visibility lower than peers. We value the regulated gas business at a 15% premium to reflect a strong growth profile and familiar regulatory exposure.

Our previous $45 price target was premised on a 5% premium to the 2020 group average water multiple of 27x applied to the $1.24 2022 earnings contribution from the water business combined with a 15% premium to the 2022 regulated utility group average multiple of 17x applied to the $0.72 2022 earnings contribution from the LDC business, less the 2022 parent drag eps of $0.15 at a blended multiple of 25.8x

WEC

Our current $107 price target is premised upon a 30% premium to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS estimate of $4.45.

Our previous $94 price target was premised upon a 30% premium to the 2022 utility group average PE multiple of 17x applied to the prior Barclays 2022E EPS estimate of $4.24.

XEL

Our current $82 price target is premised upon a 30% premium to the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E EPS estimate of $3.40.

Our previous $70 price target was premised upon a 30% premium to the 2022 utility group average PE multiple of 17x applied to the Barclays 2022E EPS estimate of $3.15.

North America Power & Utilities **Industry View: POSITIVE**

Ameren Corp. (AEE)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	5,910	5,987	6,242	6,379	2.6%
EBITDA (adj)	2,262	2,389	2,615	2,784	7.2%
EBIT (adj)	1,267	1,364	1,561	1,701	10.3%
Pre-tax income (adj)	1,016	1,087	1,233	1,348	9.9%
Net income (adj)	828	844	953	1,042	8.0%
EPS (adj) ($)	3.35	3.38	3.73	4.00	6.1%
Diluted shares (mn)	247.1	249.4	255.7	260.4	1.8%
DPS ($)	1.92	1.98	2.04	2.10	3.0%

Margin and return data					Average
EBITDA (adj) margin (%)	38.3	39.9	41.9	43.6	40.9
EBIT (adj) margin (%)	21.4	22.8	25.0	26.7	24.0
Pre-tax (adj) margin (%)	17.2	18.2	19.8	21.1	19.1
Net (adj) margin (%)	14.0	14.1	15.3	16.3	14.9
ROIC (%)	7.1	6.3	6.6	6.7	6.7
ROA (%)	3.0	2.9	2.9	3.0	3.0
ROE (%)	10.9	10.5	10.6	10.0	10.5

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	24,376	26,181	28,116	30,021	7.2%
Cash and equivalents	16	1,954	1,919	1,794	382.2%
Total assets	28,933	32,676	34,576	36,356	7.9%
Short and long-term debt	9,797	12,576	13,120	14,102	12.9%
Other long-term liabilities	9,312	9,312	9,312	9,312	0.0%
Total liabilities	20,732	23,511	24,055	25,037	6.5%
Shareholders' equity	8,059	9,023	10,379	11,177	11.5%
Net debt/(funds)	9,781	10,622	11,201	12,308	8.0%
Change in working capital	80	1,690	-613	-57	N/A
Cash flow from operations	2,170	2,381	2,989	2,486	4.6%
Capital expenditure	-2,411	-2,830	-2,988	-2,988	N/A
Free cash flow	-713	-942	-520	-1,048	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	24.1	23.8	21.6	20.1	22.4
EV/EBITDA (adj) (x)	13.0	12.7	11.8	11.5	12.2
EV/EBIT (adj) (x)	23.2	22.2	19.8	18.8	21.0
FCF yield (%)	-2.4	-3.1	-1.7	-3.3	-2.6
P/BV (x)	2.5	2.2	2.0	1.9	2.1
Dividend yield (%)	2.4	2.5	2.5	2.6	2.5
Net debt/EBITDA (adj) (x)	4.3	4.4	4.3	4.4	4.4

Selected operating metrics					Average
Payout ratio (%)	57.3	58.4	54.6	52.4	55.7
Interest cover (x)	3.3	3.3	3.4	3.5	3.4
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 80.60**
Price Target	**USD 95.00**

Why Equal Weight? AEE is a quality name with 5-7% growth that is visible for an extended period of time and we see the name deserving of a 20% premium to the group. Given the current price and premium we see increased uncertainty surrounding the regulatory construct in IL as balanced by incremental potential growth opportunities, resulting in our EW rating.

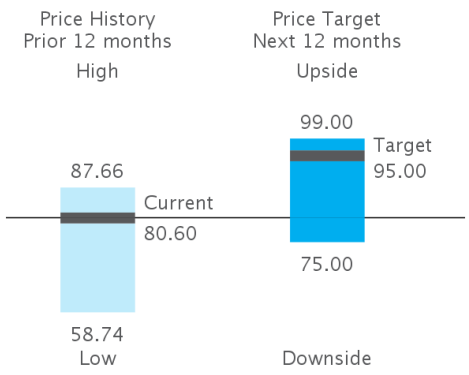
Upside case **USD 99.00**

Our upside case reflects a 25% premium to the 2023 group average P/E multiple applied to our 2023 EPS estimate.

Downside case **USD 75.00**

Our downside case reflects a 5% discount to the 2023 group average P/E multiple applied to our 2023 EPS estimate.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

American Electric Power Company, Inc. (AEP)

Stock Rating: OVERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	15,602	16,968	17,425	17,984	4.8%
EBITDA (adj)	8,504	5,675	5,998	6,516	-8.5%
EBIT (adj)	5,990	3,074	3,247	3,592	-15.7%
Pre-tax income (adj)	2,009	2,336	2,496	2,799	11.7%
Net income (adj)	2,095	2,159	2,308	2,584	7.2%
EPS (adj) ($)	4.23	4.35	4.62	5.00	5.7%
Diluted shares (mn)	494.9	496.0	499.0	516.4	1.4%
DPS ($)	2.68	2.84	3.01	3.19	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	54.5	33.4	34.4	36.2	39.7
EBIT (adj) margin (%)	38.4	18.1	18.6	20.0	23.8
Pre-tax (adj) margin (%)	12.9	13.8	14.3	15.6	14.1
Net (adj) margin (%)	13.4	12.7	13.2	14.4	13.4
ROIC (%)	12.9	6.1	6.0	6.1	7.8
ROA (%)	3.0	3.0	3.0	3.2	3.1
ROE (%)	11.0	10.4	11.0	12.0	11.1

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	79,585	85,385	91,915	99,962	7.9%
Cash and equivalents	311	931	956	855	40.1%
Total assets	72,748	76,567	80,371	85,393	5.5%
Short and long-term debt	25,648	29,166	32,478	37,120	13.1%
Other long-term liabilities	19,338	19,338	19,338	19,338	0.0%
Total liabilities	52,076	55,594	58,906	63,548	6.9%
Shareholders' equity	20,672	20,973	21,464	21,845	1.9%
Net debt/(funds)	25,337	28,236	31,523	36,265	12.7%
Change in working capital	776	14	905	503	-13.4%
Cash flow from operations	5,485	4,889	5,058	5,508	0.1%
Capital expenditure	-6,500	-5,800	-6,530	-8,047	N/A
Free cash flow	-2,341	-2,320	-2,975	-4,187	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	20.5	19.9	18.8	17.3	19.1
EV/EBITDA (adj) (x)	8.0	12.5	12.4	12.1	11.3
EV/EBIT (adj) (x)	11.4	23.1	22.9	22.0	19.8
FCF yield (%)	-3.4	-3.3	-4.0	-5.3	-4.0
P/BV (x)	2.1	2.1	2.0	2.1	2.0
Dividend yield (%)	3.1	3.3	3.5	3.7	3.4
Net debt/EBITDA (adj) (x)	3.0	5.0	5.3	5.6	4.7

Selected operating metrics					Average
Payout ratio (%)	63.3	65.3	65.1	63.8	64.4
Interest cover (x)	5.6	2.6	2.7	2.9	3.5
Regulated (%)	92.9	91.2	92.3	92.2	92.2

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	USD 86.73
Price Target	USD 107.00

Why Overweight? We assign an Overweight rating as we believe AEP should trade at a 10% premium to the average regulated utility multiple. This is supported by top-tier EPS growth target of 5-7% with a bias towards the high end.

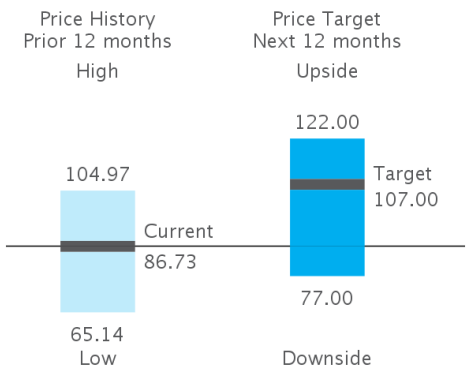
Upside case — **USD 122.00**

Our upside case reflects a 20% premium to the utility group average P/E multiple , applied to higher earnings driven by additional rate base growth and a favorable rate case outcomes.

Downside case — **USD 77.00**

Our downside case reflects a 20% discount to the utility group average P/E multiple, applied to lower earnings driven by slower rate base growth and unfavorable rate outcomes

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

American Water Works Company, Inc. (AWK)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	3,610	3,828	4,054	4,315	6.1%
EBITDA (adj)	2,032	2,231	2,382	2,541	7.7%
EBIT (adj)	1,450	1,606	1,717	1,831	8.1%
Pre-tax income (adj)	833	944	1,034	1,139	11.0%
Net income (adj)	621	705	772	850	11.0%
EPS (adj) ($)	3.77	3.89	4.25	4.63	7.1%
Diluted shares (mn)	181	181	182	184	0.5%
DPS ($)	1.96	2.15	2.34	2.55	9.2%

Margin and return data					Average
EBITDA (adj) margin (%)	56.3	58.3	58.8	58.9	58.1
EBIT (adj) margin (%)	40.2	42.0	42.4	42.4	41.7
Pre-tax (adj) margin (%)	23.1	24.7	25.5	26.4	24.9
Net (adj) margin (%)	17.2	18.4	19.0	19.7	18.6
ROIC (%)	9.3	10.0	10.2	10.3	9.9
ROA (%)	2.9	3.1	3.3	3.5	3.2
ROE (%)	10.6	11.5	11.9	12.3	11.6

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	23,941	25,741	27,496	29,426	7.1%
Cash and equivalents	60	41	47	68	4.1%
Total assets	22,682	23,272	24,369	25,609	4.1%
Short and long-term debt	9,453	9,552	9,971	10,091	2.2%
Other long-term liabilities	0	0	0	0	N/A
Total liabilities	7,917	8,341	8,326	8,605	2.8%
Shareholders' equity	6,121	6,502	6,918	7,749	8.2%
Net debt/(funds)	9,393	9,511	9,923	10,023	2.2%
Change in working capital	504	-585	7	21	-65.6%
Cash flow from operations	1,383	1,441	1,699	1,849	10.2%
Capital expenditure	-1,654	-1,650	-1,555	-1,755	N/A
Free cash flow	-859	-749	-482	-550	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	42.3	40.9	37.5	34.4	38.8
EV/EBITDA (adj) (x)	18.9	17.2	16.3	15.3	16.9
EV/EBIT (adj) (x)	26.4	23.9	22.6	21.3	23.6
FCF yield (%)	-2.2	-1.9	-1.2	-1.4	-1.7
P/BV (x)	4.7	4.4	4.2	3.8	4.3
Dividend yield (%)	1.2	1.3	1.5	1.6	1.4
Net debt/EBITDA (adj) (x)	4.6	4.3	4.2	3.9	4.2

Selected operating metrics					Average
Payout ratio (%)	57.1	55.3	55.2	55.1	55.7
Interest cover (x)	3.8	4.2	4.5	4.9	4.4
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 159.29**
Price Target	**USD 173.00**

Why Equal Weight? AWK presents a strong growth profile with top-tier management and a solid execution track record, however valuation is stretched relative to electric and gas utilties and our valuation framework implies a 15% premium to the water group average P/E multiple, all of which is fully reflected in the current stock price

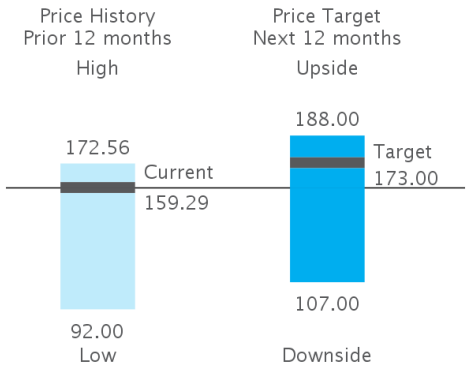
Upside case **USD 188.00**

Our upside case assumes AWK trades at a 25% premium to the group average water utility P/E multiple. We believe this scenario could materialize if ESG flows increase or general utility equity demand rises and disproportionately benefits AWK.

Downside case **USD 107.00**

Our downside case values AWK on the same 15% premium, but applies the group utitlity multiple in lieu of the water group multiple. This could materialize if investors perceive long-term growth opportunities and ESG profiles to be similar to electric and gas.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

CenterPoint Energy, Inc. (CNP)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	11,111	7,551	7,808	7,983	-10.4%
EBITDA (adj)	2,348	2,531	2,725	2,840	6.5%
EBIT (adj)	1,111	1,336	1,472	1,579	12.4%
Pre-tax income (adj)	813	995	1,099	1,204	14.0%
Net income (adj)	587	714	813	957	17.7%
EPS (adj) ($)	1.17	1.27	1.36	1.53	9.3%
Diluted shares (mn)	501.0	560.1	598.4	626.4	7.7%
DPS ($)	1.15	0.74	0.60	0.64	-18.0%

Margin and return data					Average
EBITDA (adj) margin (%)	21.1	33.5	34.9	35.6	31.3
EBIT (adj) margin (%)	10.0	17.7	18.8	19.8	16.6
Pre-tax (adj) margin (%)	7.3	13.2	14.1	15.1	12.4
Net (adj) margin (%)	5.3	9.5	10.4	12.0	9.3
ROIC (%)	4.9	6.8	6.5	7.2	6.4
ROA (%)	1.7	2.0	2.2	2.5	2.1
ROE (%)	7.1	7.2	7.7	8.6	7.7

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	20,650	21,797	23,113	24,472	5.8%
Cash and equivalents	1,124	0	6	11	-78.4%
Total assets	35,263	35,262	36,647	38,071	2.6%
Short and long-term debt	14,244	9,665	12,072	10,695	-9.1%
Other long-term liabilities	8,809	8,809	9,778	10,746	6.9%
Total liabilities	27,012	25,311	26,142	27,724	0.9%
Shareholders' equity	8,251	9,951	10,505	11,113	10.4%
Net debt/(funds)	13,120	9,665	12,066	10,684	-6.6%
Change in working capital	-3,263	-4,023	2,572	-2,005	N/A
Cash flow from operations	1,638	2,051	2,104	2,207	10.4%
Capital expenditure	2,506	2,342	2,569	2,620	1.5%
Free cash flow	3,567	3,978	4,314	4,429	7.5%

Valuation and leverage metrics					Average
P/E (adj) (x)	21.5	19.7	18.5	16.5	19.1
EV/EBITDA (adj) (x)	11.0	8.8	9.1	8.2	9.3
EV/EBIT (adj) (x)	23.2	16.7	16.8	14.8	17.8
FCF yield (%)	13.9	17.9	17.5	19.0	17.1
P/BV (x)	1.5	1.4	1.4	1.4	1.4
Dividend yield (%)	4.6	2.9	2.4	2.5	3.1
Net debt/EBITDA (adj) (x)	5.6	3.8	4.4	3.8	4.4

Selected operating metrics					Average
Payout ratio (%)	98.3	58.0	44.2	41.6	60.5
Interest cover (x)	2.0	2.7	2.6	2.8	2.5
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 25.17**
Price Target	**USD 27.00**

Why Equal Weight? We see upside potential from activist involvement and valuation expansion balanced by uncertainty on asset sales, strategic actions with Enable. We await results of the business review and see reduced risk now that the CEO and CFO positions have been filled with strong candidates.

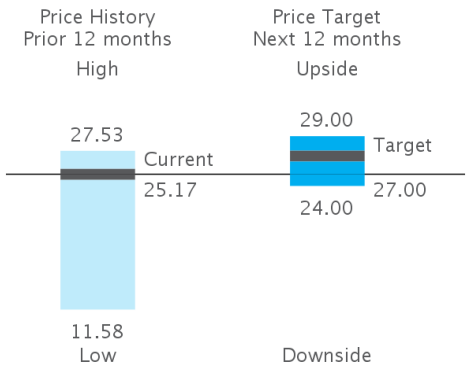
Upside case — **USD 29.00**

Our upside case for CNP values the company's Utility business on a 5% premium to the group average multiple for 2022 and utilizes the Barclays MLP upside case for ENBL.

Downside case — **USD 24.00**

Our downside case for CNP values the Utility business on a 20% discount to the group average multiple for 2022. We use the Barclays MLP team's downside case for ENBL.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

CMS Energy Corporation (CMS)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	6,845	6,949	7,096	7,299	2.2%
EBITDA (adj)	2,231	2,370	2,488	2,663	6.1%
EBIT (adj)	1,239	1,329	1,388	1,510	6.8%
Pre-tax income (adj)	829	935	1,006	1,108	10.2%
Net income (adj)	708	768	825	906	8.6%
EPS (adj) ($)	2.49	2.67	2.84	3.10	7.6%
Diluted shares (mn)	284.3	287.4	290.1	292.4	0.9%
DPS ($)	1.53	1.64	1.75	1.87	7.0%

Margin and return data					Average
EBITDA (adj) margin (%)	32.6	34.1	35.1	36.5	34.6
EBIT (adj) margin (%)	18.1	19.1	19.6	20.7	19.4
Pre-tax (adj) margin (%)	12.1	13.5	14.2	15.2	13.7
Net (adj) margin (%)	10.3	11.0	11.6	12.4	11.4
ROIC (%)	7.3	6.9	7.2	7.2	7.2
ROA (%)	2.5	2.7	2.8	2.9	2.7
ROE (%)	13.5	13.7	13.6	13.8	13.6

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	18,926	20,085	21,685	22,832	6.5%
Cash and equivalents	157	942	97	207	9.6%
Total assets	26,837	28,781	29,536	30,793	4.7%
Short and long-term debt	11,951	13,576	13,186	14,283	6.1%
Other long-term liabilities	383	383	383	383	0.0%
Total liabilities	21,782	23,177	23,462	24,209	3.6%
Shareholders' equity	5,055	5,604	6,073	6,583	9.2%
Net debt/(funds)	11,794	12,634	13,089	14,077	6.1%
Change in working capital	-217	1,015	-1,520	460	N/A
Cash flow from operations	1,790	1,811	1,928	2,061	4.8%
Capital expenditure	-2,104	-2,200	-2,700	-2,300	N/A
Free cash flow	-750	-860	-1,280	-787	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	25.6	23.9	22.4	20.6	23.1
EV/EBITDA (adj) (x)	13.4	13.0	12.5	12.1	12.7
EV/EBIT (adj) (x)	24.1	23.1	22.5	21.3	22.7
FCF yield (%)	-2.5	-2.8	-4.1	-2.4	-3.0
P/BV (x)	3.6	3.3	3.0	2.8	3.2
Dividend yield (%)	2.4	2.6	2.7	2.9	2.7
Net debt/EBITDA (adj) (x)	5.3	5.3	5.3	5.3	5.3

Selected operating metrics					Average
Payout ratio (%)	61.4	61.3	61.6	60.5	61.2
Interest cover (x)	2.8	3.1	3.3	3.5	3.2
Regulated (%)	93.1	93.3	93.4	93.6	93.3

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 63.83**
Price Target	**USD 75.00**

Why Equal Weight? We see the current valuation as fair given a constructive regulatory jurisdiction, 10-year capex backlog, above-average earnings/dividend growth, and a long history of achieveing or exceeding results through capital and O&M managment.

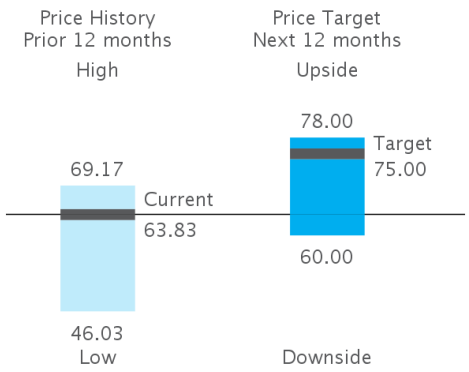
Upside case — **USD 78.00**

Our upside case values CMS at a 30% premium to the regulated utility average multiple applied to our 2023 EPS estimate.

Downside case — **USD 60.00**

Our downside case values CMS at the regulated utility average multiple applied to our 2023 EPS estimate.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Consolidated Edison, Inc. (ED)

Stock Rating: UNDERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	12,574	12,778	13,164	13,642	2.8%
EBITDA (adj)	4,360	4,776	5,041	5,316	6.8%
EBIT (adj)	6,044	6,702	7,094	7,522	7.6%
Pre-tax income (adj)	1,736	1,943	2,080	2,231	8.7%
Net income (adj)	1,438	1,438	1,546	1,666	5.0%
EPS (adj) ($)	4.36	4.25	4.47	4.72	2.7%
Diluted shares (mn)	329.5	338.7	346.0	352.8	2.3%
DPS ($)	2.96	3.06	3.17	3.28	3.5%

Margin and return data					Average
EBITDA (adj) margin (%)	34.7	37.4	38.3	39.0	37.3
EBIT (adj) margin (%)	21.3	22.3	22.7	22.8	22.3
Pre-tax (adj) margin (%)	13.8	15.2	15.8	16.4	15.3
Net (adj) margin (%)	11.5	12.0	12.5	12.9	12.2
ROIC (%)	7.3	7.1	6.8	6.8	7.0
ROA (%)	2.7	2.6	2.7	2.8	2.7
ROE (%)	8.6	8.5	8.6	8.6	8.6

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	43,889	46,355	48,337	50,171	4.6%
Cash and equivalents	1,217	2,050	1,128	1,388	4.5%
Total assets	58,079	61,378	62,438	64,532	3.6%
Short and long-term debt	18,527	20,690	23,230	24,246	9.4%
Other long-term liabilities	4,993	4,993	4,993	4,993	0.0%
Total liabilities	15,052	15,052	15,052	15,052	0.0%
Shareholders' equity	18,022	19,219	20,416	21,670	6.3%
Net debt/(funds)	17,310	18,640	22,102	22,858	9.7%
Change in working capital	139	160	0	0	-100.0%
Cash flow from operations	3,134	3,461	3,696	3,968	8.2%
Capital expenditure	-3,996	-4,392	-4,035	-4,040	N/A
Free cash flow	-1,028	-1,110	-914	-505	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	18.2	18.7	17.7	16.8	17.8
EV/EBITDA (adj) (x)	9.8	9.2	9.4	9.1	9.4
EV/EBIT (adj) (x)	7.1	6.6	6.7	6.4	6.7
FCF yield (%)	-2.4	-2.5	-1.9	-1.0	-2.0
P/BV (x)	1.4	1.4	1.3	1.3	1.4
Dividend yield (%)	3.7	3.9	4.0	4.1	3.9
Net debt/EBITDA (adj) (x)	4.0	3.9	4.4	4.3	4.1

Selected operating metrics					Average
Payout ratio (%)	67.8	72.2	71.0	69.5	70.1
Interest cover (x)	3.0	3.1	3.0	3.0	3.0
Regulated (%)	0.0	0.0	0.0	0.0	0.0

Price (17-Nov-2020)	**USD 79.25**
Price Target	**USD 83.00**

Why Underweight? We rate ED Underweight as we believe the current valuation is stretched based on a lack luster rate outcome for CECONY which drives a lower growth profile. We see the lower than group average growth as driving a 10% discount to the 2023 group average multiple.

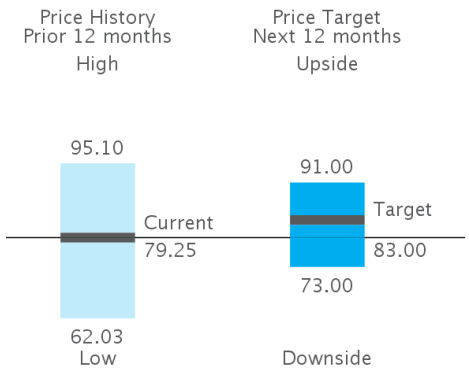
Upside case — **USD 91.00**

Our upside case reflects the utility group average P/E multiple to portray potentially higher earnings from additional rate base growth and a favorable O&R rate case outcome.

Downside case — **USD 73.00**

Our downside case reflects a 20% discount to the regulated group to reflect potentially lower earnings driven by lower sales growth and investment because of REV.

Upside/Downside scenarios



Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

North America Power & Utilities — **Industry View: POSITIVE**

Duke Energy Corporation (DUK)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	25,079	25,577	26,509	27,242	2.8%
EBITDA (adj)	10,257	10,697	11,321	11,941	5.2%
EBIT (adj)	5,709	6,000	6,431	6,861	6.3%
Pre-tax income (adj)	4,097	4,235	4,482	4,765	5.2%
Net income (adj)	3,707	3,792	4,008	4,243	4.6%
EPS (adj) ($)	5.08	5.14	5.24	5.51	2.7%
Diluted shares (mn)	729.5	737.0	765.1	770.3	1.8%
DPS ($)	3.79	3.97	4.17	4.38	5.0%

Margin and return data					Average
EBITDA (adj) margin (%)	40.9	41.8	42.7	43.8	42.3
EBIT (adj) margin (%)	22.8	23.5	24.3	25.2	23.9
Pre-tax (adj) margin (%)	16.3	16.6	16.9	17.5	16.8
Net (adj) margin (%)	14.8	14.8	15.1	15.6	15.1
ROIC (%)	5.3	5.4	5.8	6.1	5.6
ROA (%)	2.5	2.4	2.5	2.6	2.5
ROE (%)	8.5	8.2	8.2	8.8	8.4

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	146,916	156,091	164,766	173,316	5.7%
Cash and equivalents	276	779	549	290	1.8%
Total assets	156,797	161,730	164,898	168,123	2.4%
Short and long-term debt	61,947	63,177	63,714	66,277	2.3%
Other long-term liabilities	40,092	41,413	44,745	46,393	5.0%
Total liabilities	110,553	113,104	116,975	121,188	3.1%
Shareholders' equity	46,292	48,697	48,017	47,052	0.5%
Net debt/(funds)	61,671	62,399	63,165	65,987	2.3%
Change in working capital	95	950	1,202	107	3.8%
Cash flow from operations	9,086	9,220	9,629	10,053	3.4%
Capital expenditure	-11,100	-10,550	-9,675	-9,050	N/A
Free cash flow	-4,775	-4,260	-3,239	-2,372	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	18.3	18.1	17.7	16.9	17.8
EV/EBITDA (adj) (x)	12.4	12.0	11.4	11.0	11.7
EV/EBIT (adj) (x)	22.3	21.4	20.1	19.2	20.7
FCF yield (%)	-3.7	-3.3	-2.5	-1.8	-2.8
P/BV (x)	1.5	1.4	1.5	1.5	1.5
Dividend yield (%)	4.1	4.3	4.5	4.7	4.4
Net debt/EBITDA (adj) (x)	6.0	5.8	5.6	5.5	5.7

Selected operating metrics					Average
Payout ratio (%)	74.5	77.3	79.7	79.6	77.7
Interest cover (x)	2.6	2.6	2.6	2.6	2.6
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020) USD 92.92
Price Target USD 102.00

Why Equal Weight? We view DUK as a solid regulated company with a credible long-term investment plan. We see earnings growth rebounding back to the 4-6% off of a 2021 earnings base given the removal of ACP earnings from 2020 and 2021 earnings

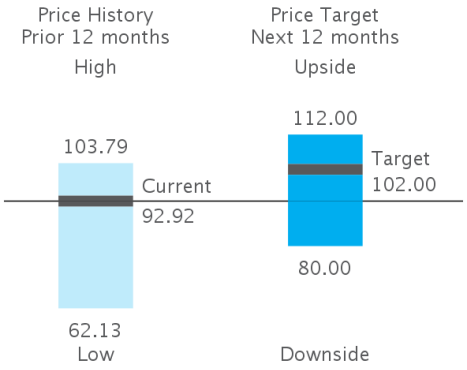
Upside case USD 112.00

Our upside case uses a 5% premium to the 2023 group average P/E multiple applied to our 2021 EPS estimate.

Downside case USD 80.00

Our downside case uses a 10% discount to the 2023 group average P/E multiple applied to our 2021 estimate.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Edison International (EIX)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	12,347	12,967	13,234	13,576	3.2%
EBITDA (adj)	3,505	4,401	4,705	5,083	13.2%
EBIT (adj)	1,775	2,410	2,559	2,762	15.9%
Pre-tax income (adj)	1,127	1,725	1,819	1,924	19.5%
Net income (adj)	1,284	1,644	1,736	1,845	12.8%
EPS (adj) ($)	4.70	4.43	4.58	4.85	1.1%
Diluted shares (mn)	339.7	371.2	378.9	380.1	3.8%
DPS ($)	2.45	2.55	2.58	2.61	2.2%

Margin and return data					Average
EBITDA (adj) margin (%)	28.4	33.9	35.5	37.4	33.8
EBIT (adj) margin (%)	14.4	18.6	19.3	20.3	18.2
Pre-tax (adj) margin (%)	9.1	13.3	13.7	14.2	12.6
Net (adj) margin (%)	10.4	12.7	13.1	13.6	12.4
ROIC (%)	5.2	6.5	6.5	6.6	6.2
ROA (%)	3.6	3.6	3.6	3.8	3.6
ROE (%)	10.1	10.6	10.2	10.4	10.4

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	54,329	59,229	64,629	70,029	8.8%
Cash and equivalents	68	470	2	38	-17.8%
Total assets	64,382	67,335	69,770	72,539	4.1%
Short and long-term debt	18,893	20,395	21,879	23,620	7.7%
Other long-term liabilities	0	0	0	0	N/A
Total liabilities	48,886	50,388	52,102	54,043	3.4%
Shareholders' equity	15,496	16,946	17,668	18,496	6.1%
Net debt/(funds)	18,825	19,925	21,877	23,582	7.8%
Change in working capital	73	-148	-1,180	-32	N/A
Cash flow from operations	-307	4,114	4,353	4,632	N/A
Capital expenditure	-4,877	-4,900	-5,400	-5,400	N/A
Free cash flow	-6,115	-1,900	-2,181	-1,906	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	14.0	14.8	14.3	13.5	14.2
EV/EBITDA (adj) (x)	11.5	9.4	9.2	8.8	9.7
EV/EBIT (adj) (x)	22.6	17.1	16.9	16.3	18.2
FCF yield (%)	-15.2	-4.6	-5.0	-4.2	-7.3
P/BV (x)	1.4	1.4	1.4	1.3	1.4
Dividend yield (%)	3.7	3.9	3.9	4.0	3.9
Net debt/EBITDA (adj) (x)	5.4	4.5	4.7	4.6	4.8

Selected operating metrics					Average
Payout ratio (%)	52.1	57.6	56.4	53.9	55.0
Interest cover (x)	2.1	2.7	2.7	2.7	2.6
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Price (17-Nov-2020)	**USD 65.60**
Price Target	**USD 69.00**

Why Equal Weight? We assign an Equal Weight rating as we believe questions around final net 17/18 liability risk, implementation of improved cost recovery parameters, and equity issuance mean EIX likely continues to trade at a discount for next 12 months.

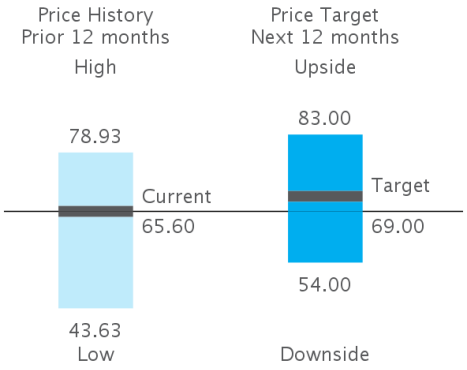
Upside case **USD 83.00**

The upside case applies a group average 2023 P/E multiple and assumes zero wildfire liability for 2017 / 2018 fires.

Downside case **USD 54.00**

Our downside case assumes $3.7bn net 2017 / 2018 wildfire liability and a 20% discount to the group average P/E multiple.

Upside/Downside scenarios



Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

North America Power & Utilities — **Industry View: POSITIVE**

Essential Utilities, Inc. (WTRG)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	890	1,880	2,056	2,315	37.5%
EBITDA (adj)	517	911	980	1,102	28.7%
EBIT (adj)	361	634	675	769	28.7%
Pre-tax income (adj)	261	436	479	551	28.2%
Net income (adj)	263	398	422	446	19.2%
EPS (adj) ($)	1.47	1.56	1.62	1.70	5.1%
Diluted shares (mn)	179	255	260	262	13.5%
DPS ($)	0.91	0.96	1.02	1.08	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	58.1	48.5	47.7	47.6	50.5
EBIT (adj) margin (%)	40.6	33.7	32.9	33.2	35.1
Pre-tax (adj) margin (%)	29.4	23.2	23.3	23.8	24.9
Net (adj) margin (%)	29.6	21.2	20.5	19.3	22.6
ROIC (%)	3.7	7.3	7.3	7.7	6.5
ROA (%)	N/A	3.1	3.1	3.1	3.1
ROE (%)	N/A	8.6	8.9	8.5	8.7

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	10,795	11,745	12,720	13,720	8.3%
Cash and equivalents	32	31	41	0	-100.0%
Total assets	12,929	13,601	14,281	14,907	4.9%
Short and long-term debt	5,225	3,950	4,075	4,572	-4.4%
Other long-term liabilities	766	2,531	2,561	2,423	46.8%
Total liabilities	8,315	8,844	9,055	9,519	4.6%
Shareholders' equity	4,613	4,765	5,226	5,388	5.3%
Net debt/(funds)	5,193	3,919	4,034	4,572	-4.2%
Change in working capital	N/A	0	-1	10	N/A
Cash flow from operations	0	713	784	802	N/A
Capital expenditure	0	-950	-975	-1,000	N/A
Free cash flow	0	-514	-767	-538	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	30.5	28.7	27.6	26.3	28.3
EV/EBITDA (adj) (x)	48.0	29.7	27.9	25.4	32.8
EV/EBIT (adj) (x)	68.8	42.7	40.5	36.4	47.1
FCF yield (%)	0.0	-1.9	-2.8	-1.9	-1.7
P/BV (x)	N/A	N/A	N/A	N/A	N/A
Dividend yield (%)	2.0	2.1	2.3	2.4	2.2
Net debt/EBITDA (adj) (x)	10.0	4.3	4.1	4.1	5.7

Selected operating metrics					Average
Payout ratio (%)	61.9	61.8	62.9	63.6	62.6
Interest cover (x)	3.0	4.6	5.1	5.3	4.5
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 44.88**
Price Target	**USD 50.00**

Why Equal Weight? We assign an Equal Weight rating to reflect transitory overhangs and a historically palatable valuation. We value WTRG on a sum of the parts basis and apply the utility group average P/E multiple, reflecting gas utility peers. The current share price reflects our valuation conclusion.

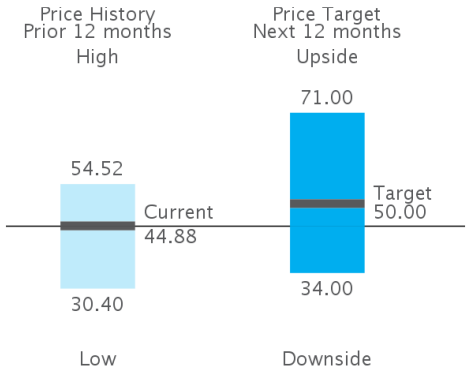
Upside case — **USD 71.00**

Our upside case assumes WTRG is valued using consolidated EPS against a water group P/E multiple. We believe this case could materialize if scarcity value persists and WTRG is deemed a pure-play water utility, despite the gas contribution to earnings.

Downside case — **USD 34.00**

Our downside case values WTRG consolidated EPS on the utility group average P/E multiple, while maintaining a 15% premium for the gas business and a 5% premium for water. We think this could materialize if ESG flows lessen or long-term growth appears unsustainable long term.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Eversource Energy (ES)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	8,526	8,915	9,155	9,413	3.4%
EBITDA (adj)	2,671	3,223	3,466	3,686	11.3%
EBIT (adj)	1,590	2,072	2,241	2,388	14.5%
Pre-tax income (adj)	1,190	1,619	1,776	1,893	16.7%
Net income (adj)	917	1,230	1,350	1,439	16.2%
EPS (adj) ($)	3.45	3.62	3.89	4.13	6.1%
Diluted shares (mn)	322.9	337.9	345.0	346.2	2.3%
DPS ($)	2.12	2.27	2.42	2.57	6.7%

Margin and return data					Average
EBITDA (adj) margin (%)	31.3	36.2	37.9	39.2	36.1
EBIT (adj) margin (%)	18.7	23.2	24.5	25.4	22.9
Pre-tax (adj) margin (%)	14.0	18.2	19.4	20.1	17.9
Net (adj) margin (%)	10.7	13.8	14.7	15.3	13.6
ROIC (%)	6.0	7.0	7.4	7.7	7.0
ROA (%)	2.2	2.8	3.0	3.1	2.8
ROE (%)	7.3	9.3	10.1	10.7	9.3

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	30,000	32,979	34,189	35,938	6.2%
Cash and equivalents	15	884	291	325	176.1%
Total assets	41,124	44,103	45,313	47,062	4.6%
Short and long-term debt	14,098	16,346	16,745	17,603	7.7%
Other long-term liabilities	9,052	9,202	9,352	9,502	1.6%
Total liabilities	28,494	30,858	31,968	33,617	5.7%
Shareholders' equity	12,630	13,245	13,345	13,445	2.1%
Net debt/(funds)	14,083	15,462	16,454	17,278	7.1%
Change in working capital	96	-1	112	110	4.7%
Cash flow from operations	2,010	2,300	2,493	2,650	9.7%
Capital expenditure	-2,911	-3,071	-2,834	-2,817	N/A
Free cash flow	-1,565	-1,538	-1,175	-1,058	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	26.6	25.4	23.6	22.2	24.4
EV/EBITDA (adj) (x)	16.4	14.0	13.3	12.7	14.1
EV/EBIT (adj) (x)	27.5	21.8	20.6	19.6	22.4
FCF yield (%)	-3.6	-3.4	-2.6	-2.3	-2.9
P/BV (x)	2.3	2.3	2.4	2.4	2.4
Dividend yield (%)	2.3	2.5	2.6	2.8	2.6
Net debt/EBITDA (adj) (x)	5.3	4.8	4.7	4.7	4.9

Selected operating metrics					Average
Payout ratio (%)	61.4	62.8	62.2	62.3	62.2
Interest cover (x)	5.0	5.4	5.6	5.6	5.4
Regulated (%)	100.0	100.0	200.0	200.0	150.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020) **USD 91.75**
Price Target **USD 100.00**

Why Equal Weight? We believe ES's diverse, high quality regulated business will grow base earnings at the midpoint of its 5-7% target through the forecast period. We apply a 25% valuation premium to reflect the above average growth, reasonable regulatory mechanisms that are in place, allowing the company to earn a prompt return on its regulatory investing.

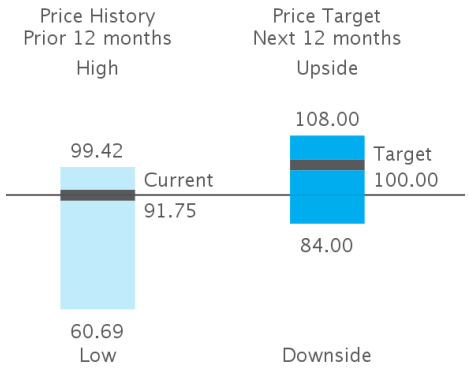
Upside case **USD 108.00**

We believe there are a number of large projects that could boost ES's earnings power and growth rate in the medium to long term. Offshore wind projects, the CGMA acquisition, grid mod, and elevated ESG fund flows could justify a 35% premium.

Downside case **USD 84.00**

An adverse change in regulation or legislation, while not expected, could result in a discount valuation for ES. We impute a 5% group discount to arrive at our downside case valuation.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

FirstEnergy Corp. (FE)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	11,035	11,733	12,076	12,365	3.9%
EBITDA (adj)	3,730	4,025	4,261	4,442	6.0%
EBIT (adj)	2,510	2,730	2,883	2,981	5.9%
Pre-tax income (adj)	1,117	1,750	1,838	1,923	19.9%
Net income (adj)	912	1,338	1,408	1,475	17.4%
EPS (adj) ($)	2.58	2.50	2.63	2.73	1.8%
Diluted shares (mn)	535.0	535.0	535.0	540.7	0.4%
DPS ($)	1.46	1.48	1.52	1.52	1.4%

Margin and return data					Average
EBITDA (adj) margin (%)	33.8	34.3	35.3	35.9	34.8
EBIT (adj) margin (%)	22.7	23.3	23.9	24.1	23.5
Pre-tax (adj) margin (%)	10.1	14.9	15.2	15.6	14.0
Net (adj) margin (%)	8.3	11.4	11.7	11.9	10.8
ROIC (%)	9.2	9.4	9.3	9.3	9.3
ROA (%)	5.1	5.0	5.1	5.0	5.1
ROE (%)	13.4	19.4	17.1	16.4	16.6

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	42,421	45,321	48,371	51,441	6.6%
Cash and equivalents	95	313	901	629	87.8%
Total assets	41,454	43,269	45,522	46,852	4.2%
Short and long-term debt	20,400	20,745	21,993	22,249	2.9%
Other long-term liabilities	11,260	11,429	11,647	11,888	1.8%
Total liabilities	34,541	35,055	36,520	37,018	2.3%
Shareholders' equity	6,913	8,214	9,002	9,835	12.5%
Net debt/(funds)	20,305	20,432	21,091	21,620	2.1%
Change in working capital	-148	223	598	-272	N/A
Cash flow from operations	2,139	3,439	3,049	3,231	14.7%
Capital expenditure	-2,952	-2,900	-3,050	-3,070	N/A
Free cash flow	-1,627	-296	-877	-769	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	11.1	11.5	10.9	10.5	11.0
EV/EBITDA (adj) (x)	9.5	8.9	8.5	8.3	8.8
EV/EBIT (adj) (x)	14.2	13.1	12.6	12.4	13.0
FCF yield (%)	-4.6	-0.8	-2.4	-2.1	-2.5
P/BV (x)	2.2	1.9	1.7	1.6	1.8
Dividend yield (%)	5.1	5.1	5.3	5.3	5.2
Net debt/EBITDA (adj) (x)	5.4	5.1	4.9	4.9	5.1

Selected operating metrics					Average
Payout ratio (%)	56.5	59.2	57.8	55.7	57.3
Interest cover (x)	2.4	2.3	2.3	2.4	2.3
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	USD 28.74
Price Target	USD 33.00

Why Equal Weight? We assign a 30% discount to the group average 23E PE against our pro forma EPS estimate, to account for potential penalties and fines along with a challenging ESG profile.

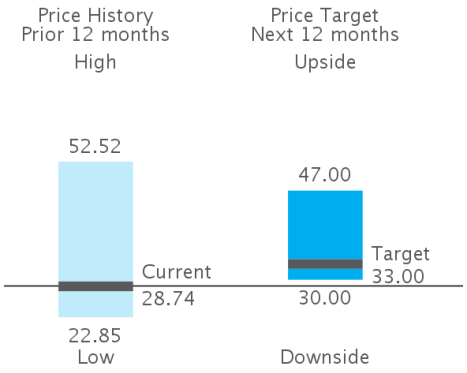
Upside case — **USD 47.00**

We apply a group average 23E PE multiple applied to our pro forma EPS estimate.

Downside case — **USD 30.00**

We apply a 35% discount to the group average 23E PE multiple applied to our pro forma EPS estimate.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

NextEra Energy, Inc. (NEE)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	19,204	19,827	20,284	20,613	2.4%
EBITDA (adj)	10,301	10,358	10,653	10,757	1.5%
EBIT (adj)	6,085	6,209	6,668	6,937	4.5%
Pre-tax income (adj)	4,568	4,609	4,934	5,208	4.5%
Net income (adj)	4,062	4,446	4,768	5,088	7.8%
EPS (adj) ($)	2.09	2.28	2.45	2.61	7.7%
Diluted shares (mn)	1,940	1,947	1,947	1,947	0.1%
DPS ($)	5.00	5.65	6.38	7.21	13.0%

Margin and return data					Average
EBITDA (adj) margin (%)	53.6	52.2	52.5	52.2	52.6
EBIT (adj) margin (%)	31.7	31.3	32.9	33.7	32.4
Pre-tax (adj) margin (%)	23.8	23.2	24.3	25.3	24.2
Net (adj) margin (%)	21.2	22.4	23.5	24.7	22.9
ROIC (%)	7.1	7.4	8.0	8.5	7.7
ROA (%)	3.9	4.0	4.2	4.5	4.1
ROE (%)	11.9	12.6	14.6	18.9	14.5

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	92,220	104,275	116,420	128,550	11.7%
Cash and equivalents	-6,221	-12,122	-20,894	-31,580	N/A
Total assets	111,836	114,089	113,734	111,620	-0.1%
Short and long-term debt	40,506	45,357	50,780	55,855	11.3%
Other long-term liabilities	22,941	22,941	22,941	22,941	0.0%
Total liabilities	71,705	76,556	81,979	87,054	6.7%
Shareholders' equity	35,289	32,691	26,913	19,724	-17.6%
Net debt/(funds)	46,727	57,479	71,674	87,435	23.2%
Change in working capital	5,402	-5,783	-10,170	-10,686	N/A
Cash flow from operations	7,747	7,147	7,227	7,263	-2.1%
Capital expenditure	-11,945	-11,680	-11,780	-11,780	N/A
Free cash flow	-13,170	-15,909	-17,348	-18,914	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	36.6	33.5	31.3	29.3	32.7
EV/EBITDA (adj) (x)	19.0	19.9	20.7	22.0	20.4
EV/EBIT (adj) (x)	32.2	33.3	33.1	34.1	33.2
FCF yield (%)	-6.7	-7.7	-7.9	-8.0	-7.6
P/BV (x)	4.2	4.6	5.5	7.6	5.5
Dividend yield (%)	6.5	7.4	8.3	9.4	7.9
Net debt/EBITDA (adj) (x)	4.5	5.5	6.7	8.1	6.2

Selected operating metrics					Average
Payout ratio (%)	238.8	247.4	260.7	276.0	255.7
Interest cover (x)	2.4	2.8	2.8	2.9	2.7
Regulated (%)	61.9	62.9	62.4	60.6	61.9

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 76.61**
Price Target	**USD 87.00**

Why Equal Weight? Top industry growth combined with an above-average regulatory environment drive the 20% premium valuation. Above-average growth provides for a larger increase to our expected price target, providing a compelling risk reward.

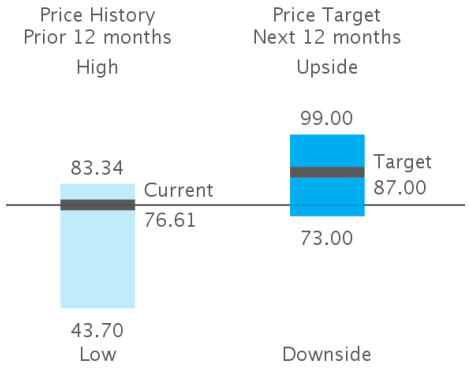
Upside case — **USD 99.00**

Our upside case applies a 30% premium multiple to the 2023 EPS estimates for the regulated utilities and assumes a 25% greater contribution from NEP and 20% greater contribution from NEER.

Downside case — **USD 73.00**

Our downside case applies an industry average multiple to 2023E earnings and assumes a 25% lower NEP value and a 15% lower contribution from NEER.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

NiSource, Inc. (NI)

Stock Rating: OVERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	5,209	5,250	5,173	5,387	1.1%
EBITDA (adj)	2,028	1,914	2,031	2,183	2.5%
EBIT (adj)	1,316	1,167	1,235	1,306	-0.2%
Pre-tax income (adj)	507	771	816	877	20.1%
Net income (adj)	495	518	551	597	6.4%
EPS (adj) ($)	1.32	1.33	1.38	1.43	2.9%
Diluted shares (mn)	376.0	389.5	400.4	415.8	3.4%
DPS ($)	0.80	0.85	0.90	0.95	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	38.9	36.5	39.3	40.5	38.8
EBIT (adj) margin (%)	17.1	22.0	23.7	24.1	21.7
Pre-tax (adj) margin (%)	9.7	14.7	15.8	16.3	14.1
Net (adj) margin (%)	9.5	9.9	10.6	11.1	10.3
ROIC (%)	5.7	7.1	7.1	7.4	6.8
ROA (%)	2.3	2.3	2.3	2.4	2.3
ROE (%)	8.6	8.6	8.5	8.5	8.6

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	16,912	18,023	19,385	21,816	8.9%
Cash and equivalents	139	-83	-295	-2,263	N/A
Total assets	22,660	23,548	24,698	25,161	3.6%
Short and long-term debt	9,629	9,840	10,332	10,038	1.4%
Other long-term liabilities	5,071	5,189	5,307	5,425	2.3%
Total liabilities	16,673	17,057	17,700	17,646	1.9%
Shareholders' equity	5,987	6,492	6,999	7,515	7.9%
Net debt/(funds)	9,490	9,923	10,627	12,301	9.0%
Change in working capital	89	1,496	-244	-2,091	N/A
Cash flow from operations	1,583	1,470	1,552	1,678	1.9%
Capital expenditure	-1,802	-1,750	-2,050	-3,200	N/A
Free cash flow	-219	-280	-498	-1,522	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	18.8	18.6	18.0	17.2	18.2
EV/EBITDA (adj) (x)	9.2	10.0	9.8	9.9	9.7
EV/EBIT (adj) (x)	14.2	16.4	16.1	16.5	15.8
FCF yield (%)	-1.2	-1.5	-2.5	-7.1	-3.1
P/BV (x)	1.6	1.5	1.4	1.4	1.5
Dividend yield (%)	3.2	3.4	3.6	3.8	3.5
Net debt/EBITDA (adj) (x)	4.7	5.2	5.2	5.6	5.2

Selected operating metrics					Average
Payout ratio (%)	60.8	63.8	65.3	66.4	64.1
Interest cover (x)	2.4	3.0	3.0	3.1	2.9
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 24.75**
Price Target	**USD 29.00**

Why Overweight? We view NI as a quality utility with a well-defined rate base growth strategy from gas and electric infrastructure modernization, which we see as relatively low risk. We believe opportunities for accelerated growth from legacy generation replacement power investments result in upside to the current valuation.

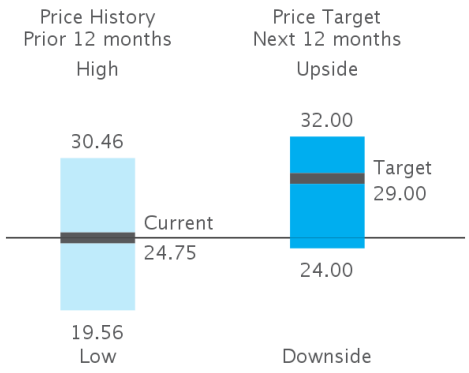
Upside case **USD 32.00**

Our upside case reflects a 5% premium to the 2023 utility group average P/E multiple applied to higher earnings driven by additional rate base growth and favorable rate case outcomes.

Downside case **USD 24.00**

Our downside case reflects a 10% discount to the 2023 utility group average P/E multiple applied to lower earnings driven by slower rate base growth and unfavorable rate case outcomes.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Northwestern Corporation (NWE)

Stock Rating: EQUAL WEIGHT

Income statement ($k)	2019A	2020E	2021E	2022E	CAGR
Revenue	1,250,610	1,256,145	1,278,443	1,296,992	1.2%
EBITDA (adj)	442,886	448,007	472,048	497,949	4.0%
EBIT (adj)	246,650	265,054	275,100	288,081	5.3%
Pre-tax income (adj)	174,895	168,261	179,547	193,468	3.4%
Net income (adj)	173,820	171,626	179,547	187,664	2.6%
EPS (adj) ($)	3.42	3.37	3.51	3.65	2.1%
Diluted shares (mn)	50.8	50.9	51.2	51.5	0.5%
DPS ($)	2.30	2.40	2.51	2.63	4.5%

Margin and return data					Average
EBITDA (adj) margin (%)	35.4	35.7	36.9	38.4	36.6
EBIT (adj) margin (%)	19.7	21.1	21.5	22.2	21.1
Pre-tax (adj) margin (%)	14.0	13.4	14.0	14.9	14.1
Net (adj) margin (%)	13.9	13.7	14.0	14.5	14.0
ROIC (%)	4.2	3.9	3.9	4.0	4.0
ROA (%)	3.1	2.9	2.9	3.0	3.0
ROE (%)	8.9	8.4	8.5	8.6	8.6

Balance sheet and cash flow ($k)					CAGR
Tangible fixed assets	N/A	N/A	N/A	N/A	N/A
Cash and equivalents	5,145	-5,215	-59,843	-163,534	N/A
Total assets	5,910,702	6,117,549	6,321,053	6,469,094	3.1%
Short and long-term debt	2,233,281	2,353,281	2,473,281	2,533,281	4.3%
Other long-term liabilities	1,638,327	1,655,982	1,668,637	1,684,292	0.9%
Total liabilities	3,871,608	4,009,263	4,141,918	4,217,573	2.9%
Shareholders' equity	2,039,094	2,108,286	2,179,135	2,251,520	3.4%
Net debt/(funds)	2,228,136	2,358,496	2,533,124	2,696,815	6.6%
Change in working capital	36,784	-28,015	-67,283	-119,346	N/A
Cash flow from operations	296,720	365,874	385,070	404,587	10.9%
Capital expenditure	-316,016	-398,800	-451,000	-456,000	N/A
Free cash flow	-134,423	-155,360	-194,628	-186,691	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	17.6	17.9	17.2	16.6	17.3
EV/EBITDA (adj) (x)	12.0	12.1	11.9	11.6	11.9
EV/EBIT (adj) (x)	21.5	20.5	20.4	20.0	20.6
FCF yield (%)	-2.5	-2.9	-3.5	-3.2	-3.0
P/BV (x)	1.4	1.4	1.3	1.3	1.3
Dividend yield (%)	3.8	4.0	4.2	4.4	4.1
Net debt/EBITDA (adj) (x)	5.0	5.3	5.4	5.4	5.3

Selected operating metrics					Average
Payout ratio (%)	67.2	71.3	71.7	72.1	70.6
Interest cover (x)	2.6	2.7	2.8	2.9	2.7
Regulated (%)	100.0	100.0	100.0	200.0	125.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 60.38**
Price Target	**USD 63.00**

Why Equal Weight? We believe a 10% discount to the group multiple is appropriate given below average growth and regulatory (although regulatory is improving). The current valuation shows the balanced risk reward profile.

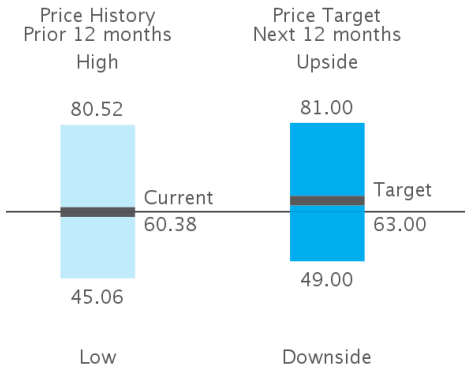
Upside case — **USD 81.00**

Our upside case assumes a 15% premium to the group average regulated utility multiple assuming a positive shift in regulatory framework and significant improvement to ratebase growth and visibility driven by self build of generation in support of capacity needs.

Downside case — **USD 49.00**

Our downside case assumes a 15% discount to the group average regulated utility multiple if regulatory issues persist and capacity needs are filled via purchased power contracts and not self build.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

OGE Energy Corp. (OGE)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	2,232	2,219	2,279	2,354	1.8%
EBITDA (adj)	859	913	961	1,025	6.1%
EBIT (adj)	504	538	569	615	6.9%
Pre-tax income (adj)	463	480	514	543	5.5%
Net income (adj)	434	432	453	467	2.5%
EPS (adj) ($)	2.16	2.15	2.26	2.33	2.5%
Diluted shares (mn)	201	201	201	201	0.0%
DPS ($)	1.51	1.59	1.65	1.72	4.4%

Margin and return data					Average
EBITDA (adj) margin (%)	38.5	41.2	42.2	43.5	41.3
EBIT (adj) margin (%)	22.6	24.2	25.0	26.1	24.5
Pre-tax (adj) margin (%)	20.8	21.6	22.6	23.1	22.0
Net (adj) margin (%)	19.4	19.5	19.9	19.8	19.6
ROIC (%)	7.0	7.4	7.7	8.2	7.6
ROA (%)	3.9	3.8	3.9	3.9	3.9
ROE (%)	10.5	10.2	10.4	10.4	10.3

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	9,045	9,244	9,578	9,898	3.1%
Cash and equivalents	0	86	6	45	N/A
Total assets	11,024	11,325	11,621	12,018	2.9%
Short and long-term debt	3,307	3,495	3,670	3,945	6.1%
Other long-term liabilities	3,032	3,032	3,032	3,032	0.0%
Total liabilities	6,885	7,073	7,248	7,523	3.0%
Shareholders' equity	4,140	4,253	4,374	4,496	2.8%
Net debt/(funds)	3,307	3,409	3,664	3,900	5.7%
Change in working capital	N/A	N/A	N/A	N/A	N/A
Cash flow from operations	682	792	802	839	7.2%
Capital expenditure	-636	-575	-725	-730	N/A
Free cash flow	46	217	77	109	33.3%

Valuation and leverage metrics					Average
P/E (adj) (x)	15.8	15.9	15.2	14.7	15.4
EV/EBITDA (adj) (x)	11.8	11.2	10.9	10.5	11.1
EV/EBIT (adj) (x)	20.1	19.1	18.5	17.5	18.8
FCF yield (%)	0.5	2.1	0.7	1.0	1.1
P/BV (x)	1.7	1.6	1.6	1.5	1.6
Dividend yield (%)	4.4	4.6	4.8	5.0	4.7
Net debt/EBITDA (adj) (x)	3.8	3.7	3.8	3.8	3.8

Selected operating metrics					Average
Payout ratio (%)	69.9	73.8	73.2	73.9	72.7
Interest cover (x)	5.7	5.9	6.0	5.9	5.9
Regulated (%)	80.8	81.5	81.7	82.8	81.7

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 34.21**
Price Target	**USD 36.00**

Why Equal Weight? While there recent developments for OK regulatory lag and ENBL options. The combination of Enable Midstream and Oklahoma Gas and Electric, while synergistic from a utility financing standpoint, is ultimately dilutive to the corporate growth rate. Fair and timely regulatory recovery remains a risk as OG&E's earned returns show a meaningful regulatory lag.

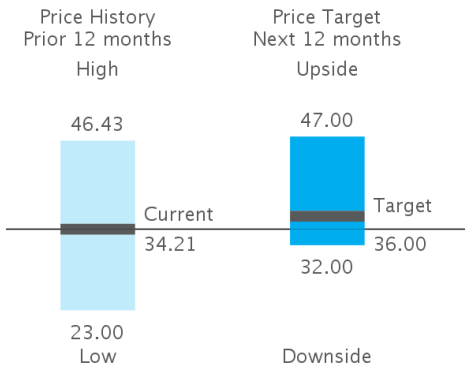
Upside case **USD 47.00**

Our upside case factors in a 10% utility P/E premium based on 2023 utility EPS combined with ENBL valued at $5/unit ($2 to OGE).

Downside case **USD 32.00**

Our downside case factors in a 20% discount to the group average at the utility, for higher regulatory risk and uncertainty. We value ENBL at $5 per unit ($2 to OGE).

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

PG&E Corporation (PCG)

Stock Rating: OVERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	17,129	18,698	19,498	19,769	4.9%
EBITDA (adj)	-6,860	6,500	6,945	7,394	N/A
EBIT (adj)	-10,094	2,977	3,149	3,341	N/A
Pre-tax income (adj)	-11,042	2,042	2,205	2,381	N/A
Net income (adj)	-7,656	2,021	2,184	2,360	N/A
EPS (adj) ($)	3.92	1.62	1.00	1.08	-35.0%
Diluted shares (mn)	528	1,250	2,180	2,190	60.7%
DPS ($)	0.00	0.00	0.00	0.00	N/A

Margin and return data					Average
EBITDA (adj) margin (%)	-40.0	34.8	35.6	37.4	16.9
EBIT (adj) margin (%)	-58.9	15.9	16.2	16.9	-2.5
Pre-tax (adj) margin (%)	-64.5	10.9	11.3	12.0	-7.5
Net (adj) margin (%)	-44.7	10.8	11.2	11.9	-2.7
ROIC (%)	-18.1	31.4	22.8	20.8	14.2
ROA (%)	-9.1	3.5	3.5	3.6	0.4
ROE (%)	-59.3	37.5	28.0	22.5	7.2

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	61,635	66,812	71,216	74,863	6.7%
Cash and equivalents	1,570	180	16	41	-70.3%
Total assets	85,196	89,013	93,253	98,025	4.8%
Short and long-term debt	52,046	1,850	3,350	3,350	-59.9%
Other long-term liabilities	21,631	19,901	19,901	19,901	-2.7%
Total liabilities	79,808	28,182	29,682	30,032	-27.8%
Shareholders' equity	5,388	7,811	10,476	12,767	33.3%
Net debt/(funds)	50,476	1,670	3,334	3,309	-59.7%
Change in working capital	-2,010	-1,664	-325	14	N/A
Cash flow from operations	4,816	5,858	6,812	5,595	5.1%
Capital expenditure	-6,313	-8,700	-8,200	-7,700	N/A
Free cash flow	-1,497	-2,842	-1,388	-2,105	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	3.0	7.2	11.7	10.9	8.2
EV/EBITDA (adj) (x)	-8.3	1.2	1.4	1.3	-1.1
EV/EBIT (adj) (x)	-5.6	2.6	3.0	2.8	0.7
FCF yield (%)	-2.6	-36.1	-14.6	-22.1	-18.9
P/BV (x)	1.1	1.9	2.4	2.0	1.9
Dividend yield (%)	0.0	0.0	0.0	0.0	0.0
Net debt/EBITDA (adj) (x)	-7.4	0.3	0.5	0.4	-1.5

Selected operating metrics					Average
Payout ratio (%)	0.0	0.0	0.0	0.0	0.0
Interest cover (x)	-7.3	6.9	7.3	7.7	3.7
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	USD 11.72
Price Target	USD 14.00

Why Overweight? We expect PCG's discount to close over the coming twelve months following resolution of the safety certification process, conclusion of the CPUC securitization regulatory proceeding, and eventual equity issuance in 2021.

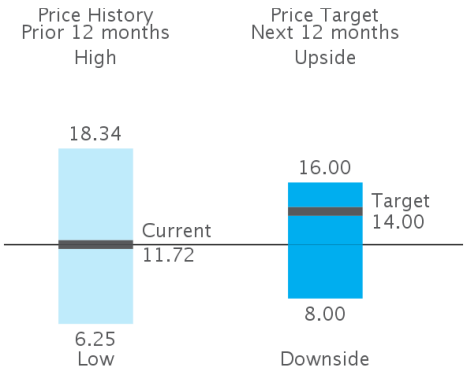
Upside case — **USD 16.00**

Our upside case assumes a group average multiple if PG&E is able to avoid large wildfires, reinstate the dividend, and execute at its guided growth rate for multiple years.

Downside case — **USD 8.00**

Our downside case assumes a 50% discount to the group average multiple. We would expect this draconian outcome to emerge if a large-scale wildfire is caused in a negligent manner without AB 1054 coverage if PCG cannot obtain a safety certificate.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Pinnacle West Capital Corporation (PNW)

Stock Rating: OVERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	3,471	3,576	3,694	3,788	3.0%
EBITDA (adj)	1,263	1,445	1,521	1,613	8.5%
EBIT (adj)	672	828	862	911	10.7%
Pre-tax income (adj)	542	679	735	770	12.4%
Net income (adj)	558	592	597	625	3.9%
EPS (adj) ($)	4.77	5.06	5.09	5.32	3.7%
Diluted shares (mn)	113	113	113	114	0.3%
DPS ($)	3.00	3.17	3.37	3.57	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	36.4	40.4	41.2	42.6	40.1
EBIT (adj) margin (%)	19.4	23.2	23.3	24.0	22.5
Pre-tax (adj) margin (%)	15.6	19.0	19.9	20.3	18.7
Net (adj) margin (%)	16.1	16.5	16.1	16.5	16.3
ROIC (%)	6.0	6.7	6.5	6.5	6.4
ROA (%)	2.9	2.9	2.8	2.8	2.8
ROE (%)	9.5	9.7	9.4	9.5	9.5

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	16,752	17,245	17,891	18,882	4.1%
Cash and equivalents	10	328	320	166	152.7%
Total assets	19,397	20,367	21,372	22,262	4.7%
Short and long-term debt	6,233	7,333	7,833	8,333	10.2%
Other long-term liabilities	N/A	N/A	N/A	N/A	N/A
Total liabilities	13,398	14,128	14,896	15,546	5.1%
Shareholders' equity	5,876	6,116	6,353	6,593	3.9%
Net debt/(funds)	6,222	7,005	7,513	8,167	9.5%
Change in working capital	2,190	107	627	49	-71.9%
Cash flow from operations	957	1,209	1,255	1,327	11.5%
Capital expenditure	-1,191	-1,263	-1,650	-1,725	N/A
Free cash flow	-504	-413	-776	-804	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	18.2	17.2	17.1	16.3	17.2
EV/EBITDA (adj) (x)	12.6	11.6	11.3	11.1	11.7
EV/EBIT (adj) (x)	23.7	20.2	20.0	19.6	20.9
FCF yield (%)	-3.2	-2.5	-4.5	-4.5	-3.7
P/BV (x)	1.7	1.6	1.5	1.5	1.6
Dividend yield (%)	3.5	3.7	3.9	4.1	3.8
Net debt/EBITDA (adj) (x)	4.9	4.8	4.9	5.1	4.9

Selected operating metrics					Average
Payout ratio (%)	62.7	62.8	66.2	67.0	64.7
Interest cover (x)	5.4	5.7	5.7	5.5	5.6
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 86.78**
Price Target	**USD 103.00**

Why Overweight? We rate PNW as Overweight based on current relative value within our regulated utility group. The price target is based on a group average 2023 EPS multiple.

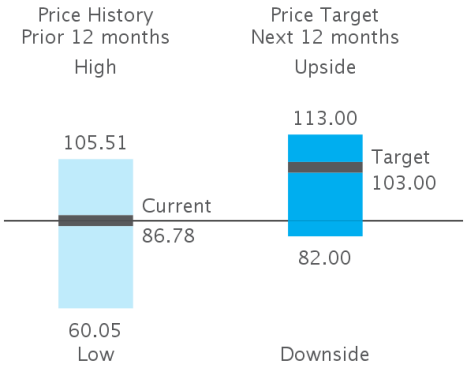
Upside case — **USD 113.00**

A 10% premium to the group P/E multiple is attributed to potential for above-average earnings and dividend growth, pending regulatory outcomes and economic conditions.

Downside case — **USD 82.00**

A 20% discount to the group P/E premised on lower-than-expected load growth combined with sub-optimal rate case, IRP, and retail competition outcomes.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

PNM Resources, Inc. (PNM)

Stock Rating: UNDERWEIGHT

Income statement ($k)	2019A	2020E	2021E	2022E	CAGR
Revenue	1,458,600	1,520,053	1,575,559	1,627,226	3.7%
EBITDA (adj)	592,681	659,408	710,685	755,341	8.4%
EBIT (adj)	324,873	369,625	399,052	427,233	9.6%
Pre-tax income (adj)	203,857	226,424	252,347	278,280	10.9%
Net income (adj)	172,540	183,665	203,623	223,103	8.9%
EPS (adj) ($)	2.16	2.28	2.37	2.60	6.4%
Diluted shares (k)	79,990	80,588	85,969	85,969	2.4%
DPS ($)	1.18	1.25	1.33	1.41	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	40.6	43.4	45.1	46.4	43.9
EBIT (adj) margin (%)	22.3	24.3	25.3	26.3	24.5
Pre-tax (adj) margin (%)	14.0	14.9	16.0	17.1	15.5
Net (adj) margin (%)	11.8	12.1	12.9	13.7	12.6
ROIC (%)	6.6	6.4	6.8	6.9	6.7
ROA (%)	2.5	2.5	2.5	2.7	2.6
ROE (%)	10.2	10.9	9.9	10.4	10.4

Balance sheet and cash flow ($k)					CAGR
Tangible fixed assets	7,918,601	8,724,601	9,700,601	10,460,601	9.7%
Cash and equivalents	3,833	301,081	-253,500	-403,382	N/A
Total assets	7,298,774	8,112,239	8,222,025	8,504,035	5.2%
Short and long-term debt	3,192,817	3,633,643	3,654,043	3,834,043	6.3%
Other long-term liabilities	2,060,565	2,060,565	2,060,565	2,060,565	0.0%
Total liabilities	5,557,024	5,997,850	6,018,250	6,198,250	3.7%
Shareholders' equity	1,678,698	2,051,337	2,140,723	2,242,733	10.1%
Net debt/(funds)	3,188,984	3,332,562	3,907,543	4,237,425	9.9%
Change in working capital	-463,542	63,016	355,018	-204,881	N/A
Cash flow from operations	503,163	488,217	530,025	565,980	4.0%
Capital expenditure	-616,273	-806,000	-976,000	-760,000	N/A
Free cash flow	-206,036	-419,337	-560,741	-315,640	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	22.7	21.5	20.6	18.8	20.9
EV/EBITDA (adj) (x)	12.0	11.0	11.0	10.8	11.2
EV/EBIT (adj) (x)	21.8	19.6	19.6	19.0	20.0
FCF yield (%)	-2.9	-5.8	-7.2	-3.9	-4.9
P/BV (x)	2.3	1.9	2.0	1.9	2.0
Dividend yield (%)	2.4	2.6	2.7	2.9	2.6
Net debt/EBITDA (adj) (x)	5.4	5.1	5.5	5.6	5.4

Selected operating metrics					Average
Payout ratio (%)	54.8	55.0	56.1	54.3	55.1
Interest cover (x)	4.9	4.6	4.8	5.1	4.9
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 48.90**
Price Target	**USD 50.00**

Why Underweight? We expect average to above-average earnings/dividend growth through the close of the transaction and believe management has provided adequate information to be confident they can achieve growth through the forecast period. Our price target and UW rating reflect the per share purchase price according to the terms of the AGR merger agreement.

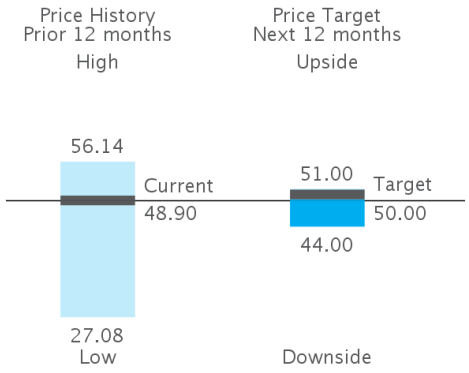
Upside case — **USD 51.00**

Our upside case comprises the small likelihood a topping bid from a competitor is seriously considered.

Downside case — **USD 44.00**

Our downside case assumes that the merger falls through and growth proceeds at a slower pace and the regulatory and/or economic landscape in NM does not improve. PNM could trade down to a 10% discount in this environment.

Upside/Downside scenarios



North America Power & Utilities **Industry View: POSITIVE**

Public Service Enterprise Group (PEG)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	10,076	8,660	8,778	8,768	-4.5%
EBITDA (adj)	3,191	3,583	3,729	3,873	6.7%
EBIT (adj)	1,943	2,272	2,344	2,418	7.6%
Pre-tax income (adj)	2,008	1,922	1,955	2,039	0.5%
Net income (adj)	1,666	1,742	1,726	1,759	1.8%
EPS (adj) ($)	3.28	3.43	3.40	3.46	1.8%
Diluted shares (mn)	508.0	508.0	508.0	508.0	0.0%
DPS ($)	1.88	1.96	2.04	2.12	4.1%

Margin and return data					Average
EBITDA (adj) margin (%)	31.7	41.4	42.5	44.2	39.9
EBIT (adj) margin (%)	19.3	26.2	26.7	27.6	25.0
Pre-tax (adj) margin (%)	19.9	22.2	22.3	23.3	21.9
Net (adj) margin (%)	16.5	20.1	19.7	20.1	19.1
ROIC (%)	6.7	7.6	7.7	7.2	7.3
ROA (%)	3.5	3.5	3.3	3.3	3.4
ROE (%)	10.9	10.9	10.3	10.1	10.6

Balance sheet and cash flow ($mn)					CAGR
Net PP&E	35,868	37,707	39,558	41,026	4.6%
Cash and equivalents	489	584	715	957	25.1%
Total assets	48,048	49,981	51,964	53,674	3.8%
Short and long-term debt	16,248	17,529	20,234	18,166	3.8%
Other long-term liabilities	13,689	13,917	13,795	16,194	5.8%
Total liabilities	32,779	33,966	35,258	36,286	3.4%
Shareholders' equity	15,269	16,016	16,705	17,387	4.4%
Net debt/(funds)	15,759	16,946	19,519	17,209	3.0%
Change in working capital	390	652	1,067	2,156	76.8%
Cash flow from operations	3,496	3,200	3,260	3,361	-1.3%
Capital expenditure	-3,149	-3,115	-3,203	-2,888	N/A
Free cash flow	-608	-910	-980	-604	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	18.0	17.2	17.4	17.1	17.4
EV/EBITDA (adj) (x)	14.3	13.1	13.3	12.2	13.2
EV/EBIT (adj) (x)	23.5	20.7	21.1	19.5	21.2
FCF yield (%)	-1.3	-1.9	-2.0	-1.3	-1.6
P/BV (x)	2.0	1.9	1.8	1.7	1.8
Dividend yield (%)	3.2	3.3	3.5	3.6	3.4
Net debt/EBITDA (adj) (x)	4.9	4.7	5.2	4.4	4.8

Selected operating metrics					Average
Payout ratio (%)	57.3	57.2	60.0	61.2	58.9
Interest cover (x)	5.6	5.8	5.7	6.0	5.7
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020) **USD 59.05**
Price Target **USD 65.00**

Why Equal Weight? PEG is a quality company that should be able to support 6%+ utility growth in our view based on current capital expenditure projections. As the merchant arm results in lower total EPS growth and the utility has risks on transmission ROE and the clean energy plan, we see PEG as an Equal Weight investment.

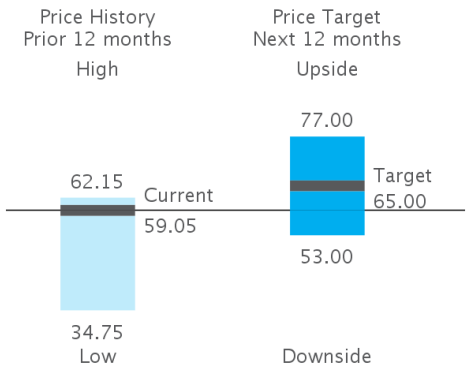
Upside case **USD 77.00**

This is a 20% premium to the 23 group average PE applied to our 23 eps estimate and a 7.5x EBITDA multiple applied to our 23 Power EBITDA.

Downside case **USD 53.00**

This is a 15% discount to the 23 group average PE applied to our 23 eps estimate, discounted to reflect lower transmission ROE and lower capital spending approved by the BPU estimate and a 5.0x EBITDA multiple applied to our 23 Power EBITDA.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Sempra Energy (SRE)

Stock Rating: OVERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	10,829	11,705	11,995	12,226	4.1%
EBITDA (adj)	4,380	4,640	4,789	5,071	5.0%
EBIT (adj)	2,811	2,994	2,992	3,131	3.7%
Pre-tax income (adj)	1,734	2,022	1,998	2,109	6.7%
Net income (adj)	2,055	2,237	2,505	2,683	9.3%
EPS (adj) ($)	7.29	7.57	7.99	8.49	5.2%
Diluted shares (mn)	282	295	313	316	3.9%
DPS ($)	3.87	4.20	4.56	4.94	8.5%

Margin and return data					Average
EBITDA (adj) margin (%)	40.4	39.6	39.9	41.5	40.4
EBIT (adj) margin (%)	26.0	25.6	24.9	25.6	25.5
Pre-tax (adj) margin (%)	16.0	17.3	16.7	17.2	16.8
Net (adj) margin (%)	19.0	19.1	20.9	21.9	20.2
ROIC (%)	6.1	6.8	6.4	6.4	6.4
ROA (%)	5.3	5.1	5.1	5.1	5.1
ROE (%)	12.0	11.2	12.0	12.2	11.8

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	36,452	40,466	44,219	46,079	8.1%
Cash and equivalents	108	993	949	1,973	163.4%
Total assets	65,665	65,864	69,573	72,456	3.3%
Short and long-term debt	25,816	23,215	25,055	26,055	0.3%
Other long-term liabilities	0	0	0	0	N/A
Total liabilities	43,860	41,259	43,099	44,099	0.2%
Shareholders' equity	19,929	20,926	22,003	23,124	5.1%
Net debt/(funds)	25,708	22,222	24,106	24,082	-2.2%
Change in working capital	-1,933	3,231	1,817	1,173	N/A
Cash flow from operations	3,088	3,566	5,111	5,405	20.5%
Capital expenditure	-3,708	-5,660	-5,550	-3,800	N/A
Free cash flow	-1,755	-3,480	-1,887	32	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	18.4	17.7	16.8	15.8	17.2
EV/EBITDA (adj) (x)	22.4	20.9	21.1	20.0	21.1
EV/EBIT (adj) (x)	34.9	32.3	33.7	32.3	33.3
FCF yield (%)	-1.8	-3.6	-1.9	0.0	-1.8
P/BV (x)	1.9	1.9	1.9	1.8	1.9
Dividend yield (%)	2.9	3.1	3.4	3.7	3.3
Net debt/EBITDA (adj) (x)	5.9	4.8	5.0	4.7	5.1

Selected operating metrics					Average
Payout ratio (%)	53.1	55.4	57.0	58.2	55.9
Interest cover (x)	2.6	3.1	3.0	3.1	2.9
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 134.06**
Price Target	**USD 159.00**

Why Overweight? We think SRE represents an attractive thematic investment opportunity to invest with a top-tier management team with exposure to the best parts of the North American energy story. We also see the CA utilities' rate case outcomes as constructive to support utility growth and stability. We believe recent sensitivity to weak global LNG prices is overdone.

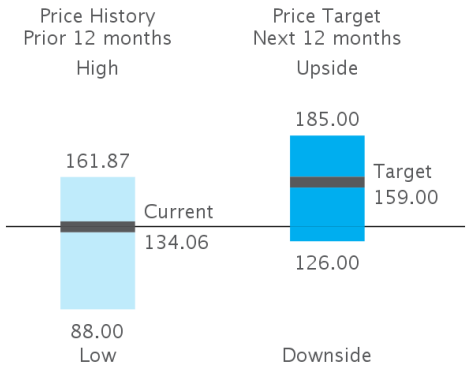
Upside case — **USD 185.00**

Our upside case assumes all LNG projects are FID'd and applies a 10% premium to SDG&E, a 15% premium in TX, and increases the SoCalGas premium to 15%.

Downside case — **USD 126.00**

Our downside case assumes no future LNG projects are FID'd, assumes the current Ienova stock price (mxn), and lowers SDG&E to a 20% discount, SoCalGas and Texas to a 10% and 15% discount, respectively.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

The Southern Company (SO)

Stock Rating: OVERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	21,419	21,943	22,397	23,008	2.4%
EBITDA (adj)	10,774	8,469	8,832	9,359	-4.6%
EBIT (adj)	7,736	5,408	5,614	5,962	-8.3%
Pre-tax income (adj)	6,542	3,951	4,057	4,447	-12.1%
Net income (adj)	4,739	3,353	3,443	3,775	-7.3%
EPS (adj) ($)	4.53	3.18	3.27	3.53	-8.0%
Diluted shares (mn)	1,046.0	1,054.0	1,054.0	1,068.4	0.7%
DPS ($)	2.30	2.38	2.46	2.54	3.4%

Margin and return data					Average
EBITDA (adj) margin (%)	50.3	38.6	39.4	40.7	42.3
EBIT (adj) margin (%)	36.1	24.6	25.1	25.9	27.9
Pre-tax (adj) margin (%)	30.5	18.0	18.1	19.3	21.5
Net (adj) margin (%)	22.1	15.3	15.4	16.4	17.3
ROIC (%)	10.8	8.0	7.7	8.1	8.6
ROA (%)	4.7	3.1	3.2	3.5	3.6
ROE (%)	12.2	9.0	9.0	9.3	9.9

Balance sheet and cash flow ($mn)					CAGR
Net PP&E	73,695	75,925	78,474	81,621	3.5%
Cash and equivalents	1,978	2,661	1,176	467	-38.2%
Total assets	109,000	106,002	109,025	113,492	1.4%
Short and long-term debt	29,834	25,295	27,728	27,529	-2.6%
Other long-term liabilities	19,063	20,552	20,851	22,249	5.3%
Total liabilities	67,393	63,447	64,038	65,922	-0.7%
Shareholders' equity	37,291	38,301	40,433	42,716	4.6%
Net debt/(funds)	27,856	22,634	26,552	27,062	-1.0%
Change in working capital	-1,567	-3,232	2,742	464	N/A
Cash flow from operations	5,781	6,418	6,664	7,175	7.5%
Capital expenditure	-7,555	-7,200	-6,900	-6,200	N/A
Free cash flow	-181	-3,291	-2,828	-1,739	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	13.8	19.6	19.1	17.7	17.6
EV/EBITDA (adj) (x)	8.4	10.1	10.1	9.6	9.6
EV/EBIT (adj) (x)	11.8	15.9	16.0	15.1	14.7
FCF yield (%)	-0.2	-3.8	-3.2	-1.9	-2.3
P/BV (x)	1.7	1.7	1.6	1.6	1.7
Dividend yield (%)	3.7	3.8	3.9	4.1	3.9
Net debt/EBITDA (adj) (x)	2.6	2.7	3.0	2.9	2.8

Selected operating metrics					Average
Payout ratio (%)	50.8	74.8	75.3	71.9	68.2
Interest cover (x)	-6.2	-4.3	-4.4	-4.6	-4.9
Regulated (%)	94.0	94.0	194.0	294.0	169.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 62.36**
Price Target	**USD 73.00**

Why Overweight? Southern is a high-quality company with above-average dividend payments, which has traded to a discount based on construction risk for Vogtle. With schedule and cost risks still lessening and the risks being schedule and cost, not technology, we see SO as rerating over the next 12 months, thus justifying our Overweight rating.

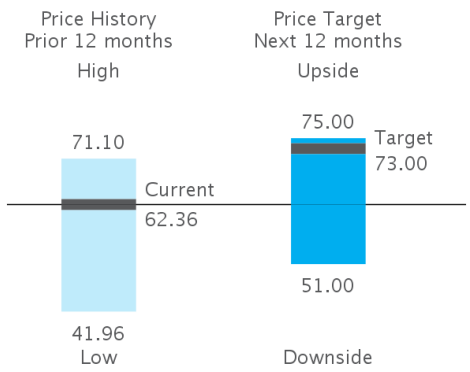
Upside case **USD 75.00**

We apply a 15% premium to group average 2023 P/E multiple on our 2023 EPS which includes the assumption that both Vogtle are in commercial operation in 2022

Downside case **USD 51.00**

We apply a 15% discount to the 2022 group average multiple applied to our 2022 EPS estimate and give no credit for future Vogtle earnings uplift

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

WEC Energy Group, Inc. (WEC)

Stock Rating: UNDERWEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	7,523	7,795	7,975	8,132	2.6%
EBITDA (adj)	2,458	2,701	2,840	2,971	6.5%
EBIT (adj)	1,531	1,734	1,805	1,870	6.9%
Pre-tax income (adj)	1,260	1,494	1,593	1,693	10.4%
Net income (adj)	1,134	1,195	1,273	1,353	6.1%
EPS (adj) ($)	3.58	3.77	4.02	4.27	6.1%
Diluted shares (mn)	316.7	316.7	316.7	316.7	0.0%
DPS ($)	2.36	2.53	2.68	2.84	6.3%

Margin and return data					Average
EBITDA (adj) margin (%)	32.7	34.7	35.6	36.5	34.9
EBIT (adj) margin (%)	20.4	22.2	22.6	23.0	22.1
Pre-tax (adj) margin (%)	16.7	19.2	20.0	20.8	19.2
Net (adj) margin (%)	15.1	15.3	16.0	16.6	15.8
ROIC (%)	5.0	4.9	4.9	5.0	4.9
ROA (%)	3.4	3.4	3.3	3.3	3.4
ROE (%)	11.6	11.8	12.1	12.4	12.0

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	32,751	35,725	38,817	41,866	8.5%
Cash and equivalents	38	427	303	-146	N/A
Total assets	34,952	38,473	40,598	42,190	6.5%
Short and long-term debt	12,692	14,048	15,122	15,710	7.4%
Other long-term liabilities	10,304	12,184	12,810	13,359	9.0%
Total liabilities	24,838	27,964	29,664	30,801	7.4%
Shareholders' equity	10,113	10,508	10,934	11,389	4.0%
Net debt/(funds)	12,654	13,621	14,819	15,857	7.8%
Change in working capital	-5	-569	615	-1,149	N/A
Cash flow from operations	2,346	2,763	2,909	3,055	9.2%
Capital expenditure	-2,261	-2,974	-3,093	-3,048	N/A
Free cash flow	-660	-1,011	-1,032	-892	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	28.0	26.6	24.9	23.4	25.7
EV/EBITDA (adj) (x)	18.1	16.8	16.4	16.0	16.8
EV/EBIT (adj) (x)	29.0	26.2	25.8	25.4	26.6
FCF yield (%)	-1.5	-2.2	-2.2	-1.9	-2.0
P/BV (x)	3.1	3.0	2.9	2.8	3.0
Dividend yield (%)	2.4	2.5	2.7	2.8	2.6
Net debt/EBITDA (adj) (x)	5.1	5.0	5.2	5.3	5.2

Selected operating metrics					Average
Payout ratio (%)	65.9	67.0	66.6	66.4	66.5
Interest cover (x)	3.1	3.4	3.5	3.5	3.4
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	USD 100.18
Price Target	USD 107.00

Why Underweight? We rate WEC as Underweight on its group high valuation, though meaningful dividend growth, significant free cash flow, and steady ratebase growth in a constructive regulatory jurisdiction provide a lower risk profile. We give WEC a 30% premium to the 2023 group average P/E multiple.

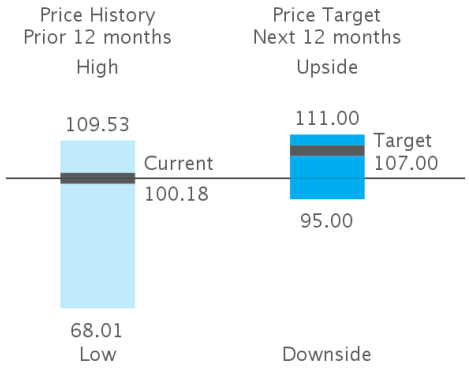
Upside case — **USD 111.00**

Our upside case assumes a 35% premium to the 2023 group average P/E multiple applied to our 2023 EPS estimate.

Downside case — **USD 95.00**

Our downside case assumes a 15% premium the group average multiple on our 2023 EPS estimate.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Xcel Energy Inc. (XEL)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	11,529	11,482	11,932	12,376	2.4%
EBITDA (adj)	4,038	4,154	4,463	4,800	5.9%
EBIT (adj)	2,273	2,243	2,417	2,602	4.6%
Pre-tax income (adj)	1,500	1,457	1,604	1,737	5.0%
Net income (adj)	1,372	1,455	1,604	1,737	8.2%
EPS (adj) ($)	2.64	2.77	3.01	3.21	6.8%
Diluted shares (mn)	520	526	533	541	1.3%
DPS ($)	1.62	1.72	1.82	1.93	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	35.0	36.2	37.4	38.8	36.8
EBIT (adj) margin (%)	19.7	19.5	20.3	21.0	20.1
Pre-tax (adj) margin (%)	13.0	12.7	13.4	14.0	13.3
Net (adj) margin (%)	11.9	12.7	13.4	14.0	13.0
ROIC (%)	4.1	4.2	4.2	4.1	4.1
ROA (%)	3.0	2.9	3.1	3.1	3.0
ROE (%)	9.5	8.7	10.8	9.0	9.5

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	39,483	42,291	45,325	48,785	7.3%
Cash and equivalents	248	-880	-65	1,077	63.1%
Total assets	50,448	52,125	55,993	60,615	6.3%
Short and long-term debt	18,704	19,804	21,405	22,775	6.8%
Other long-term liabilities	13,739	14,797	14,434	14,106	0.9%
Total liabilities	33,765	37,209	36,604	38,415	4.4%
Shareholders' equity	16,683	14,916	19,389	22,200	10.0%
Net debt/(funds)	18,456	20,684	21,471	21,698	5.5%
Change in working capital	-88	750	-704	1,161	N/A
Cash flow from operations	3,263	3,370	3,513	3,544	2.8%
Capital expenditure	-4,225	-4,800	-4,450	-4,900	N/A
Free cash flow	-1,753	-2,333	-1,907	-2,398	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	27.5	26.3	24.1	22.6	25.1
EV/EBITDA (adj) (x)	13.9	14.1	13.3	12.4	13.4
EV/EBIT (adj) (x)	24.7	26.1	24.5	22.9	24.5
FCF yield (%)	-3.1	-4.0	-3.2	-4.0	-3.6
P/BV (x)	2.3	2.6	2.0	1.8	2.1
Dividend yield (%)	2.2	2.4	2.5	2.7	2.4
Net debt/EBITDA (adj) (x)	4.6	5.0	4.8	4.5	4.7

Selected operating metrics					Average
Payout ratio (%)	61.3	62.0	60.4	60.0	60.9
Interest cover (x)	2.9	2.9	3.0	3.0	2.9
Regulated (%)	100.0	100.0	100.0	100.0	100.0

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020)	**USD 72.63**
Price Target	**USD 82.00**

Why Equal Weight? We rate XEL as Equal Weight as it is a well-run core large-cap utility whose mix of businesses and locations, coupled with solid operating results and visible growth, supports a 30% premium to the group average 2023 P/E multiple. XEL has rerated close to our expected premium.

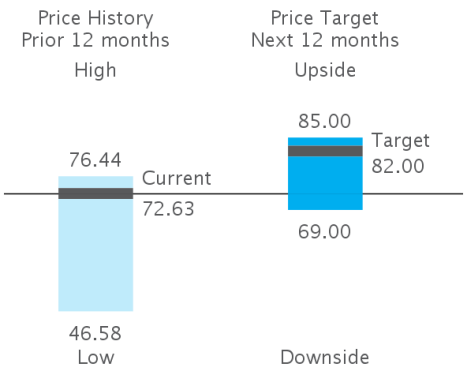
Upside case — **USD 85.00**

We use a 35% premium to the 2023 group average multiple applied to our 2023 EPS estimate.

Downside case — **USD 69.00**

We use a 10% premium to the 2023 group average multiple applied to our 2023 EPS estimate.

Upside/Downside scenarios



North America Power & Utilities **Industry View: POSITIVE**

Alliant Energy Corporation (LNT)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	3,648	3,678	3,780	3,890	2.2%
EBITDA (adj)	1,345	1,356	1,446	1,549	4.8%
EBIT (adj)	777	737	782	826	2.1%
Pre-tax income (adj)	635	553	567	625	-0.5%
Net income (adj)	556	610	630	695	7.7%
EPS (adj) ($)	2.33	2.46	2.52	2.78	6.1%
Diluted shares (mn)	239.0	247.5	250.0	250.0	1.5%
DPS ($)	1.41	1.52	1.61	1.71	6.5%

Margin and return data					Average
EBITDA (adj) margin (%)	36.9	36.9	38.3	39.8	38.0
EBIT (adj) margin (%)	21.3	20.0	20.7	21.2	20.8
Pre-tax (adj) margin (%)	17.4	15.0	15.0	16.1	15.9
Net (adj) margin (%)	15.3	16.6	16.7	17.9	16.6
ROIC (%)	6.6	5.7	5.7	5.6	5.9
ROA (%)	3.7	3.7	3.6	3.8	3.7
ROE (%)	12.1	11.7	10.4	10.5	11.2

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	13,527	14,263	14,870	15,749	5.2%
Cash and equivalents	16	346	511	809	267.5%
Total assets	16,701	17,791	18,587	19,788	5.8%
Short and long-term debt	6,528	6,776	6,974	7,514	4.8%
Other long-term liabilities	0	0	0	0	N/A
Total liabilities	11,296	11,544	11,742	12,282	2.8%
Shareholders' equity	5,205	6,048	6,645	7,306	12.0%
Net debt/(funds)	6,511	6,430	6,463	6,705	1.0%
Change in working capital	1,155	-165	193	-275	N/A
Cash flow from operations	660	1,239	1,304	1,428	29.3%
Capital expenditure	-1,640	-1,380	-1,295	-1,625	N/A
Free cash flow	-1,328	-527	-404	-634	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	23.5	22.2	21.7	19.7	21.8
EV/EBITDA (adj) (x)	14.8	14.6	13.7	13.0	14.0
EV/EBIT (adj) (x)	25.6	26.9	25.4	24.3	25.6
FCF yield (%)	-6.7	-2.7	-2.0	-3.2	-3.6
P/BV (x)	2.5	2.2	2.1	1.9	2.2
Dividend yield (%)	2.6	2.8	2.9	3.1	2.9
Net debt/EBITDA (adj) (x)	4.8	4.7	4.5	4.3	4.6

Selected operating metrics					Average
Payout ratio (%)	60.7	61.7	63.9	61.4	61.9
Interest cover (x)	2.8	2.7	2.8	2.7	2.8
Regulated (%)	92.5	92.5	92.3	92.4	92.4

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (17-Nov-2020) **USD 54.73**
Price Target **USD 65.00**

Why Equal Weight? We assign an Equal Weight rating to LNT given our view that the current premium to the 2023E group average multiple is appropriate for a name with strong renewable growth potential and an improving regulatory profile.

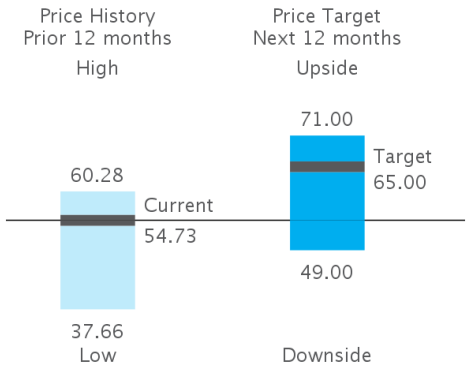
Upside case **USD 71.00**

Our upside case assumes a 25% premium to the group average 2023 utility P/E multiple, which we believe can be realized if LNT receives additional renewable capex approval, translates rate base growth to EPS growth more efficiently, or consistently beats guidance for 4-6 quarters.

Downside case **USD 49.00**

Our downside case assumes a 10% discount to the group average multiple, which we believe may occur if the WPL rate case is unfavorable or sales volumes are lower than expected and cash flow and earnings are put at risk.

Upside/Downside scenarios



Valuation Methodology and Risks

North America Power & Utilities
Alliant Energy Corporation (LNT)
Valuation Methodology: Our LNT price target is $65. We utilize a relative target P/E multiple to value LNT shares. We apply a 20% premium to the 18.5x group average 2023 P/E multiple to reflect LNT's strong track record for execution, visible earnings growth, attractive rate base growth opportunities driven by renewable generation that limit customer bill inflation, and constructive regulatory oversight.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Upside risks to our estimates and price target include better-than-expected regulatory outcomes, defensive equity flows, and increased M&A activity. Downside risks include inflation (commodity and PCE- leading to higher interest rates), adverse regulatory outcomes, project execution issues, or broad economic slowdown in LNT's service territories.
Ameren Corp. (AEE)
Valuation Methodology: Our $95 price target is derived by applying a 20% premium to the group average multiple of 18.5x to our 2023 EPS estimate of $4.28/share. We believe a premium multiple is appropriate at this time given the favorable regulatory structures AEE operates under in its primary jurisdictions of Missouri and Illinois.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Volatility of the US 30 Year Treasury Bond given formulaic rates in IL adds upside and downside risk. Threats to the IL QIP and uncertainty regarding the regulatory construct in IL and MO provide downside risk. Incremental spending opportunities from the MO IRP or clean energy legislation providing for higher levels of capex provide upside risk
American Electric Power Company, Inc. (AEP)
Valuation Methodology: Our price target for AEP is $107. We use a 10% premium to the 2023 regulated group average multiple of 18.5x applied to our 2023 estimate of $5.28 to reflect above average regulatory and long-term growth.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the company are: fair and timely rate recovery, regional economic impacts resulting in lower-than-expected usage, execution on cost controls to manage customer bill impacts.
American Water Works Company, Inc. (AWK)
Valuation Methodology: We utilize a group average water P/E multiple for 2023 earnings and apply a 15% premium to AWK's consolidated 2023 EPS estimate of $5.01. The premium reflects strong management, constructive regulatory exposure, and top-tier growth visibility.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to AWK include rate case outcomes, public system M&A deals and integration, external financing needs, and general interest rate environments.
CenterPoint Energy, Inc. (CNP)
Valuation Methodology: Our $27 price target is premised upon the 2023 utility group average P/E multiple of 18.5x against our 2023 EPS estimate. We use the current ENBL unit price adjusted for CNP's owned shares to account for the midstream segment value.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Equity needs if ENBL cuts its distribution, reaching EPS guidance through 2023, and realizing capex opportunities in IN remain as material upside/downside risks. Broader items that could also impact the shares: 1) economic growth impacting sales volumes, 2) constructive gubernatorial and commission changes benefiting regulation and legislation, and 3) cost control to manage customer bill impacts.
CMS Energy Corporation (CMS)
Valuation Methodology: Our $75 price target is derived by applying a 25% premium to the group average multiple of 18.5x to our 2023 EPS estimate of $3.25. CMS has a constructive regulatory relationship in Michigan and above-average earnings/dividend growth forecast.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major company risks are: broad economic impact slowing sales growth, inability to gain fair and timely regulatory recovery, gubernatorial and commission changes impacting regulation and legislation, Ability to control costs in order to manage customer bill impacts.
Consolidated Edison, Inc. (ED)
Valuation Methodology: Our ED price target is $83. We use a 10% discount to the 2023 group average P/E multiple of 18.5x applied to our 2023 EPS estimate of $4.94 to reflect an average regulatory environment, a more challenged earnings outlook, and low-risk profile.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the upside are: ED being able to achieve the full allowed ROE at CECONY, competition for growing NY transmission opportunities, and competition for behind-the-meter infrastructure based on REV.
Duke Energy Corporation (DUK)
Valuation Methodology: We derive our $102 price target for DUK by applying a 5% discount to the 2023 regulated group average multiple of 18.5x to 2023E regulated utility earnings for DUK of $5.81 per share. We believe a discount to the group average multiple is appropriate given the lack of earnings growth historically.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the company are: the ability to obtain fair and timely rate recovery,and recovery of coal ash costs. The ability to maintain credit metrics in order to avoid equity needs, regional economic impacts driving lower-than-expected usage, lower than expected regulatory recovery
Edison International (EIX)

Valuation Methodology and Risks

Valuation Methodology: Our $69 price target is based on a 20% discount to the 2023 group average multiple of 18.5x applied to an adjusted, post wildfire liability and additional funding, Barclays 2023 EPS estimate of $5.12. The 20% discount is based upon perceived wildfire risk absent a test of AB 1054 cost recovery standards and remaining uncertainty on 2017 and 2018 wildfire liabilities.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major upside/downside risks to the company are: final wildfire liability for 17/18 fires, ultimate legislation on inverse condemnation, and regulatory outcomes in pending and future rate cases.

Essential Utilities, Inc. (WTRG)

Valuation Methodology: We value WTRG's water business using a 5% premium to the group average water multiple. The 5% premium reflects strong regulatory exposure and public M&A opportunities, balanced by growth visibility lower than peers. We value the regulated gas business at a 15% premium to reflect a strong growth profile and familiar regulatory exposure.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to WTRG include rate case outcomes and general regulatory treatment, gas price inflation impacts on customer bills, and general interest rate environments.

Eversource Energy (ES)

Valuation Methodology: We derive our $100 price target by applying a 25% premium to the group average P/E multiple of 18.5x, to our 2023 earnings estimate of $4.34 per share. We believe a premium multiple is appropriate at this time given the nature of ES's growth profile, regulatory relationships, accretion from the Columbia Gas of MA acquisition and recovery mechanisms.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: The primary risk to our investment thesis is a change in regulation. We don't expect significant regulatory change in any of ES's jurisdictions at this time.

FirstEnergy Corp. (FE)

Valuation Methodology: Our $33 price target for FE is based on a 30% discount to the group average 2023 multiple of 18.5x applied to our pro forma FY23 EPS estimate, adjusted for an assumed $2bn equity issuance to reflect balance sheet repair following fines or penalties. The 30% discount is based on our expectation that the ongoing Ohio corruption investigation serves as an overhang to the stock valuation regardless of the financial impact.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major company risks are: OH corruption investigation, regulatory recovery in pending and future cases as well as prudency of spending associated with rate riders and formulaic rates; the ability to finance and execute on capital investment plans; broad economic impacts driving customer usage trends; and cost control execution to manage customer bill increases.

NextEra Energy, Inc. (NEE)

Valuation Methodology: Our price target of $87 is premised upon a SOTP with a 20% premium to the 2023 group average PE multiple of 18.5x applied to our 2023 EPS estimate of $1.74, a 17.5x 23E EV/EBITDA for the NEER business – comparable to valuations of renewables developers such as Ørsted. We then add $3 for NEP as we take the Barclays $67 NEP price target and flow it through to represent NEE's ownership.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: The major company risks are: ability to achieve fair and timely rate recovery, competition for renewable energy projects at NEER, federal legislation impacting profitability or competition of renewable generation, and regional economic impacts resulting in lower-than-expected usage.

NiSource, Inc. (NI)

Valuation Methodology: Our $29 price target is derived using the 2023 regulated utility group average P/E of 18.5x applied to our 2023 EPS estimate of $1.55. This reflects our view that NiSource, despite near-term headwinds, is a quality utility with a above-average medium-term rate base growth strategy from coal replacement power and gas and electric infrastructure modernization.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the company are: the ability to obtain fair and timely rate recovery, regional economic impacts driving lower-than-expected usage, and cost controls to manage customer rates.

NorthWestern Corporation (NWE)

Valuation Methodology: Our $63 price target is derived using the 2023 regulated utility group average P/E of 18.5x discounted by 10% to account for lower than average growth, applied to our 2023 EPS estimate of $3.79. We believe favorable geographic attributes of the state are outweighed by regulatory challenges and uncertainties in Montana.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the company are: fair and timely rate recovery; regional economic impacts; potential ability to manage customer bill impacts. Upside risks include positive regulatory outcomes and potential for new build of capacity resources in Montana.

OGE Energy Corp. (OGE)

Valuation Methodology: We derive our $36 price target by applying a 10% discount to the group average multiple of 18.5x applied to our 2023 utility earnings estimate combined with the current ENBL price $5 applied to the 111 units that OGE owns.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: OGE's capital plans impute less than 5% rate base growth. This is lower than the group average and is indicative of a below average regulatory jurisdiction. The upside is that as most companies grow earnings at or below the rate base growth level, OGE has the opportunity to grow regulated earnings in the 4-6% level on solid customer growth combined with potential to close the earned to allowed ROE gap that exists. The key (upside and downside risk) to enhancing growth lies in gaining rider approvals in Oklahoma. As significant generation and environmental spending is winding down, grid modernization, reliability, resiliency and technology are the next set of major spending programs.

PG&E Corporation (PCG)

Valuation Methodology and Risks

Valuation Methodology: Our $14 price target is based on a 35% discount to the group average 2023E P/E multiple of 18.5x against a $1.25 EPS estimate, reduced by the NPV of wildfire fund contributions, assuming the fund lasts 15 years.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: There is additional downside risk if capital structure changes lead to additional equity, future wildfires occur, or earnings are negatively impacted by regulatory outcomes.

Pinnacle West Capital Corporation (PNW)

Valuation Methodology: Our $103 price target is derived by applying the group average multiple of 18.5x, to our 2023 EPS estimate of $5.56. We expect the company to deliver average EPS and above-average dividend growth through 2023. In our view, the current regulatory uncertainty and geographic attributes justify a discount to the group average P/E multiple on a 2023 utility earnings.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major company risks to the downside include: 1) poor regulatory outcome of current APS rate case, 2) economic impact of lower sales growth, 3) ability to control costs in order to manage customer bill impacts and potential to allow retail choice, 4) deterioration of the regulatory construct.

PNM Resources, Inc. (PNM)

Valuation Methodology: Our $50 price target is premised upon the 2023 utility group average PE multiple of 18.5x applied to the Barclays 2023E eps $2.68 estimate. Our price target is consistent with the terms of the AGR acquisition offer.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Events and outcomes that could result in under performance are: lack of regulatory support for the acquisition or a change in management sentiment regarding the acquisition.

Public Service Enterprise Group (PEG)

Valuation Methodology: Our price target for PEG is $65. We use a sum of the parts methodology, where we use a 5% premium to the 2023 regulated group average PE multiple of 18.5x applied to our 2023 EPS estimate for the utility and parent earnings of $3.18 and apply a 5X EBITDA multiple to the 2023 genco earnings.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Volatility in power prices, changes to the structure of the PJM, NYISO of NEPOOL capacity or energy markets. FERC ROE changes, or NJ BPU approval or changes to the pending Clean Energy Future capital spending plans.

Sempra Energy (SRE)

Valuation Methodology: We utilize a sum of the parts valuation framework for SRE. We apply a relative P/E multiple premium / discount to the North American utility businesses a base group average (10% premium for Texas, 15% for SoCalGas, group average for SDG&E). We utilize the Barclays Ienova Price Target and adjust for SRE ownership and spot USDMXN for Peso translation. We utilize a probability-weighted DCF approach for the LNG business depending on where each facility is on securing contracting for export capacity.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks include incremental equity needs, FIDs at LNG projects, construction problems, and negative regulatory outcomes.

The Southern Company (SO)

Valuation Methodology: We derive our $73 price target by applying the 2023 regulated group average P/E multiple of 18.5x to our 2023 EPS estimate of $3.92 for SO

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the company are: Adverse regulatory outcomes for Vogtle or the upcoming Georgia rate case; additional, unexpected delays to the plant Vogtle schedule; economic impacts that would drive lower electric usage; competition for renewable and contract generation impacting Southern Power's growth; and ability to drive O&M lower in order to earn the allowed ROE in each jurisdiction.

WEC Energy Group, Inc. (WEC)

Valuation Methodology: Our price target of $107 represents a 30% premium valuation relative to the utility peer group P/E multiple of 18.5x on our 2023 EPS estimate of $4.45. We believe this premium valuation is justified by the strong performance record the company has achieved and our belief that its forward growth goals are both realistic and achievable.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to the upside are: Continued load growth; higher than regulated returns from nonregulated renewable investments; ability to get fair and timely rate recovery; execution on cost controls; continued flight to safety and flows into the "comfort" group of utilities.

Xcel Energy Inc. (XEL)

Valuation Methodology: Our $82 price target is based on a 30% premium to the group average multiple of 18.5x applied to our 2023 EPS estimate of $3.40. We believe this premium valuation fairly reflects the quality, strength, and potential endurance of the company's growth.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Major risks to the company are: ability to obtain fair and timely rate recovery, execution on coal to renewable generation transformation, ability to maintain credit metrics while financing its long-term capital plan, and execution on cost control to manage customer bill impact.

Source: Barclays Research.

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Primary Stocks (Ticker, Date, Price)

Alliant Energy Corporation (LNT, 17-Nov-2020, USD 54.73), Equal Weight/Positive, CE/J/K/M

Ameren Corp. (AEE, 17-Nov-2020, USD 80.60), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

American Electric Power Company, Inc. (AEP, 17-Nov-2020, USD 86.73), Overweight/Positive, A/CD/CE/D/E/J/K/L/M/N

American Water Works Company, Inc. (AWK, 17-Nov-2020, USD 159.29), Equal Weight/Positive, CE/J

CenterPoint Energy, Inc. (CNP, 17-Nov-2020, USD 25.17), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

CMS Energy Corporation (CMS, 17-Nov-2020, USD 63.83), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

Consolidated Edison, Inc. (ED, 17-Nov-2020, USD 79.25), Underweight/Positive, A/CD/CE/D/J/K/L/M

Duke Energy Corporation (DUK, 17-Nov-2020, USD 92.92), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

Edison International (EIX, 17-Nov-2020, USD 65.60), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

Essential Utilities, Inc. (WTRG, 17-Nov-2020, USD 44.88), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

Eversource Energy (ES, 17-Nov-2020, USD 91.75), Equal Weight/Positive, A/CD/CE/D/E/J/K/L/M

FirstEnergy Corp. (FE, 17-Nov-2020, USD 28.74), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

NextEra Energy, Inc. (NEE, 17-Nov-2020, USD 76.61), Equal Weight/Positive, A/CD/CE/D/E/J/K/L/M

NiSource, Inc. (NI, 17-Nov-2020, USD 24.75), Overweight/Positive, A/CD/CE/D/J/K/L/M

NorthWestern Corporation (NWE, 17-Nov-2020, USD 60.38), Equal Weight/Positive, CD/CE/J

OGE Energy Corp. (OGE, 17-Nov-2020, USD 34.21), Equal Weight/Positive, CE/J

PG&E Corporation (PCG, 17-Nov-2020, USD 11.72), Overweight/Positive, A/CD/CE/D/J/K/L/M

Pinnacle West Capital Corporation (PNW, 17-Nov-2020, USD 86.78), Overweight/Positive, A/CD/CE/D/E/J/K/L/M

PNM Resources, Inc. (PNM, 17-Nov-2020, USD 48.90), Underweight/Positive, CD/CE/FA/J

Public Service Enterprise Group (PEG, 17-Nov-2020, USD 59.05), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

Sempra Energy (SRE, 17-Nov-2020, USD 134.06), Overweight/Positive, A/CD/CE/D/J/K/L/M

The Southern Company (SO, 17-Nov-2020, USD 62.36), Overweight/Positive, A/CD/CE/D/J/K/L/M

WEC Energy Group, Inc. (WEC, 17-Nov-2020, USD 100.18), Underweight/Positive, A/CD/CE/D/J/K/L/M

Xcel Energy Inc. (XEL, 17-Nov-2020, USD 72.63), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

Materially Mentioned Stocks (Ticker, Date, Price)

NextEra Energy Partners LP (NEP, 17-Nov-2020, USD 64.77), Equal Weight/Neutral, CE/J

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Brookfield Renewable Energy Partners LP (BEP_u.TO)	Covanta Holding (CVA)	Enphase Energy (ENPH)
Enviva Partners LP (EVA)	First Solar (FSLR)	GFL Environmental (GFL)
GFL Environmental (GFL.TO)	NextEra Energy Partners LP (NEP)	Plug Power, Inc. (PLUG)
SolarEdge Technologies Inc. (SEDG)	SunPower (SPWR)	Sunrun Inc. (RUN)
North America Power & Utilities		
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American Water Works Company, Inc. (AWK)	Brookfield Infrastructure Partners LP (BIP)	Brookfield Infrastructure Partners LP (BIP_u.TO)
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Exelon Corporation (EXC)	FirstEnergy Corp. (FE)	NextEra Energy, Inc. (NEE)
NiSource, Inc. (NI)	NorthWestern Corporation (NWE)	OGE Energy Corp. (OGE)
PG&E Corporation (PCG)	Pinnacle West Capital Corporation (PNW)	PNM Resources, Inc. (PNM)
Portland General Electric Company (POR)	Public Service Enterprise Group (PEG)	Sempra Energy (SRE)
The Southern Company (SO)	WEC Energy Group, Inc. (WEC)	Xcel Energy Inc. (XEL)

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BARCLAYS

Equity Research
22 April 2021

North America Power & Utilities

Straight from the Tap: US Water Utility Monthly

INDUSTRY UPDATE

North America Power & Utilities
POSITIVE
Unchanged

For a full list of our ratings, price target and earnings changes in this report, please see table on page 2.

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In this month's Straight from the Tap, we preview 1Q21 earnings for AWK and WTRG and discuss recent regulatory updates and potential implications of forthcoming water infrastructure legislative efforts.

AWK 1Q21 preview summary - 1Q21E EPS: $0.73. We expect a very straightforward 1Q21E earnings release for AWK as the company enters a relative quiet period now that PA, NJ, and MO rate cases are in the rear view mirror. We expect management commentary to highlight the strong regulated M&A execution YTD following the York deal (*AWK: Regulated M&A Train Rolls Through York, PA*, published 4/7/21), in line with upsized guidance on the 4Q20 call in February. We also anticipate commentary on potential legislative packages at the federal and state level. AWK's New York divestiture is the only remaining overhang, albeit unlikely to prove material in our view, as Governor Cuomo's efforts to push for municipalization as part of a larger budget bill seemingly stalled in the legislature. We reiterate our Equal Weight rating for AWK given our view that the sizable premium to the regulated utility group captures growth upside from regulated M&A amidst a broader ESG prioritization in both politics and financial markets.

WTRG 1Q21 preview summary - 1Q21E EPS: $0.66. We expect a cleaner 1Q21 EPS print as YoY comps now reflect the Peoples deal, though regulatory and legal updates could prove to be more nuanced. We are interested to hear management's perspective on the recent Delcora ALJ stay order, legal case progress, and how the process interacts with financing planning. We expect additional color on Peoples Gas rate case timing following WTRG's commitment to file a base rate case by year-end 2023. The company made the commitment as part of its repairs tax settlement to placate intervenor concerns about potential overearning from ongoing tax benefits above forecast. We expect management to provide a summary of the settlement terms and how the flow-through regulatory accounting interacts with earnings given the agreement compensates customers for 100% of catch-up benefits via a fixed annual surcredit for five years, while WTRG will not monetize the tax benefits as long as it retains an NOL position. We reiterate our Equal Weight rating on WTRG and believe the discount to AWK reflects a lower growth outlook and AWK's pure-play water scarcity. We do not expect near-term Delcora uncertainty to have a material impact longer term, but acknowledge risk that a protracted process serves as an overhang. With repairs tax nearly complete, we think a simplified profile with upside potential from regulated M&A should resonate with investors after Delcora is resolved.

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Completed: 22-Apr-21, 01:26 GMT Released: 22-Apr-21, 04:10 GMT Restricted - External

Summary of our Ratings, Price Targets and Earnings Changes in this Report (all changes are shown in bold)

Company	Rating		Price	Price Target			EPS FY1 (E)			EPS FY2 (E)		
	Old	New	21-Apr-21	Old	New	%Chg	Old	New	%Chg	Old	New	%Chg
North America Power & Utilities	Pos	Pos										

Source: Barclays Research. Share prices and target prices are shown in the primary listing currency and EPS estimates are shown in the reporting currency.
FY1(E): Current fiscal year estimates by Barclays Research. FY2(E): Next fiscal year estimates by Barclays Research.
Stock Rating: OW: Overweight; EW: Equal Weight; UW: Underweight; RS: Rating Suspended
Industry View: Pos: Positive; Neu: Neutral; Neg: Negative

AWK 1Q21 Earnings Expectations

1Q21E EPS Bridge

Our $0.73 1Q21E EPS estimate contemplates various rate increases from infrastructure surcharges, limited issue trackers, and partial realization of rate relief following GRC decisions at AWK's largest operating companies in PA and NJ. Surcharges and general rate relief is expected to provide more than enough offset to incremental financing and operational costs throughout FY21, though rate relief pacing shifts much of the cash benefit post 1Q21. We note that AWK's guidance basis EPS now includes DD&A benefits associated with the NY sale, the impact on Q1 is de minimis, as only $0.01 is added back to reported 1Q20 adjusted EPS.

FIGURE 1

AWK 1Q21E YoY Drivers

AWK EPS Walk	
1Q20A	**$0.67**
Rates and Customer Growth	$0.05
Infrastructure	$0.03
NY DD&A	$0.01
MBB	$0.01
Weather	$0.01
Additional DD&A	-$0.02
Interest Drag	-$0.03
1Q21E	**$0.73**

Source: Barclays Research

Expected Call Topics:

Regulated M&A Execution

We are expecting management to highlight the York wastewater deal and the general market strength for regulated M&A across AWK's national footprint (FMV laws cover 10 states and water quality accountability laws cover 3). We do not anticipate changes to the guidance provided during AWK's combined 4Q20 earnings and Investor Day in February, but expect a reiteration of confidence amidst strong early execution.

Sentiment on regulated M&A has been strong in recent months as muni budgets are strained following Covid-19 and environmental compliance costs are expected to rise as EPA enforcement rates increase under President Biden's administration. However, numerous federal policy proposals being floated to provide direct investment or bolster funding access for municipal water infrastructure could, all else equal, reduce the impetus to sell to AWK.

We believe it is too early to predict final terms of any water infrastructure package, as Republicans have not presented a counter proposal, but President Biden's proposal indicates that lead pipe replacement and water quality standards (contaminant regulations, PFAS monitoring and remediation) are going to be prioritized (see: *link*). While specific earmarks for rural and disadvantaged communities could help, we note that major cities and large municipal systems have historically received the bulk of federal funding versus smaller systems that AWK tends to prefer as acquisition opportunities. Regardless of likely concession and compromises, the President's proposal allocates $45bn for lead pipe replacement (WIIN grants), $56bn for disadvantaged and rural communities (upsize existing programs), and $10bn to remediate PFAS in drinking water and upgrade small rural systems. $110bn compares to the American Society of Civil Engineers estimate that $1tn of water

infrastructure investment is needed in the US over the coming 25 years. The infrastructure package is light on wastewater systems, which we anticipate will continue to make up the bulk of regulated M&A moving forward. Thus, we see plenty of opportunities for AWK in small to medium wastewater systems (5,000-30,000 average customer systems).

NYAW Exit Headaches Persist

At Governor Cuomo's direction, on March 29, 2021, the New York Department of Public Service (DPS) presented a municipalization feasibility study that concluded a public takeover of AWK's Nassau County system is the optimal and least cost option. The primary concern from lawmakers is the outsized customer bill (a result of high local property and franchise taxes that make up 38%-60% of total bills) and an upcoming rate increase (26% increase in some rate classes) set to take effect on May 1, 2021. The DPS report found that municipalization was the optimal path because the inefficient tax collection structure creates numerous inequities and inefficiencies, including paying higher federal taxes when compared to a scenario where NYAW becomes tax exempt and those tax revenues are replaced with higher property taxes. The recommendations from the DPS were to immediately pass legislation to remove the property tax burden on NYAW and create a public authority to acquire NYAW and operate the assets as a public provider.

There was a push to include municipalization authority in the 2021-2022 budget, however efforts stalled in the Assembly on concerns about how special franchise taxes might be absorbed by Long Island utilities under the proposed process. Standalone bills to defer the rate increase and authorize a public takeover were introduced after the budget efforts collapsed, and the Senate passed a version on Tuesday (4/20/21) as negotiations are ongoing with the Assembly.

We see the outcome of the NYAW process as highly uncertain, but remain confident that the PSC will stand by the authorized rate increase if needed and do not see a scenario where AWK receives less than the Liberty offer. However, we stress that the size of the system likely means AWK will comfortably absorb any near-term financial impacts from a delay. The DPS study assumes the $608mn sale price that Liberty agreed to, plus $84.5mn in rate base investment in 2022, less ~$25mn for upstate assets that would be retained and deferrals owed to customers, resulting in a net purchase price of $669.2mn. However, the study is explicit that the math is illustrative and likely inflated (maintaining negotiating options).

CA American Water Cost of Capital

CA water utilities will file updated cost of capital proceedings by May 1, 2021, to determine authorized ROE and capital structures for test years 2022-2024. CA American Water is currently authorized a 9.2% ROE on 55.39% equity layer from a 2018 CPUC decision. It is worth noting that the ALJ proposed decision suggested an 8.23% ROE (avg US water ROE was 9.5%), which was met with significant industry backlash before commissioners decided on the higher 9.20%. It is also important to note that the WRAM decoupling mechanism was a critical element that the ALJ relied upon to justify below industry returns given lower risk. In 2020, the CPUC decided that the WRAM decoupling mechanism used by CA American Water will be replaced by a new structure to be determined during the next rate case covering test years 2024-2026. It is unclear how the cost of capital proceeding will handle the overlap and uncertainty around a replacement. For additional thoughts on the WRAM decision, see our Straight from the Tap note published 9/8/2020 (*link*).

WTRG 1Q21 Earnings Expectations

1Q21E EPS Bridge

Our 1Q21E EPS estimate of $0.66 accounts for small rate relief via water infrastructure surcharges and a full year of Peoples integration. Our estimate is in line with management's projections for first quarter earnings weighting of 35%-45% of $1.64-$1.69 FY21E EPS

guidance (implicit 1Q21 guidance range of $0.58-$0.74 using the FY21 guidance midpoint). We anticipate a small amount of volumetric help YoY given customer growth (guidance 2%-3% annually) and degree day comps for gas usage in PA. We also note residential water usage trends have been strong during the covid-19 shutdowns and margin help may continue to pace favorably relative to 1Q20, providing additional flexibility to meet FY21 guidance. We also forecast small organic growth and operational efficiencies for Peoples relative to the early days of the integration in 1Q20, in line with WTRG's O&M initiatives across the business.

FIGURE 2
WTRG 1Q21E YoY Drivers

WTRG EPS Walk	
1Q20A	**$0.60**
Water Rates	$0.01
Weather and Usage	$0.03
Peoples	$0.02
1Q21E	**$0.66**

Source: Barclays Research

Expected Call Topics:

Peoples Rate Case Timing

As part of WTRG's settlement on the catch-up component of repairs tax, Peoples committed to filing a general rate case no later than December 31, 2023 (Peoples will also likely implement the DSIC mechanism in 2023). Under the initial proposal, WTRG proposed a sharing mechanism that would have allowed Peoples Gas to stay out through 2026.

The settlement effectively provides customers 100% of $381mn catch-up deduction tax savings benefits via a $27.9mn annual surcredit over five years (true up in sixth year). The settlement acknowledges that Peoples is operating in an NOL position and thus cannot monetize the benefit near term, thus justifying the five-year deferral and includes various true up and reconciliation terms to ensure surcredits track actual tax benefits flowing through to Peoples.

Taking Steps Forward at Delcora but Stuck in Regulatory and Legal Maze

We discussed the ALJ PD calling for the PA PUC to reject the Delcora acquisition in the January 22 monthly, *Straight from the Tap*. The PD had three main concerns; 1) commercial customer objections to the deal, 2) the effective rate stabilization plan creation via trust refunds on bills, and 3) the ongoing legal challenge to the sale contract. The Commission took into account new settlements with numerous customers and clarifying comments from WTRG around its willingness to provide trust benefits off of customer bills to avoid being a 'de facto' rate stabilization plan and decided not to adopt the ALJ PD.

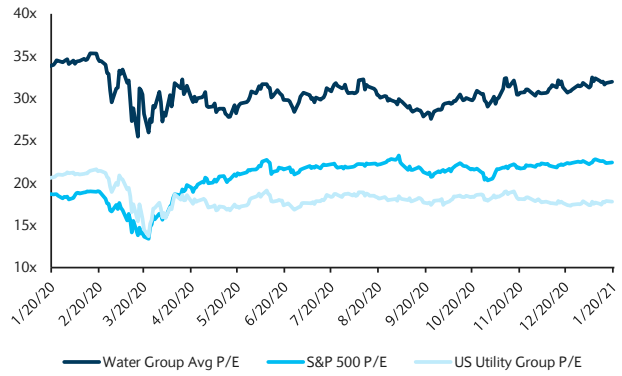
The PUC vacated the PD and remanded back to the ALJ level to reopen the docket. Importantly, as part of the reopening of the docket WTRG agreed to waive the statutory timeline requirements for a decision. The new ALJ on April 16 issued a stay order for the PA PUC proceeding until a final, un-appealable decision is reached in the county court case on whether an enforceable contract exists. Our understanding is that the appeals process could be lengthy and that WTRG will likely seek to have the ALJ order changed to allow for approval while legal appeals on contract validity play out.

We view the Delcora situation as bureaucratically complicated but the deal remains achievable if WTRG continues to execute settlements and legal decisions are upheld, however the timeline remains unclear. WTRG's $300mn forward equity mechanism must be pulled

down by August. We still believe WTRG is likely to issue all authorized equity regardless of whether Delcora is approved in time. We also see the guidance range as intact regardless of the deal given strong M&A activity outside of Delcora. We anticipate management will highlight the strength of their deal backlog and general market activity.

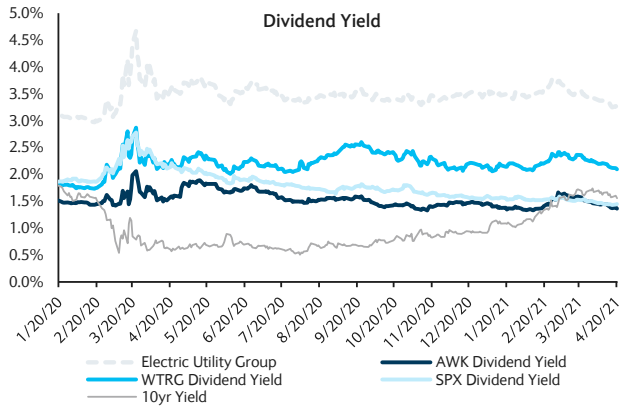
Monthly Valuation Trends

FIGURE 3
Group P/E Trends



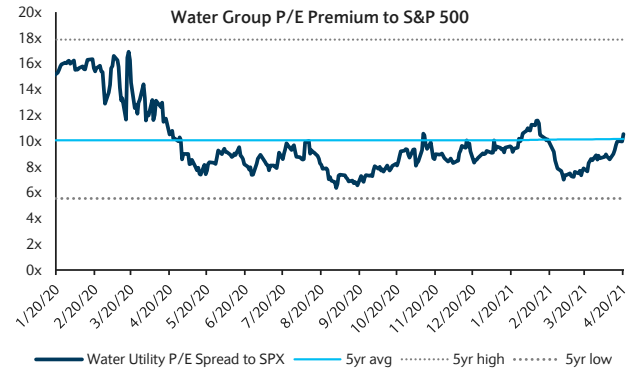
Source: Barclays Research, Bloomberg

FIGURE 4
Group Yield Trends



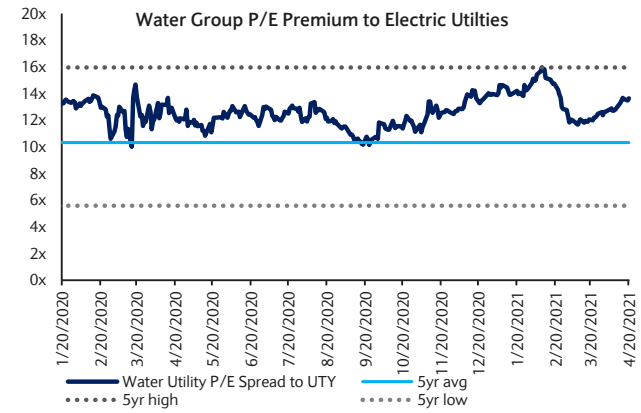
Source: Barclays Research, Bloomberg

FIGURE 5
Water Group Premium to S&P 500



Source: Barclays Research, Bloomberg

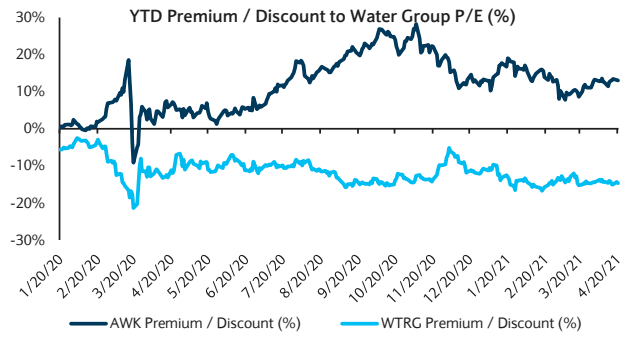
FIGURE 6
Water Group Premium to Regulated Utility Group



Source: Barclays Research, Bloomberg

FIGURE 7

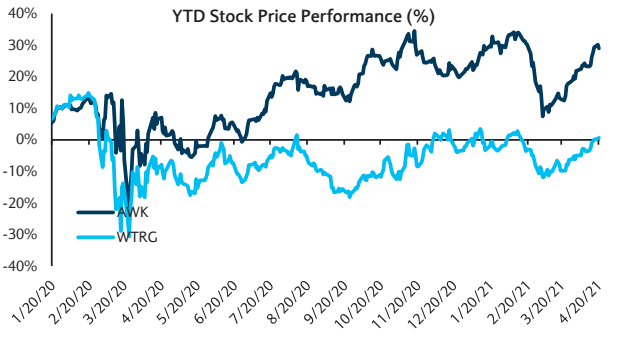
AWK and WTRG Premium (Discount) to Water Group



Source: Barclays Research, Bloomberg

FIGURE 8

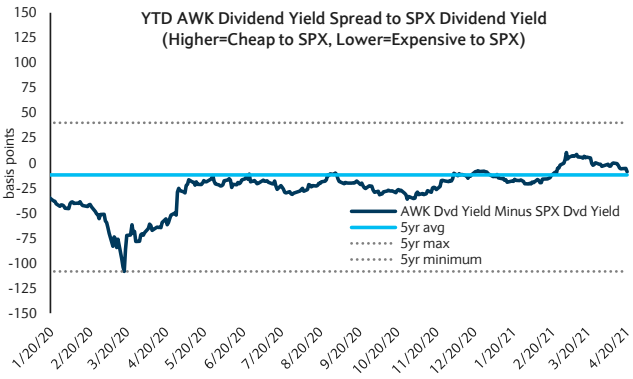
AWK and WTRG YTD Stock Performance



Source: Barclays Research, Bloomberg

FIGURE 9

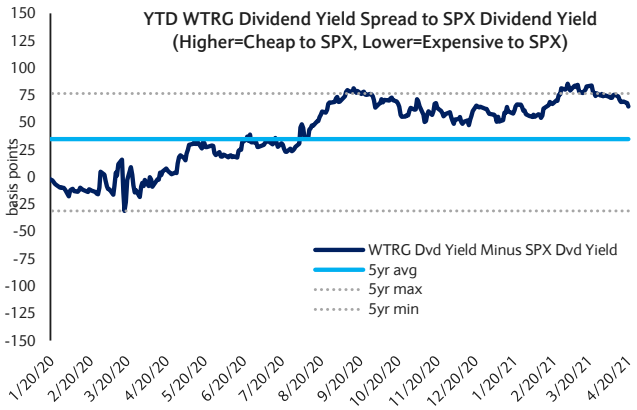
AWK Dividend Spread



Source: Barclays Research, Bloomberg

FIGURE 10

WTRG Dividend Spread



Source: Barclays Research, Bloomberg

North America Power & Utilities — **Industry View: POSITIVE**

American Water Works Company, Inc. (AWK)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2020A	2021E	2022E	2023E	CAGR
Revenue	3,777	4,111	4,405	4,658	7.2%
EBITDA (adj)	2,155	2,338	2,507	2,681	7.6%
EBIT (adj)	1,551	1,687	1,810	1,939	7.7%
Pre-tax income (adj)	924	1,017	1,124	1,230	10.0%
Net income (adj)	709	770	851	930	9.5%
EPS (adj) ($)	3.91	4.24	4.64	4.99	8.5%
Diluted shares (mn)	182	182	184	187	0.9%
DPS ($)	2.15	2.34	2.55	2.78	9.0%

Margin and return data					Average
EBITDA (adj) margin (%)	57.1	56.9	56.9	57.6	57.1
EBIT (adj) margin (%)	41.1	41.0	41.1	41.6	41.2
Pre-tax (adj) margin (%)	24.5	24.7	25.5	26.4	25.3
Net (adj) margin (%)	18.8	18.7	19.3	20.0	19.2
ROIC (%)	8.9	9.6	10.1	10.3	9.7
ROA (%)	3.1	3.1	3.4	3.5	3.3
ROE (%)	11.6	11.9	12.4	12.1	12.0

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	25,614	27,369	29,299	31,229	6.8%
Cash and equivalents	547	35	78	173	-31.9%
Total assets	24,766	25,357	26,634	27,917	4.1%
Short and long-term debt	10,940	10,671	10,291	10,265	-2.1%
Other long-term liabilities	0	0	0	0	N/A
Total liabilities	8,979	9,165	9,478	10,262	4.6%
Shareholders' equity	6,454	6,868	7,701	8,562	9.9%
Net debt/(funds)	10,393	10,636	10,214	10,092	-1.0%
Change in working capital	621	-512	43	95	-46.4%
Cash flow from operations	1,426	1,668	1,821	1,971	11.4%
Capital expenditure	-1,822	-1,555	-1,755	-1,755	N/A
Free cash flow	-920	-513	-578	-478	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	41.2	38.0	34.7	32.3	36.5
EV/EBITDA (adj) (x)	18.6	17.1	15.8	14.7	16.5
EV/EBIT (adj) (x)	25.9	23.7	21.8	20.4	22.9
FCF yield (%)	-2.3	-1.3	-1.5	-1.2	-1.6
P/BV (x)	4.5	4.3	3.8	3.5	4.0
Dividend yield (%)	1.3	1.5	1.6	1.7	1.5
Net debt/EBITDA (adj) (x)	4.8	4.5	4.1	3.8	4.3

Selected operating metrics					Average
Payout ratio (%)	55.0	55.3	55.1	55.8	55.3
Interest cover (x)	3.9	4.3	4.7	5.1	4.5
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (21-Apr-2021)	**USD 161.00**
Price Target	**USD 154.00**

Why Equal Weight? AWK presents a strong growth profile with top-tier management and a solid execution track record, however valuation is stretched relative to electric and gas utilties and our valuation framework implies a 15% premium to the water group average P/E multiple, all of which is fully reflected in the current stock price

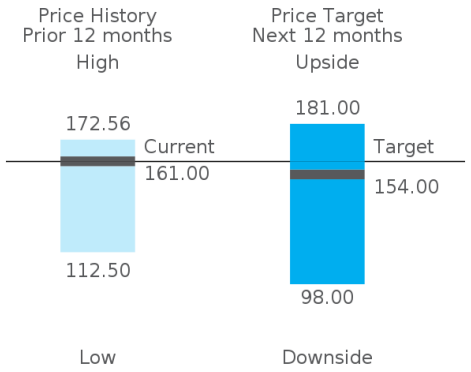
Upside case **USD 181.00**

Our upside case assumes AWK trades at a 25% premium to the group average water utility P/E multiple. We believe this scenario could materialize if ESG flows increase or general utility equity demand rises and disproportionately benefits AWK.

Downside case **USD 98.00**

Our downside case values AWK on the same 15% premium, but applies the group utitlity multiple in lieu of the water group multiple. This could materialize if investors perceive long-term growth opportunities and ESG profiles to be similar to electric and gas.

Upside/Downside scenarios



Valuation Methodology and Risks

North America Power & Utilities
American Water Works Company, Inc. (AWK)
Valuation Methodology: We utilize a group average water P/E multiple for 2023 earnings and apply a 10% premium to AWK's consolidated 2023 EPS estimate of $5.01 to arrive at our $154 price target. The premium reflects strong management, constructive regulatory exposure, and top-tier growth visibility.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to AWK include rate case outcomes, public system M&A deals and integration, external financing needs, and general interest rate environments.

Source: Barclays Research.

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Primary Stocks (Ticker, Date, Price)

American Water Works Company, Inc. (AWK, 21-Apr-2021, USD 161.00), Equal Weight/Positive, CE/J

Materially Mentioned Stocks (Ticker, Date, Price)

Essential Utilities, Inc. (WTRG, 21-Apr-2021, USD 47.84), Equal Weight/Positive, A/CD/CE/D/J/K/L/M

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North America Power & Utilities

Alliant Energy Corporation (LNT)	Ameren Corp. (AEE)	American Electric Power Company, Inc. (AEP)
American Water Works Company, Inc. (AWK)	Brookfield Infrastructure Partners LP (BIP)	Brookfield Infrastructure Partners LP (BIP_u.TO)
CenterPoint Energy, Inc. (CNP)	CMS Energy Corporation (CMS)	Consolidated Edison, Inc. (ED)

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Edison International (EIX)	Essential Utilities, Inc. (WTRG)	Eversource Energy (ES)
Exelon Corporation (EXC)	FirstEnergy Corp. (FE)	NextEra Energy, Inc. (NEE)
NiSource, Inc. (NI)	NorthWestern Corporation (NWE)	OGE Energy Corp. (OGE)
PG&E Corporation (PCG)	Pinnacle West Capital Corporation (PNW)	PNM Resources, Inc. (PNM)
Portland General Electric Company (POR)	Public Service Enterprise Group (PEG)	Sempra Energy (SRE)
The Southern Company (SO)	WEC Energy Group, Inc. (WEC)	Xcel Energy Inc. (XEL)

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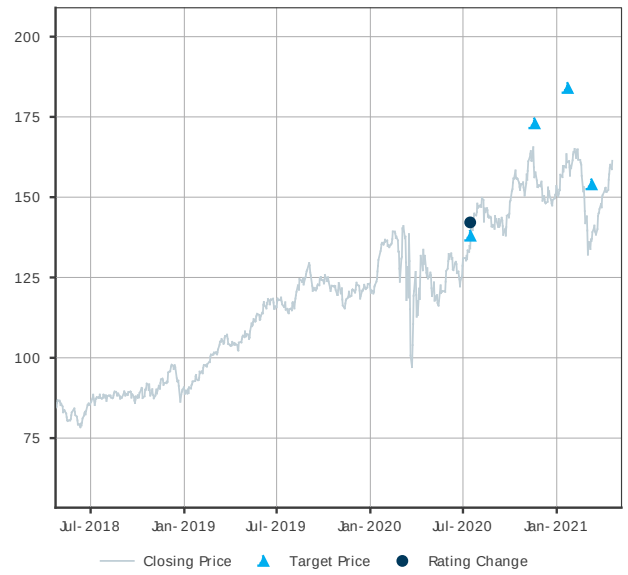
IMPORTANT DISCLOSURES

American Water Works Company, Inc. (AWK / AWK)

Stock Rating	Industry View
EQUAL WEIGHT	**POSITIVE**

USD 161.00 (21-Apr-2021)

Rating and Price Target Chart - USD (as of 21-Apr-2021)



Source: IDC, Barclays Research

Currency=USD

Publication Date	Closing Price	Rating	Adjusted Price Target
10-Mar-2021	136.38		154.00
22-Jan-2021	160.91		184.00
18-Nov-2020	156.19		173.00
15-Jul-2020	134.06	Equal Weight	138.00

Source: Bloomberg, Barclays Research

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Link to Barclays Live for interactive charting

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Valuation Methodology: We utilize a group average water P/E multiple for 2023 earnings and apply a 10% premium to AWK's consolidated 2023 EPS estimate of $5.01 to arrive at our $154 price target. The premium reflects strong management, constructive regulatory exposure, and top-tier growth visibility.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to AWK include rate case outcomes, public system M&A deals and integration, external financing needs, and general interest rate environments.

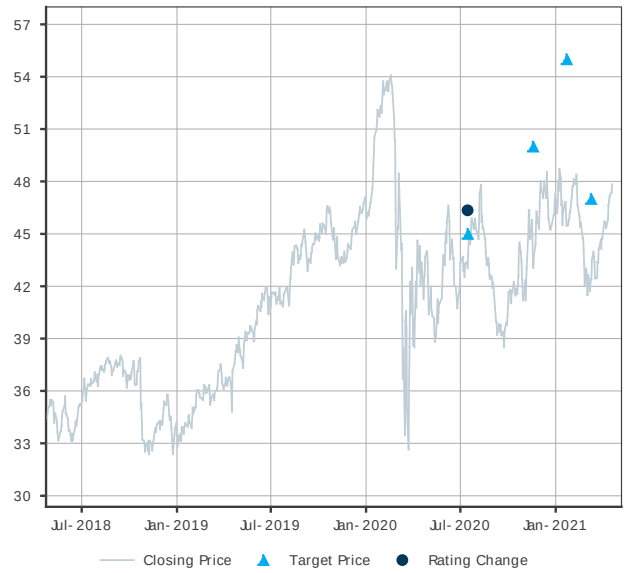
IMPORTANT DISCLOSURES

Essential Utilities, Inc. (WTRG / WTRG)

USD 47.84 (21-Apr-2021)

Stock Rating	Industry View
EQUAL WEIGHT	**POSITIVE**

Rating and Price Target Chart - USD (as of 21-Apr-2021) **Currency=USD**



Publication Date	Closing Price	Rating	Adjusted Price Target
10-Mar-2021	42.39		47.00
22-Jan-2021	45.46		55.00
18-Nov-2020	43.18		50.00
15-Jul-2020	43.04	Equal Weight	45.00

Source: Bloomberg, Barclays Research

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Source: IDC, Barclays Research

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Valuation Methodology: We have a $47 price target for WTRG. We value WTRG's water business using a group average water multiple of 28x. The valuation reflects strong regulatory exposure and public M&A opportunities, balanced by growth visibility lower than peers and near-term risk from closing recent public M&A deals. We value the regulated gas business at a 5% premium to the average 2023 multiple of 17x for our electric and gas group coverage, reflecting a strong growth profile and familiar regulatory exposure.

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BARCLAYS

Equity Research
15 July 2020

North America Power & Utilities

Water valuations are hot, but have they boiled over?

We initiate coverage on AWK and WTRG with Equal Weight ratings: Water valuations have seemingly lost all correlation to electric and gas utilities, as the group P/E multiple has expanded to a ~10-turn premium. However, we see little evidence of the spread contracting near term, as we view investor expectations as reasonable and near-term earnings headwinds as scarce. Increasing reliance on rate cases throughout the forecast period represent the largest sector-wide risk factor through our 2022 forecast horizon, but customer bill offsets exist for some, and overall customer bill inflation appears palatable.

Scarcity value and ESG narrative likely to drive premium for foreseeable future, in our view: Regardless of fundamental similarities to electric and gas utility counterparts, we expect the water premium to persist as scarcity and index composition drive ownership diversity and support water valuations for the foreseeable future. Water utilities also benefit from their lack of electric generation exposure that disqualifies some utilities on ESG screens, and we see increased environmental regulation on water quality coupled with fair market value legislation as adding a compelling qualitative ESG narrative as investor-owned water utilities provide needed financing for cash-strapped public agencies, particularly following the impact of COVID-19 on public budgets.

Recent execution and industry tailwinds likely mean EPS CAGRs moderate somewhat, but growth backlog and visibility still exceed electric peers: AWK and WTRG possess unique scale that position both to play leading roles in a national water infrastructure replacement cycle in the US. Chronic under-investment in water infrastructure has led the American Society of Civil Engineers to estimate that $1tn of total infrastructure spending is needed over the coming 25 years to repair and replace aging infrastructure. The market position dominance is unmatched in the electric utility space (NEE is probably closest with NEER). We see the scale advantage and reputation for best-in-class management providing greater confidence and visibility into capital deployment and growth. External financing needs likely increase relative to previous years given cash tax positions and balance sheet limitations; we see modest ROE lag between cases as possible, but still believe EPS and rate base growth exceed the average electric utility.

Valuation framework: We arrive at a $138 price target for AWK and a $45 price target for WTRG and rate both Equal Weight. We utilize a 27x 2022 P/E group average multiple base for water utilities and a 17x general utility group average multiple for WTRG's gas business. We apply our standard premium and discount valuation framework to arrive at a 15% water premium for AWK and a 5% and 15% premium for WTRG's water and gas business, respectively.

INITIATING COVERAGE

North America Power & Utilities
POSITIVE
Unchanged

For a full list of our ratings, price targets and earnings in this report, please see table on page 2

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Summary of our Ratings, Price Targets and Earnings Estimates in this Report

Company	Rating		Price	Price Target			EPS FY1 (E)			EPS FY2 (E)		
	Old	New	13-Jul-20	Old	New	%Chg	Old	New	%Chg	Old	New	%Chg
North America Power & Utilities	Pos	Pos										
American Water Works Company, Inc. (AWK)	N/A	**EW**	132.97	N/A	**138.00**	-	N/A	**3.86**	-	N/A	**4.22**	-
Essential Utilities, Inc. (WTRG)	N/A	**EW**	43.37	N/A	**45.00**	-	N/A	**1.56**	-	N/A	**1.67**	-

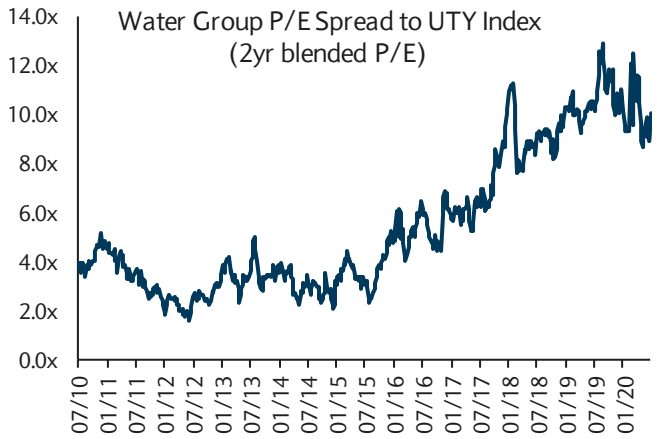
Source: Barclays Research. Share prices and target prices are shown in the primary listing currency and EPS estimates are shown in the reporting currency.
FY1(E): Current fiscal year estimates by Barclays Research. FY2(E): Next fiscal year estimates by Barclays Research.
Stock Rating: OW: Overweight; EW: Equal Weight; UW: Underweight; RS: Rating Suspended
Industry View: Pos: Positive; Neu: Neutral; Neg: Negative

Is Water Just Worth More Than Electricity?

Water Valuation Premium Continues to Expand

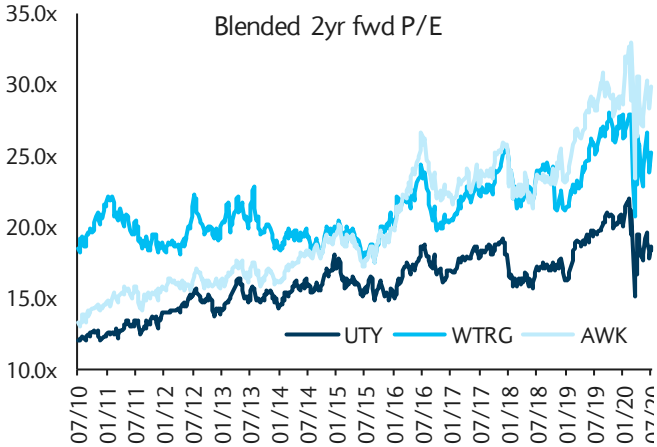
Water utilities have seemingly broken free of any tether to electric and gas utilities in recent years and there are no signs that the gap will close. We use AWK, WTRG, CWT, and AWR as our water utility basket for all group average calculations. The premium would screen even greater, but we exclude securities with a market cap below $2bn (MSEX, SJW, YORW), as we believe limited trading liquidity and embedded takeout premiums would misrepresent comparisons to the traditional US utility under coverage. The pace of the expansion has been particularly notable as the group hovered between 2x-4x premium from 2010 through 2015 before expanding to >10x since early 2019. AWK currently trades at a record 11.5x premium to the UTY.

FIGURE 1
Water P/E Spread to UTY Index



Source: Bloomberg, Barclays Research

FIGURE 2
AWK and WTRG P/E Spread to UTY Index



Source: Bloomberg, Barclays Research

Is That Premium Justified?

Valuation has dominated the debate for the water sector as a whole for the last few years. The duration and apparent sustainability of the premium is notable, in our view, and cannot be dismissed as irrational or transient.

We present our view of current market sentiment on water utilities in the following "Bulls say, Bears say, Barclays says" section before going into additional detail on what we view as the three most compelling justifications for the premium.

Bulls, Bears, Barclays

Bulls say: *Water utilities are advantaged to electric and gas given a more visible long-term capital deployment and earnings growth opportunity, lower earnings and operational risk, and cleaner ESG attributes.*

- **1) Long-term EPS and dividend growth are more than enough to justify price:** AWK's 7-10% growth guidance is ongoing and sustainable long term and justify prices when applied to DCF and dividend-based valuation frameworks. If recently authorized ROE decisions made by state regulatory commissions are correct (most use some derivation of CAPM), the cost of equity capital for most US utilities like AWK and WTRG is ~9.0-9.5x. Assuming AWK can maintain a 7-10% CAGR, the current <2.0% dividend yield is more than adequate for equity investors.
- **2) Rate base growth opportunity is larger and more visible than electric and gas:** Average system age indicates the US is approaching a multi-generational water infrastructure replacement cycle. The investment need is larger than electric and gas, and AWK and WTRG have the scale to become the 'first call' from public officials and legislators when towns are unable to afford upgrades required to stay in compliance. The recent wave of fair market value legislation (FMVL) that passed state legislatures is evidence that public officials understand the need for and support private investment in water systems. The economic impact of COVID-19 on public tax revenues and financial positions will also increase the likelihood of reaching agreement with systems previously unwilling. Additionally, water utilities have greater residential customer bill headroom to pursue rate base growth compared to typical residential electric and gas bills.
- **3) Water utility ESG profiles are more attractive than electric or gas:** Water utilities provide ESG-constrained funds, which may be barred from owning generation or gas assets, an opportunity to gain utility sector exposure. The core growth driver of a water utility is to deploy capital that ensures reliable, efficient, and safe delivery of drinking water and treatment of wastewater, which sustainability-focused funds should find attractive (particularly as water scarcity issues grow). There is also an environmental angle for water utilities, as they could benefit from a wave of environmental regulations (emerging contaminants, like PFAS, are a near-term focus as capex / rate base growth will increase and local municipalities turn to investor-owned utilities with greater capital access and operational expertise.
- **4) Lower operational and earnings risk:** Water infrastructure compares favorably to common electric and gas utility risk factors such as workplace safety, environmental violations and related lawsuits, wildfires, and cost recovery uncertainty as renewable replacement accelerates. Earnings are also more predictable, as revenues are less reliant on weather than electric and gas. Water capex plans consist of thousands of small, diverse projects, lacking the large project risk (execution, environmental permitting, legal challenges) that electric and gas utilities are often exposed to.

Bears say: *Valuations are overdone, equity capital raises will be larger and more frequent, regulated acquisitions are becoming more challenging, ROE lags, and rate case exposure presents greater risk.*

- **1) Current valuations are unapproachable:** All-time high valuations are pricing in unsustainable long-term growth assumptions based on earnings outperformance over the past five years that will settle closer to consensus electric EPS CAGRs over time. With no other apparent distinctions between an electric and water utility with similar regulatory exposure, water stocks carry a 10-turn 'air pocket' on a P/E basis that will fall out as long-term growth assumptions converge.
- **2) Future equity needs will be higher than the past few years:** Debt metrics and parent leverage will approach rating agency thresholds given cash flow projections relative to the size of current capex and regulated M&A plans, requiring greater and more frequent reliance on equity capital markets. The equity need will be amplified as utilities become cash taxpayers (AWK sees payments starting in modest ~2021; $~200mn annual cash source currently). Early evidence can be seen with AWK's inclusion of $500mn of equity in its five-year capital plan and WTRG's $300mn planned issuance in late 2020/1Q21 (timing depends on Delcora outcomes).
- **3) Municipal acquisitions are not the panacea that some think they are:** M&A executed immediately following passage of fair market value bills likely attracted public systems that needed financing most desperately and were most motivated to sell. Recent complications and community pushback relates primarily to concerns about losing both control over freshwater supply and public tax revenues. Negotiating leverage will continue to strengthen over time and municipalities will likely require more onerous terms like customer bill commitments and employee retention, in addition to a pure financial contribution. Regulatory commissions that employ single-tariff ratemaking structures have also limited the ability for utilities to get 'back door' rate recovery without a new general rate case (GRC).
- **4) Rate case reliance and risk of under-earning is higher for water than for electric or gas:** The public M&A component (driven by fair market value legislation discussed in greater detail on page 9) of rate base growth means water companies often carry newly-acquired assets for a time before integrating the assets in rate calculations (leads to regulatory lag). As noted above, the negotiating table for public M&A is likely to become more competitive and investor-owned utilities will often compete for deals with commitments on customer bill increases.

***Barclays says**: Valuations are objectively high, but there is no clear catalyst for compression; scarcity value is likely the main rationale for valuation premium; long-term earnings and rate base growth could moderate somewhat but still outpace electric and gas growth, and visibility clearly leads peers.*

1) Water utilities are still utilities, but valuation premium shows little: We believe any new fundamentals-driven investment in US water utilities requires a long time horizon and the view that the infrastructure replacement cycle will drive EPS growth in excess of most electric utilities. However, there are non-financial factors (e.g. ESG, thematic) attracting capital to the sector. We note AWK's spread to the UTY has been at or near all-time highs since diverging in 2013 (including the current all-time high). We see no imminent catalyst for water valuations to compress to electric utility levels, and thus we utilize a water group average P/E multiple of 27x for our valuation framework.

2) Earnings execution and outlook is strong, but scarcity value is the most compelling justification for the premium: We see scarcity value for publicly traded water equities as a large component of the premium that AWK and other regulated water utilities command. AWK represents ~10% of the S&P Global Water Index and security-specific shareholder composition implies a broader base of investors for both AWK and WTRG than the typical electric utility (both in geography and fund style).

3) Recent execution and industry tailwinds likely mean EPS CAGRs moderate somewhat, but growth backlog and visibility still exceeds electric peers: AWK and WTRG possess unique scale that position both to play leading roles in any water infrastructure replacement programs in the US. The American Society of Civil Engineers estimates that $1tn of total infrastructure spending is needed over the coming 25 years to repair and replace aging infrastructure. The market position dominance is unmatched in the electric utility space (NEE is probably closest with NEER). We also see the scale advantage and reputation for best-in-class management providing greater confidence and visibility into capital deployment and growth. External financing needs likely increase relative to previous years given cash tax positions and we see modest ROE lag between cases as possible, but overall we still believe EPS and rate base growth exceed the average electric utility.

4) ESG is often highlighted as a justification for higher valuations – we agree that the lack of generation allows some funds to own water utilities that cannot own electric and that a strong sustainability narrative exists, however there are material ESG risks inherent to the water utility business model that must be weighed by ESG-focused investors. The ESG pitch for water utilities is that a water utility's core business model is to invest capital in a chronically under-invested US water infrastructure system in order to enhance of an increasingly scarce resource and ensure safe drinking water and more environmentally-responsible wastewater treatment and management. The infrastructure investment embedded in water utility capex plans is based on the need to update pipelines that can be centuries old, improving both water quality (replace lead pipes and lower total effluents) and leakage (water scarcity issues should increase scrutiny on 'treated but not delivered' volumes). We also see a 'social' benefit when classifying customer disposable income as a social benefit, as investor-owned utilities have the unique opportunity to socialize and smooth community and customer financial impacts by utilizing single-tariff ratemaking and longer amortization periods given stronger capital market access. However, for all the positive ESG narratives that water utilities have exposure, there are material ESG risks inherent to doing business as a water utility – including spills, chemical usage, politicized under-investment and customer bill impacts, potential bribery, and workplace safety. The risk exposure to potential ESG disasters make management competency, ethics, Board oversight, and technical expertise critical to any ESG analysis.

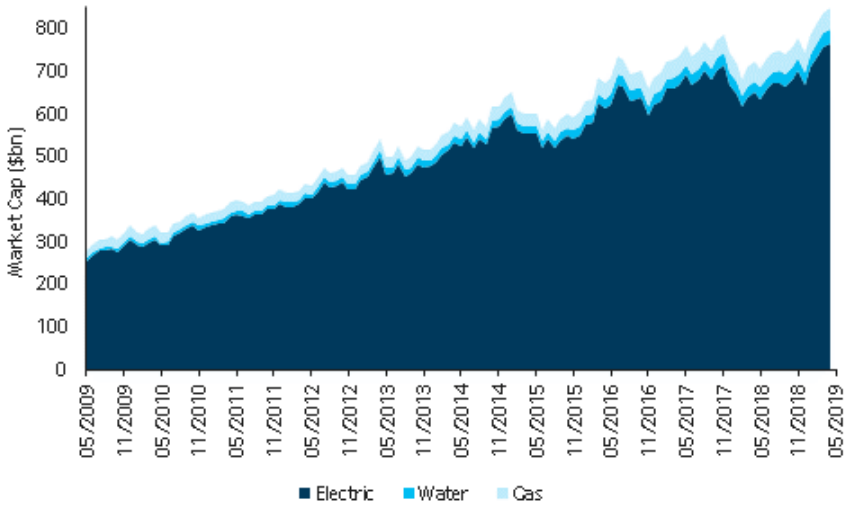
Diving Deeper on Valuation Premium Drivers

Scarcity Value

Scarcity value for water-focused equity securities likely plays a significant role in driving premiums for water utilities when compared to electric utilities with similar growth and regulatory profiles. The market capitalization of each sector directionally illustrates investable supply (Figure 3), but the true float should be adjusted for insider and passive/index stakes.

ETFs (e.g. CGW) tracking the S&P Global Water Index are popular vehicles for investors to gain broad equity exposure to the global water industry. The index, as described by S&P, seeks to provide liquid and tradable exposure to growing global demand for water and ancillary services (infrastructure, equipment, and materials).

FIGURE 3
US Utility Market Cap by Sub-Sector



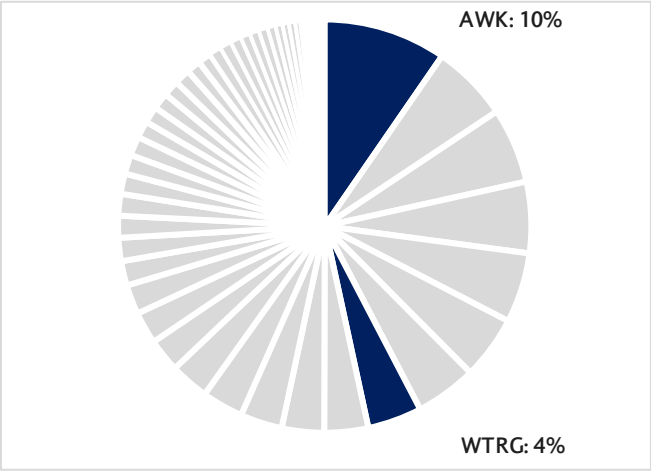
Source: Bloomberg, Barclays Research

FIGURE 4
Top 10 Holding in S&P Global Water Index

Company	Weight (%)
American Water Works Co Inc	10
Xylem Inc/NY	6
Danaher Corp	6
Geberit AG	6
Halma PLC	5
Veolia Environnement SA	5
IDEX Corp	5
Essential Utilities Inc	4
United Utilities Group PLC	3

Source: Bloomberg, Barclays Research

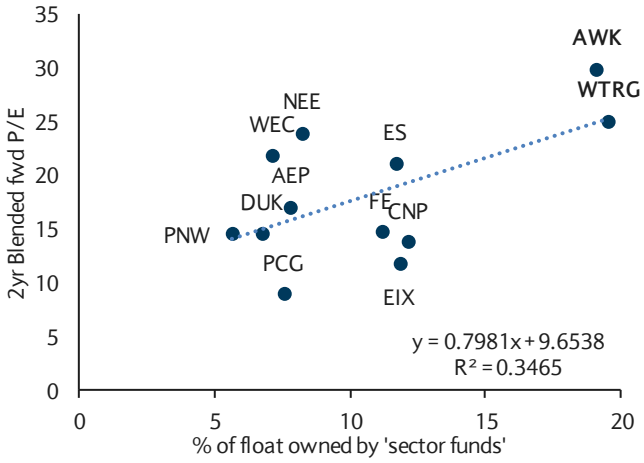
FIGURE 5
S&P Global Water Index



Source: Bloomberg, Barclays Research

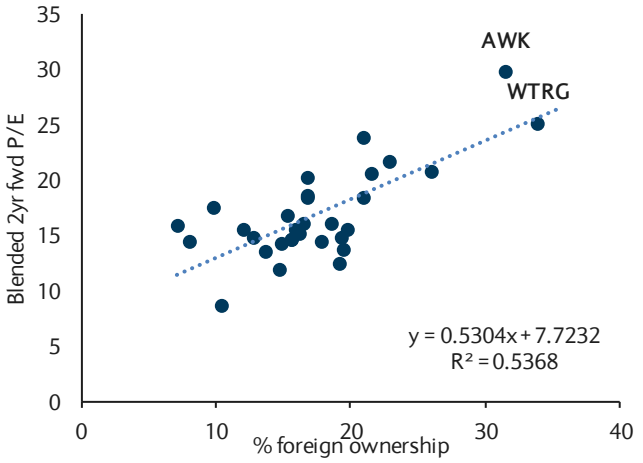
This global index exposure is unique to water utilities when compared to electric and gas utilities who receive passive ownership in US utility benchmark indices (AWK and WTRG are also present in most) and is reflected in AWK and WTRG's sector fund and ETF ownership displayed in figures 6 and 9 below. We also believe this added index exposure is reflected in AWK and WTRG's foreign ownership (ESG also likely plays a role) levels. AWK's recent and projected EPS and rate base growth further qualifies the company for growth fund mandates that help broaden the stocks appeal to industry generalists and help to explain the valuation spread between AWK and WTRG (figure 10).

FIGURE 6
% of shares owned by 'sector funds' vs P/E



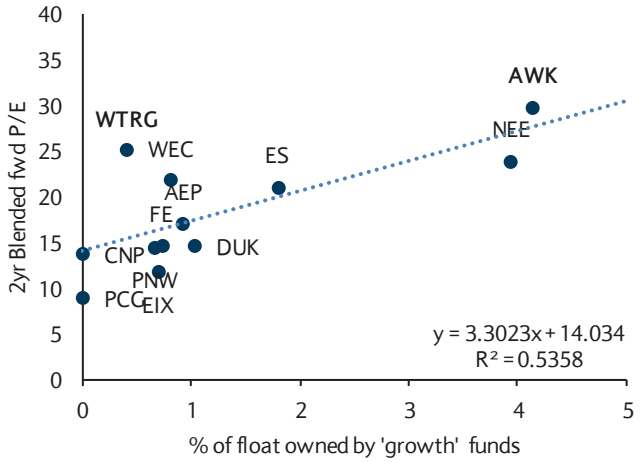
Source: Bloomberg, Barclays Research

FIGURE 7
% of shares owned by investors outside of US vs P/E



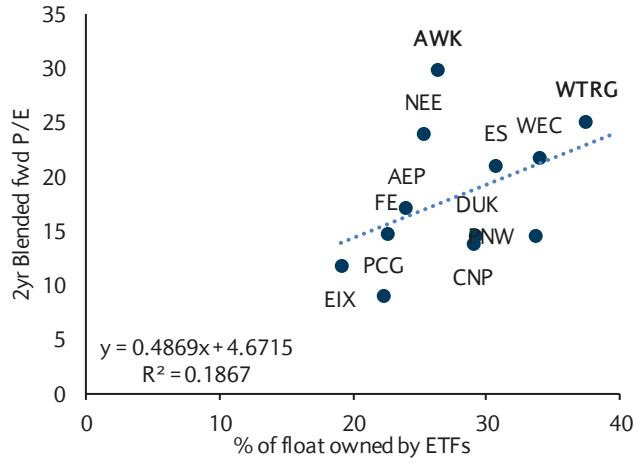
Source: Bloomberg, Barclays Research

FIGURE 8
% of shares owned by 'growth funds' vs P/E



Source: Bloomberg, Barclays Research

FIGURE 9
% of shares owned by ETFs



Source: Bloomberg, Barclays Research

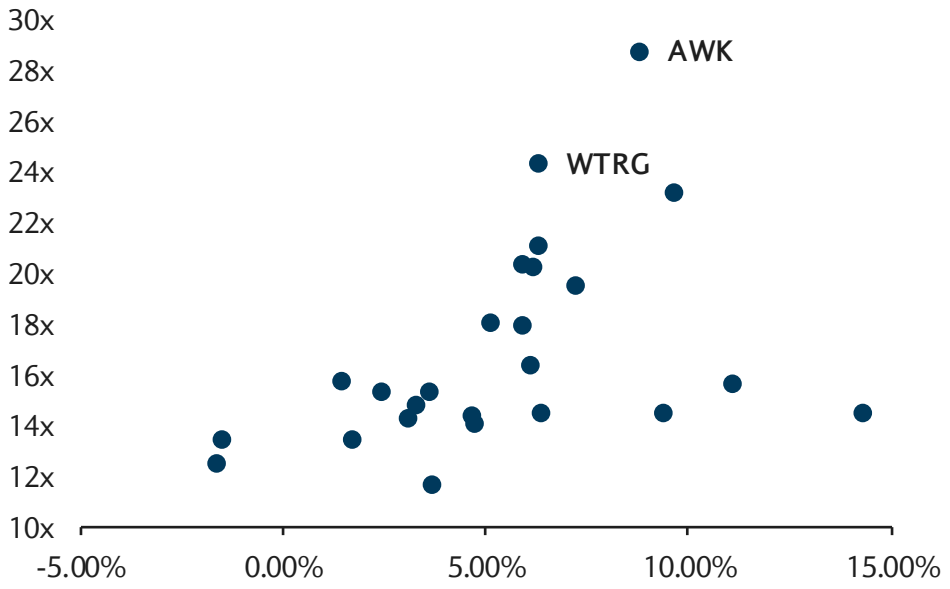
Long-term Growth Outlook

With an average asset age of ~50 years for water and wastewater pipes, the water industry appears to be nearing a generational replacement cycle that should drive capital deployment and rate base growth for the foreseeable future. This opportunity is bolstered by fair market value legislation passed in twelve states (including Virginia as of April 2020 and Texas as of 2019).

There is clearly a strong correlation between realized and expected long-term EPS growth and relative P/E multiples, as investors attempt to ascertain the sustainability of realized growth and CAGR guidance beyond forecast periods and estimate terminal growth assumptions for DCF-based valuation frameworks.

FIGURE 10

EPS CAGR Estimate through 2022 (2018 Base) vs 22E P/E



Source: Barclays Research, Bloomberg

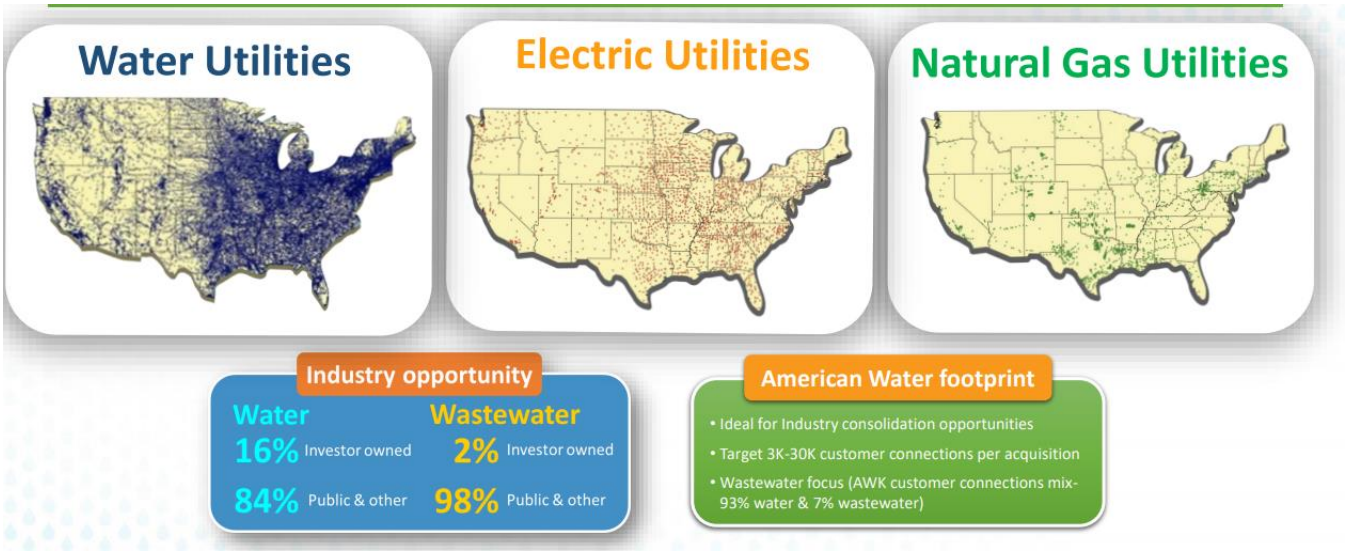
Fair Market Value Laws for Public System Acquisitions

Fair Market Value Legislation (FMVL) allows water utilities to purchase fresh water and wastewater systems from public municipalities and add the total cost of the transaction to rate base, rather than the traditional accounting-based asset cost standards held by many regulatory commissions. The opportunity provides incentive for private industry to financial support to public entities and provides water utilities a streamlined way to grow rate base and often provides outsized ongoing capital deployment opportunities given public systems are often under-invested or face strict environmental regulations that require investment that the public agency does not have financial means to make.

The nation-wide asset replacement narrative is bolstered by water utilities' unique opportunity provided by fair market value legislation, allowing IOUs like AWK and WTRG to participate via public system acquisitions. To date, fair market value legislation has passed in twelve states (including Virginia as of April of this year). The FMVL opportunity is unique to water given the far more fragmented nature of public water and waste water systems in the US when compared to electric or gas. While instances of heavy pushback to private acquisitions of public water distribution systems has been seen in recent years, 98% of US wastewater systems are owned by municipalities or other public entities and generally do not carry the same anxieties associated with freshwater distribution assets, making the public

perception and path to acquisition approval less burdensome. As such, we expect wastewater acquisitions to dominate transaction volume moving forward.

FIGURE 11
Industry Fragmentation



Source: American Water June Investor Presentation

Can FMVL Start to Really Flow?

There are three key recent and ongoing dynamics driving a view that regulated M&A will increase. The first is the significant capital investments required. The second is a reaction to COVID-19 impacts on tax revenues and local government budgets and the need for alternative and external means for municipalities to finance water and wastewater system investment. The third is an outlook for increasing environmental regulation and legislation to address emerging contaminant treatment (primarily PFAS and aging / lead pipelines).

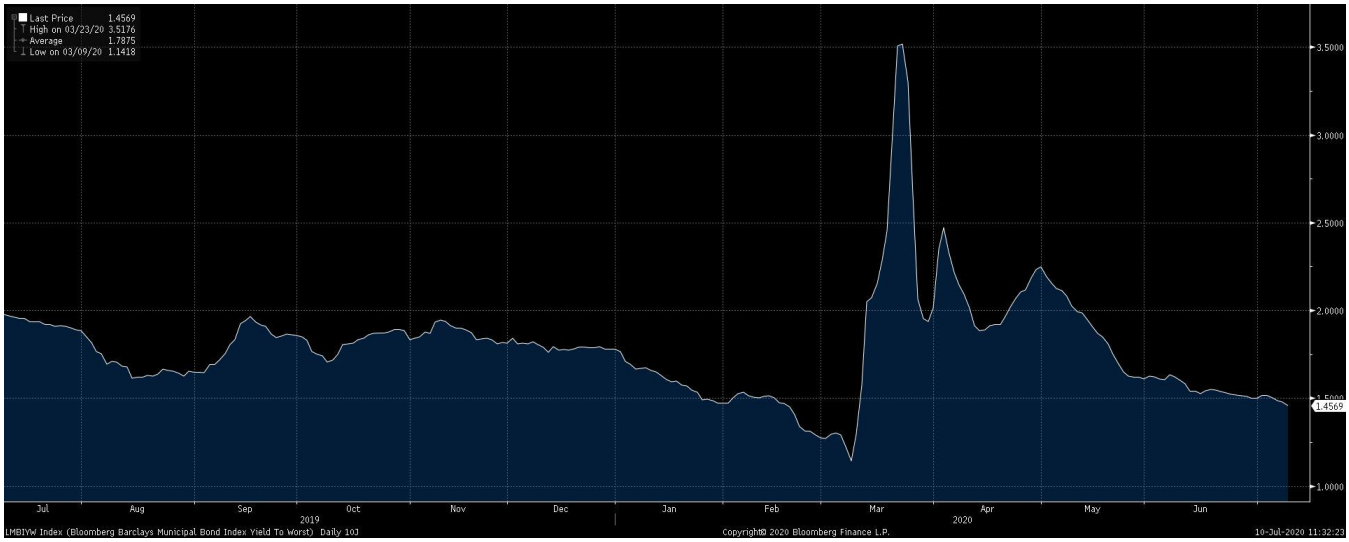
1) **Significant capital investment required**

   A majority of the water and waste-water systems in the US are approaching or beyond their useful lives. This results in increasing annual capital needs, which if not met put reliability, resiliency and public health and safety at risk. The chronic under investment is generally a function of available tax bonding authority combined with pressured municipality budgets.

2) **Municipal financing cost:**

   We view the pressure from COVID-19 related shutdowns on local government finances as a potential driver of increased M&A. Investor-owned utilities can provide capital to execute needed system investments, and public budgets can receive relief in the form of immediate cash inflows (while losing a long-term revenue source). However, all-in financing costs appear to have avoided worst-case scenarios, as evidenced by municipal bond yields as a proxy for total municipal financing costs.

FIGURE 12
Barclays Bloomberg Municipal Bond Index Yield to Worst



Source: Bloomberg

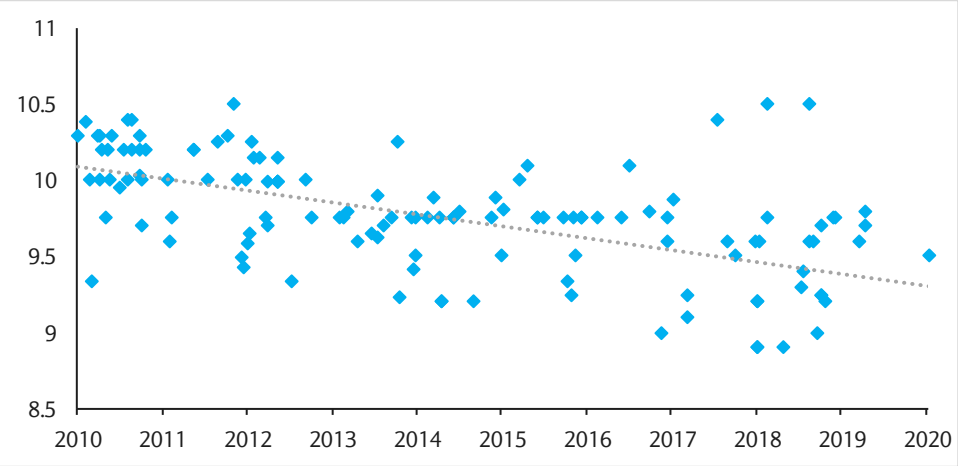
3) Environmental Regulations:

Emerging contaminants like PFAS or 1,4-dioxane have received increased regulatory and legislative attention recently. Numerous new state laws have been introduced over the past few years and national efforts have taken shape to introduce PFAS legislation at a federal level. Emerging contaminants like PFAS are only a health advisory at the EPA, but states have recently chosen to regulate these 'forever chemicals' through state legislatures. Local towns and municipalities with aging infrastructure are already challenged to make investments needed to remain in compliance with many existing environmental regulations and could face further financial pressure given requirements to install water treatment facility upgrades necessary to address new contaminants. Many water companies have already implemented PFAS standards across all systems (~13 parts per trillion seems to be industry standard), but there has been increased pressure from groups like National Association of Water Companies (NAWC) to apply legal requirements to require similar treatment across state and federal jurisdictions.

Trade Off: Added Rate Case Reliance

The nature of the opportunity provides a strong rate base growth avenue; however, it increases water utility reliance on rate cases. It increases susceptibility to ROE lag as larger acquisitions often under-earn until added rate base can be reflected in the revenue requirement recovered in customer bill. This dynamic could be further stretched depending on whether public entities include terms on bill increases as part of the acquisition terms. We assume an average 300bp net lag to authorized for newly-acquired systems, slowly moving back to authorized ROE within three years of the acquisition date after the system is reflected through broader general rate cases. As nationwide ROEs remain under pressure from low interest rates (CAPM), water utilities face more frequent rate cases.

FIGURE 11
Authorized Water ROEs



Source: S&P Market Intelligence, Barclays Research

ESG Analysis

As discussed on page 6, ESG is often viewed as a differentiator for water utilities when compared to their electric and gas counterparts given the lack of generation-related GHG emissions and a perception that operations are safer and more immune to environmental disasters (wildfires, workplace safety, fossil and nuclear waste management). While we agree that water utilities often screen better than electric and gas on scope 1 greenhouse gas emissions and do not directly utilize or transport fossil fuels, they are by no means immune to significant ESG risk exposures from emerging contaminants, wastewater and stormwater chemical use and treatment shortcomings, and potential environmental and safety disasters from spills. This exposure makes management competence and oversight crucial to any ESG-focused investment analysis.

We view the following ESG risks as most critical to discuss with management teams:

- Emerging contaminant standards: Emerging contaminants like PFAS and other effluents are regulated by a rapidly evolving state and federal framework. Top-tier management teams deploy significant research and internal resources to identify risks and play an active role in policy discussions. Best-in-class management teams have scenario planning completed for a variety of regulatory paths and abide by effluent standards that often exceed legally mandated levels to ensure safe drinking water. Utilities should publicly disclose the number of EPA violations related to effluents in annual reporting material.
- Chemical usage and wastewater treatment standards: Wastewater treatment requires heavy chemical usage that can lead to adverse environmental impacts when improperly managed and disposed. Incident histories and internal policies can be supplemented by analyzing EPA violation trends to approximate the relative risk.
- Board oversight: Given the high exposure to potential bribery inherent to any heavily regulated industry and the political nature of public system M&A, the Board should be directly involved in business ethics decisions.
- Energy consumption: Water transportation and treatment is an energy-intensive operation, requiring high levels of electricity usage. Water utilities should disclose total consumption and electricity sources. Analysis of electricity usage and sources can help quantify indirect GHG emission contributions.
- Bill affordability and outlook: We classify customer affordability as a social attribute given the non-discretionary nature of water consumption. With a robust capital outlook, customer affordability and the pace of bill inflation will be critical. The EPA guidelines suggest keeping water bill costs to 2.5% of average family income for residential customers.
- Emergency management plans: Risk of water and chemical spills are inherent to any water utility. We believe strong mitigation systems and quantified risk exposure must be supplemented by a robust and frequently updated environmental response plan to spill events. The plan should be designed to mitigate environmental and social impacts while maintaining safe water services to communities impacted.
- Workplace safety: Workplace safety trends DART rates and OSHA reportable incidents should be analysed to gauge safety program efficacy in recent years.

American Water Works (AWK)

Equity Research
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BCI, US

Company description – American Water Works Co., Inc. provides drinking water, wastewater, and other water-related services in multiple states and Ontario, Canada. The company's primary business involves the ownership of regulated water and wastewater utilities that provide water and wastewater services to residential, commercial, and industrial customers.

American Water Works Company, Inc.

Blocks show how a company is scored by ESG providers (one block is worst, five are best). Icons show the dispersion of those views (no bars indicates only one score provider, two bars indicate dispersion between providers, full bars indicate aligned views). Source: Barclays Research, Sustainalytics, Vigeo Eiris

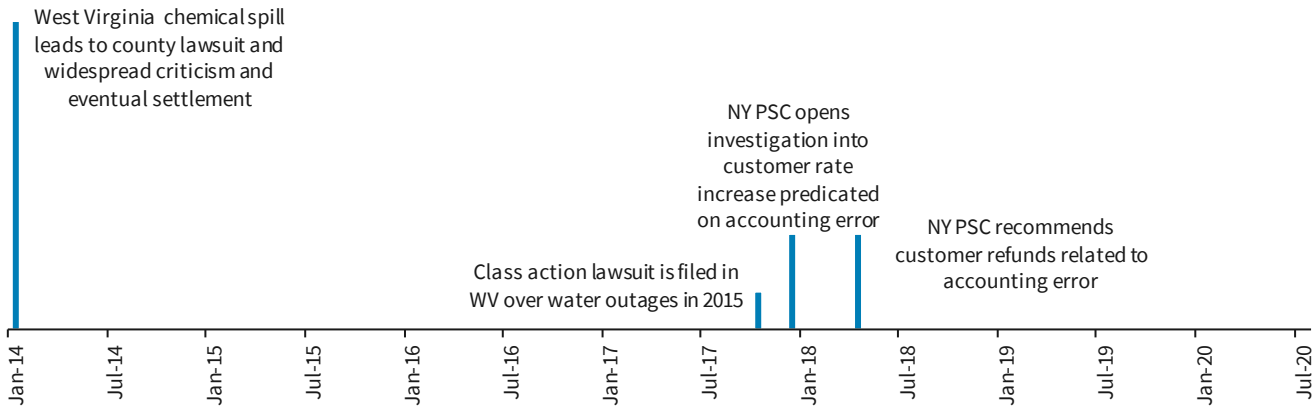
Key conclusions

E AWK receives average environmental ratings, which may be lower than how the average investor thinks about environmental attributes, but accurately reflects negative risk factors balanced by the positive environmental treatment services provided by the company's core operating function, in our view. Said differently, we believe E scores provided by ESG ratings agencies reflect risk factors, rather than the environmental attributes of the business itself. AWK is exposed to environmental risk from effluents that may be insufficiently addressed at AWK's wastewater treatment facilities or leaks and ruptures could lead to environmental disasters when storm water and wastewater contaminate nearby watercourses. American Water has faced minor fines related to improper chemical and hazardous waste, but fewer than industry peers. AWK has experienced no major releases of untreated wastewater or storm water in recent years, while other industry participants have. The risk of large spills of untreated wastewater or storm water remains a material environmental consideration given the impact such releases have on nearby wildlife and water supply.

S AWK's social scores screen as average. We view the social category as inclusive of water waste and water quality. Water scarcity has grown in terms of public knowledge and attention and AWK's (along with the entire water pipeline industry's) lost water amounts could come under increased scrutiny. Lost water can be defined as water that is treated for consumption, but is never delivered to the end use customer due to leakage. This issue is likely to both drive investment capital and risk as average pipe age increases (some pipes are over 100 years old). Our perception is that AWK leads the industry on emerging contaminants, evidenced by environmental policies that often exceed legal requirements and the number of PhD-level specialists and dedicated research labs focused on mitigating potentially harmful particulates not yet regulated directly. However, with growing attention paid to lead levels and other water quality metrics, freshwater delivery quality will remain a risk. Other standard social considerations also apply to American Water, including workplace diversity, community giving, and community relations. Customer bills are a material consideration as water infrastructure ramps up in the United States. AWK highlights average residential bill costs of ~1.9% of average customer family income, versus EPA guidance to keep water bills ~2.5%, however AWK appears to lag WTRG on average customer bill rates.

G American Water's governance scores are above average, which we agree with. As previously noted, our perception is that AWK takes the aggressive and proactive approach necessary to prepare and combat significant safety and environmental risks inherent to the water delivery and treatment business. AWK's Board composition, management compensation structure, and audit quality are consistently ranked among the best in the country. Combined with strong shareholder voting rights and transparent disclosure, we believe governance should be viewed as a differentiator for AWK.

Past and present ESG issues



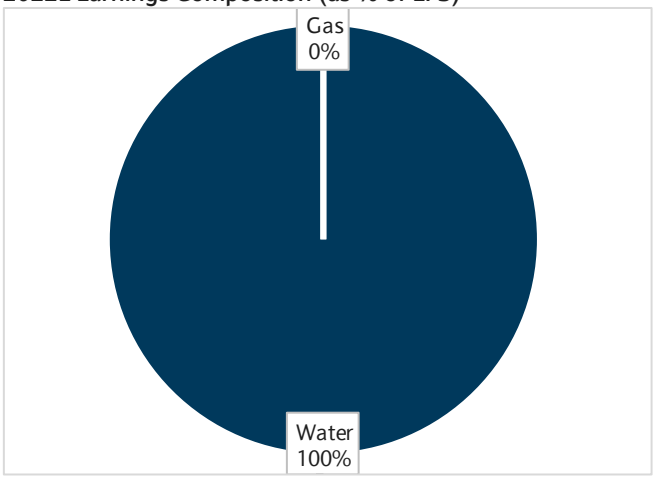
Source: Barclays Research

Risks and management

Category	Risk	Mitigant
E	Wastewater/storm water management	Has effectively avoided major releases of untreated storm and wastewater in prior years.
S	Employee diversity and experience	AWK has workplace diversity working groups and has won numerous inclusion and diversity awards and is recognized in the Bloomberg gender equality index.
S	Health and safety	Has reduced DART rates to 1.13 in 2018 from 2.19 in 2015. Has reduced high-consequence injury rate from 5.26 in 2015 to 3.1 in 2018.
G	Incentive alignment	American Water has published explicit targets tied to ESG performance targets at a board level and has compensation metrics linked to ESG performance.

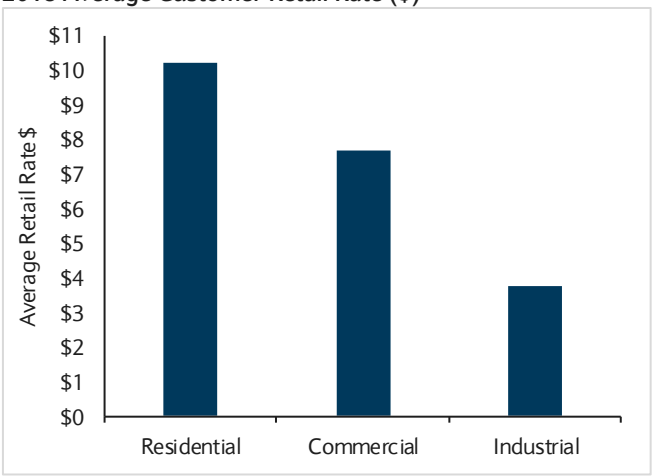
Source: Barclays Research

2022E Earnings Composition (as % of EPS)



Source: Company reports, Barclays Research

2018 Average Customer Retail Rate ($)



Source: Company reports, Barclays Research

Essential Utilities (WTRG)

Equity Research
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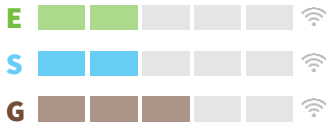
Company description – Essential Utilities, Inc. operates as a water utility company. The company supplies water to residential, commercial, industrial, and public customers. Essential Utilities serves residents through its water and wastewater operations in the Northeastern, Southeastern, and Midwestern United States.

Essential Utilities, Inc.



Blocks show how a company is scored by ESG providers (one block is worst, five are best). Icons show the dispersion of those views (no bars indicates only one score provider, two bars indicate dispersion between providers, full bars indicate aligned views). Source: Barclays Research, Sustainalytics, Vigeo Eiris

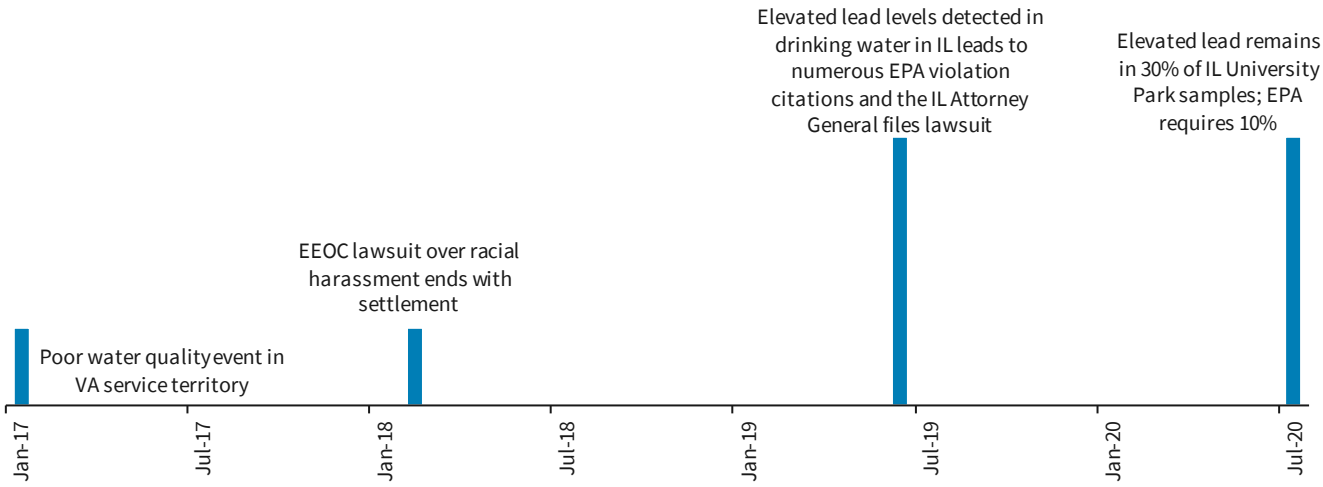
Key conclusions

E Essential receives slightly below average scores for environmental risk factors given below average preparedness and management of potential disasters. We view the ratings as somewhat dated as ratings providers do not contemplate the Peoples natural gas business. WTRG is negatively impacted by a view that the hazardous waste management program lacks management oversight, seemingly from WTRG's lack of EMS certification and emergency response program. While ratings providers take specific issue with the management of environmental risks, we see little evidence that WTRG is lacking relative to other management teams in the water industry. Overall, we view WTRG as equally exposed to environmental risks inherent to the water industry as any other industry participant and applaud WTRG for a robust data disclosure on environmental issues.

S Essential receives below average social ratings due to similar management issues as discussed in the environmental section. We note WTRG has disclosed a fairly robust effluent management system with data supporting its claim that it takes emerging contaminants seriously (citing 95.5% of days in compliance and 272 effluent quality 'events' in 2019). We also highlight that WTRG's average retail rate is lower than the average industry rate on a consolidated average basis across its service territory. DART rates hover around 2.1, slightly higher than industry average. Similar to industry peers, community giving is also prioritized.

G WTRG's Governance ratings are average. Governance risk factors material to WTRG's ratings include a high susceptibility to bribery concerns given the public regulated nature of operations and previous reliance on municipality O&M contracts (though largely divested now). We view the ratings as somewhat stale given the immaterial contribution of municipal O&M contracts. Balancing the downside risks, we note significant management compensation incentives aligned with shareholder and public stakeholder interests. WTRG has explicit long-term and short-term incentives linked to realized ROE, public M&A growth, and O&M inflation management, all of which we view as material to the holistic stakeholder value proposition for a consolidated WTRG.

Past and present ESG issues



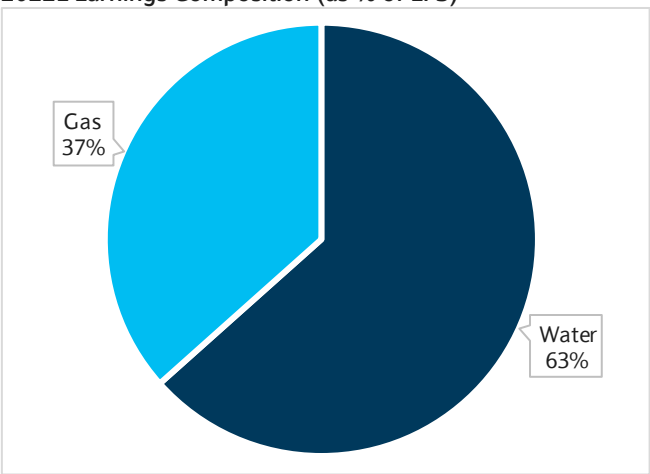
Source: Barclays Research

Risks and management

Category	Risk	Mitigant
E	Wastewater/storm water management	Has effectively avoided major releases of untreated storm and wastewater in prior years.
S	Employee diversity and experience	WTRG has workplace diversity working groups.
S	Health and safety	Has maintained DART rates near 2.1 in 2016-2018. Has reduced lost workdays rate to 102 in 2019 from 568 in 2017.
G	Incentive alignment	We view WTRG's compensation incentives as strongly transparent and well aligned with all stakeholders, with explicit ROE, O&M, public M&A financial targets and strong community involvement and safety targets also embedded.

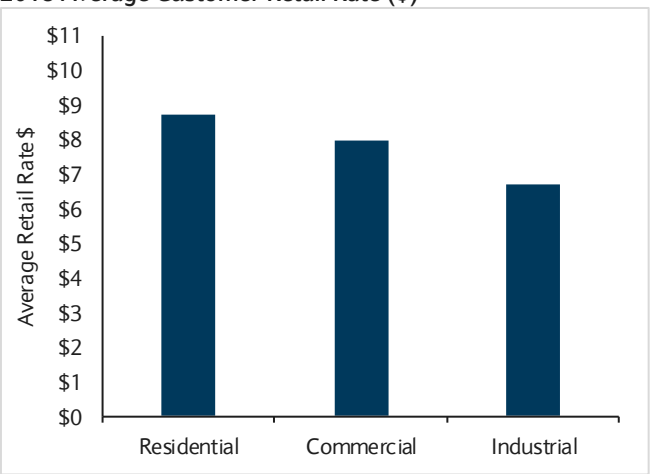
Source: Barclays Research

2022E Earnings Composition (as % of EPS)



Source: Company reports, Barclays Research

2018 Average Customer Retail Rate ($)



Source: Company reports, Barclays Research

Applying Views to Individual Stocks

Barclays Valuation Framework Refresher:

We apply our standard valuation framework used for electric and gas utilities to derive a premium or discount to a group average multiple (in this case we use a water group average multiple of 27x). Our valuation framework takes into account regulatory jurisdiction exposure (capital trackers, ROE trends, other recent commission decisions), geographic trends (population growth, GDP per capita, other general economic activity), long-term growth guidance and visibility, and a qualitative assessment of investor sentiment. The qualitative investor sentiment attribute seeks to encapsulate ESG characteristics and general risk exposures to idiosyncratic issues potentially impacting earnings and providing added earnings variability relative to published financial estimates.

Barclays Water Valuation Framework:

We apply a 15% premium to the group average water multiple for AWK and a 5% premium for WTRG. AWK's premium reflects diversified regulatory and geographic exposure, disproportionate exposure to jurisdictions with DSIC and other constructive capital recovery mechanisms, strong management and competitive position as industry leader, ESG exposure, peer-leading EPS CAGR and multi-decade capex visibility.

WTRG receives a 5% premium to the group average multiple also reflecting disproportionate exposure to strong PA regulatory environment and capital recovery mechanisms, balanced by lower EPS growth, capital guidance visibility and some risk around current M&A deals (namely Delcora). We apply a 15% premium to the 17x utility group average multiple used for all other utility valuation for the regulated gas business (Peoples acquisition) in PA, strong EPS and rate base growth, and our view that constructive regulatory relationships will translate to stable earnings growth in PA.

FIGURE 12

Water Valuation and Price Targets

WTRG PT Methodology	
Regulated Water Business	
22E EPS	$1.24
Group P/E	27.0x
Premium / Discount	5%
Effective 22 P/E	28.4x
PT Contribution	$35
Regulated Gas Business	
22E EPS	$0.72
Group P/E	17.0x
Premium / Discount	15%
Effective 22 P/E	19.6x
PT Contribution	$14
Parent drag	
22E EPS	-$0.15
Blended 22 P/E	25.8x
PT Contribution	-$4
Total Price Target	
Price Target	**$45**
Current Price	$42.90
Price Return	5.8%
Dividend Yield	2.4%
Total Return	**8.2%**

AWK PT Methodology	
Regulated Water Business	
22E EPS	$4.46
Group P/E	27.0x
Premium / Discount	15%
Effective 22 P/E	31.1x
PT Contribution	$138
Regulated Gas Business	
22E EPS	N/A
Group P/E	N/A
Premium / Discount	N/A
Effective 22 P/E	N/A
PT Contribution	N/A
Parent drag	
22E EPS	N/A
Blended 22 P/E	N/A
PT Contribution	N/A
Total Price Target	
Price Target	**$138**
Current Price	$131.00
Price Return	5.7%
Dividend Yield	1.7%
Total Return	**7.4%**

Source: Barclays Research

Upside Scenario:

For our upside scenario we apply the same relative premium / discount framework for WTRG, but we assume all of WTRG earnings receive a consolidated water group multiple and we assume AWK's premium expands to trade at a 25% premium to the water group average multiple.

FIGURE 13
Upside Scenario

WTRG Upside Scenario	
Regulated Water Business	
22E EPS	$1.82
Group P/E	27.0x
Premium / Discount	5%
Effective 22 P/E	28.4x
Contribution	$52
Regulated Gas Business	
22E EPS	$0.00
Group P/E	17.0x
Premium / Discount	15%
Effective 22 P/E	19.6x
Value	$0
Parent drag	
22E EPS	$0.00
Blended 22 P/E	28.4x
Value	$0
Upside Value	
Upside Value	**$52**
Current Price	$43.44
Price Return	18.8%
Dividend Yield	2.3%
Total Return	**21.1%**

AWK Upside Scenario	
Regulated Water Business	
22E EPS	$4.46
Group P/E	27.0x
Premium / Discount	25%
Effective 22 P/E	33.8x
Value	$151
Regulated Gas Business	
22E EPS	N/A
Group P/E	N/A
Premium / Discount	N/A
Effective 22 P/E	N/A
Value	N/A
Parent drag	
22E EPS	N/A
Blended 22 P/E	N/A
Value	N/A
Upside Value	
Upside Value	**$151**
Current Price	$132.92
Price Return	13.2%
Dividend Yield	1.7%
Total Return	**14.9%**

Source: Barclays Research

Downside Scenario:

For our downside scenario, we apply the same relative premium / discount framework for both names, but assume AWK and WTRG trade back to the US utility group average multiple.

FIGURE 14
Downside Scenario

WTRG Downside Scenario	
Regulated Water Business	
22E EPS	$1.25
Group P/E	17.0x
Premium / Discount	5%
Effective 22 P/E	17.9x
Value	$22
Regulated Gas Business	
22E EPS	$0.72
Group P/E	17.0x
Premium / Discount	15%
Effective 22 P/E	19.6x
Value	$14
Parent drag	
22E EPS	-$0.15
Blended 22 P/E	18.5x
Value	-$3
Downside Value	
Downside Value	**$34**
Current Price	$43.44
Price Return	-22.6%
Dividend Yield	2.3%
Total Return	**-20.3%**

AWK Downside Scenario	
Regulated Water Business	
22E EPS	$4.46
Group P/E	17.0x
Premium / Discount	15%
Effective 22 P/E	19.6x
Value	$87
Regulated Gas Business	
22E EPS	N/A
Group P/E	N/A
Premium / Discount	N/A
Effective 22 P/E	N/A
Value	N/A
Parent drag	
22E EPS	N/A
Blended 22 P/E	N/A
Value	N/A
Downside Value	
Downside Value	**$87**
Current Price	$132.92
Price Return	-34.4%
Dividend Yield	1.7%
Total Return	**-32.7%**

Source: Barclays Research

American Water Works (AWK)

Investment Thesis:

AWK provides a peer-leading 7-10% EPS CAGR through 2024 (off of 2018 EPS) driven by regulated investment (5-7% annual contribution to EPS growth), public M&A (likely weighted more toward wastewater; 1-2% annual contribution to EPS growth), and market-based businesses (homeowner services and military services provide 1-2% contribution to annual EPS growth).

We expect AWK to continue to identify accretive capex and public system acquisition opportunities throughout the forecast period, balanced by $500mn of block equity financing weighted toward the middle of the forecast period (we reflect $450mn in 2022 in our model assumptions, but see optionality to delay to 2023), which helps to address increasing parent leverage. Customer bills remain a material consideration as needed investment and public acquisition costs are recovered in rates. O&M efficiency should remain the center of focus for management, and we expect bills to be managed at or below inflation, while also seeking to keep total water bills <2.5% of average family income, per EPA best practices (AWK current avg ~1.9%).

We concede that AWK screens expensive on a P/E basis to any water, electric and gas comps. However, we do not get the impression that earnings expectations are unreasonable, nor do we expect any material unconsidered risk factors to emerge. ESG factors (lack of generation primarily) and scarcity value have led to a sustainable demand premium to electric equities, requiring the use of a water group multiple separate from electric and gas. We apply a 15% premium to the group average multiple (discussed in greater detail in valuation section) to reflect AWK's strong long-term growth visibility, peer-leading EPS CAGR, and constructive regulatory treatment.

Key Regulatory Proceedings:

Pennsylvania: PA represents ~28% of AWK's regulated rate base and benefits from strong capital tracking mechanisms via Distribution System Improvement Charges (DSIC). ROE for the DSIC investment rider is updated via the state's quarterly earnings review. PA's most-recent update held water ROEs at 9.9%. American Water's current Pennsylvania general rate case requests a $92mn rate step up effective January 1, 2021, and a step-up of $46mn in 2022 reflecting a 10.8% ROE (current 10%) and a rate base of $3.98bn in 2021 and $4.29bn in 2022. We assume the 10% ROE currently reflected in rates remains in place and rate increases sufficient to allow PA to earn its allowed returns in 2021 and 2022.

New Jersey: AWK's New Jersey general rate case is seeking an $88mn base rate increase in 2021, reflecting a $3.63bn rate base, 10.5% ROE (current 9.6% authorized), and an assumed 54% equity layer. We note that the $88mn request is incremental to an expected $35mn rate increase contribution from the NJ DSIC mechanism. We assume NJ receives a 9.6% ROE and comparable cap structure, with rate increases adequate to earn implied authorized returns against a $3.6bn rate base as of year-end 2020.

California: CA benefits from forward-looking rate cases with strong precedent of including attrition and capital cost adjustments and a disaggregated cost of capital proceeding reducing general rate case risk (current ROE set at 9.2% with 55.39% equity layer). AWK's current CA rate case requests a $27mn increase effective 1Q21 and a $9.8mn step-up in 2022.

Virginia: AWK's current VA rate case reflects only $196mn of total rate base and requests a $5.6mn rate increase. Interim rates became effective on May 19, 2020, and the case contemplates ~$100mn of infrastructure investments since 2017.

Missouri: AWK's most-recently filed rate case is in Missouri, where the company is requesting a $74mn rate increase to reflect $490mn of investment since the last filing.

Earnings Estimates and Rate Base Model:

FIGURE 15
AWK EPS Model Summary

	2017A	2018A	2019A	2020E	2021E	2022E
Average Shares Outstanding - Diluted	179.0	180.0	181.0	181.3	181.8	183.5
Earnings per Share	**$2.38**	**$3.15**	**$3.43**	**$3.86**	**$4.22**	**$4.60**
Guidance CAGR Implied EPS - Midpoint		*$3.30*	*$3.58*	*$3.88*	*$4.22*	*$4.57*
Guidance CAGR Implied EPS - Low		*$3.30*	*$3.53*	*$3.78*	*$4.04*	*$4.33*
Guidance CAGR Implied EPS - High		*$3.30*	*$3.63*	*$3.99*	*$4.39*	*$4.83*
Regulated Utility EPS	**$3.12**	**$3.34**	**$3.61**	**$3.92**	**$4.20**	**$4.46**
% of total AWK EPS	*94%*	*96%*	*93%*	*91%*	*90%*	*89%*
Market-Based EPS	**$0.21**	**$0.16**	**$0.25**	**$0.39**	**$0.45**	**$0.53**
% of total AWK EPS	*6%*	*4%*	*7%*	*9%*	*10%*	*11%*
Parent EPS	**($0.99)**	**($0.38)**	**($0.51)**	**($0.44)**	**($0.43)**	**($0.38)**
Dividend per share	$1.62	$1.78	$1.96	$2.15	$2.34	$2.55
Payout - target 50-60%	*68%*	*57%*	*57%*	*56%*	*56%*	*56%*
Growth Yoy - target top end of 7-10%		*9.9%*	*10.1%*	*9.7%*	*9.0%*	*9.0%*

Source: Barclays Research, Company presentations

FIGURE 16
Rate Base Summary

Rate Base ($mn)	2020E	2021E	2022E
Total American Water			
Starting Year Rate Base	13,700	14,731	15,625
Capex	1,600	1,500	1,700
Capex Guidance (8.2bn 20-24)	*1,600*	*1,500*	*1,600*
DD&A	569	607	649
Ending Year Rate Base	14,731	15,625	16,676
7-8% Guidance CAGR Implied	*14,445*	*15,529*	*16,693*
Growth YoY (%)	*7.5%*	*6.1%*	*6.7%*
Average Rate Base	**14,216**	**15,178**	**16,150**
Equity Layer (%)	52.65%	52.65%	52.65%
Authorized ROE (%)	9.77%	9.77%	9.77%
Implied Net Income	731	781	831
Below the line items / adjustments	(21)	(17)	(13)
Modeled Net Income	710	763	818

Source: Barclays Research

Risks:

Upside

AWK will likely outperform if M&A opportunities outpace current expectations and EPS grows faster than expected. AWK will also likely outperform if ESG flows increase, general demand for utility equities increase and disproportionately benefit water utilities, O&M reductions are above expectations, or ROE trends benefit earnings.

Downside

AWK will likely underperform if interest rates remain low or decline and impact authorized ROEs, volumes decline materially as a result of COVID-19, heightened M&A activity and competitiveness result in increased ROE lag, FFO metrics deteriorate and require increased equity financing contributions, or operational and environmental accidents impact ESG scores and flows.

Essential Utilities (WTRG)

Investment Thesis:

Essential Utilities closed its transformative acquisition of Peoples Gas in March 2020. The transaction is likely to be accretive to earnings and long-term rate base growth, but it took WTRG from a pure-play water utility to a combined water and natural gas LDC company. The impact from an ESG perspective will be fully reflected over time, but we believe the earnings and growth accretion from the deal helps to put WTRG on a financial trajectory more competitive with industry leaders like AWK. The deal provides gas rate base growth of 8-10%, versus 6-7% water rate base growth through the same forecast period. We view the backlog of necessary gas system investment as providing a strong runway of capital eligible for recovery under the DSIC mechanism, and we highlight the updated pipe replacement programs that provide visibility into 15+ years of investment opportunity and assumes ~200 miles of pipe per year is sustained.

Near-term focus for the investment community is on repairs tax implications to earnings and the closing of the Delcora water system acquisition. While repairs tax election (discussed below) is already helping to support financials in 2020, the remaining catch-up portion remains a key point of debate. We see repairs tax as less likely to provide material upside to estimates, but moreso as a useful tool to upcoming rate case negotiations in PA that should allow WTRG to earn its allowed ROE moving forward while limiting customer bill impacts from otherwise necessary rate increases.

Key Regulatory Proceedings:

Repairs tax and PA rate case outlook: - Repairs tax allows immediate expensing of capex deployed for infrastructure repairs for tax purposes, providing significant tax savings relative to tax rates assumed in ratemaking. The repairs tax situation has two components that contribute to the expected earnings outlook for WTRG. The initial component of repairs tax election is already flowing through financials and is expected to provide $0.08-$0.12 of EPS help for FY20. The second component is the 'catch up' component of repairs tax election – or how much income tax saving is passed through to customers versus retained for shareholders. The prior commission precedent allocated shareholders seven of the ten total years of amortization benefits from the tax savings to shareholders. We view that prior decision as a very constructive outcome. While we do not assume the same treatment in the current round, we again view the repair tax situation as a helpful tool that WTRG possesses for purposes of negotiation in the context of its PA rate case plans (likely to allows for rate case stay outs and other customer commitments rather than purely incremental to growth guidance and assumptions).

DELCORA: - WTRG signed with the Delaware County Regional Water Control Authority (DELCORA) to purchase its wastewater system serving 42 municipalities and ~500k customers for $277mn. DELCORA has line of sight to ~$700mn capex through 2028; however, increasing environmental requirements with the Philadelphia Water Department (one of DELCORA's wastewater offtake and treatment facilities) imply potential investment requirements of >$1bn will be needed ahead of contract renewal in 2028. The investment would require significant customer bill increases and heavy financing strain on the public authority.

WTRG's purchase agreement effectively takes the $277mn of transaction proceeds and allocates it to a customer bill trust that would mitigate customer bill impacts following system investment. As part of WTRG's solution, the wastewater would be directed away from the Philadelphia Water Department facility to one of its own treatment facilities, avoiding worst-case environmental-related capex requirements and providing WTRG opportunities to

acquire other fragmented local wastewater systems that currently send wastewater through the DELCORA system.

The process has become heavily politicized, as some Delaware County representatives seek to block the transaction and restructure the customer bill trust established in the binding sale agreement. The county officials have intervened in the PUC approval process and have filed a lawsuit alleging the transaction is not permitted under current legal provisions. We expect the transaction to remain 'noisy' given the politicized nature, but ultimately we expect the deal to go through without significant changes. We note delays and ultimate approval are not material to financial estimates throughout the forecast period.

Earnings Estimates and Rate Base Model:

FIGURE 17
WRTG: Water Rate Base Summary

Water Summary	2020E	2021E	2022E
Capex ($mn)			
Pennsylvania	376	393	410
Ohio	38	39	41
Illinois	39	41	43
Texas	33	34	36
New Jersey	22	23	24
North Carolina	25	26	27
Indiana	9	10	10
Virginia	9	9	9
Total Regulated Capex	**550**	**575**	**600**
Year End Rate Base ($mn)			
Pennsylvania	3,691	3,962	4,243
Ohio	370	397	425
Illinois	385	413	442
Texas	321	345	369
New Jersey	215	231	247
North Carolina	247	265	284
Indiana	90	97	104
Virginia	84	90	97
Total Year End Water Rate Base	**5,402**	**5,800**	**6,211**
Implied Earnings (($mn)			
Rate Base Implied Net Income	277	293	309
Net Income from Acquisitions	1	8	16
Implied Total Regulated Water Net Income	**278**	**301**	**326**
Modeled Regulated Net Income	*286*	*302*	*328*

Source: Barclays Research

FIGURE 18
WRTG: Gas Rate Base Summary

Gas Summary	2020E	2021E	2022E
Capex ($mn)			
Pennsylvania	376	380	374
West Virginia	20	16	16
Kentucky	4	4	4
Total Regulated Capex	**400**	**400**	**394**
Year End Rate Base ($mn)			
Pennsylvania	2,405	2,666	2,906
West Virginia	131	139	146
Kentucky	28	30	32
Total Year End Gas Rate Base	**2,565**	**2,834**	**3,083**
Implied Earnings (($mn)			
Rate Base Implied Net Income	152	170	186
Modeled Regulated Net Income	*142*	*166*	*188*

Source: Barclays Research

Risks:

Upside

WTRG would likely outperform if repairs tax accretion exceeds expectations and results in incremental growth relative to guidance, currently contemplated M&A is approved in an expedited timeframe, or new M&A deals are announced and provide greater-than-anticipated accretion to growth. WTRG could also outperform if ESG flows increase, general demand for utility equities increases and disproportionately benefits water utilities, O&M reductions are above expectations, or ROE trends benefit earnings.

Downside

WTRG would likely underperform if Peoples integration faces operational challenges, volumes decline materially as a result of COVID-19 or mild weather in gas service territories, rate case outcomes negatively impact earnings, M&A deals face increased scrutiny and legal challenges, deal competitiveness results in increased ROE lag, FFO metrics deteriorate and require increased equity financing contributions, or operational and environmental accidents impact ESG scores and flows.

North America Power & Utilities — **Industry View: POSITIVE**

American Water Works Company, Inc. (AWK)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	3,610	3,817	4,041	4,303	6.0%
EBITDA (adj)	2,032	2,222	2,373	2,532	7.6%
EBIT (adj)	1,450	1,598	1,708	1,822	7.9%
Pre-tax income (adj)	833	937	1,027	1,131	10.7%
Net income (adj)	621	700	766	844	10.8%
EPS (adj) ($)	3.77	3.86	4.22	4.60	6.9%
Diluted shares (mn)	181	181	182	184	0.5%
DPS ($)	1.96	2.15	2.34	2.55	9.2%

Margin and return data					Average
EBITDA (adj) margin (%)	56.3	58.2	58.7	58.8	58.0
EBIT (adj) margin (%)	40.2	41.9	42.3	42.3	41.7
Pre-tax (adj) margin (%)	23.1	24.6	25.4	26.3	24.8
Net (adj) margin (%)	17.2	18.3	19.0	19.6	18.5
ROIC (%)	9.3	10.0	10.1	10.2	9.9
ROA (%)	2.9	3.1	3.3	3.5	3.2
ROE (%)	10.6	11.4	11.8	12.2	11.5

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	23,941	25,741	27,496	29,426	7.1%
Cash and equivalents	60	34	33	46	-8.4%
Total assets	22,682	23,265	24,355	25,588	4.1%
Short and long-term debt	9,453	9,552	9,971	10,091	2.2%
Other long-term liabilities	0	0	0	0	N/A
Total liabilities	7,917	8,339	8,322	8,599	2.8%
Shareholders' equity	6,121	6,496	6,907	7,733	8.1%
Net debt/(funds)	9,393	9,518	9,938	10,045	2.3%
Change in working capital	504	-592	-1	13	-70.3%
Cash flow from operations	1,383	1,434	1,691	1,841	10.0%
Capital expenditure	-1,654	-1,650	-1,555	-1,755	N/A
Free cash flow	-859	-756	-490	-558	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	35.3	34.4	31.5	28.9	32.5
EV/EBITDA (adj) (x)	28.4	26.1	24.6	23.2	25.6
EV/EBIT (adj) (x)	39.8	36.2	34.2	32.2	35.6
FCF yield (%)	-1.5	-1.3	-0.8	-0.9	-1.1
P/BV (x)	3.9	3.7	3.5	3.2	3.6
Dividend yield (%)	1.5	1.6	1.8	1.9	1.7
Net debt/EBITDA (adj) (x)	4.6	4.3	4.2	4.0	4.3

Selected operating metrics					Average
Payout ratio (%)	57.1	55.7	55.6	55.5	56.0
Interest cover (x)	3.8	4.2	4.5	4.9	4.3
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (13-Jul-2020)	**USD 132.97**
Price Target	**USD 138.00**

Why Equal Weight? AWK presents a strong growth profile with top-tier management and a solid execution track record, however valuation is stretched relative to electric and gas utilties and our valuation framework implies a 15% premium to the water group average P/E multiple, all of which is fully reflected in the current stock price

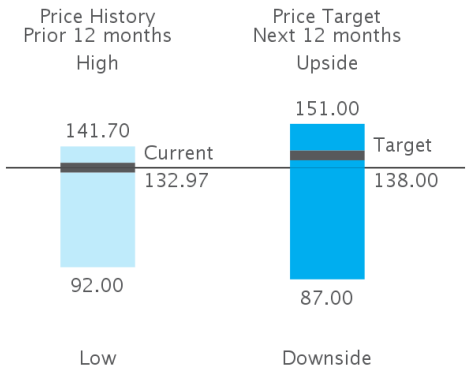
Upside case **USD 151.00**

Our upside case assumes AWK trades at a 25% premium to the group average water utility P/E multiple. We believe this scenario could materialize if ESG flows increase or general utility equity demand rises and disproportionately benefits AWK.

Downside case **USD 87.00**

Our downside case values AWK on the same 15% premium, but applies the group utitlity multiple in lieu of the water group multiple. This could materialize if investors perceive long-term growth opportunities and ESG profiles to be similar to electric and gas.

Upside/Downside scenarios



North America Power & Utilities — **Industry View: POSITIVE**

Essential Utilities, Inc. (WTRG)

Stock Rating: EQUAL WEIGHT

Income statement ($mn)	2019A	2020E	2021E	2022E	CAGR
Revenue	890	1,880	2,081	2,312	37.5%
EBITDA (adj)	517	911	995	1,100	28.6%
EBIT (adj)	361	634	690	767	28.6%
Pre-tax income (adj)	261	436	493	551	28.3%
Net income (adj)	263	398	433	476	21.9%
EPS (adj) ($)	1.47	1.56	1.67	1.82	7.4%
Diluted shares (mn)	179	255	260	262	13.5%
DPS ($)	0.91	0.96	1.02	1.08	6.0%

Margin and return data					Average
EBITDA (adj) margin (%)	58.1	48.5	47.8	47.6	50.5
EBIT (adj) margin (%)	40.6	33.7	33.2	33.2	35.2
Pre-tax (adj) margin (%)	29.4	23.2	23.7	23.8	25.0
Net (adj) margin (%)	29.6	21.2	20.8	20.6	23.0
ROIC (%)	3.7	7.3	7.4	7.7	6.5
ROA (%)	N/A	3.1	3.2	3.3	3.2
ROE (%)	N/A	8.6	9.1	9.1	8.9

Balance sheet and cash flow ($mn)					CAGR
Tangible fixed assets	10,795	11,745	12,720	13,720	8.3%
Cash and equivalents	32	31	55	0	-100.0%
Total assets	12,929	13,601	14,295	14,907	4.9%
Short and long-term debt	5,225	3,950	4,075	4,572	-4.4%
Other long-term liabilities	766	2,531	2,561	2,423	46.8%
Total liabilities	8,315	8,844	9,058	9,492	4.5%
Shareholders' equity	4,613	4,765	5,236	5,429	5.6%
Net debt/(funds)	5,193	3,919	4,020	4,572	-4.2%
Change in working capital	N/A	0	-1	24	N/A
Cash flow from operations	0	713	798	884	N/A
Capital expenditure	0	-950	-975	-1,000	N/A
Free cash flow	0	-514	-753	-456	N/A

Valuation and leverage metrics					Average
P/E (adj) (x)	29.5	27.8	26.0	23.8	26.8
EV/EBITDA (adj) (x)	46.3	28.4	26.3	24.4	31.3
EV/EBIT (adj) (x)	66.2	40.8	38.0	35.0	45.0
FCF yield (%)	0.0	-2.0	-2.9	-1.7	-1.6
P/BV (x)	N/A	N/A	N/A	N/A	N/A
Dividend yield (%)	2.1	2.2	2.4	2.5	2.3
Net debt/EBITDA (adj) (x)	10.0	4.3	4.0	4.2	5.6

Selected operating metrics					Average
Payout ratio (%)	61.9	61.8	61.4	59.5	61.1
Interest cover (x)	3.0	4.6	5.2	5.3	4.5
Regulated (%)	N/A	N/A	N/A	N/A	N/A

Source: Company data, Bloomberg, Barclays Research
Note: FY End Dec

Price (13-Jul-2020)	**USD 43.37**
Price Target	**USD 45.00**

Why Equal Weight? We believe the recent Peoples acquisition is constructive given its accretion to growth and EPS, however we value WTRG on a sum of the parts basis and apply the utility group average P/E multiple, reflecting gas utility peers. The current share price reflects our valuation conclusion.

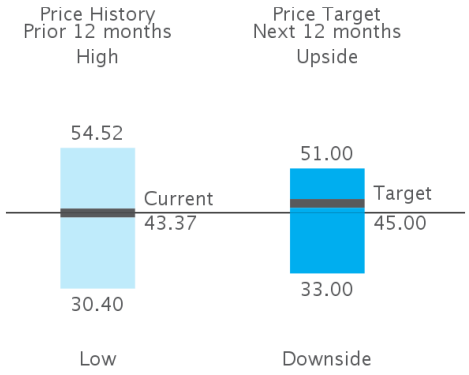
Upside case — **USD 51.00**

Our upside case assumes WTRG is valued using consolidated EPS against a water group P/E multiple. We believe this case could materialize if scarcity value persists and WTRG is deemed a pure-play water utility, despite the gas contribution to earnings.

Downside case — **USD 33.00**

Our downside case values WTRG consolidated EPS on the utility group average P/E multiple, while maintaining a 15% premium for the gas business and a 5% premium for water. We think this could materialize if ESG flows lessen or long-term growth appears unsustainable long term.

Upside/Downside scenarios



Valuation Methodology and Risks

North America Power & Utilities
American Water Works Company, Inc. (AWK)
Valuation Methodology: We utilize a group average water P/E multiple for 2022 earnings and apply a 15% premium to AWK's consolidated 2022 EPS estimate. The premium reflects strong management, constructive regulatory exposure, and top-tier growth visibility.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to AWK include rate case outcomes, public system M&A deals and integration, external financing needs, and general interest rate environments.
Essential Utilities, Inc. (WTRG)
Valuation Methodology: We value WTRG's water business using a 5% premium to the group average water multiple. The 5% premium reflects strong regulatory exposure and public M&A opportunities, balanced by growth visibility lower than peers. We value the regulated gas business at a 15% premium to reflect a strong growth profile and familiar regulatory exposure.
Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to WTRG include rate case outcomes and general regulatory treatment, gas price inflation impacts on customer bills, and general interest rate environments.

Source: Barclays Research.

ANALYST(S) CERTIFICATION(S):

I, Eric Beaumont, CFA, hereby certify (1) that the views expressed in this research report accurately reflect my personal views about any or all of the subject securities or issuers referred to in this research report and (2) no part of my compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this research report.

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Primary Stocks (Ticker, Date, Price)

American Water Works Company, Inc. (AWK, 13-Jul-2020, USD 132.97), Equal Weight/Positive, CE/J

Essential Utilities, Inc. (WTRG, 13-Jul-2020, USD 43.37), Equal Weight/Positive, A/CD/CE/D/E/J/K/L/M

Unless otherwise indicated, prices are sourced from Bloomberg and reflect the closing price in the relevant trading market, which may not be the last available price at the time of publication.

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North America Power & Utilities

Alliant Energy Corporation (LNT)	Ameren Corp. (AEE)	American Electric Power Company, Inc. (AEP)
American Water Works Company, Inc. (AWK)	Brookfield Infrastructure Partners LP (BIP)	Brookfield Infrastructure Partners LP (BIP_u.TO)
CenterPoint Energy, Inc. (CNP)	CMS Energy Corporation (CMS)	Consolidated Edison, Inc. (ED)
Dominion Energy (D)	DTE Energy (DTE)	Duke Energy Corporation (DUK)
Edison International (EIX)	Essential Utilities, Inc. (WTRG)	Eversource Energy (ES)
Exelon Corporation (EXC)	FirstEnergy Corp. (FE)	NextEra Energy, Inc. (NEE)
NiSource, Inc. (NI)	NorthWestern Corporation (NWE)	OGE Energy Corp. (OGE)
PG&E Corporation (PCG)	Pinnacle West Capital Corporation (PNW)	PNM Resources, Inc. (PNM)

IMPORTANT DISCLOSURES CONTINUED

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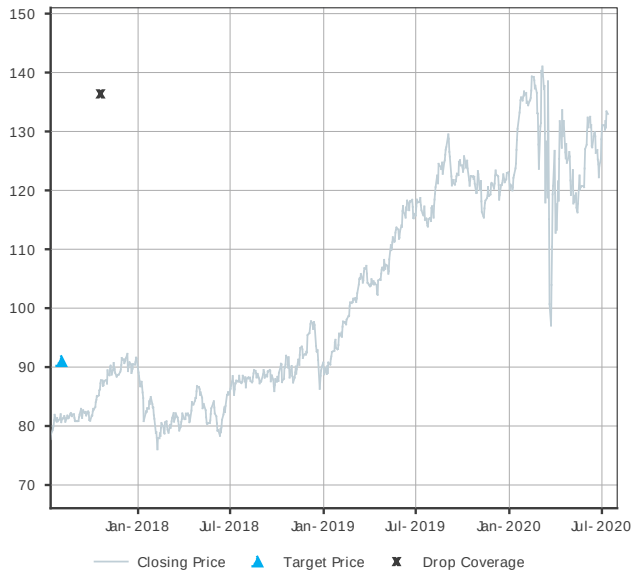
IMPORTANT DISCLOSURES CONTINUED

American Water Works Company, Inc. (AWK / AWK)

	Stock Rating	Industry View
USD 132.97 (13-Jul-2020)	**EQUAL WEIGHT**	**POSITIVE**

Rating and Price Target Chart - USD (as of 13-Jul-2020) **Currency=USD**



Publication Date	Closing Price	Rating	Adjusted Price Target
13-Oct-2017	85.02	Coverage Dropped	
03-Aug-2017	80.65		91.00

Source: Bloomberg, Barclays Research

Historical stock prices and price targets may have been adjusted for stock splits and dividends.

Source: IDC, Barclays Research

Link to Barclays Live for interactive charting

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Valuation Methodology: We utilize a group average water P/E multiple for 2022 earnings and apply a 15% premium to AWK's consolidated 2022 EPS estimate. The premium reflects strong management, constructive regulatory exposure, and top-tier growth visibility.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to AWK include rate case outcomes, public system M&A deals and integration, external financing needs, and general interest rate environments.

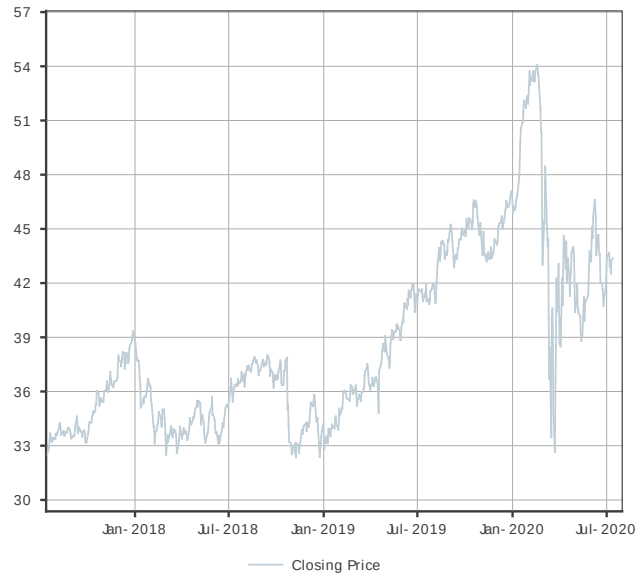
IMPORTANT DISCLOSURES CONTINUED

Essential Utilities, Inc. (WTRG / WTRG)

USD 43.37 (13-Jul-2020)

Stock Rating	Industry View
EQUAL WEIGHT	**POSITIVE**

Rating and Price Target Chart - USD (as of 13-Jul-2020) **Currency=USD**



Publication Date	Closing Price	Rating	Adjusted Price Target

Source: Bloomberg, Barclays Research

Historical stock prices and price targets may have been adjusted for stock splits and dividends.

Source: IDC, Barclays Research

Link to Barclays Live for interactive charting

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Valuation Methodology: We value WTRG's water business using a 5% premium to the group average water multiple. The 5% premium reflects strong regulatory exposure and public M&A opportunities, balanced by growth visibility lower than peers. We value the regulated gas business at a 15% premium to reflect a strong growth profile and familiar regulatory exposure.

Risks which May Impede the Achievement of the Barclays Research Valuation and Price Target: Risks to WTRG include rate case outcomes and general regulatory treatment, gas price inflation impacts on customer bills, and general interest rate environments.

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North American Utilities & IPPs

The ESG Antidote: Why Water is a Win/Win

Industry Overview

Takeaways from our 2nd Annual Water on Wall Street

Late last week, we hosted our Second Annual Water on Wall Street conference with ARTNA, AWK, AWR, CWT, ES, MSEX, SJW, WTRG, as well as a number of state regulators, industry experts and water equipment makers. There were a variety of panels throughout both days with updates from company management teams and a wide range of perspectives on the latest trends and the state of the water industry. We left our latest conference increasingly bullish on the water sector, seeing elevated EPS and DPS growth well into the future along with ESG tailwinds that seem unlikely to abate. We prefer WTRG- with its similarly elevated EPS growth to AWK – and very much intact view of EPS despite tax nuance; mgmt. could very well extend out growth targets over time as water & gas normalized (expect 'normal' 3-yr view in Jan still). Bottom line, this remains our 'go to' in the space- even *after* its recent recovery trade. Finally, while the loss of California decoupling provides varying degrees of exposure across the sector, we perceive protracted implementation enables appeal process & mitigating processes to work their way into planning. We see continued positive bias for water utilities alongside renewable energy investments earning renewable returns as among the more desirable opportunities for investors seeking compounding, sustainable earnings and div growth while desiring clean attributes. See parallel AWK upgrade to Neutral today here.

LT visibility to elevated growth & ESG tailwinds

We came away particularly impressed by the elevated EPS and dividend trajectories for the sector, and see visibility to long term organic rate base and accelerating acquisition prospects as municipal budget deficits and FMV legislation drive further privatization efforts (appears '20 acceleration already). With ~44% of all of the water pipe across the US currently classified as poor (up from ~10% in 1980), we see no shortage of investment opportunities and discussions highlighted that about a trillion dollars in spend is currently needed to bring all of the systems up to date. Meanwhile, relative to more carbon-heavy electric and gas peers, we think water remains the clear cut way to play ESG themes as a utility investor. That said, the water sector has materially underperformed relative to other ESG friendly US renewable names (vs. FSLR, BE, RUN, NOVA, and ENPH; see table one in the full note for latest stock performance). Aside from the unfavorable decoupling decision by the CPUC likely to increase rate base contention and drive earnings volatility for companies exposed to the state (a small part of AWK's consolidated biz) , discussions around regulatory treatment for the sector were generally constructive and we don't see particular discrete concerns looking forward. Bottom line, we see increasing merit to premiums for the water sector well above electric and gas peers – due to both sustainable earnings growth justifying P/E-to-G ratios & comps across Clean & YieldCo spaces. If anything else, expanded est of elevated multiples in adjacent clean spaces (well above that of Water & AWK) – justifies valuations, in our view. We believe the water sector *overall* could perform relatively well – and could still eek out a further bid vs electric peers.

14 December 2020

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FMV: Fair Market Value

CPUC: California Public Utilities Commission

EPA: Environmental Protection Agency

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Why are we so constructive on water utilities *now?*

We bullet out the key factors in our mind below but stress for those investors who have only looked at just AWK and WTRG, the entire sector is full of consistent EPS and DPS growth (even if lumpy at times due to discrete rate cases). The outsized growth of the two largest peers in the space understates the consistent trend of growth across the wider sector. We include historical table below; bottom line, while this trend is exceptional relative to the ~5% growth achieved in utilities, the elevated P/E multiple that is 60% higher on average could be explained by its relative P/E-to-G multiple at a minimum (an *increasingly* employed metric given growth co's involved), but ever more supported by emerging high multiple clean alternatives across sector.

Our growing confidence in long-term compounding prospects alongside what is an increasingly supported multiple offer our improved confidence against what is otherwise an admittedly elevated peer group multiple. While it is difficult to have a more positive view on AWK given its 30x+ P/E on '23 EPS, we perceive WTRG as a key opportunity given its compounding re-rating and what should prove meaningfully less contentious EPS growth trajectory. While we acknowledge dilutive effect of its gas LDC acquisition, we stress its ability to drive a consistent 3-year EPS CAGR (irrespective of what happens on repairs tax true-up) and growing ability to articulate a longer term growth outlook (perhaps in future updates beyond Jan '21 release of latest guidance). As integration is fully reflected, we see a normalized outlook without adjustments and clean baseline for growth. On balance, this remains our favorite name in the Water sector at just 25x '23 P/E.

COVID just the latest push for industry consolidation

The latest conference highlighted the incredibly fragmented nature of the water industry, with over 50K community water systems & 15K wastewater systems relative to ~3200 electric and ~1000 gas LDCs (Local Distribution Company). This remains particularly glaring given 16% of water systems are Investor owned (with an even more notable ~2% investor owned for wastewater) and with 92% of systems serving less than 10K customers. Even prior to COVID, the industry was ripe for consolidation against a backdrop of favorable legislation and higher compliance burdens around emerging contaminants. Twelve states have now adopted FMV legislation with both Consolidated Tariff and Water Quality Legislation also continuing to gain momentum. The EPA has currently established health advisory levels for PFA at 70 parts per trillion, but we perceive a broader mandate for the industry as on the horizon amid some discrete state-level requirements already. That said, the latest pressures put on munis from the ongoing pandemic are just another factor in the perfect storm to accelerate the consolidation trend. Meanwhile, a further environmental push under a Biden administration could provide additional capital opportunities as compliance costs with PFAs (per- and polyfluoroalkyl substances) and water quality concerns have already started contributing to the push away from muni owned water systems

Contemplating the Setup for the Sector

We left our Second Annual Water on Wall Street Conference increasingly constructive on prospects for the sector for the foreseeable future. We see visibility well into the future for earnings trajectory given both organic opportunities and the clear cut industry consolidation trends that we expect to continue to accelerate amid the lingering pandemic.

Meanwhile, we stress the water utility sector as the clear cut way for utility investors to play the ESG theme over the coming years given their lack of carbon exposure vs. both electric and gas utility peers. Despite this, the sector has materially underperformed other ESG friendly US renewable names (vs. FSLR, BE, RUN, NOVA, and ENPH). The exhibit below reflects water utilities stock performance on a one week, one month, three month, and YTD vs. US solar plays, with the sector materially underperforming despite a much better proven track record.

Table 1: Stock Performance: Water Utilities Materially Underperforming US Renewables by a good bit…

Water Utilities	Ticker	One Week	One Month	Three Month	YTD
American Water	AWK	-1.4%	-8.1%	3.3%	20.7%
Essential Utilities	WTRG	0.7%	6.4%	20.8%	1.4%
American States Water	AWR	3.7%	-0.1%	6.4%	-11.0%
SJW Group	SJW	3.7%	4.8%	15.4%	-2.4%
Artesian Water	ARTNA	2.2%	0.8%	15.0%	5.8%
Middlesex Water Company	MSEX	6.1%	5.0%	15.6%	17.3%
California Water Services	CWT	4.9%	-0.2%	21.0%	1.4%
York Water	YORW	5.9%	6.8%	13.5%	7.0%
US Renewables	Ticker	One Week	One Month	Three Month	YTD
First Solar Inc	FSLR	-2.7%	8.0%	18.5%	54.3%
SunPower Corp	SPWR	2.1%	13.2%	95.1%	321.0%
Bloom Energy	BE	-10.7%	36.7%	70.6%	230.4%
SunRun	RUN	-0.6%	5.2%	-4.5%	322.0%
Sunnova Energy	NOVA	1.5%	20.4%	48.8%	252.2%
Enphase	ENPH	8.2%	20.0%	93.9%	435.4%

Source: BofA Global Research, Bloomberg

But just how fast has the sector actually grown?

Consistently better than Utility alternatives: we provide comments provided by companies across the sector on both historical and prospective growth commitments. Bottom line, we see nearly uniform high single digits ratebase growth across the sector (rather than AWK being the unusually elevated company). We perceive ratebase growth as still in the midst of execution – rather than reaching the 'end' of its reinvestment cycle. We perceive few specific regulatory consternations – with in fact many pointing to the need for more consolidation to enable greater scale. If anything what remains critical to the industry is ensuring cost efficiencies to offset otherwise bill inflation. This remains critical as FMV acquisitions drive shifts in tariffs across customers as well.

Table 2: Contrasting commitments on EPS, DPS, and Ratebase across sector: mixed disclosures – but trajectory is clear

Companies	EPS (CAGR)	DPS (CAGR)	Rate Base
American Water Works (AWK)	2020-2024 expected 7-10%	2020-2024 projected high end of 7-10%	NA
American States Water (AWR – Not Rated)	2009-2019: 10.7%	2010-2020: 9.4%, guiding 7% going forward	Planned capex going forward remains at 3.5-4x depreciation
Aquarion – Eversource (ES)	NA	NA	2017-2024 expected 8% rate base CAGR
Artesian Resources (ARTNA – Not Rated)	NA	Expected 3%	NA
California Water Service Group (CWT – Not Rated)	NA	NA	2008-2019: 9.7%
Essential Utilities (WTRG)	Expected 5-7% through 2022	NA	NA
Middlesex Water (MSEX - Not Rated)	NA	NA	Capex forecast of $295Mn in 2020 through 2022
SJW Group (SJW – Not Rated)	5% LT	Committed to a dividend payout ratio of 50-60%	2016-2021 projected: 13%

Source: BofA Global Research estimates & Bloomberg; industry presentations & commentary from conference for uncovered companies

We also include the existing historical EPS growth rates across the sector to provide a bit more perspective across the peers- admittedly AWK stands out clearly vs. peers on its ability to consistently execute and explains its notable premium. If anything, we perceive re-acceleration of growth underway across peers beyond just AWK's consistency.

Table 3: EPS Growth over Time Across the Water Industry: entire sector's performance is well in excess of trends elsewhere

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Average EPS Growth - over decade	EPS CAGR - over decade	EPS Growth 2019-2020E	EPS CAGR - 5YR - 2015-2020E
AWK	22%	18%	17%	4%	10%	9%	8%	7%	9%	9%	8%	9%	7%	11%	11%	8%	8%
WTRG	17%	4%	40%	10%	3%	5%	5%	4%	3%	4%	6%	6%	9%	10%	9%	6%	4%
SJW	60%	-28%	27%	-5%	121%	-25%	39%	11%	-12%	-29%	16%	16%	7%	16%	8%	16%	2%
ARTNA	3%	-17%	36%	-17%	14%	18%	12%	7%	2%	4%	11%	4%	na	6%	5%	11%	7%
CTWS	-5%	14%	19%	8%	16%	6%	2%	2%	-35%	na	na	na	na	3%	na	na	na
MSEX	33%	-13%	7%	14%	10%	8%	13%	0%	42%	3%	6%	4%	3%	12%	11%	6%	12%
CWT	-7%	-6%	37%	-13%	17%	-21%	7%	39%	-3%	-4%	28%	1%	7%	5%	3%	28%	12%
Avg	18%	-4%	26%	0%	27%	0%	12%	10%	1%	-2%	13%	7%	7%	9%	6%	13%	3%

Source: BofA Global Research, Bloomberg; consensus applied for uncovered names (we only cover AWK and WTRG)

Contemplating the Regulatory & Legislative Backdrop

Aside from the unfavorable decoupling decision by the CPUC likely to increase rate base contention and drive earnings volatility for companies exposed to the state, discussions around regulatory treatment for the sector were generally constructive. We perceive continued support in surcharges like the DSIC (Distribution System Improvement Charge) to drive critical investment spend longer term and see commissions as continuing to engage with companies around COVID challenges and navigating through as the pandemic continues to linger. As we await a broader mandate around PFAs and water quality, regulatory support across states will remain critical to watch: We don't expect it to be too controversial. Meanwhile, we perceive legislation such as Fair Market Value legislation, Single Tariffs, and the Water Quality Accountability Act will all continue to gain momentum, setting up opportunities for further consolidation.

Company Highlights

We include our latest company takeaways below:

Essential Utilities (WTRG)

Latest discussions with WTRG management stressed confidence around execution of their strategy with the company successfully navigating the pandemic while integrating their Peoples Gas acquisition. Despite COVID, the company previously noted expectations to be at the top end of the 2020 range and affirmation of their 5-7% EPS growth through '22. The company is poised to roll forward their guidance on January 11th, and we perceive more announcements to come on the acquisition front. Recall the company has elected to use Repairs Tax accounting treatment and has effectively implemented the last several months – with guidance of $0.08-$0.12 benefit annually. We await developments around the regulatory process of the catch up component after the earlier filing, with resolution expected early in April of 2021. Rather than drive incremental upside to their 5-7% EPS CAGR, the filing seeks to extend the growth without a need for a rate case. As opposed to going in for new rates in 2023 to take effect in 2024, a constructive outcome from the catch up filing would benefit '23, with incremental benefits in '24, and '25 to help drive earned returns for the segment in outer years without any rate relief until 2026: the repairs tax debate boils down to Peoples Gas ROE lag in '23 likely to a modest degree. On balance we are comfortable in mgmt's ability to manage lag around its ROEs at core water utilities including PA into a potential water filing next year.

With FMV legislation now in all eight water & wastewater states in WTRG's footprint following the passage in Virginia earlier this year, the company continues to execute on tuck in acquisitions and discussions continue to highlight a robust pipeline of opportunities. Management remains confident on the DELCORA process, with a regulatory approval expected in mid-March. This would put the company on track to

potentially close the transaction in April or May after the 30 day appeal window. Meanwhile, a decision is expected from a judge within 60 days after the recent hearing regarding the litigation around the trust. Recall the company has until August to pull on the ~$300Mn equity forward to be used for DELCORA and other acquisitions.

We reiterate our Buy rating, seeing upside risk in the event of better than expected execution on their long-term growth rate.

American Water Works (AWK)

Ahead of their upcoming 2021 guidance and outlook roll forward, AWK management continued to highlight confidence across their business and around their ability to execute on their strategy through both the lingering pandemic and the longer term. Despite the ongoing impact of COVID, latest disclosures with their 3Q update brought the midpoint of full year 2020 guidance back to the original 2020 guidance on an adjusted basis – and we see the company as poised to extend expectations another year: We don't perceive a pivot from the strategy with management seemingly committed to their growth triangle and the largely regulated portfolio. As such, we expect continued guide towards 7-10% EPS growth through 2025 with their full year results.

As the largest publicly traded water utility with a regulated footprint across 14 states, AWK is poised to benefit from enabling legislation and the continuing acceleration in consolidation across the industry. FMV legislation has been enacted in ten of their states including the top 7 (which make up 88 % of their biz by revenue).

95% of their acquisitions over the last five years have been in states that have enacted the legislation. Meanwhile, the company now enjoys consolidated tariffs in 12 states and water accountability legislation in three. We see the latest pressures from both COVID and water quality standards as likely to further accelerate the trends. After our event, the company announced the latest completed tuck in acquisition of Four Lakes Water Distribution System in Illinois American Water's Chicago Metro Area ($900K and 1300 households). With a line of sight to $20-$22Bn of investment over the ten year period, we see no slowdown in opportunities even through the longer term, particularly given the consolidation backdrop. The earlier decision to de-lever the balance sheet should further provide additional flexibility to pursue acquisitions.

We upgrade AWK shares to Neutral following the latest constructive conference and a more fairly balanced risk/reward. Click here for the parallel upgrade.

Aquarion – Eversource (ES)

We hosted meetings with Aquarion Water, ES' regulated water utility subsidiary that comprises 5% of the company's rate base. The company is one of the ten largest privately-owned water utilities in the US and the largest investor-owned water utility in NE serving ~214K customers in NH, MA, and CT. Following the sale to ES, Aquarion's rate base is expected to grow nearly 3x faster than before the acquisition to a rate base of ~1.3Bn in 2024, reflecting an 8% rate base CAGR off the 2017 base. We perceive opportunities beyond this as the industry continues to consolidate from the 50,000+ water systems that are in the US today. Since 2011, Aquarion has closed 24 transactions, with two small acquisitions currently before regulators – and discussions stressed the constructive regulatory backdrop to further promote muni deals. We see the M&A focus going forward on larger opportunities over a thousand connections in both water & wastewater. Maintain our Neutral rating on ES given balanced risk/reward.

American States Water (AWR – Not Rated)

American States Water Company (AWR) is a consolidated low volatility water company that operates through 3 subsidiaries: 1) Golden State Water Company (GSWC), Bear Valley Electric Service, Inc. (BVESI), and 3) American States Utility Services (ASUS). The company recently spun out BVESI to insulate it from the rest of the company, but stressed the higher elevation (7000ft) and stronger build to whether ice and snow required above 3000ft – stressing the differences in risk relative to some other parts of

California. The regulated water and electric utility serves 261,000 and 24,000 customers across California, respectively, while ASUS is a contracted service for water/wastewater systems that serves military bases under 50-year contracts, largely competing with AWK.

The EPS breakdown is comprised 72% from GSWC, 7% from BVESI, and 21% from ASUS with the company growing earnings at a ten year CAGR of 10.7% through 2019. Going forward, the company is guiding to dividend growth of 7%, stressing potential room to grow from the company's earnings prospects: planned capex going forward remains at 3.5-4x depreciation. Given the rate case filing in July, the company doesn't expect to lose decoupling until 2025 (after the commission subsequently opted to eliminate it on August 27th) and view the language in the decision as supporting Golden State Water's position that it does not apply to its general rate case application filed earlier this summer (which will set new rates for '22-24). The company may still have the ability to use the Monterey-style WRAM for partial price adjustment protection.

Artesian Resources (ARTNA – Not Rated)

ARTNA is a $400Mn market cap water utility headquartered in Newark, DE providing water services in parts of Delaware, Maryland, and PA. The company services more than 118K metered customers and supplies over 8.3Bn gallons of water per year through more than 1,331 miles of water mains. Through public-private partnerships, the company provides a variety of water and wastewater-related services to several municipalities with latest discussions suggesting the primarily resi based business as not materially impacted by COVID. The company continues to focus on organic growth on the Delmarva Peninsula and growth has been around 1-2% across their footprint in addition to several recent acquisitions. The company alluded to 3% dividend growth.

California Water Service Group (CWT – Not Rated)

We hosted meetings with management of CWT – the second largest ($2.5Bn market cap) pure play water company in the US. The latest 2018 California GRC adopted on Dec 3rd allows 3-year CapEx of $828m, adopting a $1.5bn rate base in 2020, with the company growing investment at a ten year CAGR of 9.7% through 2019. As they appeal the recent CPUC decision to eliminate decoupling in California, discussions stressed any overturn as unlikely before the next GRC and they expect the shift to make rate cases more contentious and drive rate design changes, potentially reducing conservation incentives and increasing volatility. COVID has increased the number of delinquencies with 60,000 customers behind on payments - raising the company's bad debt reserve to $2.7Mn (albeit the state has provided an emergency memo account for COVID related expenses). Overall, the capital program remains robust and running 3x depreciation, while acquisition opportunities remain strong with five more acquisitions in progress after closing the Rainier View deal in June.

Middlesex Water (MSEX - Not Rated)

We hosted meetings with MSEX, a $1.3Bn regulated water utility with operations in NJ and DE. Discussions emphasized robust investment opportunities, with a capex forecast of $295Mn in 2020 through 2022, including a $70Mn CJO plant upgrade in New Jersey anticipated to complete in mid-2021. MSEX is subject to a Distribution System Improvement Charge (DSIC) in both its NJ and DE jurisdictions which allows accelerated recovery of certain pre-approved investments subject to a cap. While favorable legislation such as FMV is helping drive consolidation across the industry, MSEX doesn't currently enjoy such legislation in their states at this point in time. Nonetheless, discussions still suggested muni opportunities materializing with the Water Quality Act in NJ and as more and more munis look to get help from IOUS. The company has not articulated a formal EPS target.

SJW Group (SJW – Not Rated)

We hosted meetings with SJW, the second-largest pure-play water/wastewater utility by rate base in the US. Discussions emphasized the company's growth strategy including Capex, constructive regulatory relations, and acquisitions. After the earlier transformative M&A, the footprint now includes San Jose Water (regulated utility in California), Conneticut Water, Maine Water, SJWTX (regulated utility in TX), and SJW Land Company (unregulated biz in California). The company is committed to a dividend payout ratio of 50-60% and seeks to grow earnings around 5% longer term – and stressed additional capital opportunities above plan including further municipal acquisitions. The company estimated over $230m of Capex in 2021, implying 5 year CAGR of 13% through 2021. Despite the latest decoupling setbacks for the water industry in the state of California with the CPUC's decision to eliminate it, SJW didn't employ the mechanism and instead remains well protected with the Monterey-style WRAM in place. After earlier issues with guidance, the company noted that guidance will be released after the rain season going forward in order to more accurately reflect any water costs.

The Tech Angle: AQUA, BMI, Ionic Water & XYL

We held meetings with AQUA, BMI, Ionic Water, and XYL for perspective and latest updates from technology providers.

Ionic: Start-up company by same developer of EOS stationary batteries. Focused on PFOA solution with regenerative (reusable) activated carbon solution. See potentially material cost reductions to cost of water purification along with substantial reductions in use of activated carbon (presently consumed in large quantities).

AQUA: Evoqua is a $2.8Bn market cap company that provides water treatment equipment and services through two segments, Integrated Solutions and Services and 2) Applied Product Technologies. Discussions stressed that COVID had led to rapid growth in outsourced water, creating short term revenue challenges but paving a way for long term success as projects take 12-24 months until they are fully operational. Looking forward, their base case guidance into 2021 is flat to slightly up sales and adjusted EBITDA y/y as the pandemic continues to linger.

BMI: Badger Meter is a $2.6Bn market cap company that manufactures and markets flow measurement and control products focused on smart meters in the water sector. Latest discussions stressed that after a very challenging second quarter, business bottomed in April and organic growth has started to resume. While the company doesn't provide formal guidance, they expect 5% growth on the utility business longer term on higher average selling prices, and expect software as a service to grow to 10% of their biz. Only ~60% of the US market currently has some form of AMR/AMI (automated meter reading / advanced metering infrastructure), and while likely slow to adopt, this provides a long runway of potential growth along with upgrades from AMR to AMI. Meanwhile, with 80% of their utility biz in the US, discussions noted potential for international tailwinds through the strategic cycle. While small, their recent acquisition of S:CAN has an installed base in 50 countries to help further accelerate their international push.

XYL: Xylem Inc is an $18Bn market cap designer, manufacturer, equipment, and service provider for water and wastewater applications addressing the full-cycle of water from collection, distribution, and use to the return of water to the environment. By geography, the bulk of revenue is generated in the US (45%) while Western Europe, Emerging Markets, and the rest of the world comprise 26%, 21%, and 8%, respectively, while end markets are broken down by utilities at 50%, industrial at 35%, commercial at 10%, and resi at 5%. Discussions stressed the company as well positioned to grow faster than the market the next several years and a likely pickup in growth in 2H as we start to recover from the pandemic – with signed contracts building up given the delay in work.

Table 4: Stocks mentioned

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
AWK	AWK US	American Water	US$ 148.55	B-2-7
WTRG	WTRG US	Essential Utilities	US$ 47.07	B-1-7
ES	ES US	Eversource Energy	US$ 85.46	B-2-7

Source: BofA Global Research

Price objective basis & risk

American Water Works (AWK)

Our PO for American Water Works is $155. We apply the sector average 27.8x to American Water's 2023E earnings based on the water peer multiple and a 8.1% group EPS CAGR for '18-'23E. We think this multiple is justified as in our view AWK largely drives the peer multiple as the largest publicly traded water utility. We ascribe a 3x premium for NJ, PA, and IL, and a -3x discount to the non-regulated Retail biz. Also a -1x P/E for Cali utility. no prem/discount for 'Other' segment with smaller state exposures.

Risks to the downside are increase in market interest rates, potential impact of tax reform on utilities, operational errors, changes in valuation levels for water utilities. Risks to the upside are accelerating muni acquisitions, multiple expansion, and constructive legislation in regulatory jurisdictions.

Essential Utilities (WTRG)

Our price objective is $51 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. These peer multiples are 25.5x and 13.9x. We apply a 3.0x premium to Peoples Gas given the organic growth opportunities, while applying a variety of premiums to its water (2x previously) subsidiaries: +4x to PA, +3x to IL, +2x to OH, +2x for TX, +2x for OH, and no premium for balance of biz. We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Eversource Energy (ES)

Our sum of the parts based price objective of $93 uses P/E multiples on 2023E earnings. For electric utilities, we attribute a 4x premium NSTAR, and 3x premium to PSNH and CL&P to peer 16.6x multiple, reflecting future potential positive revisions to capex and earnings. For gas, we apply a 3x premium to the peer 15.0x multiple, given capex upside particularly in MA and a 2x for Columbia Gas. Both electric and gas peer P/E multiples are grossed up by 5% to reflect capital appreciation across the sector. We value Aquarion at a 1x premium to the 26.5x water multiple. We reflect ES's 50% ownership in Revolution and South Fork offshore wind sites on an NPV basis. We further reflect a devco value with an assumption of an additional 3GW through 2031. We take out 50% of parent debt, and 50% of interest to accurately reflect parent leverage.

Upside risks to our price objective are additional capex announcements on the T&D side, as well as success in offshore wind RFPs.

Downside risks are reduction in authorized ROEs, inability to meet earned ROE expectations, as well as failure to receive permitting on incremental capex opportunities

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also

certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AES	AES	AES US	Julien Dumoulin-Smith
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Enphase Energy	ENPH	ENPH US	Aric Li
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
NEUTRAL				
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	TransAlta Renewables Inc.	YRNW	RNW CN	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith

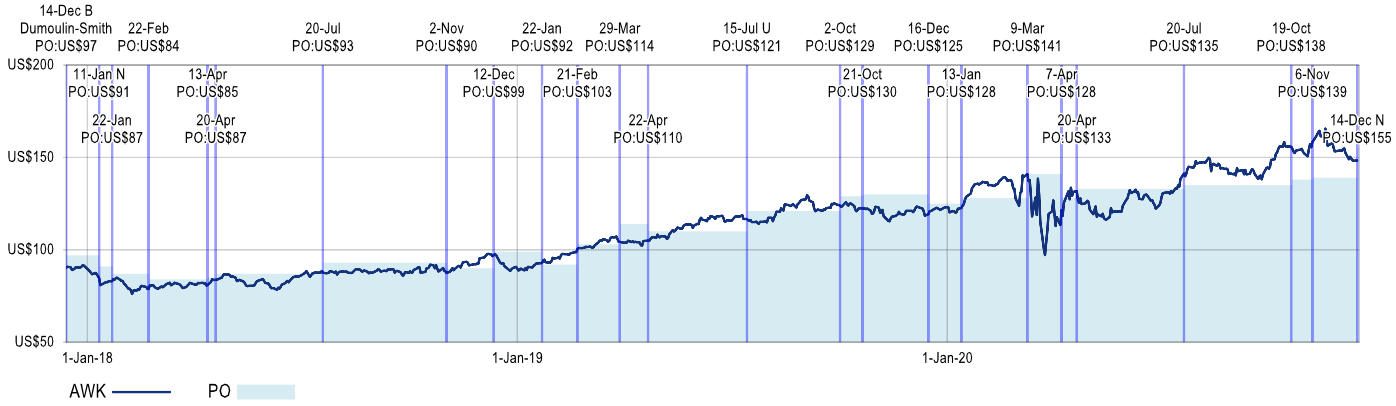
North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	Southwest Gas Holdings	SWX	SWX US	Richard Ciciarelli, CFA
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	Atlantica Sustainable Infrastructure	AY	AY US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith

Disclosures

Important Disclosures

American Water (AWK) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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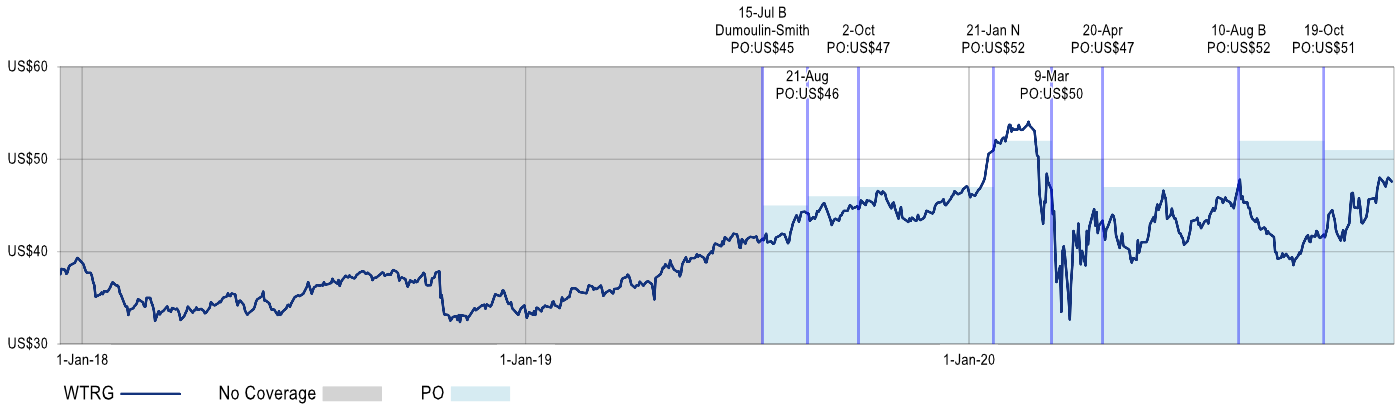
Essential Utilities (WTRG) Price Chart



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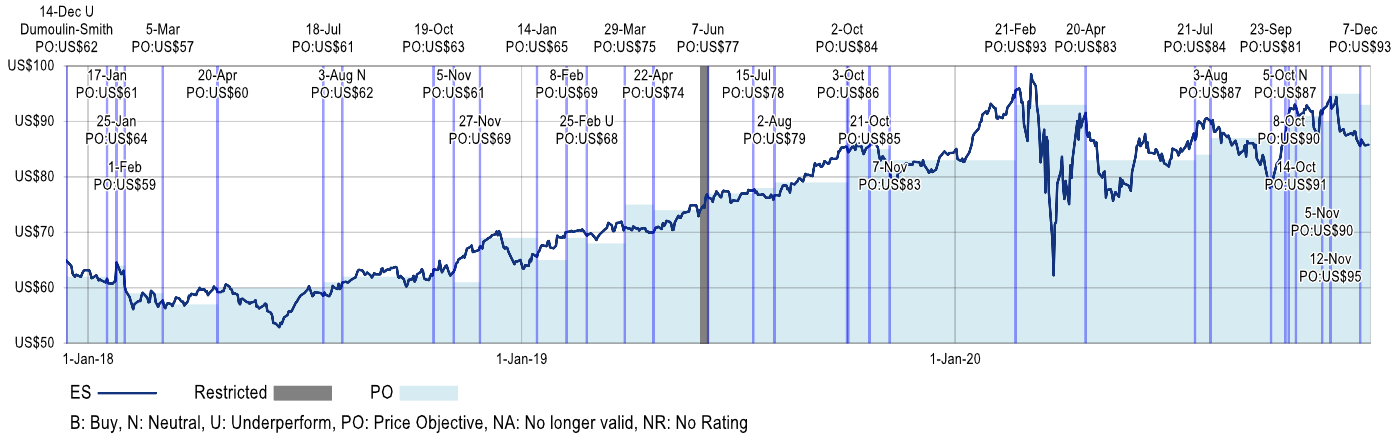
Eversource Energy (ES) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Utilities Group (as of 30 Sep 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	79	51.63%	Buy	59	74.68%
Hold	36	23.53%	Hold	24	66.67%
Sell	38	24.84%	Sell	25	65.79%

Equity Investment Rating Distribution: Global Group (as of 30 Sep 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1749	54.79%	Buy	1114	63.69%
Hold	677	21.21%	Hold	415	61.30%
Sell	766	24.00%	Sell	386	50.39%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

* Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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Essential Utilities

We Are Confident on the Near & 3-Yr View

Reiterate Rating: BUY | PO: 54.00 USD | Price: 48.18 USD

Latest Guide Intact Indeed – But Only Rolls to 3-yr view

On Monday morning, WTRG management provided 2021 EPS expectations of $1.64-1.69 - with the midpoint a touch above our prior estimate of $1.65 and prior consensus of $1.66 – while rolling forward their 5-7% EPS CAGR through 2023 (vs. '22 earlier). While the three year look is admittedly less than other utility peers, we expect a consistent roll forward of the outlook beyond '23 as well despite all the noise around tax credits and rate case timing. We perceive few meaningful impediments for shares despite perceived noise around tax credits this is simply rate case timing issue. See upside from further deals not contemplated in the plan, with only a ~$60Mn annual run rate considered outside of the known transactions, providing support for a water rate base CAGR well above their organic 6-7%. Discounted ESG opportunity remains clear among water peers

No Shortage of Muni Opportunities

With no shortage of municipal acquisition opportunities, we see the company as a prime beneficiary of further consolidation across the industry as COVID continues to pressure muni budgets and against a backdrop of favorable legislation: recall WTRG currently enjoys FMV legislation in all eight of their legacy water states. Following the acquisition of ~$63Mn in rate base in 2020, the company has five signed APAs totaling over $420Mn in rate base with another two winning bids totally ~$30Mn waiting a formal agreement. We see a long trajectory of further deals and suspect a potential run rate well above historical norms going forward given the increasingly constructive backdrop.

PO Shifts to $54 on Latest Multiples

Our 2021 estimate comes up slightly to the midpoint of management's guidance. We update our valuation to apply the current peer multiples to our latest estimates: 27.4x for water and 14.2x for gas (vs. 25.5x and 13.9x previously). Our premiums remain unchanged and continue to reflect confidence in ability to consistently deliver, strong muni acquisition prospects, and an underappreciated ESG angle. Our PO is raised to $54 (from $51 previously). Bottom line, see shares as poised to re-rate higher alongside wider water sector: The ESG Antidote: Why Water is a Win/Win.

Estimates (Dec)

(US$)	2018A	2019A	2020E	2021E	2022E
EPS	1.41	1.47	1.57	1.67	1.80
GAAP EPS	1.41	1.47	1.57	1.67	1.82
EPS Change (YoY)	3.7%	4.3%	6.8%	6.4%	7.8%
Consensus EPS (Bloomberg)			1.58	1.67	1.80
DPS	0.86	0.92	0.99	1.06	1.13

Valuation (Dec)

	2018A	2019A	2020E	2021E	2022E
P/E	34.2x	32.8x	30.7x	28.9x	26.8x
GAAP P/E	34.2x	32.8x	30.7x	28.9x	26.5x
Dividend Yield	1.8%	1.9%	2.0%	2.2%	2.3%
EV / EBITDA*	9.6x	37.1x	20.3x	18.6x	17.2x
Free Cash Flow Yield*	-1.1%	-1.8%	-3.6%	-3.2%	-2.5%

* For full definitions of *iQmethod*℠ measures, see page 9.

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Timestamp: 12 January 2021 06:08AM EST

12 January 2021

Equity

Key Changes

(US$)	Previous	Current
Price Obj.	51.00	54.00

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Stock Data

Price	48.18 USD
Price Objective	54.00 USD
Date Established	12-Jan-2021
Investment Opinion	B-1-7
52-Week Range	30.40 USD - 54.52 USD
Mrkt Val (mn) / Shares Out (mn)	11,817 USD / 245.3
Average Daily Value (mn)	48.16 USD
BofA Ticker / Exchange	WTRG / NYS
Bloomberg / Reuters	WTRG US / WTRG.N
ROE (2020E)	8.6%
Net Dbt to Eqty (Dec-2019A)	31.1%

ESG: Environmental Social Governance

PFA: Perfluoroalkoxy Polymer-Chemical Compound

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iQprofile℠ Essential Utilities

*iQ*method℠ – Bus Performance*

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Return on Capital Employed	3.9%	3.5%	5.4%	5.0%	5.1%
Return on Equity	9.7%	8.9%	8.6%	8.1%	8.6%
Operating Margin	38.7%	38.4%	64.7%	66.8%	67.0%
Free Cash Flow	(127)	(212)	(425)	(375)	(300)

*iQ*method℠ – Quality of Earnings*

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Cash Realization Ratio	1.9x	1.3x	1.7x	1.8x	1.7x
Asset Replacement Ratio	3.4x	3.5x	3.1x	2.9x	2.7x
Tax Rate	NM	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	127.1%	31.1%	98.3%	95.5%	103.1%
Interest Cover	2.8x	3.1x	3.4x	3.4x	3.6x

Income Statement Data (Dec)

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Sales	835	886	959	1,006	1,077
% Change	3.7%	6.2%	8.2%	4.8%	7.1%
Gross Profit	838	890	1,555	1,661	1,785
% Change	3.5%	6.2%	74.8%	6.8%	7.5%
EBITDA	1,941	504	920	1,006	1,084
% Change	-86.4%	-74.1%	82.6%	9.4%	7.8%
Net Interest & Other Income	(99)	(100)	(181)	(200)	(202)
Net Income (Adjusted)	192	263	373	410	464
% Change	-19.9%	36.9%	42.1%	9.8%	13.1%

Free Cash Flow Data (Dec)

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Net Income from Cont Operations (GAAP)	192	225	400	429	470
Depreciation & Amortization	147	156	338	376	412
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	(15)	(10)	(75)	(75)	(75)
Other Adjustments, Net	45	(32)	(38)	(6)	(6)
Capital Expenditure	(496)	(550)	(1,050)	(1,100)	(1,100)
Free Cash Flow	-127	-212	-425	-375	-300
% Change	-31.5%	-66.5%	-100.5%	11.6%	20.1%

Balance Sheet Data (Dec)

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Cash & Equivalents	4	1,869	6	6	7
Trade Receivables	101	108	188	201	216
Other Current Assets	42	36	50	52	55
Property, Plant & Equipment	5,930	6,346	10,657	11,381	12,069
Other Non-Current Assets	887	1,003	1,003	1,003	1,003
Total Assets	6,964	9,362	11,905	12,644	13,350
Short-Term Debt	160	131	126	135	151
Other Current Liabilities	239	188	244	253	263
Long-Term Debt	2,398	2,943	4,594	4,909	5,485
Other Non-Current Liabilities	2,158	2,219	2,144	2,069	1,994
Total Liabilities	4,955	5,481	7,108	7,366	7,893
Total Equity	2,009	3,881	4,797	5,278	5,457
Total Equity & Liabilities	6,964	9,362	11,905	12,644	13,350

* For full definitions of *iQ*method℠ measures, see page 9.

Company Sector

Water Utilities

Company Description

Essential Utilities is a regulated water/gas providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI - along with a natural gas presence through the recently acquired Peoples Gas providing distribution services to 740,000 customers in PA, WV, and KY.

Investment Rationale

We are Buy rated on shares of WTRG, seeing shares as poised to re-rate higher given consistent execution, acquisition upside, and increasing conviction around the premium story.

969,084

Quarterly Earnings Estimates

	2019	2020
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NAE

Rolling Forward the EPS CAGR with More Muni Upside

WTRG management provided 2021 EPS expectations of $1.64-1.69 - with the midpoint a touch above our prior estimate of $1.65 and prior consensus of $1.66 – while rolling forward their 5-7% EPS CAGR through 2023 (vs. '22 earlier). While the three year look is admittedly less than other utility peers, we expect a consistent roll forward of the outlook beyond '23 as well despite all the noise around tax credits and rate case timing.

With the latest update, management noted plans to file a rate case at Aqua Pennsylvania later this year, keeping with their three year rate case cadence for their water biz in the state while the company continues to implement Repairs Tax accounting treatment at Peoples Gas: recall earlier guidance of $0.08-$0.12 benefit annually from the repairs election. After the earlier subsequent filing of the catch up component, hearings are scheduled for the end of this month with resolution expected in the second quarter. Rather than drive incremental upside to their 5-7% EPS CAGR, the filing seeks to extend the growth without a need for a rate case. As opposed to going in for new rates in 2023 to take effect in 2024, a constructive outcome from the catch up filing would benefit '23, with incremental benefits in '24, and '25 to help drive earned returns for the segment in outer years without any rate relief until 2026. On balance, we feel comfortable in management's ability to manage around lag, particularly if the company is able to opt out of going in for rates longer.

Muni opportunities Increasingly Robust

We expect the growing pipeline of municipal opportunities to provide a long term tailwind for the water biz. Following the adoption of Fair Market Value legislation in TX and VA, the company now has the constructive legislation in all eight states of their water footprint. We expect this to help further accelerate consolidation in the industry as muni budgets are further flex'd from the crisis - and any further resulting acquisitions would be upside to mgmt.'s latest extended targets with guidance *only assuming ~$60Mn* in annual tuck ins through the forecast period (this is relative to ~$420 Mn of ratebase acquisitions pending). We stress clear positive re-rating potential within this guide range – and see this as also helping to take pressure off execution at Delcora too.

De-risking DELCORA

Late last year, the Delaware County Court of Common Pleas issued an order supporting the pending acquisition of DELCORA by rejecting the county's attempt to block the sale. The order ruled the asset purchase agreement is fully binding and enforceable and that the funds to offset DELCORA customer bills is legal – helping derisk the deal and mitigating prior concerns about the ability for the transaction to close. While we perceive there could still yet be a potential appeal around the decision, the order supports the anticipated closing timeline for the transaction: the Recommended Decision from the PA ALJ is anticipated next week (1/20/21), setting up a decision by the commission in early March and a transaction close in early 2Q. Final resolution should help alleviate some overhang given the forward that needs to be pulled by August.

Overall, we think the $420Mn in rate base opportunities from signed APAs is should generate ~$21Mn in earnings with further muni opportunities still to materialize (*this is roughly +4% to EPS and should help mgmt. execute towards upper end of targeted range*). We see upside to the plan given the more conservative approach to guide, and expect shares to rerate higher relative to AWK as investors continue to appreciate the premium story amid consistent management execution.

We reiterate our Buy rating on shares of WTRG following the latest guidance update. We have increasing conviction in management's ability to consistently deliver and see the company as a prime beneficiary of further consolidation across the water industry. – while the ongoing docket for the catch up component of Repairs Tax treatment in PA should provide further latitude to stay out of rate cases for the gas segment. We struggle to reconcile the sharp discount to peer AWK and see the overhang from gas as nearsighted, particularly given the pipeline of water opp's to further dilute gas as a percentage of their biz. With a growing focus on ESG – and mgmt.'s proactive action around PFAs and emission reductions – we see this an underappreciated angle not reflected at the current valuation.

WTRG 4Q20 Earnings Walk

We forecast 4Q20 adjusted EPS of $0.45 compared to 4Q19 adjusted results of $0.34 and consensus of $0.45.

• **Key Drivers:** The primary driver of the quarter is the contribution from the Peoples Gas acquisition after closing the transaction earlier this year with additional dilution offsetting growth at the legacy water biz.

Table 1: 4Q20 EPS Walk

WTRG 4Q20 Earnings Walk		EPS
WTRG 4Q19 EPS	$	0.34
Aqua		0.03
Peoples Gas		0.11
Dilution		-0.03
4Q20 BofAe Adjusted EPS	$	0.45
Consensus		$0.45
WTRG Guidance		$1.53-$1.58
2020 Consensus		$1.58
4Q20 Adjusted Shares Outstanding		254
4Q19 Adjusted Shares Outstanding		233

Source: BofA Global Research estimates, company report, Bloomberg

EPS Estimates: already towards top end of 5-7%

The exhibit below reflects our latest EPS Estimates. Our 2021 estimates come up slightly to the midpoint of management's newly rolled out guidance of $1.64-$1.69. Longer term, we continue to model to the high end of their 5-7% EPS CAGR. We perceive further upside from a likely acceleration in industry consolidation out of the pandemic as municipal budgets are further stretched and constructive legislation continues to enable transactions. With prospective EPS growth likely more consistent than earlier trajectory (which proved more 'lumpy,' we perceive the trajectory as ever more appealing for those seeking a de-risked outlook).

We continue to see positive bias on EPS execution as 5-7% could be implicitly reset off high end of '20 EPS guide – and see our estimates already at the top end of the EPS CAGR without the full inclusion of contemplated acquisitions (~$1.90 is high end of 5-7% for '23 off $1.55 midpoint). While financing details are pending, we see clear latitude to achieve high end and even re-base slightly higher too.

Table 2: EPS Estimates

EPS Estimates	2020E	2021E	2022E	2023E
PA	$0.75	$0.76	$0.88	$0.94
OH	$0.07	$0.07	$0.07	$0.08
IL	$0.07	$0.08	$0.08	$0.09
TX	$0.06	$0.07	$0.07	$0.07
NC	$0.04	$0.04	$0.05	$0.05
Other States	$0.07	$0.07	$0.08	$0.08
Water Utility	1.06	1.09	1.23	1.31
Peoples Gas	0.62	0.67	0.71	0.76
Parent & Other	*-0.10*	*-0.10*	*-0.13*	*-0.14*
EPS	1.57	1.67	1.80	1.92
YoY Growth	*7%*	*6%*	*8%*	*7%*
Guidance	1.53-1.58	1.64-1.69		
Fully Diluted Shares O/S	*254*	*258*	*261*	*261*
Previous EPS	*$1.56*	*$1.65*	*$1.80*	
Consensus	1.58	1.66	1.80	
DPS	0.99	1.06	1.13	1.21
Payout Ratio	*63%*	*63%*	*63%*	*63%*
Guidance		*60-65%*		

Source: BofA Global Research, Bloomberg

Valuation: PO Raised to $54 on Multiples

The exhibit below reflects our latest SOTP. We update our valuation to apply the current peer multiples to our latest estimates: 27.4x for water and 14.2x for gas (vs. 25.5x and 13.9x previously). Our premiums remain unchanged and continue to reflect confidence in ability to consistently deliver, strong muni acquisition prospects, and an underappreciated ESG angle. Our PO ultimately shifts to $54 (from $51 previously). Reiterate Buy given deep discount and upside catalysts.

Table 3: SOTP

Water Utilities	2023 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*27.4x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		29.7x							
Water Utilities									
States	2023E EPS	ROE embedded							
PA	$0.94	10.0%	4.0x	32.7x	33.7x	34.7x	$31	$32	$33
OH	$0.08	9.2%	2.0x	30.7x	31.7x	32.7x	$2	$2	$3
IL	$0.09	9.1%	3.0x	31.7x	32.7x	33.7x	$3	$3	$3
TX	$0.07	10.0%	2.0x	30.7x	31.7x	32.7x	$2	$2	$2
NC	$0.05	9.2%	2.0x	30.7x	31.7x	32.7x	$1	$2	$2
Other (including acquisitions)	$0.08	9.2%	0.0x	28.7x	29.7x	30.7x	$2	$2	$3
Water utilities total (ex-Peoples)	$1.31			*32.1x*	*33.1x*	*34.1x*	$42	$43	$45
Gas Utilities									
Peer Gas P/E		*14.2x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		15.0x							
	2023E EPS	ROE embedded							
Peoples Gas	$0.76	11.9%	3.0x	17.0x	18.0x	19.0x	$13	$14	$14
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			-985	50%			($492)	($492)	($492)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($444)	($412)	($482)
50/50 Weighted Drag from HoldCo Drag							($937)	($904)	($975)
Fully Diluted Shares Outstanding							*261*	*261*	*261*
PO								$54.00	
Current Price								$48.18	
Dividend Yield								2.2%	
Total Potential Return								14.27%	

Source: BofA Global Research, Bloomberg

Price objective basis & risk

Essential Utilities (WTRG)
Our price objective is $54 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. These peer multiples are 27.4x and 14.2x. We apply a 3.0x premium to Peoples Gas given the organic growth opportunities, while applying a variety of premiums to its water (2x previously) subsidiaries: +4x to PA, +3x to IL, +2x to OH, +2x for TX, +2x for OH, and no premium for balance of biz. We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
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	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Enphase Energy	ENPH	ENPH US	Aric Li
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	Ormat Technologies	ORA	ORA US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
NEUTRAL				
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Atlantica Sustainable Infrastructure	AY	AY US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	TransAlta Renewables Inc.	YRNW	RNW CN	Julien Dumoulin-Smith
	UGI Corp.	UGI	UGI US	Richard Ciciarelli, CFA
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	Southwest Gas Holdings	SWX	SWX US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith

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Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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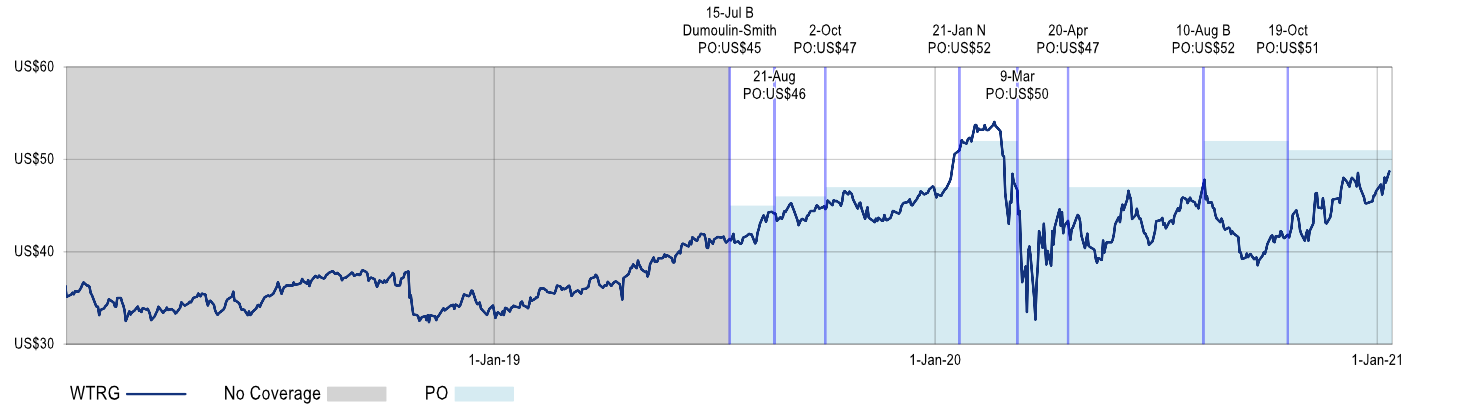
Essential Utilities (WTRG) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Utilities Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	80	51.61%	Buy	58	72.50%
Hold	37	23.87%	Hold	28	75.68%
Sell	38	24.52%	Sell	22	57.89%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1863	56.90%	Buy	1185	63.61%
Hold	686	20.95%	Hold	426	62.10%
Sell	725	22.14%	Sell	358	49.38%

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North American Utilities & IPPs

2Q20 Regulated Utility Preview: The Covid Compendium Condensing What We Know

Price Objective Change

20 July 2020

Equity
North America
Utilities & IPPs

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'20 looks intact for most across Regulated space

We provide our 2Q20 Regulated utility preview for AEE, AEP, AWK, CMS, DTE, DUK, EIX, LNT, WTRG, EVRG, FE, PNW, PPL, WEC, and XEL. The group trod water during Q2 with the IXU index returning +1.8% from Mar 31 through June 30, a tough comp against the broader market with the S&P 500 rallying +20% in the same period. Nonetheless, we see a more constructive story across the board than one quarter ago with weather largely serving as a cushion on Q2 results, offsetting expected losses linked to COVID. If Anything those with pitfalls into 2Q are largely of their own discrete nature, rather than wider (unknown) Covid concerns – along with a handful who didn't update earlier.

Q2 shaping up (much) better than initially feared

For **EIX** we see a miss on 2Q, although comparability continues to remain outside of reach given pending O&M recovery; instead, expect focus to remain on the upcoming fire season and mitigation efforts (PSPS, Blackhawks, fire retardants) as well as updates on '17/18 liabilities (where we remain biased to the upside on the $4.9bn low-end range) although could see further clarity on B/S help w/ re-rating potential. For **DUK**, we see a weak 2Q given more material COVID impacts with O&M offsets back half weighted; we remain concerned around mgmt.'s messaging *of re-base its growth trajectory* given an expected weak '21 outlook following cancelation of ACP and capex backfilled in the later part of the program; longer-term the IRP presents a clear opportunity for further capex deployment (post-21 given litigated process) as well as legislation stemming from the NC clean energy agenda. With large resi compositions and constructive recovery mechanisms/orders across most jurisdictions, we see **AWK** and **WTRG** as relatively protected from COVID challenges. After electing not to reset expectations with 1Q results, *we see more risk to **PPL**'s 2020 guidance* – albeit our latest model still suggests the low end of their range: full quarter impact and ongoing expectations around UK in particular will prove critical given two year lag with true up mechanism. **LNT** continues to move ahead with its WI solar filing with an expected order in '21, while the rate stabilization filing in the state should be decided in Q3 with unchanged ROE and equity and escrow treatment for pension and bad debt. **DTE** appears to have largely offset Covid impacts (among the higher Industrial sales declines posted in Apr) thanks to a strong weather uplift in the quarter (across MIS); we also see approval for rate case filing delay until Q2 202; among best for 2Q outlook. We expect similar benefits for CMS with further details and confidence in cost savings to support a firmer reaffirmation of FY20 guidance. **EVRG** received approval of its accounting order in KS (historically its more difficult jurisdiction) and has a pending request in MO; we see a largely in-line quarter though the focus remains on the outcome of its strategic process with committee recommendation in late July and Board decision in August. **PNW** has a tricky regulatory setup in 2H with rate case staff testimony due in early August, though mgmt. recently affirmed that they do not see a path to settlement in '20, with likely decision coming from a new bench of commissioners after Nov elections; we do expect capex clarity as unexpected angle into 2Q to drive partial offset to outlook; pos '20 affirmation too. We expect **WEC** to post a Q2 print at the top of its already-increased guide range on the back of warm June weather, and see their '20 guidance as very much intact (we raise ests to high range); here too pos framing ahead.

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2Q Summary and PO Changes

We include a brief summary of our 2Q estimates compared vs Street as well as PO changes reflected in this report.

Table 1: PO Changes

Regulated		New PO	Old PO
Alliant Energy Corp	LNT	$54.50	$52.00
Ameren Corp.	AEE	$79.00	$79.00
American Electric Power, Inc	AEP	$88.00	$80.00
American Water	AWK	$135.00	$133.00
DTE Energy Co.	DTE	$115.00	$115.00
Duke Energy	DUK	$87.00	$84.00
Edison International	EIX	$65.00	$65.00
Essential Utilities	WTRG	$47.00	$47.00
Evergy, Inc	EVRG	$68.00	$63.00
FirstEnergy Corp.	FE	$45.50	$45.50
Pinnacle West Capital Co.	PNW	$78.00	$78.00
PPL Corporation	PPL	$27.00	$27.00
WEC Energy Group Inc.	WEC	$83.00	$83.00
Xcel Energy Inc.	XEL	$62.50	$62.50

Source: BofA Global Research

Table 2: 2Q Estimate Summary

Regulated		2Q20 - BofAe	2Q20 - Cons	Delta
Alliant Energy Corp	LNT	$0.51	$0.44	16%
Ameren Corp.	AEE	$0.86	$0.86	0%
American Electric Power, Inc	AEP	$1.07	$1.02	5%
American Water	AWK	$0.97	$0.96	1%
DTE Energy Co.	DTE	$1.27	$1.19	7%
Duke Energy	DUK	$1.01	$1.01	0%
Edison International	EIX	$0.95	$1.15	-17%
Essential Utilities	WTRG	$0.24	$0.22	4%
Evergy, Inc	EVRG	$0.70	$0.68	3%
FirstEnergy Corp.	FE	$0.54	$0.55	-2%
Pinnacle West Capital Co.	PNW	$1.55	$1.43	8%
PPL Corporation	PPL	$0.54	$0.56	-4%
WEC Energy Group Inc.	WEC	$0.69	$0.67	3%
Xcel Energy Inc.	XEL	$0.43	$0.49	-12%

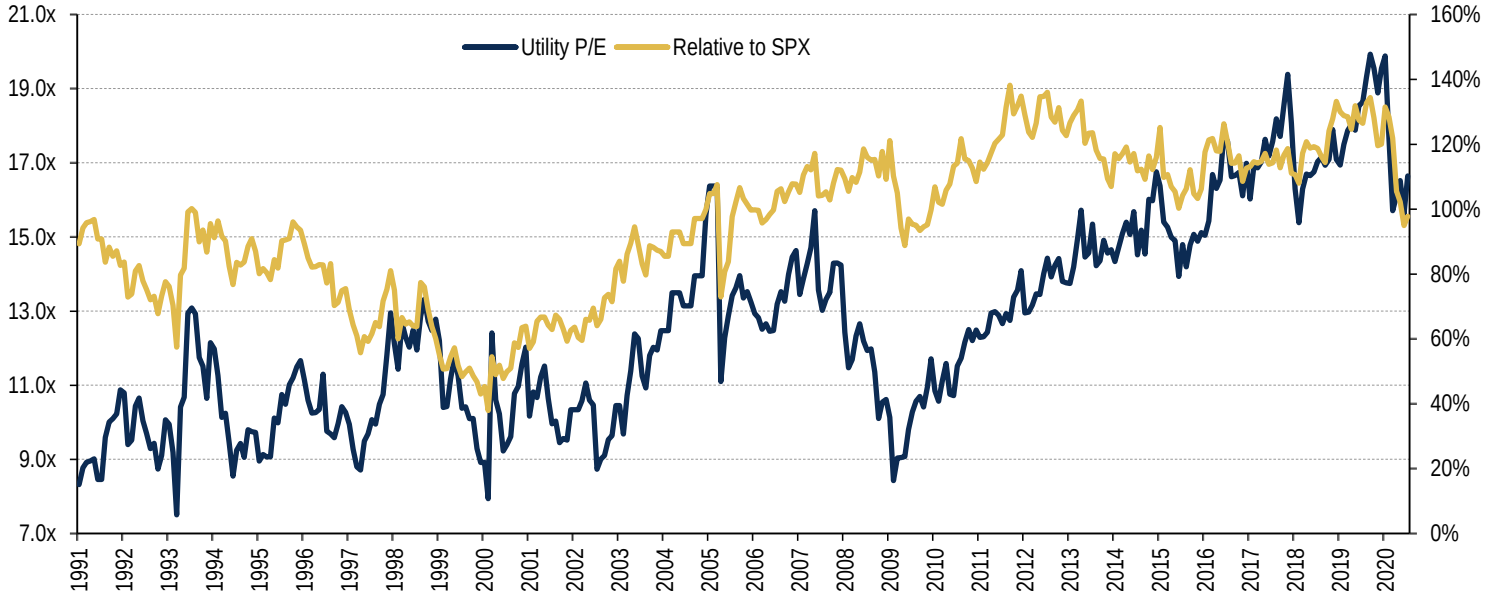
Source: BofA Global Research, Bloomberg

Macro Backdrop

We perceive investors are generally skeptical of current sector valuations – and see the continued upward trajectory of the sector as still showing an expensive backdrop from a high level perspective. The chart below shows the latest mark-to-market of the group on an absolute basis and against the SPX; utilities continue to trade near their all-time highs on both a relative and absolute basis.

We continue to see the backdrop as among the single most intriguing backdrops in recent memory with the sector having traded off relative to its historic relationship between rates and the S&P to its lowest levels since the 2000 tech bubble – off its highest relative trading levels in 3Q19 (almost -60% under-performance), making the sector incredibly compelling against historic valuation metrics. With few material risks to estimates, dividends, or outlook, the question is just whether the market will remain oriented towards growth equities with elevations. Much of this is dependent on recovery from recession ironically – where recovery has historically driven a bid towards value relative to growth (per our Equity strategist Savita Subramanian).

Chart 1: Utility PE relative to SPX

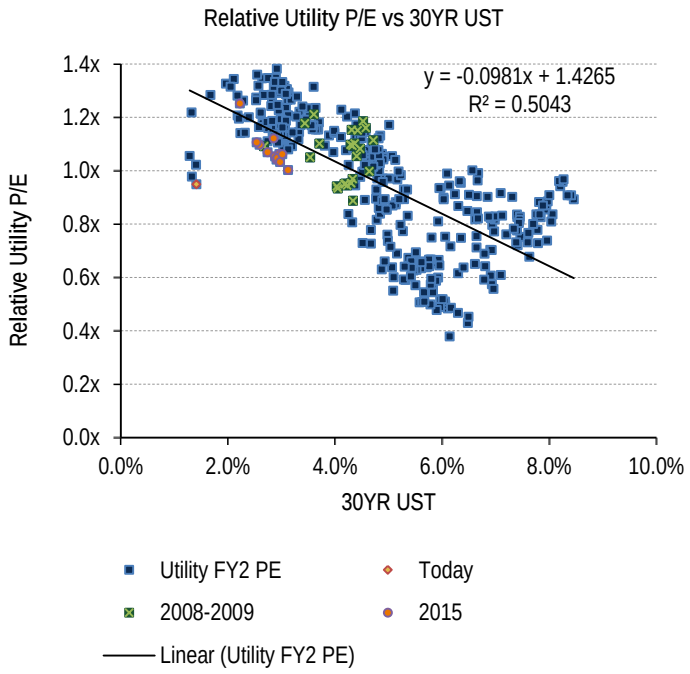


Source: Bloomberg

When adjusting for the S&P itself *and* the treasury environment: different story

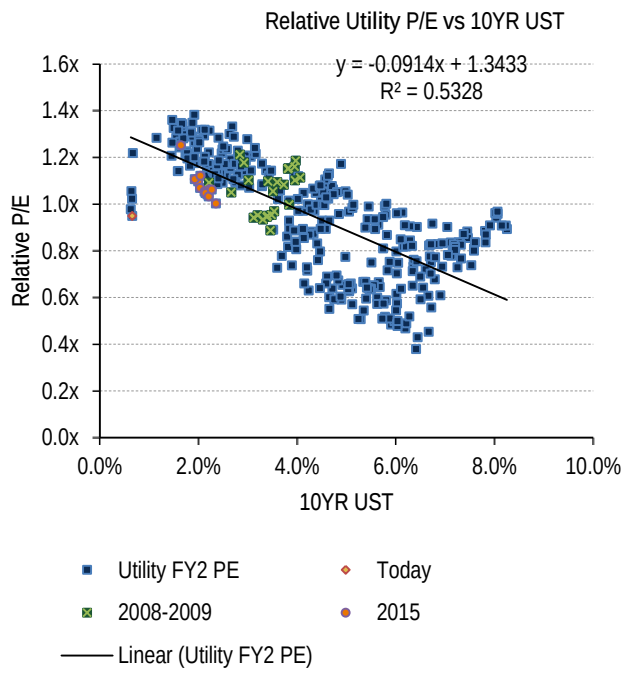
In the exhibits below, we show a time series of where the sector has traded relative to the linear regression on a relative and absolute basis for Treasuries to illustrate the premium; the group has started to trade more in line with its historical linear relationship with 10Yr and 30 Yr Treasuries on a relative basis.

Chart 2: Relative Utility PE vs 30YR UST



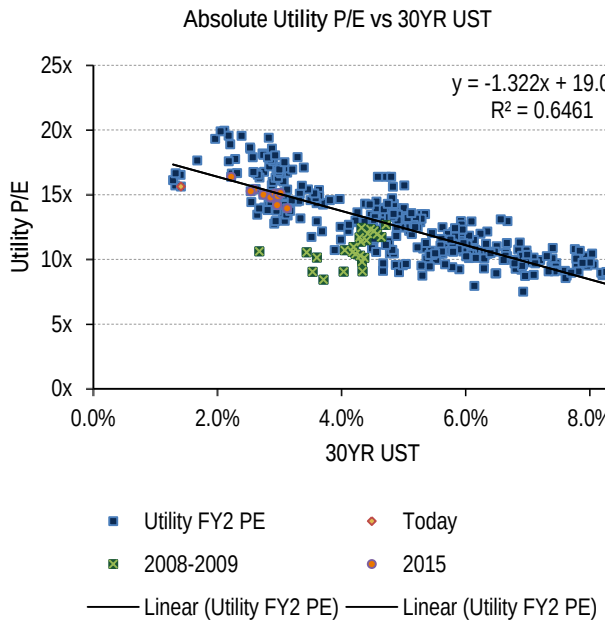
Source: BofA Global Research, Bloomberg

Chart 3: Relative Utility PE vs 10YR UST



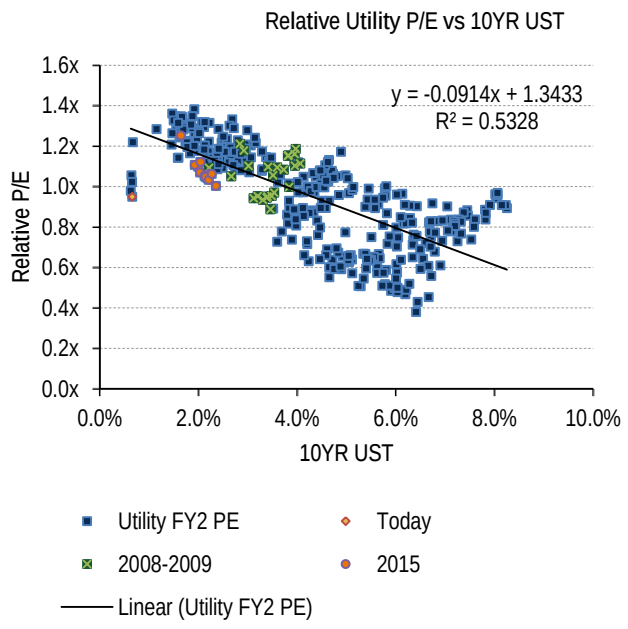
Source: BofA Global Research, Bloomberg

Chart 4: Absolute Utility PE vs 30YR UST



Source: BofA Global Research, Bloomberg

Chart 5: Absolute Utility PE vs 10YR UST



Source: BofA Global Research, Bloomberg

Tax Reform Perspectives For Utilities In Brief

Tax Reform & Utilities: Not as Concerned as Investors

We recently hosted a call with our BofA Public Policy expert regarding potential tax reform with Biden as President. Critically, our expert asserts only if there is a Democratic sweep in November (Biden wins, and Democrats regain control of both the House and Senate) would it be likely for Democrats move to pass a meaningful tax bill in 2021. Many utility investors have been concerned about tax reform prospects and focusing on this scenario as if this was directly tied to a Biden win of late- rather than appreciating the very more narrow under which comprehensive tax reform would once again pass. Note the budget reconciliation vehicle, allows Congress to move tax legislation with only a bare majority in the Senate (cannot be filibustered); this remains a critical vehicle seeing it being used for the last tax reform effort. Notably, Biden's platform currently has three major likely tax proposals, which include: 1) raising the U.S. corporate tax rate from 21% to 28%, 2) implementing a new minimum tax on companies' GAAP earnings, and 3) tightening of the Global Intangible Low Tax Income (GILTI). The first two matter to utilities, while the third really would only apply to AES among utilities/IPPs. Think tanks and private revenue estimators believe raising the tax rate (the most likely of the three proposals) would lead to government revenue of $1.3 trillion over ten years, the highest potential revenue source of the three proposals. The exact rate increase is still subject to change, but 28% is the current proposal. We address many of the tax reform debates in latest election note. The minimum tax on GAAP earnings specifically impacts U.S. corporations that currently do not pay taxes of at least 15% of their GAAP earnings. The proposal would bring the tax level up to 15% for the companies that currently "habitually pay less" than this rate; this could very well still allow for renewable tax credits to be netted even against this minimum requirement (hence giving reprieve to much of the utility industry, albeit this remains unclear). A tightening of GILTI impacts multinational corporations where a company's rate would be increased from 10.5% (current as of 2017) to 21%, effectively doubled. It remains unclear just how this would manifest itself for AES (B-1-7; $14.44). Overall, we see utilities as net beneficiaries under a tax reform context given the muted impact vs other industries despite what is likely delayed ability to recoup the higher tax rates from customers given the need to file rate cases (and likely suffer ROE drops too).

But the real low prob kicker is dividend tax rate hike risk

Separately on the income tax front, but critical for utility investors, Biden has also proposed to tax capital gains and dividends at the same rate as ordinary income, which would go back up to 39.6% in the top income bracket (above $1mn/year). However, we acknowledge that this would be a relatively dramatic proposal, and it is unclear if moderate democrats would support this or even move in the context of a Democratic sweep according to our internal expert. Bottom line, although it is unlikely there is desire to move legislation on capital gains and dividends, and a democratic sweep presents notable vulnerability for utilities under this proposal in addition to the three aforementioned major tax proposals.

King Coal: How Much Exposure is Left?

Measuring the value of remaining coal across the sector

We present our analysis of estimated rate base, earnings, and in turn, value of coal as a % of market cap across our Wider Power & Utilities universe. While disclosures vary with most companies under our coverage (explicitly) disclosing coal rate base many provide some very helpful clues enabling us to estimate ratebase (particularly of more recently built) scrubbers, leveraging FERC Form 1 data and estimates around deferred tax and related adjustments. We also highlight the impact on rate base of scrubber and other pollution control retrofits that have left many utilities with the challenge of dealing with undepreciated plant in what are increasingly uncompetitive generation assets - though some states such as MI have addressed the challenge head on with existing securitization laws, we see opportunities for acceleration of retirements in other jurisdictions such as WI, KS, MO among others where securitization is yet on the books.

Leaders and laggards among our coverage

Our analysis shows that on average Regulated and SMID-cap names have earnings exposure linked to coal in rate base of 10-15% while Diversified peers are meaningfully lower with the exception of SO, although w/ constructive regulatory relationships. EVRG stands out w/ 2019 EPS estimated at 39% derived from its coal-heavy fleet given an estimated ~$5B of coal in rate base. We continue to see this as a key angle to watch in the ongoing strategic process given a largely undepreciated amount w/an estimated $1-$1.5B in rate base linked to scrubber retrofits (highlights need for securitization in both the KS and MO). Elsewhere, we continue to see ETR's unscrubbed fleet as representing a significant renewable investment opportunity with minimal rate base remaining - though the overall share of coal-fired generation in the company's portfolio remains 9% by nameplate capacity. CNP screens as the single highest exposure to coal by % of its portfolio at 83% of nameplate, but the small size of its overall fleet and minimal ratebase associated with its assets (including scrubbers on all assets) mitigate its overall exposure. Meanwhile we expect DTE's relatively high exposure estimated at 19% of EPS to decline in coming years with scheduled 2022 retirements of three facilities - while we estimate some undepreciated rate base associated with the assets, the regulatory environment is broadly supportive of transitioning away from coal with securitization legislation in place in the state since 2000. NEE is unsurprisingly a leader in terms of minimizing exposure among utilities, with less than 1% of rate base tied to coal on our estimates. PNW provides particularly limited (no) disclosure on the composition of its coal rate base (we estimate modest exposure), although is seeking to meaningfully add to its coal rate base. DUK too stands out given ~13% of EPS made up of coal where it also intends to add through coal ash clean-up on one hand, although is looking to make strides through the IRP w/ coal retirements and potential for securitization/accelerated D&A in legislation/rate cases: only DUK, SO, and PNW are still really adding to coal (ash) ratebase. While AES' earnings are ~35% coal and our SOTP indicates ~30% value (among highest for entire sector) are from coal, co is rapidly selling & de-carbonizing (anticipate closer to ~20% end of year): more here. With ESG investors focused on this question of exposure typically from a revenue perspective we thought it appropriate to reposition the debate on a more relevant set of metrics. Please refer the link for full details here.

ESG in the Utility Sector: The Inaugural Diversity Handbook

Diversity & inclusion across the utilities

We provide an inaugural deep dive on diversity and inclusion efforts across our coverage universe. We perceive the issue of diversity in its various forms as increasingly relevant to the investor community, with a growing body of evidence linking financial performance to an inclusive and equitable business environment. We highlight our BofA ESG Research Team's recent report, Womentum! Our report on company initiatives and efforts covers nearly 60 companies across the Diversified, Regulated, SMID Utilities, Gas Utility, Water Utility, Power, LNG, and Residential Solar sectors.

Selecting our diversity metrics

We compiled data and information to assess D&I practices using a range of relevant diversity metrics. In particular, our analysis is focused on: 1) board representation of women & minorities, 2) senior leadership representation of women & minorities, 3) supplier diversity programs and % diverse spend, 4) availability of Employee Resource Groups, and 5) LGBTQ equality policies and practices. Based on public data regarding gender equality, we note a major push across the sector in recent years: on average, women now comprise ~30% of Board members and ~25% of executive leadership roles. Racial/ethnic minority representation is slightly lower with ~20% BoD and 15-20% executive leadership representation in companies in our coverage universe; these averaged statistics also fall slightly below company-reported workforce percentages. Further, fewer disclosures were provided on POC representation than on gender, suggesting that these figures may be even lower. We also provide LGBTQ equality ratings as assessed by the Human Rights Campaign's Corporate Equality Index. While the majority of companies with CEI ratings received full scores (100), a handful of companies scored below, a couple did not respond to repeated requests, and a few of the smaller-cap names were not included given their size. On supplier diversity, nearly all companies stated that they had supplier diversity programs but many did not disclose % spend; on the high end; we note that some companies had up to 30-40% diverse spend. Finally, we include company summaries with more qualitative information (e.g. ERGs, other initiatives).

How did the companies stack up? Stocks in focus...

After examining the quantitative/qualitative metrics, we highlight the companies which stood out within each subsector. SRE has 38% female and 31% POC Board representation, has signed on to the "Paradigm for Parity" for full gender parity in senior executive roles by 2030, and maintains ~40% diverse spend at SoCalGas and SDG&E. ETR has 40% female representation on its BoD, with 30% female executives and 20% POC executives. For 2020, ETR has a diverse spend target of 14% of managed spend. EIX has 36%/36% representation on the BoD by women and POC, respectively, with 35%/34% women and POC in executive roles. Edison is part of the Paradigm for Parity effort. Diverse spend comprises ~40% of total spend. PCG has 34% and 35% female and POC executives, respectively. Total diverse supplier spend represents ~41% of total purchases. CMS has 45% female representation and 27% POC representation on its Board. Women and POC comprise 32% and 18% of executive roles, respectively. Please refer the link for full details here.

Contrasting US Utility Performance Against Global Peers

A Sector Trip Around the Globe

Our macro series continues, with our latest analysis providing some color around BofA utility performance vs regional markets relative to the US Outlook. We include perspectives from our colleague's from Asia, Australia, Europe, and LatAm in an attempt to contrast against the latest backdrop for US utilities. Across the world, we have seen wide dispersions in performance by geography, subsector, and company - with our included tables highlighting performance on a one week, one month, three month, and YTD basis and reflecting averages by subsector across the durations (on a market-cap weighted basis). Most geographies show *relative performance similar or even out-performing their regional markets (admittedly what would be expected in a global defensive pivot*). See each relative performance trends below by region.

So how Does this Stack up with the US?

In our full note, we include the latest stock performance for our core US utility coverage (Diversified, Regulated, SMIDs, Gas, and Water) along with the latest charts showing utility valuations vs. risk free rates & bond yields - with discrepancies recently reached having not been seen in the last several decades. We view US Utilities as substantially intact despite earlier fears of widespread Covid impacts. While admittedly revisions could still prove slightly downwards (2-3%) on '21 given delayed rate recovery & under-earning vs. authorized returns, we see this as much more intact than peer S&P sectors. While a potential 'twin' headwind remains around corporate tax reform into '21, this admittedly is a factor for all utilities. On a market cap weighted basis, Diversified Utilities and Large CapRegulated Utilities remain down low double digits YTD, while SMIDs and Gas utilities are off a more material 25% and 14%, respectively. Water utilities are down a more modest 1% for the year. More specifically, with the utility sector primed for the return of the value cycle, we see SMIDs particularly well positioned to recover from the underperformance this year. With the economy reopening in many states across the nation, we could see a reversal of the 2Q liquidity environment that has favored growth stocks, with value stocks starting to outperform with the latest improving data trends amid re-openings and estimate revisions. With the BofA strategy team calling for value stocks to outperform at least for the next quarter, we believe this bodes well for the sector going forward. Into the next several months. We continue to see the most opportunity in **ETR** and **AEE** among larger-cap regulated names. We also highlight **AES** with its global footprint; down -33% YTD, we perceive this as outsized relative to any relevant geography for the company globally (with even Latam Utilities only down on average -8%). The wider under-performance of the US utilities as part of a near record downtick in 'Value' allocations (see macro note on this trend in US) is also highlighted by the near record relative dispersions *among* utilities, seeing near all-time highs in P/E spreads between 'quality' (those have a record of stable & consistent EPS growth) and 'value' (those with historically lower & less consistent EPS growth alongside higher leverage).

Please refer the link for full details here.

Why are US Utes so Cheap? Let's Look at the Balance Sheet- and P/BV

Tackling the Price/Book Value Debate for Utilities

With the evolving backdrop and strong market comeback more recently, we continue to analyze the US utilities sector against the latest macro data and trends. We continue to see utilities trading at a wide valuation gap on a relative basis to historical relationships to risk free rates and bond yields - with discrepancies recently reached having not been seen in the last several decades. Our latest analysis dives deeper by looking at Price/Book Values across our coverage at both a sector (vs. SPX and other S&P sectors) and company specific level vs. historical norms. Broadly speaking, the group is trading at a ~1.2x discount on this metric, slightly above the -1.0x discount to the S&P over the last decade while the majority of sectors (ex. Financials, Materials, and Energy) are all elevated from an absolute level vs historic norms but off their peaks. While admittedly P/BV value trends don't show the sector trading as cheap as comparisons vs yields (both risk-free and corporate IG bond yield relationships) would otherwise indicate, it admittedly is still wider than historical norms by -20%, this metric controversially shows the sector trading at one of its most elevated levels in recent years in absolute terms (see full tables below). Critically, his has been one of the arguments from bears or those otherwise Neutral on Utility sector valuation, suggesting it just doesn't 'screen' well for a hard asset sector. Admittedly, most sectors are already trading at near record historical levels on a P/BV basis (likely with tech & other growth sectors reflecting an increasing premium for intangible assets). Looking at the spread between the wider S&P and Utilities, the discount on a P/BV basis today is at its widest (eg-utility discount) since the GFC. Altogether, while not quite as bullish a characterization we still see even this valuation metric as meriting an investment case in utilities. Meanwhile looking at sector balance sheet more holistically, metrics have seen a steady uptick in leverage in recent years (both net Debt/EBITDA and FFO/debt) reflecting wider de-risking (fewer non-reg subs, etc) and acceptance of greater leverage by rating agencies

EV to Ratebase yields similar outcomes

In our latest analysis, we also highlight EV/Rate base as a further proxy of P/BV valuation: notable companies on EV/Ratebase metric include DUK, FE, ES, WEC, LNT among others with larger non-regulated/tax items.

So What are Our Top Picks these Days?

We see the utility sector as primed for the return of the value cycle, with SMIDs particularly well positioned to recover from the underperformance this year. With the economy reopening in many states across the nation, we could see a reversal of the 2Q liquidity environment that has favored growth stocks, with value stocks starting to outperform with the latest improving data trends amid re-openings and estimate revisions. With the BofA strategy team calling for value stocks to outperform at least for the next quarter, we believe this bodes well for the sector going forward. Into the next several months. Our favorite opportunities remain ETR and AEE among larger-cap regulated opportunities.

Please refer the link for full details here.

The ABC's of Utilities: ROE, leverage, debt capital, and capex tell the story

Evaluating GAAP ROEs and ratio trends

Below we compile a series of ratios to show aggregate trends for sector wide returns and balance sheet metrics. We find this a useful compilation for investors to gauge wider sector trends on largely sustained balance sheet metrics and consistent ROEs across the space in spite of sector gyrations from year to year & provides a baseline for comparison across each of the sub-sectors against 'normal'. We include full tables of both projected and historical earned ROEs and balance sheet metrics below for review. Credit metrics are intact, despite continued acceleration in capex in recent years. We anticipate 2020 could prove a pause on this accelerating trend.

Risks to sector linger as Corp Tax & Covid Combined

We increasingly see some risks of compounding rate case delays given consumer impacts of Covid (& low rates at that) exacerbated by the prospects of higher corporate taxes through a change in administration: this could drive more meaningful rate lag. This could specifically impact '22 and '23 ests as years of rate stay outs eventually take their toll on earned ROEs despite cost cutting efforts. While earlier (lower) corporate taxes were readily passed through to consumers, the reverse could be reflected potentially in a delayed fashion through new rate cases (unclear if trued up) and would present potentially unpalatable rate increases despite covid sensitivities. This could also serve to reduce authorized equity ratios.

Subsector breakdown: Regulated have higher GAAP ROEs

We find that Diversifieds, SMIDS, and gas utes have roughly an average of 9% GAAP ROEs, while Water and Regulateds are higher at 10%, and 11%, respectively. Canadian utes are at 7% - reflecting non-regulated segments and commodity risk. In '20 we see 40-100bps YoY decreases in all subsectors but gas (flat) & Canadian names (increasing).

Could we see more capex shifts?

In response to balance sheet pressures, a number of co's reduced capex in '20, shifted capex from '20 into later years, or reduced capex overall in the next few years; we adjusted capex in our models for co's including CNP, EXC, AEP, CMS, EIX, POR, NI, EMA and AQN. Not all companies reduced '20 capex; some have upside potential including co's positioned to benefit from replacing generation with ratebase opps (AEE, ETR) working with states in what we see as stimulus (i.e. accelerate or increase capex to create jobs) (XEL, PEG), and pursing renewables opps that benefit from the PTC continuity safe harbor guideline expansion (NEE, AQN). Across our coverage, we find a net $419mn capex reduction in '20 and a $1.5bn capex reduction for '20-25 - a mere -0.3% reduction in total spending but indicative of co-level differences. Looking forward this year, we believe there remains risk of negative capex revisions still for the sector, given potential further balance sheet pressure going into 2Q (what many expect is the hardest quarter on sales) and apparent delays in rate case timing (as companies are rightfully sensitive of the economic backdrop to not file too soon). We see this risk as largely overlooked.

Please refer the link for full details here.

Alliant Energy (LNT)

We forecast 2Q20 adjusted EPS of $0.53 vs. consensus of $0.40 (we note upside to Street estimates as these are not updated yet) and 2Q19 results of $0.40. We reflect a 2020 EPS estimate of $2.44/sh, above the midpoint of mgmt.'s $2.34-2.48/sh guidance range as LNT continues to respond to Covid-related sales impacts, though we note that Q2 provided an estimated weather-related uplift, in contrast with Q1. We expect an update on LNT's WI rate stabilization filing which is currently making its way through the PSC process with staff recommendations forthcoming. With this approval expected sometime in Q3 and the recent solar filing, we see the LNT story as increasingly de-risked and set up for continued execution into '21with our forecast EPS CAGR at 6-7% off 2019 vs. mgmt. range of 5-7% .

Key Drivers: Weather is expected to be a benefit of $0.05/sh as we normalize for the negative effects of 2Q19 (2 cents) and account for milder weather in 2Q20 that drove the number of CDDs across LNT's service area higher than normal – in particular in the month of June which sees a heavier weighting toward its degree days. We estimate a Covid-related impact (sales and O&M offsets) of approximately -3 cents for the quarter as LNT reported residential sales up 4% with C&I down 12% for the first 2 months of Q2. We also note a tax timing item which we estimate at+4 cents in Q2 related principally to PTCs, which along with the 8 cent gain reported by LNT in Q1 is expected to reverse during the balance of the year.

Unknowns: Weather is expected to be a benefit to LNT – we estimate a 3 cent uplift – thought given the shoulder quarter he exact impact is difficult to ascertain. We note the relative weighting of degree days varies from Apr-Jun, though with Q2 CDDs weighted toward June for LNT, this trend should provide a tail wind. Additionally, we note that while most states have lifted strict stay-at-home orders, higher-margin residential sales may have benefitted as more people remained indoors than during a 'normal' year. While the tax timing impact related mostly to PTCs is expected to be flat for the year, it is difficult to estimate the precise impact though we expect it to be directionally lower in Q2 relative to 8 cents in Q1.

Table 3: LNT Q2 EPS walk: a nice beat off lowered expectations from 1Q

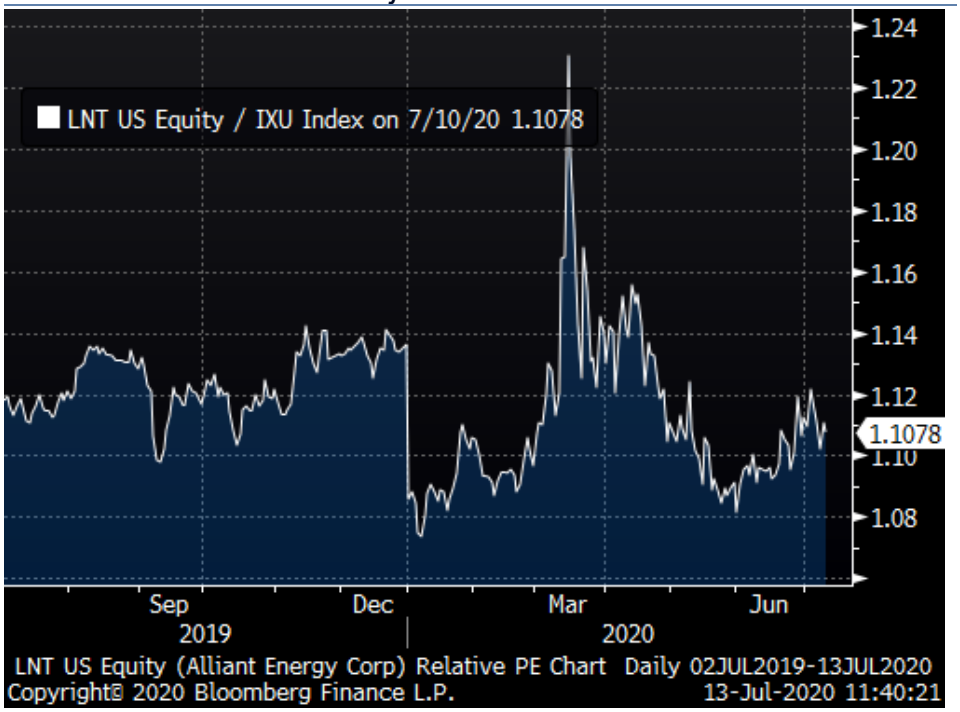
2Q20 EPS Walk	Notes	EPS Impact
2Q19 Starting Point		$0.40
Weather impact 2Q19		$0.02
Weather impact 2Q20	*June CDDs higher than normal*	$0.03
IPL Base rate increase	*IPL Electric effective 1/8/20; IPL Gas effective 12/18/19*	$0.09
WPL Electric	*New rates at WPL*	$0.05
Depreciation	*-$0.18/sh for full year; weighted more heavily later in yr*	($0.03)
AFUDC increases	*-$0.13/sh for full year*	($0.02)
Other items / O&M / ATC	*-$0.08/sh for full year*	($0.02)
Int Expense	*Debt issuance at WPL and IPL*	($0.01)
COVID	*Stay at home mid-March*	($0.03)
Tax timing	*Related mostly to PTCs – flat for the year*	$0.04
Dilution	*Incremental equity dilution*	($0.02)
2Q20 EPS		$0.51
Consensus		$0.40
2020 EPS		$2.44
2020 Consensus EPS		$2.40
2020 Guidance		2.34-2.48
2Q19 Sharecount		238
2Q20 Sharecount		250

Source: BofA Global Research, Quick, Bloomberg

Stock trading dynamics

Shares of LNT have traded up in recent weeks relative to the electric utility peer group, exceeding the relative trading levels of pre-Covid Q1. We note several constructive developments of late including the filing of the company's first tranche of its intended 1 GW solar projects in WI – the company's request for 675 MW continues to move through the permitting process in the state where we note appetite for renewables is strong with ample precedent for including utility-scale projects in rate base, as MGEE has done. Mgmt. has also recently affirmed that it is not seeking to expand its non-reg business aside from a small wind footprint and transport business. We see LNT as offering above-peer EPS growth in its regulated biz of 6-7%, among the more constructive Midwest utility stories among our coverage.

Exhibit 1: LNT shares relative to IXU on 2yr forward PE



Source: Bloomberg

Covid impact: Q2 trending in the right direction

We note the most recent Covid sales update from mgmt. indicates an uptick in C&I sales in the month of May. While weather-normalized Residential sales held steady at +4% for the Apr-May period (in-line with prior Apr reporting), C&I ticked up to -12% from -13% previously reported in April, indicative of a modest though encouraging uptick. We note this trend largely supports MISO data which shows electricity demand bottoming in Apr and then beginning a gradual and somewhat uneven recovery. We note that LNT's service territory highlights the different state-level approaches to handling the pandemic, with IA having never issued a statewide shelter-in-place order (leaving this to the county level) while WI initially issued a lockdown order which has since been lifted, following by gradual re-introduction of distancing measures. We received further comfort from mgmt. on our recent fireside chat where the company affirmed the recent uptick in sales – a notable positive given one of the more conservative sales guidance outlooks and further bolstering what we expect to be a reaffirmation of full-year guidance as we remain above the midpoint. Among the other positive developments of late, the WI commission lifted the moratorium on disconnections effective Jul 25, after IA had issued a similar order effective Jul 1. WI utilities are likewise able to resume charging late payment fees on accounts in arrears effective Jul 15, all factors that are trending toward gradual normalization – though the PSC had previously issued an order

for deferral of Covid-related costs included those associated with bad debts and the disconnect moratorium.

Table 4: LNT sales earnings sensitivity

	EPS sens to 1% move	Apr	Apr-May
All Classes		-9%	-8%
Residential	$0.02	4%	4%
Commercial	$0.01	-13%	-12%
Industrial	$0.01	-13%	-12%

Source: Company report

WI stabilization in Q3, Solar approval expected in 1H21

LNT's rate WI stabilization asks for the same ROE & Equity layer, and escrow treatment of pension & bad debt. With ~$500mn in rate base additions, 1/3 will be offset with lower fuel costs and the remainder related to taxes. The decision on the stabilization plan is expected to come down in Q3, with staff recommendations to the PSC the next meaningful milestone.

During Q2 announced plans for the initial 675MW tranche of its eventual 1 GW solar portfolio at a purchase consideration of $900m of which tax equity partner would sponsor 35-40% of the investment outlay with the rest being financed by LNT's Wisconsin subsidiary - $780m is included in the capex plan across the full 1 GW portfolio. The company indicated to purchase tax equity's ownership in the projects within 10 years of operation. We note that LNT already signed purchase and sale agreements with the developers, subject to pending approval from the regulators, however, none of the projects are currently under construction. The company anticipates 425MW to be placed in service by 2022 and 250MW in 2023 – see below. We note positive signs toward eventual approval given the state PSC's pro-renewables stance (recently appointed third commissioner comes from a renewable advocacy group) and overall constructive utility-regulator relationships across the state.

Table 5: LNT initial 675 MW solar projects

Name	Capacity (MW)	In Service
Crawfish River	75	2022
Onion River	150	2022
Richland County	50	2022
Wood County	150	2022
Grant County	200	2023
North Rock	50	2023

Source: Company report

Estimates

We had previously forecast Covid impact into our '20 estimates for LNT and remain 1 cent below the midpoint of the $2.34-2.48 guidance range at $2.40, tweaking our forecast incrementally to reflect updated ATC ROE following the FERC's MISO ruling. We note that positive weather trends in late Q2 and early Q3 bode well for a sales tailwind during the peak cooling season, with encouraging sales trends as previously highlighted by the mgmt. team further de-risking the near-term outlook. We remain near the upper end of mgmt.'s 5-7% EPS range looking out further ahead.

UPDATE TABLE

Table 6: LNT updated ests

EPS by Segment	2017A	2018A	2019A	2020E	2021E	2022E	2023E
IPL	$0.94	$1.13	$1.19	$1.35	$1.43	$1.50	$1.52
WPL	$0.80	$0.89	$0.97	$0.95	$1.04	$1.13	$1.21
ATC	$0.11	$0.13	$0.13	$0.14	$0.14	$0.15	$0.15
Parent/Other	$0.09	$0.02	$0.01	-$0.04	-$0.04	-$0.03	-$0.03
Total	$1.93	$2.17	$2.31	$2.40	$2.58	$2.75	$2.86
Prior Estimates	$1.93	$2.17	$2.31	$2.40	$2.57	$2.74	$2.85
EPS Guidance							
IPL +WPL		*2.04 - 2.07*	*2.21 - 2.23*				
ATC		*0.10 - 0.12*	*0.11 - 1.13*				
Parent/Other		*(0.01) - 0.00*	*(0.05) - (0.03)*				
Guidance	$1.89-$1.97	$2.13-$2.19	2.27-2.33	2.34-2.48			
Non-GAAP EPS Growth Off $2.26 in '19 (5-7%)				6.35%	6.82%	6.78%	6.04%
Consensus	$1.95	$2.16	$2.30	$2.40	$2.58	$2.71	$2.85
Consensus CAGR					6.86%		
Mid				$2.41	$2.56	$2.71	$2.87
High				$2.48	$2.65	$2.84	$3.04
Low				$2.34	$2.46	$2.58	$2.71
Model Embedded ROEs / Equity	2017A	2018A	2019E	2020E	2021E	2022E	2023E
IPL							
Regulatory ROE (Avg)	9.2%	9.8%	9.0%	9.0%	9.3%	9.5%	9.7%
GAAP ROE (AVG)	8.4%	8.9%	8.5%	9.4%	9.5%	9.4%	9.2%
WPL							
Regulatory ROE (Avg)	10.5%	10.1%	10.1%	9.7%	9.9%	9.9%	10.0%
GAAP ROE (AVG)	10.1%	10.3%	10.3%	9.8%	10.4%	11.0%	11.4%
ATC							
Earned ROE	10.5%	10.8%	10.5%	10.5%	10.5%	10.5%	10.5%

Source: BofA Global Research, Bloomberg

Valuation

We update the peer multiple to 17.1x for electric. We reiterate Buy with a $54.50/sh PO.

Table 7: LNT updated SOTP

2022E SotP Analysis - BofAe										
All figures in USD millions except per share										
Regulated Utilities	2022 Net Income	EPS	P/E Multiple					Equity Value		
			Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric			-	17.1x	-	-	-	-	-	-
Group EPS '18-'22 CAGR - Electric			-	5.00%	-	-	-	-	-	-
			-	-	-	-	-	-	-	-
Relative Utility Group P/E Multiple				18.0x						
IPL	$376	$1.50	19.0x	18.0x	2.0x	20.0x	21.0x	$7,135	$7,512	$7,888
WPL	$284	$1.13	20.0x	18.0x	3.0x	21.0x	22.0x	$5,669	$5,953	$6,237
ATC (LNT Share)	$37	$0.15	19.0x	18.0x	2.0x	20.0x	21.0x	$699	$736	$773
EPS (w/o Parent)	$697	$2.78						$13,504	$14,201	$14,898
Parent NI	-$7	-$0.03	18.0x	18.0x	1.0x	19.0x	20.0x	($132)	($140)	($147)
Add Back: Parent Interest Exp	$14	$0.05	18.0x	18.0x	1.0x	19.0x	20.0x	$245	$129	$272
Less: Parent Debt (Term Loan AEF)					*50% weighting*			($500)	($500)	($500)
								($388)	($511)	($375)
Total Implied			19.0x			19.8x	21.0x	$13,116	$13,690	$14,523
Shares Outstanding (2022E)								251	251	251
Total Equity Value Per Share								$52.00	$54.50	$58.00
Total Return Analysis										
Price Objective									$54.50	
Implied Return									7.60%	
Dividend Yield									2.80%	
Total Return									10.40%	

Source: BofA Global Research, Bloomberg

Ameren (AEE)

Among the positive drivers we see for Q2 is normalization of weather from 2019, partially offset by cooler weather as expressed by Heating Degree Days (HDDs), though this impact is tempered by fewer Cooling Degree Days (CDDs) both y/y and vs. normal. We estimate the positive impact from new rates in MO effective Apr 1 as 7 cents based on a pre-tax revenue net of fuel estimate of $83m, of which AEE is expected to realize ~80% during 2020 and which we assume is spread proportionally through the year. Normalization to account for a Callaway outage in 2019 would represent a further 8 cent uplift. We estimate 8 cents positive impact from O&M, which is roughly evenly split between Company Owned Life Insurance (COLI) benefit and additional non-fuel O&M savings included in the MO order (~5 cents each), offset partially by 2 cents of additional O&M inflation as per AEE's original guidance. On the negative side of the ledger we estimate 7 cents associated with COVID-19 impact relative to the company's expectation of 10 cents drag for the year given that MO began lifting its stay at home orders in early May. We also see 2 cents of interest expense as Ameren MO issued $465m at 2.95% in late Q1 and AEE issued $800m at 3.50% in early Q2, though only $435m of these issuances were allocated to refinancing with the remainder representing incremental interest expense. We also reflect proportional impact of an estimated 2 cent effect from higher bad debt expense, as well as a partial offset resulting from the Federal Energy Regulatory Commission (FERC) ROE ruling which effectively raised Ameren Transmission Company of Illinois's (ATXI) authorized ROE by 14 bps (~1 cent impact annualized). We estimate AEE EPS at $0.86/sh for Q2, slightly above $0.84/sh consensus estimates; we see upside risk to Street estimates as they are updated to fully reflect Q2 drivers, in particular the constructive MO rate ruling.

Q2 earnings walk

Table 8: AEE Q2 walk

Ameren 2Q20 Earnings Walk	Notes	EPS
2Q19 EPS		$0.72
Return to normal weather	Mild	$0.06
2Q20 weather impact	Cooler weather y/y	($0.04)
AEE Illinois		
IL Electric	2019 Average 30 YR UST was 2.75% vs. Current @ 1.431%	($0.02)
IL Gas		$0.01
IL Transmission/Dist./ATXI	Ratebase growth largely balanced by ROE change	$0.01
AEE Missouri		
New Rates	Effective 2Q20	$0.07
Callaway refueling		$0.08
PISA Benefit		$0.00
MEEIA Benefits	2020 impact weighted to 2H	$0.00
O&M, Other	Lower O&M over the year (a change for 2Q)	$0.08
Interest Refinancings	Two refis in Q2	($0.02)
Parent Company income tax exp		$0.00
Dilution	Dividend reinvestment plan and employees - $100Mn/yr	($0.00)
COVID-19	Reduced demand (2Q lift in May)	($0.07)
Other	Bad debt (2c for the year) & FERC (14bps adder)	($0.01)
2Q20E BofA Adjusted EPS		$0.86
2Q20E BofA Modeled EPS		$0.86
2Q20 Consensus		$0.84
BofA 2020E EPS		$3.45
2020 Consensus		$3.42
2Q19 Shares outstanding		247
2Q20 Shares outstanding		248

Source: BofA Global Research estimates, Bloomberg

Framing the latest debates and items to watch

We catch up on the latest moving parts across AEE's territory ahead of the Q2 call.

MO rate case a positive near term, appears underappreciated by investors

Among the key takeaways from the recent MO rate case settlement, in our view, are a reduction in revenues of -$32m, and a further reduction of fuel cost expenses (-$115m) and other costs by an additional -$50m. The net impact on an annualized basis is +$133m given AEE's ability to effectively manage these costs. With rates taking effect April 1st AEE should realize a partial year impact in 2020 - we calculate the annual impact of this result is $0.40/sh, or a 2020E impact of $0.30 (previously reflected in our estimates). Given the constructive nature of this rate case outcome, we think AEE is unlikely to seek to file another rate case in 2020. We believe the key considerations in terms of timing remain the impact of COVID-19-related shutdowns on lost sales and additional expenses as well as the placement of additional wind assets into service. The Street consensus estimates are anchored toward the low end of mgmt.'s guidance range following Q1 reporting and the outbreak of COVID-19 – though we believe a constructive rate case outcome could provide AEE with an O&M tailwind going into H2, with potential for an upside surprise to full-year results.

700 MW wind projects in service in late '20/early '21

AEE MO is adding 700 MW of wind generation to its fleet in two tranches: a 400 MW facility expected to be in service by year end 2020 and a second 300 MW facility which is largely expected to be in service in 2020 with approx. $100m of assets in Q1 2021. Prior to being added to AEE's rates as part of a rate case, the projects qualify for a partial return under the MO Plant in Service Accounting (PISA) framework and existing renewable rider. MO's PISA mechanism allows the wind assets that are placed into service to earn a partial return until a formal rate case: AEE plans to defer 85% of the depreciation on the newly installed project and earn a debt return on the non-equity portion of the assets placed in service, with the remaining 15% depreciation qualifying for cash recovery under the existing renewable rider. While the company would not receive full recovery until its wind projects are added to rates, we note the PISA mechanism allows for partial recovery – likewise the expected filing date for a new rate case in the first half of 2021 is not significantly later than prior indications from mgmt.

Next filing in MO – looking like '21

Given the announced in-service timing of the wind assets, the constructive rate order received earlier this year, COVID-19 uncertainty likely to persist through the balance of 2020, and ability to earn an interim return on newly-installed wind assets, we expect AEE to file its next case sometime in 1H21 at the earliest. We believe this is largely reflected in Street estimates as the company has continued to refrain from providing specifics as to its rate case filing strategy while highlighting the need to place its wind assets in service as well as account for COVID-19 uncertainty.

IL legislation – potentially post-Nov election

While the 2020 IL spring legislative session passed without action taken on the Downstate Clean Energy legislation, we note additional opportunities for action in the coming months. The state typically holds a veto session in October or November, with potential for this session to fall after state and national elections are held. The following opportunity if no action is taken during the veto session is a lame duck session held in January, prior to the seating of the new group of legislators. Our estimates reflect the current ROE base rate of 580 basis points with the potential of an additional 100 bps in the event of passed legislation representing upside risk.

30Y UST rate visibility is limited, we assume a more conservative stance

We tweak our forecast for the 30Y UST lower by 15-25 bps across 2021-25, with our updated forecast rates remaining below 2% until 2025 when they reach 2.20%. We perceive limited visibility of Street consensus estimates of long-term rates beyond 2021

and see little consensus among investors. Accordingly we adjust our forecast to reflect a "lower for longer" outlook, which we see as appropriate given the path of rates of late and Fed signaling long-term support for the economy in the wake of COVID-19.

IRP coming in Sep, will mgmt. deliver on further retirements?

AEE's next triannual MO IRP filing is due in Oct with the company expecting to file in Sep. Likely of particular interest among investors are prospects for the announcement of additional coal retirements other than Meramec, which is scheduled for retirement in 2022. The 2017 filing gave planned retirement dates for Sioux and Labadie as 2033 and 2036, respectively – though we see potential for one of these to be accelerated (note Sioux and Rush Island have the lowest levels of undepreciated rate base of AEE's fleet at $0.5B and $0.6B, respectively). AEE's decision on whether it accelerates retirements of unscrubbed coal is partially tied to the unresolved 8th Circuit Case (i.e. appealing the EPA Clean Air Act mandate) and partially tied to a lack of securitization legislation. Some coal experts have questioned whether the company would rush to accelerate the retirement of the fleet if the case were still pending. In the event that the company did pursue accelerated retirement in its IRP before case resolution, we could see Labadie as a more likely target since it faces just sulphur dioxide controls rather than Rush Island's bigger violation. On the other hand, if the 8th Circuit Case were resolved and AEE's plants were ordered to install scrubbers, this hundreds of million dollar requirements could make the plants uneconomic and more ripe for accelerated retirement. We believe additional potential hurdles could be in the form of lack of securitization legislation as well as sensitivity around potential job reductions, particularly in the wake of the COVID-19 outbreak.

EVRG process: clarity should drive re-rating in AEE

Our most recent accretion analysis as well as feedback from our conversations with stakeholders in both MO and Kansas (KS) suggest that while AEE has been linked to the Evergy (EVRG) strategic process in media reports, the company is likely not a front runner were it to secure a bid. In particular, we see potential for resistance from environmentally-aligned interveners in both KS and MO should AEE emerge as the winning bidder – given EVRG's coal-heavy fleet and AEE's own slow adoption of renewables and unscrubbed legacy generation, we think there could be less potential opposition to an EVRG bidder with a proven track record of accelerated coal retirements and renewable transition. Some investors appear to have largely focused on other names such as NextEra Energy (NEE) as potential bidders, and we could see a modest degree of drag in AEE shares associated with the possibility of its participation in a protracted bidding process. We attribute much of the recent pressure on AEE shares to these concerns – and clarity on EVRG strategic direction in 2H could potentially drive relative outperformance of AEE shares.

Evergy, Inc: AEE linked to strategic review in news; looking at dilution from possible AEE bid 17 June 2020

Updated estimates

We see a positive skew to Street consensus estimates for 2020, particularly driven by the positive MO rate order which went into effect on Apr 1. As COVID-related shutdowns and resulting load shifts continue to pressure utilities into Q3, we believe the O&M portion in particular of the MO order could provide a key near-term tailwind. We detail our tweaked assumptions below.

- **Raising MO ROE forecast in '20 to reflect O&M savings.** We raise our EPS estimate by 3 cents to $3.45 for 2020 driven by an earned ROE of 9.8% in MO (upper end of 9.4-9.8% authorized range). We remain confident in mgmt's ability to execute.

- **Assuming a more conservative 30Y UST forecast in IL.** We tweak our forecast for the 30Y UST, reducing our forecast for yields (and corresponding IL authorized ROE) by 20-25 bps across the 2021-25 timeframe – in line with our forecast for EXC's ComEd - such that our forecast yield remains below 2% until 2025.

- **Reflecting 10.02% base ROE for transmission.** We tweak the authorized ROE at the ATXI segment to reflect the latest FERC order, reflecting a base rate of 10.02% plus 50 bps adder through the forecast. This effectively increases our estimates by ~1 cent annually through the forecast period.

We make additional tweaks to our earned ROE forecast, assuming that MO remains near the high end of its authorized range through the forecast period. We believe our forecast embeds relatively conservative assumptions – in particular in IL where we apply a more punitive UST forecast and do not reflect potential upside from possible legislation resulting in a 100 bps adder to the base authorized electric ROE. With these assumptions in place our forecast has an EPS CAGR that declines to below the midpoint of the 6-8% guidance range through 2024, though we see upside risk to our estimates as detailed above.

Table 9: Updated estimates

Consolidated Projections	2019A	2020E	2021E	2022E	2023E	2024E	2025E	Segment CAGR ('20-'24E)	Segment CAGR ('19-'24E)
Ameren Missouri	$1.72	$1.86	$2.06	$2.18	$2.28	$2.38	$2.48	6.41%	6.68%
Ameren Illinois	$1.39	$1.34	$1.46	$1.63	$1.79	$1.99	$2.19	10.36%	7.43%
ATXI	$0.32	$0.32	$0.31	$0.30	$0.29	$0.29	$0.28	-2.92%	-2.43%
Other	-$0.09	-$0.07	-$0.07	-$0.07	-$0.07	-$0.07	-$0.06		
Total EPS	$3.35	$3.45	$3.76	$4.05	$4.30	$4.59	$4.88	7.01%	6.50%
Guidance		*$3.40-3.60*							8.70%
EPS CAGR off 2020 ($3.50)			7.47%	7.52%	7.11%	7.01%	6.87%		
YoY Growth	-0.53%	2.97%	9.02%	7.57%	6.30%	6.72%	6.31%		
Prior Estimates	*3.35*	*3.42*	*3.70*	*3.99*	*4.27*	*4.61*	*4.91*		
Consensus	$3.29	$3.42	$3.76	$4.05	$4.32	$4.47		6.31%	6.33%
Average Earned ROE (Auth in parenthesis)									
Missouri (Auth: electric 9.4-9.8%, gas 9.4-9.95%)	10.3%	9.8%	10.3%	9.8%	9.8%	9.8%	9.8%	9.8%	9.8%
Illinois (Auth: electric 580bps + 30yr T, gas 9.87%)	10.0%	8.8%	10.0%	8.8%	9.0%	9.2%	9.2%	9.3%	9.4%
BofA 30-yr Treasury assumption		*1.50%*		*1.50%*	*1.50%*	*1.60%*	*1.70%*	*1.95%*	*2.20%*
ATXI (10.02% plus 50bps adder)	10.82%	10.52%	10.82%	10.52%	10.52%	10.52%	10.52%	10.52%	10.52%
Consolidated FFO/Debt	20.9%	18.0%	18.4%	18.5%	18.6%	18.8%	19.2%		
Guidance (6-8% '20-'24 off of $3.50) --> *Midpoint*		$3.50	$3.75		$3.50	$3.75	$4.01	$4.29	$4.59
Low Implied		$3.50	$3.71	$3.93	$4.17	$4.42	$4.68		
High Implied		$3.50	$3.78	$4.08	$4.41	$4.76	$5.14		

Source: BofA Global Research estimates, Bloomberg

Valuation

We reiterate our Buy rating on AEE. We embed a more conservative set of assumptions around UST rates, and remain well within mgmt.'s guidance range while seeing potentially upside looking ahead. We believe shares of AEE could continue to outperform vs. the peer group driven by near-term catalysts including the expected IRP filing, IL legislation potential, and updated long term plan which the company historically provides with Q4 results. We raise our PO to $79 from $75 to reflect the updated Electric peer group multiple of 16.3x and our tweaked estimates. Reiterate Buy on solid +6-7% EPS growth through our forecast period as we believe AEE is one of the better-positioned names in our coverage universe.

Table 10: SOTP valuation

Ameren Sum of the Parts Valuation - 2022E									
All figures in $Mn except per share									
Regulated Utilities	2022E EPS	P/E Multiple					Equity Value		
		Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric		-	16.3x	-	-	-	-	-	-
Group EPS '18-'22E CAGR - Electric		-	5.00%	-	-	-	-	-	-
		-	-	-	-	-	-	-	-
		-	17.1x	-	-	-	-	-	-
Ameren Missouri	$2.18	18.1x		2.0x	19.1x	20.1x	$39.57	$41.75	$43.93
Ameren Illinois	$1.63	19.1x		3.0x	20.1x	21.1x	$31.10	$32.73	$34.36
Ameren Transmission (ATXI)	$0.30	16.1x		0.0x	17.1x	18.1x	$4.87	$5.17	$5.47
Parent/Unallocated Items	-$0.07	16.1x		0.0x	17.1x	18.1x	-$1.08	-$1.15	-$1.22
Total Implied Utilities	$4.05						$74.45	$78.50	$82.55
Shares outstanding	263								
Implied P/E		19.5x							
Valuation								$79.00	
BofAe Implied Multiple								19.5x	
PO								$79.00	
Upside/downside potential								7.7%	
NTM Dividend Yield								2.70%	
Total potential return								10.6%	

Source: BofA Global Research estimates, Bloomberg

American Electric Power (AEP)

We forecast a strong 2Q20 with EPS of $1.07 vs. $1.00 in 2Q19 and $1.02 consensus, driven primarily by previously announced 2020 O&M savings in addition to $100mn COVID-related cost savings (most of these, however, will likely be temporary in nature). Weather should also likely provide some uplift. A Transmission HoldCo true-up in 2Q should be effectively offset at the VIUs and T&D utilities (by rate changes, etc.). North Central should be on schedule with the latest PUCT decision; despite the TX rejection, AEP will reallocate MW to SWEPCO's LA and AR customers and will proceed with the full 1485 MW project. We highlight concerns of over-equitizing North Central, given guidance for 50-66% equity; we now assume he high end of this range. However, the possibility of Kentucky asset sales for further equity could provide upside; we accordingly adjust for a 2x premium in our SOTP to the Kentucky Power breakout. The one-year PTC extension should act as a safeguard if there are any delays for the final two wind farms, although no delays currently expected vs. the current YE-21 timeline). We watch progress on rate cases including Kentucky Power (filed June 29th, with procedural schedule starting in early Nov, 6-month timeline, new rates could go into effect YE-21), AEP Ohio (base rate case filed June 1st, expected one-year procedural schedule), and APCo Virginia (filed March 31st, still in initial stages, with intervenor testimony on July 30th). It would seem strategic action on utilities is still dependent on the outcome of its pending rate cases. While more equity from North-Central to be disclosed formally in its cash flow outlook could be cautious, much better clarity on where it stands on its 5-7% EPS CAGR could be the bigger (offsetting) positive. Maintain Neutral.

2Q20 Earnings Walk

We estimate EPS of $1.07 for 2Q20. This compares to $1.00 in 2Q19 and consensus of $1.02.

- **Drivers:** Aside from weather, we anticipate a strong 2Q will be driven by 2020 planned O&M savings in addition to $100mn COVID-related cost savings (the majority of which will likely be non-recurring). Expect a Transmission HoldCo true-up in 2Q to be effectively offset by rate changes at OH, TX, and by the VIUs (transmission revenues).
- **Other:** A number of 2020 full-year items are weighted heavier towards 2Q. This includes COVID-related wholesale load impact (mostly in 2-3Q), 2020 O&M savings (mostly after 1Q), Texas carrying charges (a 2Q item, reversal of 2Q19), and a Transmission HoldCo true-up (a 2Q item).
- **Wildcard:** Weather should likely prove a positive with a reversion to more normalized weather from weak 2Q19 weather, in addition to more favorable weather in 2Q20.

Table 11: AEP 2Q20 Earnings Walk: nice sized beat

American Electric Power 2Q20 Earnings Walk	EPS
2Q19 adjusted earnings	$1.00
Vertically Integrated Utilities	$0.11
Wholesale/Normal Load	($0.05)
Rate Changes	$0.03
Weather	
Return to Normal	$0.01
Current Quarter	$0.02
Transmission revenues	$0.06
O&M	$0.09
Depreciation and Other	($0.04)
Int/AFUDC	$0.00
Other	($0.01)
Trans./Dist. Utilities	$0.01
Rate Changes (AEP Ohio, TX DCRF)	$0.03
OH Legacy Riders	($0.01)
OH Reg Prov	$0.00
Weather	
Weather (Texas) Normalization	$0.00

Table 11: AEP 2Q20 Earnings Walk: nice sized beat

American Electric Power 2Q20 Earnings Walk	EPS
Weather (Texas) Impact	$0.00
AEP TX transmission revenues (T-cost filings pre-ratecase)	$0.00
O&M	$0.06
TX Carrying Chgs	($0.03)
Depreciation and Other	($0.02)
Other Taxes	($0.02)
Other/AFUDC	($0.00)
Transmission Holdco	($0.05)
Investment growth (ahead of schedule)	$0.04
O&M	$0.00
True-Up	($0.09)
Other	$0.01
Generation and Marketing	$0.01
Corporate/Other	($0.01)
Dilution	($0.00)
2Q20E Adjusted EPS	$1.07
2Q20 BAML EPS	$0.98
2Q20 Consensus	$1.02
2020 BAML EPS	$4.23
2020 Consensus	$4.28
2020 Guidance	4.25-4.45

Source: BofA Global Research Estimates

North Central: Moving forward despite TX rejection

AEP has received its final regulatory decision for its multi-state 1485 MW North Central wind project and can now move ahead with its construction plans. The Public Utility Commission of Texas (PUCT) rejected SWEPCO's request to acquire a 54.5% stake in Invenergy's three wind North Central Energy Facilities. AEP's subsidiary PSO (Public Service Company of Oklahoma) will be acquiring the remaining 45.5% equity interest in the wind farms. AEP reaffirmed its plans to develop close to 1,500 MW of wind capacity in OK despite the TX rejection. SWEPCO and PSO already have received approval from AR, LA, and OK regulators, as well as from FERC. The wind farms to be owned by AEP include Traverse Wind (999 MW), Maverick Wind (288 MW), and Sundance Wind (199 MW); all three are expected to complete construction within the next two years. With the TX rejection, capacity will be allocated with 464 MW to SWEPCO's Louisiana customers, 268 MW to SWEPCO's Arkansas customers, 78 MW to SWEPCO's wholesale customers, and 675 MW to PSO's customers. On balance, this is not a meaningful setback and was somewhat anticipated given the prior pushback from the PUCT.

Concerns of over-equitizing North Central Wind

We highlight recent concerns of AEP potentially over-equitizing the North Central Wind project, following prior mgmt commentary of expectations for 50-66% equity financing. While we had previously assumed 50% equity, we now assume 66% equity/34% debt for a more conservative approach. Timing of equity needs should align with wind farms going into service; the bulk of the needs will be in 2021 (~$1.7bn capex of the $2bn total). Note that we also update our projections to reflect a shift in MW allocation to SWEPCO – AR and SPEPCO – LA, following the PUCT rejection in Texas.

For 2Q, we expect to see updated guidance on equity and capex for North Central, following a 1Q decision to defer $500mn of capex out of 2020; this update (deferral year) should be made with 2Q results. We continue to assume $2bn capex for the project, with 66% equity financing (previously 50%). Expect AEP's next published capex forecast to include North Central Wind.

We see upside, however, from the possibility of Kentucky asset sales for further equity. We thus now include a 2x premium to the Kentucky Power breakout at the VIUs in our SOTP valuation (KY Power contributes $3.40/sh to valuation).

Estimating North Central's EPS Contribution

Below we include our latest earnings impact from the North Central Wind project. We assume the company earns a regulated return based on each subsidiary's equity ratio and ROE, indicating a $13mn Net Income impact in '21 (since just 200MW would be slated to come online by year-end) and $95mn in '22. Our equity need calculation now assumes 66% equity financing for the project, and we'd expect $0.17/sh of EPS impact when the full project is online (i.e. starting in '22).

The first wind farm to be constructed in '20 will receive the 100% PTC, while the other two wind farms to be constructed by YE-21 will receive the 80% PTC. The one-year PTC extension should act as a safeguard if there are any delays at the second two wind farms.

Exhibit 2: North Central EPS Impact

North Central EPS impact	2021	2022	2023	2024	2025
Wind Additions MW	199	1485	1485	1485	1485
PSO	*90*	*675*	*675*	*675*	*675*
SWEPCO - AR	*36*	*268*	*268*	*268*	*268*
SWEPCO - LA	*62*	*464*	*464*	*464*	*464*
SWEPCO - TX	*0*	*0*	*0*	*0*	*0*
SWEPCO - FERC	*10*	*78*	*78*	*78*	*78*
Assumed Capex $M	268	1997	1997	1997	1997
Ownership Interest	100%	100%	100%	100%	100%
Equity Ratio	50%	50%	50%	50%	50%
PSO	*49%*	*49%*	*49%*	*49%*	*49%*
SWEPCO - AR	*48%*	*48%*	*48%*	*48%*	*48%*
SWEPCO - LA	*52%*	*52%*	*52%*	*52%*	*52%*
SWEPCO - TX	*43%*	*43%*	*43%*	*43%*	*43%*
SWEPCO - FERC	*50%*	*50%*	*50%*	*50%*	*50%*
ROE	9.6%	9.6%	9.6%	9.6%	9.6%
PSO	*9.4%*	*9.4%*	*9.4%*	*9.4%*	*9.4%*
SWEPCO - AR	*9.5%*	*9.5%*	*9.5%*	*9.5%*	*9.5%*
SWEPCO - LA	*10.0%*	*10.0%*	*10.0%*	*10.0%*	*10.0%*
SWEPCO - TX	*9.4%*	*9.4%*	*9.4%*	*9.4%*	*9.4%*
SWEPCO - FERC	*10.0%*	*10.0%*	*10.0%*	*10.0%*	*10.0%*
NI $M	13	95	95	95	95
Shares outstanding	499	520	531	534	538
Total Equity Needed ($M)	177	1318	1318	1318	1318
Issuance Price (current price)	87.5	87.5	87.5	87.5	87.5
Incremental Shares outstanding (mn)	2.0	15.1	15.1	15.1	15.1
Dilution %	0.4%	2.9%	2.8%	2.8%	2.8%
New Shares outstanding	501	535	546	550	553
EPS	0.03	0.18	0.17	0.17	0.17

Source: BofA Global Research estimates

Rate cases: Kentucky Power, APCo Virginia, AEP Ohio

Kentucky Power filed a rate case on June 29th requesting a ~$70mn rate increase at a 10.0% ROE (43.25% equity ratio). AEP expects to receive a response in June, with a procedural schedule starting in early November and new rates likely going into effect by YE-21. The timing could line up with the $1.7bn investment needs for North Central.

APCo Virginia filed a rate case on March 31st, requesting ~$65mn rate increase at a 9.90% ROE (50.31% equity ratio). This filing is still in the initial stages of the procedural schedule, and is expected to kick off with intervenor testimony on July 30th.

AEP Ohio filed a base rate case on June 1st, requesting a ~$400mn rate increase at a 10.15% ROE (54.43% equity ratio). Expect the OH procedural schedule to be roughly a year in length (in line with historical trends).

Signs PPA for 400 MW IL wind project

AEP Energy recently signed a PPA with CIP (Copenhagen Infrastructure Partners) for production of the 400 MW Panther Grove Wind Energy Facility in IL. Construction of the wind farm will start in early 2021, with COD (commercial operation date) expected in late 2022. The PPA will be secured to serve C&I customers, such as Google, looking to source clean energy for retail supply.

ApCo issued RFPs to procure 50MW solar

AEP subsidiary Appalachian Power Co. recently issued RFPs for 50MW solar capacity in West Virginia with projects having a minimum bid capacity of 10MW and in-service date of 15 December 2022, besides the projects should be located in West Virginia and interconnected to Appalachian Power's West Virginia distribution system or to the PJM Interconnection market to qualify for the federal investment tax credit. The deadline for bid submission is Aug 6 2020. This was not unexpected. We also look for parallel efforts in WV by Mon Power/FE on its future generation resource needs as well.

EPS Estimates

We provide our latest EPS estimates for AEP below.

Exhibit 3: AEP EPS Estimates

EPS	2017A	2018A	2019E	2020E	2021E	2022E	2023E
APCo	$0.67	$0.73	$0.78	$0.79	$0.82	$0.83	$0.87
I&M	$0.38	$0.53	$0.51	$0.52	$0.55	$0.54	$0.55
SWEPCO	$0.25	$0.30	$0.37	$0.36	$0.38	$0.40	$0.43
PSO	$0.15	$0.17	$0.25	$0.24	$0.27	$0.30	$0.32
Other Utes (incl. KY)	$0.17	$0.27	$0.24	$0.24	$0.24	$0.24	$0.25
KY break out	$0.13	$0.14	$0.15	$0.16	$0.17	$0.17	$0.17
North Central Wind					$0.03	$0.18	$0.17
Vertically Integrated	$1.64	$2.00	$2.17	$1.91	$2.28	$2.32	$2.42
Guidance		$2.00	$2.17	$2.19			
Ohio	$0.66	$0.66	$0.67	$0.58	$0.63	$0.64	$0.67
Texas	$0.39	$0.41	$0.41	$0.43	$0.52	$0.59	$0.63
T&D	$1.01	$1.05	$1.00	$1.01	$1.15	$1.23	$1.30
Guidance		$1.05	$1.00	$1.03			
Transmission HoldCo	$0.72	$0.75	$1.05	$1.10	$1.17	$1.26	$1.34
Guidance		$0.75	$1.05	$1.08			
AEP Energy Supply	$0.30	$0.29	$0.30	$0.32	$0.21	$0.23	$0.24
Guidance		$0.29	$0.30	$0.35			
Corp & Eliminations	$0.01	($0.14)	($0.28)	($0.33)	($0.30)	($0.28)	($0.21)
Guidance		($0.14)	($0.28)	($0.30)			
Consolidated EPS without North Central	$3.68	$3.95	$4.24	$4.25	$4.51	$4.76	$5.09
CONSOLIDATED EPS with NORTH CENTRAL WIND	$3.68	$3.95	$4.24	$4.25	$4.53	$4.94	$5.26
EPS Growth (%)		*7.5%*	*7.3%*	*0.1%*	*6.8%*	*9.0%*	*6.5%*
Previous EPS (without North Central)	*$3.68*	*$3.95*	*$4.24*	*$4.25*	*$4.52*	*$4.83*	*$5.16*
Consensus		$3.93	$4.22	$4.28	$4.63	$4.99	$5.32
BAMLe CAGR without North Central (vs '18 mid)			10.2%	5.0%	5.4%	5.5%	5.7%
BAMLe CAGR with North Central (vs '18 mid)			10.2%	5.0%	5.6%	6.4%	6.5%
Annual Guidance	3.55-3.68	3.88-3.98	4.14-4.24	4.25-4.45			
Guidance: 5-7% EPS CAGR off of '18 (or '19 orig midpt)		$3.85	$4.19	$4.35	$4.59	$4.86	$5.15
Low			$4.14	$4.25	$4.46	$4.68	$4.91
High			$4.24	$4.45	$4.72	$5.05	$5.40
Share Count	492	493	494	496	499	520	531

Source: BofA Global Research Estimates

Valuation: Maintain Neutral, raise PO to $88

We maintain our Neutral rating and raise our Price Objective to $88 from $80. We update for the regulated peer ute multiple of 17.1x (previously 15.3x), which is the main driver of the PO change. We additionally now include a 2x premium for the Kentucky Power break out valuation. We tweak our estimates for North Central and also now reflect the associated equity issuance for the project (BofA ests at 66% equity financing up from prior 50%) for '21 and '22 (majority in '22, tied to construction needs). This implies <$1/sh accretion from the North-Central asset build now.

Exhibit 4: AEP SOTP Valuation

AEP SoTP	2022 EPS				P/E Multiple	Premium/ Discount	Value ($mn)	Value ($/Sh)
Group Peer Multiple - Electric					17.1x			
Group EPS '18-'22 CAGR - Electric					5.00%			
Vertically Integrated Utilities (SWEPCO, PSO, APCo) excl KY	$2.15				18.0x	0.0x	$20,073	$38.6
Kentucky Power break out	$0.17				18.0x	2.0x	$1,746	$3.4
T&D Utilities (Principally D) - TNC/TCC, Ohio Power	$1.23				18.0x	1.0x	$12,159	$23.4
Transmission-Only Utilities - Mostly FERC	$1.26				18.0x	1.0x	$12,374	$23.8
Parent & Other - Principally HoldCo Debt	($0.28)				18.0x	0.0x	($2,606)	($5.0)
Total Regulated & HoldCo Value	$4.53						$43,745	$84.2
Renewables								
Legacy Energy Supply + Marketing/ Increasingly Renewables	$0.23				18.0x	-3.0x	$1,789	$3.4
Total AEP Equity Value - Existing Assets								$87.6
Upside	2022E EPS (or discounted)	Capex	FFO	Earnings Impact (50% Equity)	P/E Multiple	Premium	Probability Weighted	
SWEPCO 1200MW RFP - in service '21 (mostly 80% PTC)	0.09	1,089	$75		18.0x	0.0x	100%	$1.7
PSO 1000MW RFP - in service '21 (mostly 80% PTC)	0.07	908	$55		18.0x	0.0x	100%	$1.3
Total	0.16	1,997						3.0
Probability-Weighted EPS	0.17							
Discount Factor by year	10%							
Total Capex (probability weighted)				1,997				
Total Equity Needed ($M) (assuming 50%)				1,318				
Issuance Price (current price)				87.51				
Shares Issued (mn)				15				
Dilution %				3%				
Value Dilution				($1,268)			($1,268)	($2.4)
Shares Outstanding								520
Total Equity Value Per Share								$88.0
							Price Appreciation	0.6%
							+2020 Dividend Yield	3.1%
							Total Return	3.7%

Source: BofA Global Research Estimates

American Water Works (AWK)

Amid the evolving COVID pandemic, we expect continued execution by AWK with their inaugural ten year capital forecast of $20-22Bn intact. We have less concerns on the margin around bad debt given ten of their fourteen states have already adopted accounting orders or other recovery mechanisms. We don't perceive any meaningful delays in spend or regulatory filings (albeit note the timing shift for new rates to take effect for NYAW) and remain confident in the management team following recent succession. Further acceleration in muni consolidation remains a critical tailwind out of recovery without any meaningful infrastructure bill materializing. While we appreciate the scarcity element and higher sustained investment trajectory for the subsector, we ultimately see the steep premium as unwarranted. We maintain our Underperform rating.

AWK 2Q20 Earnings Walk

We forecast 2Q20 adjusted EPS of $0.97, slightly above consensus and a $0.03 uptick y/y.

- **Key Drivers:** The primary positive drivers y/y are new rates implemented across a number of states in their footprint as well as various infrastructure surcharges. Weather tailwinds y/y and cost savings should help offset any COVID impacts and the reversal of gain on sale in the prior period, while MBB will have contribution from the new military bases.

Table 12: AWK 2Q20 Walk

AWK 2Q20 Earnings Walk		EPS
AWK 2Q19 EPS	$	0.94
Regulated		0.06
Infra Charges, Rate Cases & Step Increases		0.08
Depreciation		-0.02
COVID Challenges offset by Weather & O&M		0.00
MBB		0.02
Parent		-0.05
Interest/Other Impact		-0.02
Legacy Gain Last Year		-0.03
2Q20 BofAe Adjusted EPS	$	0.97
Consensus		$0.96
BofAe 2020 EPS	$	3.85
Guidance		3.79-3.89
2020 Consensus		$3.84

Source: BofA Global Research, Bloomberg

Reg., Leg., Muni & Military Prospects

We see AWK as particularly poised to execute on their LT plan despite the ongoing COVID pandemic. Earlier this year, the company announced a 10% dividend increase, in line with their targeted payout ratio of 50-60% and their targeted high end of the 7-10% outlined range. Along with continued regulatory filings – the company recently announced that Pennsylvania American Water filed a rate case request with the Pennsylvania Public Utility Commission for rates over a two-year period – we see the developments as affirmation by the company around their ability to manage through the crisis with its plan largely intact. With a largely resi customer base, bad debts have been our principal concern on the margin for water utilities. That said, we note accounting orders or mechanisms from the commission around recovery already in ten of the 14 states in which they operate, with discussions ongoing in all of their jurisdictions.

Following military business wins at San Antonio and West Point, both are now fully operational with contribution starting in 2Q and no delays despite the ongoing pandemic. Five other military bases remain potential candidates, with two to three expected to be awarded sometime during 3Q. Outside of the military business, we

expect some drag on new partnerships for Homeowners services – the other component of AWK's non-regulated business.

Meanwhile, municipal opportunities continue to arise despite the crisis, and we perceive particular acceleration of opportunities given the latest financial strain on munis from the pandemic shock – particularly if no infra bill or lifeline materializes.

We reiterate our Underperform rating on AWK shares given the steep premium vs. electric & gas peers.

EPS Estimates

The exhibit below reflects our latest EPS estimates with annuals remaining unchanged into upcoming results. We continue to expect sustained long term growth within their 7-10% LT EPS CAGR and 7% rate base growth longer term.

Table 13: EPS Estimates

AWK	2019A	2020E	2021E	2022E	2023E
Earnings Metrics					
Regulated Water EPS	3.60	3.84	4.19	4.43	4.66
Market Based EPS	0.45	0.47	0.51	0.53	0.57
Parent and Other EPS	-0.44	-0.46	-0.43	-0.40	-0.36
Adjusted EPS	3.61	3.85	4.27	4.56	4.87
Consensus	3.61	3.84	4.21	4.54	4.95
Guidance	3.56-3.64	3.79-3.89			
Previous BofA Adj. EPS	3.61	3.85	4.27	4.56	4.87

Source: BofA Global Research, Bloomberg

Valuation

The exhibit below reflects our latest valuation: We mark to market our valuation for the latest water utility multiple of 26.9x (vs. 26.3x), with our PO shifting to $135 (vs. $133). We maintain our Underperform rating given the large premium vs. electric & gas peers, which we see as unjustified given its only modest relative growth premium.

Table 14: SOTP

Water Utilities	2022 EPS	P/E Multiple					Equity Value		
		Peer	Prem/ Discount	Low	Base	High	Low	Base	High
AWK Earnings		26.9x							
Group EPS '18-'22 CAGR		8.30%							
Water Utilities		29.1x							
NJ	$1.12		3.0x	31.1x	32.1x	33.1x	$34.86	$35.98	$37.10
PA	$1.27		3.0x	31.1x	32.1x	33.1x	$39.64	$40.91	$42.18
IL	$0.35		3.0x	31.1x	32.1x	33.1x	$10.80	$11.14	$11.49
MO	$0.50		2.0x	30.1x	31.1x	32.1x	$14.96	$15.46	$15.96
IN	$0.29		1.0x	29.1x	30.1x	31.1x	$8.46	$8.75	$9.04
CA	$0.19		-1.0x	27.1x	28.1x	29.1x	$5.16	$5.35	$5.54
Other	$0.71		0.0x	28.1x	29.1x	30.1x	$19.96	$20.67	$21.38
Regulated Water EPS	$4.43						$133.83	$138.25	$142.68
Parent/Other Drag	-$0.40		0.0x	28.1x	29.1x	30.1x	-$11.29	-$11.69	-$12.10
Market Based Business									
Military (40%)	$0.21	26.9x	-3.0x	22.9x	23.9x	24.9x	$4.87	$5.08	$5.29
Non Military (60%)	$0.32			11.0x	12.0x	13.0x	$3.51	$3.83	$4.15
Total Market Based Business	$0.53						$8.38	$8.91	$9.44
Valuation	$4.56						$131.00	$135.00	$140.00
Current Price as of 07/17/20								*$138.32*	
Dividend Yield								1.4%	
Total Return							-3.86%	-0.97%	2.65%

Source: BofA Global Research, Bloomberg

CMS Energy (CMS)

Into 2Q, we perceive the critical update for CMS to be around FY20 guidance both around the extent of ongoing pandemic load impacts as well as the ability to drive cost savings. With a stronger-than-expected 2Q with favorable weather offsetting 1Q headwinds and the ability to materialize cost savings, we expect heightened confidence around FY20 EPS from mgmt and expect CMS to more firmly reaffirm its FY20 guidance range of $2.64-$2.68 (though likely contingent upon no escalation in shutdowns from a potential pandemic resurgence). In particular, we see a comfortable cushion for CMS to meet the mid-point of its guidance range relative to consensus expectations for the low-end of the range as we raise our forecast to the mid-point of the range. We expect CMS to provide an update around run-rate load impacts in June. Further with mgmt confidence emphasizing ability to drive cost savings beyond historically demonstrated 15c offset, we expect CMS to provide greater details around the extent of cost savings. With cost savings sustained, we express CMS as better positioned around a potential increase in corp tax rates under a Dem win in Nov '20 elections, with mgmt confidence around offsets to maintain customer affordability and headroom to support capex. Indeed, we expect improved confidence into the 2Q call to further support CMS shares in light of the latest re-rating across the group to defensive premium utilities focusing on reliable earnings. Maintain Buy.

2Q20 EPS Walk: Favorable weather, softer COVID impact

We forecast 2Q20 adjusted EPS of $0.45 vs. $0.33 in 1Q19 and $0.36 consensus.

- **COVID load impact, eased from peak:** Among most meaningful negative y/y drivers are load impacts from COVID-19 shifts with shelter-in-place orders implemented in Michigan, particularly around C&I load noting 3-4c negative impact monthly based on electric load impact through April. Load impact has since halved into May and again into June with businesses mostly reopen (though many such as restaurants and bars are at 50% capacity). As such, we estimate ~7c drag from COVID load impacts for 2Q20 as a key negative y/y driver. *Expect an update around run-rate impact based on Jun/Jul trends on the 3Q call.*

- **Very 2Q favorable weather, offsetting 1Q weather headwind:** We highlight substantially favorable weather trends (9% higher CDDs relative vs. normal), which we estimate at an 8c uplift y/y (in-line with 2Q18) with higher HDDs earlier in the quarter as well driving another 1c uplift y/y (shoulder month). Further, we highlight additional positive driver of normalization of 6c/sh favorable weather in 2Q19.

- **Key drivers:** Among additional drivers include ~6c contribution from new gas rates effective Oct '19, offset by ~6c negative impact from D&A and interest (closing of larger projects drive up depreciation costs). With mgmt having emphasized its ability to drive 15c O&M flex spend to offset COVID load impacts (not a cap but rather historically demonstrated), we estimate ~5c per quarter positive impact. We estimate 2c negative impact at Enterprises/DIG given 6c delivered in 1Q20 already relative to 8-9c embedded within FY20 guidance, with mgmt noting management of the business such as timing of plant outages.

Table 15: CMS 2Q Walk

CMS Energy 2Q20 Earnings Walk		EPS
Adjusted EPS 2Q19	$	0.33
Utility		
Weather/Load		
Return to normal		$0.06
Current quarter		$0.09
COVID Load Impact		($0.07)
Rate Changes		
New gas rates effective Oct 2019		$0.06
Other		
D&A, Interest, Other expenses		($0.06)
O&M Flex Spend		$0.05
Cost savings		$0.01
Pension benefit normalization		$0.01
Parent interest		($0.01)
Enerbank Variance		$0.00
Enterprise		
New DIG contracts 2H19		($0.02)
Dilution	$	(0.00)
2Q20 Adjusted EPS	$	0.45
2Q20 Consensus		0.36
2020 BAML EPS		$2.64
2020 Consensus		$2.64
2020 Guidance		*2.64-2.68*
Shares Outstanding 2Q19		284
Shares Outstanding 2Q20		285

Source: BofA Global Research estimates, company report

FY20 guidance confidence with solid 2Q, cost execution

With highly favorable weather in 2Q offsetting 1Q unfavorable weather headwinds (~18c hit), as well as eased COVID load impacts (on a run-rate basis into June), we perceive greater mgmt confidence around FY20 guidance range. *We expect CMS to more firmly reaffirm its FY20 guidance range, though contingent upon no escalation in shutdowns driven by a potential pandemic resurgence in the state*.

In particular with our 2Q20 EPS estimate, we see 1H20 EPS of $1.21 with $1.45 remaining for 2H20 to reach the mid-point of the FY20 guidance range. Accordingly, relative to 2H19 EPS of $1.41, assuming additional COVID load impact of 6c remaining (1c per quarter based on estimated run-rate in June), against remaining 10c O&M cost savings as an offset, ~32c new gas rates offset by ~8c non-recurring benefit opportunities (mainly around favorable 2H19 sales mix) and ~12c D&A, interest, and other expense (~6c quarterly drag), we see ~10c cushion to offset any negative weather or further COVID impacts and *still* reach the mid-point of the FY20 guidance range.

Accordingly, we raise our FY20 EPS estimate to the mid-point of guidance at $2.66 ($2.64 at the low-end prior). With improved FY20, we expect CMS to maintain *its long term EPS CAGR of 6-8%*, we slightly raise forward EPS estimates as well given that CMS typically rebases EPS based on year-end results. We expect the improved confidence in ability to maintain earnings through best-in-class execution to manage earnings, further reaffirming CMS as among the most reliable utilities from an earnings trajectory perspective to investors, even without full revenue decoupling, further supporting the latest re-rating across the group to defensive premium utilities in favor of CMS.

Table 16: CMS EPS Estimates: 7.0% CAGR through '24, back to mid-point for FY20 with improved confidence around costs against easing pandemic impacts

EPS	2017A	2018E	2019E	2020E	2021E	2022E	2023E	2024E	CAGR ('19-'24)
Electric	1.62	1.89	1.79	1.94	2.02	2.12	2.22	2.33	5.4%
Gas	0.62	0.60	0.82	0.91	0.99	1.09	1.20	1.31	9.8%
Utility	2.24	2.48	2.61	2.85	3.01	3.22	3.42	3.64	6.9%
Guidance				*2.84-2.88*					
IPPs	0.08	0.10	0.12	0.10	0.12	0.12	0.12	0.12	0.4%
Guidance				*0.08-0.10*					
Enerbank	0.11	0.13	0.15	0.18	0.20	0.21	0.22	0.23	9.6%
Guidance				*0.18-0.20*					
Parent	(0.28)	(0.38)	(0.38)	(0.47)	(0.48)	(0.48)	(0.48)	(0.49)	5.4%
Guidance				*(0.46)-(0.50)*					
Consolidated	2.17	2.33	2.49	2.66	2.86	3.07	3.28	3.50	7.0%
Guidance		2.30-2.34	2.47-2.51	2.64-2.68					
Consensus			2.50	2.64	2.85	3.07	3.28		

Source: BofA Global Research estimates, company report

Extent of cost savings, key 2Q call update to be provided

With the 2Q update, among most notable of updates, we expect mgmt to emphasize its cost savings strategy and provide greater details around the extent of cost savings it has been able to realize and expectations on a forward basis. Notably, mgmt has expressed that while it has highlighted historic ability to flex cost levers up to 15c of EPS offset, mgmt has been vocal in emphasizing that this *does not represent a cap on potential cost levers*.

In terms of cost levers, *mgmt emphasized sustainable cost reduction and management systems* rather than one-time cost cuts, with lower costs rolling into '21. In particular, mgmt emphasized leverage of its *lean operating system* implemented 4 years ago, focusing on waste elimination (both through process improvements and digital technology-enabled improvements) on an ongoing basis. Additionally, mgmt emphasized outperformance already on supply chain optimization, which has been underway for 12-18 months *already*. Additionally, mgmt highlighted O&M cost reductions including work at power plant units in economic reserve to lower costs and improve reliability into the summer peak, as well as shifting O&M employees to pre-approved capital work as well. Mgmt noted remote work by employees is expected to continue to an extent post-COVID as well. *We view confidence from mgmt around extent of cost savings against improving load trends as a positive data-point, and expect a detailed update with 2Q.*

Sustaining cost savings support rate headroom, critical with election dynamic

With sustained cost savings, mgmt emphasized initiatives continuing to provide long-term rate headroom into '21-'22 given carryover benefits, with incremental customer bill headroom for capital investments continuing to make for smooth regulatory approvals, with MPSC generally supportive of capex spend proposed in proceedings.

We emphasize ability to drive customer bill headroom as particularly important against the backdrop of Nov 2020 presidential elections. With Biden tax plan proposing an increase in the corporate tax rate to 28% (from 21%), we note that in contrast to 2017 tax reform, this would have a reverse impact to customer bill headroom. In particular the change in tax rate would drive ~$60mn impact to customer rates on raised rates, with the benefit of deferred income taxes (DFITs) halved as well (relative to prior 35%) reducing to $20mn annually (from $40mn prior with 21% tax rate). Recall, CMS currently already has a DFITs pass-through to customer approved for gas (and near-term for electric), with 21% tax rate driving a $1.6Bn reevaluation of DFITs passed back over a 40-year period (~$40mn a year), with a 28% lowering the reevaluation to ~$800mn over 40 years (reduced to ~$20mn customer benefit annually). Accordingly, CMS would need to support $80mn in savings to neutralize the impact for customers on a bill basis, critical to supporting capital spend on a forward basis.

Beyond cost savings, CMS emphasizes further customer bill headroom support and comfort to offset impacts from potential increase in the corporate tax rate, with ~$90mn reduction from roll-off of Palisades PPA and ~$$30mn O&M savings from retirements of Karn 1 and 2, among other opportunities. We view mgmt's best-in-class forward-planning around cost savings and confidence in maintaining customer affordability even with tax rate headwinds as further supportive of CMS' smooth and longer-dated capex outlook relative to peers.

MPSC ratecases on track, supportive of proposed spend

With prolonged ratecase schedules driven by pandemic delays across the utility group and subsequent ROE risks, CMS notes that all MPSC meetings have continued virtually and ongoing ratecase proceedings remain on schedule, *continuing to expect a final order in its pending Gas case in late October and a final order in its pending Electric case in Dec,* given respective 10 month statutory deadlines. With both ratecases, CMS emphasizes a constructive regulatory environment as well as alignment with MPSC commissioners and staff through both its IRP and long-term gas plan in place. Accordingly, CMS emphasizes MPSC support for proposed capital spend in proceedings, further supported by its customer bill affordability efforts.

Electric case remains on track of Dec 2020 order, staff supportive of capex

Indeed with the latest MPSC staff recommendation in CMS pending electric, MPSC staff filed testimony recommending a $90mn rate increase at a 9.75% ROE, 52.5% equity ratio and $11.71Bn rate base ('21 test-year). CMS had initially filed for a $244mn rate increase at a 10.5% ROE, 52.5% equity ratio, and $11.84Bn rate base. Critically, mgmt expresses alignment on capital spend, with main difference between Staff and request being around ROE as usual (with staff proposing 9.75% ROE in the prior ratecase as well before settling at 10%). Mgmt expresses proposed investment spend as in-line with its latest capital plan as well as its 5-Yr electric distribution infrastructure investment plan filed with the MPSC in Mar '18. With O&M spend requested, mgmt expresses approx. equal split between safety/reliability spend that it is currently earning upon, discretionary spend that CMS will not spend if not approved (including tree-trimming), and spend that it is not currently earning upon but still spending.

New gas rates remain on track for Oct 2020 order, staff supportive of capex

With its latest gas case filed at the MPSC in Dec 2019, CMS requested a $244.7mn rate increase at a 10.5% ROE, 52.5% equity ratio, and $7.38Bn rate base for test year ending Sept 30, 2021. Along with its ratecase, CMS filed its 10-year Natural Gas Delivery Plan (2021-2030), which aligns with its current 10-year capital plan, including upside (*$10Bn gas capex with $1.5-2.0Bn gas upside*). In its testimony filed, MPSC staff recommended a $139.1mn rate increase at a 9.6% ROE, 52.5% equity ratio, and $7.42Bn rate base. Notably, proposed spend was largely supported with lower ROE in staff testimony as typical of proceedings. In terms of procedural schedule, a target PFD is currently scheduled for Aug 12. *A final MPSC order is expected in Oct 2020 with a 10 month requirement in place.*

With its latest gas rate case approved in late Sept 2019, mgmt highlights ~2/3rd of rate step-up contribution for FY20 as already approved. Recall, the MPSC approved a $143.5mn rate increase (inclusive of $13mn deferred taxes) at a 9.9% ROE, 52.5% equity ratio, and $6.429Bn average ratebase in Consumers Gas ratecase (U-20322), relative to CMS' requested $204mn request at a 10.75% ROE, 52.5% equity ratio, and $6.54Bn average ratebase. *Mgmt. views the approval as supportive of gas capex, with 98% of requested capex spend approved* and PUC actually calling for main pipe replacement acceleration to ~$100mn/yr (from ~$75mn/yr). As such, we see the approval as in-line with the near-term plan, with mgmt. highlighting '19 and '20 capex plan covered with the order ($1.2Bn of gas infrastructure capex supported).

Duke Energy (DUK)

With the ACP overhang in the rearview, we see the story swiftly transitioning to a utility-centered story (albeit with ~$200mn per annum in renewables) where we still see rate case risk ahead with the DEC/DEP rate cases. Ability to garner a settlement on ROE/Cap structure would be clearly constructive for shares, although with a tight timeline ahead until hearings start we perceive downside risk to a 9.75% authorized ROE (inked with industrials). Meanwhile, we expect Duke's capex outlook to be reset higher with the upcoming September IRP that is likely broader than usual with the commission likely looking for a balance between the lowest cost plan and de-carbonization efforts. The IRP is likely to be an adjudicated process with multiple scenarios in which the commission will chose from, implying that a fully defined capex update is not likely to occur until the 4Q update. As such, we perceive a particularly weak '21 outlook given the loss of ACP earnings (30-35cents) and capex likely to be backfilled post-21, although with load trending slightly more favorable vs. expectations (-2-5% annualized) we could see some cost savings sustained into next year. Nevertheless, we expect mgmt. could rebase its 4-6% growth rate off a lower 2021 number, particularly cautious for shares. Longer-term improved regulatory mechanisms (multi-year rate plans, ROE banding, riders, etc.) stemming from the Clean Energy report recommendation to the legislature remain a possibility. Net-net, we maintain our Neutral rating seeing the ~15.2x P/E multiple (adjusted for renewables) as fairly capturing the growth outlook and risks ahead.

DUK 2Q20 EPS walk

We forecast 2Q20 EPS of $0.95 compared to 2Q19 results of $1.12 (-14% YoY) and consensus estimates of $1.01. Despite the loss of ACP (-13cent headwind YoY) and COVID related pressure, we see 2020 EPS at $5.07 near the bottom-end of mgmt.'s $5.05-$5.45 range.

- **Key drivers**: Positive YoY drivers include the implementation of rates and riders at the electric utilities (+$0.06), the wholesale contract moving to formula rates (+$0.01), new rates at Piedmont (+$0.001), still AFUDC on Atlantic Coast Pipeline (+$0.01), and the contribution from the Palmer commercial renewable projects and tax benefits from previously installed projects (+$0.03). Offsetting results are regulatory lag (-$0.04), impacts from COVID on load growth (-$0.10), higher interest expense (-$0.01), preferred coupon interest expense (-$0.04), share dilution (-$0.01), and reversal of weather benefits from 1Q19 (-$0.08).
- **Unknowns**: Weather is expected to be flattish to slightly favorable, although the exact magnitude is unclear. Another unknown impact is the decline in load growth from COVID19; while mgmt. provides sensitivity for the full-year impact of $0.25-$0.35, we expect a greater proportion of this to show up in 2Q given the timing of state re-openings. Further, it remains unclear if the company was able to bend the cost curve on O&M costs, which could be a potential offset as it experience 7cent favorable variance in 2Q19 and the majority of the 40cents offset are expected to show up in 2H; we could see a push to slightly favorable O&M variance.

Table 17: DUK 2Q EPS walk

DUK 2Q20 Earnings Walk	EPS
DUK 2Q19 EPS	1.12
Weather - normalize from 1Q19	-$0.08
Weather- 1Q20	$0.01
Electric	-$0.06
Rate implementation:	
DEC SC rates (full quarter)	$0.006
DEP SC rates (full quarter)	$0.004
Florida - multi-year plan	$0.01
SOBRA - FL	$0.00
Other Riders - IN and OH	$0.04
Regulatory lag	-$0.04
Load Growth - 1%	-$0.10
AFUDC equity	$0.01
Wholesale - fixed to formula rates	$0.01
Gas	$0.01
LDC Growth	$0.00
New Rates - PNY	$0.001
AFUDC for ACP	$0.01
Tax true-up reversal	$0.00
Renewables	$0.03
Palmer (60MW) and tax benefits	$0.03
Other	-$0.07
O&M	$0.00
Interest expense	-$0.01
Other - preferred	-$0.04
Dilution	-$0.01
DUK 2Q BofAe Adjusted EPS	$0.96
Consensus	$1.01
BofAe 2020 EPS	5.07
Guidance	5.05-5.45
2020 Consensus	5.11
DUK 2Q20 Shares Outstanding	736
DUK 2Q19 Shares Outstanding	728
Tax Rate	12%

Source: BofA Global Research estimates, company report, Bloomberg

Capex: look for details in 2Q but not defined until 4Q

Following the recent cancellation of ACP, we look ahead to the 2Q call where we expect mgmt. to articulate how it intends to backfill capex after reaffirming its 5yr $56bn capex plan. While Duke Energy Florida is proposing to spend ~$1bn on 750 MW of solar projects across Florida in the next three years with ~$500mn incremental, we perceive spending associated with the IRP and looping/laterals to source gas would occur in the *latter half* of the 5yr plan. The IRP is likely to be an adjudicated process with multiple scenarios in which the commission will chose from, implying that a fully defined capex update is not likely to occur until the 4Q update. As such, we expect capex will be delayed into 2021 with potential upside to capex stemming from the IRP and gas capex not likely defined until the 4Q call.

Upcoming IRP to potentially drive upside to capex and FFO

We expect Duke's capex outlook to be reset higher with the upcoming September IRP that is likely broader than usual with the commission likely looking for a balance between the lowest cost plan and de-carbonization efforts. We see the likelihood for meaningful clean energy capex opportunities underpinned by the IRP combined with the early retirement of coal plants in a similar fashion to Dominion's in Virgina. Critically, the IRP could also add to FFO via potential for the accelerated depreciation of coal plants driving further balance sheet improvement, and we even see an angle where Duke could utilize accelerated depreciation without the IRP (i.e. rate case).

NC rate cases remain key to watch: ROE and coal ash

We continue to expect DUK's rate case in the Carolinas to have a similar outcome to Dominion's coal ash order potentially further cautious for earned/recoverable ROEs where we already assume $0.10-$0.13/sh eventual drag. With upcoming hearings for the DEC/DEP rate case slated for July 27 and commentary suggesting the process could take 3-4weeks, it remains unclear if a settlement can be garnered with staff despite recently inked deals w/ industrials for a 9.75% ROE as we could still see downside to authorized levels. While we continue to account for coal ash impacts with 30-40bps of lag in the outer years, a less constructive outcome on ROEs could put further pressure our EPS CAGR. Rate cases remain cautious although see risks of the negative revisions priced-in/largely known.

FERC denied DEP's request to dismiss ROE complaint

We note FERC denied DUK subsidiary Duke Energy Progress' (DEP) request to reject the complaint filed by North Carolina Eastern Municipal Power Agency (MPA) in Oct 2019 against DEP on the matter of 11% ROE included in the Fifth Amended and Restated Full Requirements Power Supply Agreement executed between MPA and DEP. The agency found 11% ROE is excessive and also produced an affidavit from GDS Associates that comprised of a couple of approaches to determine the "zones of reasonableness" in favor of its argument. While the approaches yielded ROE zone of reasonableness of 7.66–12.02% with a median of 9.41%, and 7.26–10.55%, with a median of 8.17%, respectively, MPA forecasted a reduction of 1% in the ROE would reduce the charges by $5.8m per year. FERC dismissed DUK's argument of MPA's inability to establish the unreasonableness of the agreement, and ordered to appoint a settlement judge for a hearing with a refund effective date of Oct 11, 2019. *We note DEP has a wholesale ratebase of $3.2B including both South and North Carolina and as of 3Q19; unclear what portion of this* wholesale *ratebase* the *ROE update would have* been*. We see this as the latest (modest) negative impact from rate case activity to Duke. This is a small portion of overall earnings with likely in ~1c ($5.8M/yr) range but admittedly represents the latest pressure on generation – and highlights* the *latest FERC datapoint on where ROEs* (*even for generation*) *are deemed too high (as has been a focus for peers* like E*TR's SERI already). We expect this to prove as a premium to base ROEs for transmission and as such see a ~10% figure on MtM basis as a broad proxy for generation assets.*

Alternative rate mechanism legislation

We note continued progress, although still very early stages such that Duke is still pushing the Public Utilities Commission (PUC) for alternative rate mechanisms to move forward, such as Performance Based Rates (PBRs), Multi-year rate plans (MYRPs), ROE banding, securitization, riders and others. We believe there remains potential for Duke to have a recommendation back to the legislation that would include one of these alternative mechanisms. Management did make clear that is still early on in the process, but it seems like they are headed in the right direction especially with the upcoming report due from the Governor's committee on Clean Energy. The company is currently in the education phase and there are a number of different tools to look at. All of these tools would be positive for Duke, but there are a number of steps it will take to get there as past efforts stalled/failed. With that said, we see both increased confidence from the company and corresponding stakeholder commentary as supportive for DUK's legislative prospects in the 2021 long session, although wouldn't be implemented in a rate case until 2023.

EPS estimates

We tweak our EPS estimates lower to reflect expectations that 2021 capex will be delayed and now assume a 9.7% authorized ROE for the DEP/DEC rate cases (w/ potential for further downside if litigated). Given the difficulty in attaining its 4-6% EPS outlook, we wonder if DUK mgmt. will elect to re-base on the upcoming call or defer for a later period of time. At a minimum, we expect messaging to be somewhat squishy in regards to the 2021 outlook.

Table 18: DUK EPS Estimates

EPS Estimates	2019A	2020E	2021E	2022E	2023E	2024E
Electric						
Carolinas	1.95	1.90	1.89	1.96	2.02	2.09
Indiana	0.60	0.61	0.62	0.63	0.66	0.68
Ohio - Electric	0.22	0.25	0.25	0.27	0.30	0.35
Progress- Carolinas	1.12	1.15	1.17	1.21	1.24	1.26
Progress- Florida	0.96	0.97	1.01	1.03	1.05	1.06
Commercial Transmission	0.00	0.00	0.00	0.00	0.00	0.00
Eliminations	-0.04	0.00	0.00	0.00	0.00	0.00
Consolidated Earnings	4.81	4.88	4.94	5.10	5.26	5.45
Guidance	4.77	4.94				
Gas						
Ohio - Gas	0.12	0.14	0.16	0.19	0.20	0.21
Piedmont (PNY)	0.27	0.31	0.33	0.37	0.41	0.45
Midstream Pipelines	0.24	0.11	0.04	0.05	0.06	0.08
Eliminations	0.00	0.00	0.00	0.00	0.00	0.00
Consolidated Earnings	0.62	0.56	0.53	0.61	0.67	0.74
Guidance	0.51	0.72				
Commercial Renewables	0.27	0.32	0.33	0.30	0.28	0.29
Guidance	0.32	0.33				
Parent/Other	-0.64	-0.69	-0.58	-0.53	-0.46	-0.41
Guidance	-0.60	-0.73				
Adjustments						
BofAe EPS	5.07	5.07	5.23	5.48	5.75	6.06
Previous Estimates	*5.06*	*5.07*	*5.27*	*5.53*	*5.81*	*6.12*
Guidance	*4.95-5.15*	*5.05-5.45*				
Consensus	5.02	5.08	5.34	5.60	5.89	6.20
Mgmt EPS CAGR: 4-6% from 2019-2023E	5.00	5.25	5.51	5.79	6.08	6.39
Low End	4.80	5.05	5.41	5.62	5.85	6.08
High End	5.20	5.45	5.62	5.96	6.31	6.69
BofAe CAGR '19-'24e						3.9%

Source: BofA Global Research estimates, company report, Bloomberg

The open question remains how management could reposition its long-term EPS CAGR. While ACP should force some degree of guidance update by the time of its 2Q call in coming weeks, we anticipate a more meaningful roll-forward (and rebasing of its 4-6%) is likely only with 4Q. We anticipate a more comprehensive view of mitigating offsets to the outlook including initial expectations from its September IRP filing in the Carolinas and other mitigating capex (transmission, gas) to address ACP delays.

Valuation: PO of $87

We move our PO to $87 (from $84) based on mtm of peer utility multiples of 17.1x and 15.9x for gas and electric (from 16.4x and 15.6x), our lower EPS estimates. Net-net, we maintain our Neutral rating seeing the ~15.2x P/E multiple (adjusted for renewables) as fairly capturing the growth outlook and rate case risks ahead -> just what earned ROEs assumed in the Carolinas will be key.

Table 19: DUK SOPT Analysis

Duke Energy Sum of the Parts Valuation
2022E
All figures in $Mn except per share

	Metric	P/E Multiple					Equity Value		
	2022 EPS	Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric	-	-	17.1x	-	-	-	-	-	-
Group EPS '18-'22 CAGR - Electric	-	-	5.00%	-	-	-	-	-	-
	-	-	-	-	-	-	-	-	-
Electric Utilities			18.0x						
Duke Energy Carolinas	$1.96	17.0x		0.0x	18.0x	19.0x	$33.22	$35.18	$37.14
Duke Energy Progress/Carolinas	$1.20	17.0x		0.0x	18.0x	19.0x	$20.42	$21.63	$22.83
Duke Energy Florida	$1.02	18.0x		1.0x	19.0x	20.0x	$18.37	$19.39	$20.41
Duke Energy Indiana	$0.63	18.0x		1.0x	19.0x	20.0x	$11.40	$12.03	$12.67
Duke Energy Ohio/Kentucky	$0.27	17.0x		0.0x	18.0x	19.0x	$4.57	$4.84	$5.10
Total Electric Utility Value	$5.09						$87.97	$93.07	$98.16
Group Peer Multiple - Gas			15.9x						
Group EPS '18-'22 CAGR - Gas			5.10%						
Gas Utilities	2022 EPS		16.7x						
Duke Energy Piedmont	$0.37	15.7x		0.0x	16.7x	17.7x	$5.81	$6.18	$6.55
Duke Energy Ohio/Kentucky Gas	$0.19	15.7x		0.0x	16.7x	17.7x	$2.93	$3.12	$3.30
Total Gas Utility Value	$0.56						$8.74	$9.29	$9.85
Commercial Segment	2022 EBITDA								
Remaining Midstream assets	$107	8.0x	9.0x	0.0x	9.0x	10.0x	859	967	1,074
Transmission Segment	$6	8.0x	9.0x	0.0x	9.0x	10.0x	52	58	64
Segment Net Debt	-$3,623						-3,623	-3,623	-3,623
Add back Renewable Debt	$2,468						2,468	2,468	2,468
Renewables Segment NPV @ 8% Discount	$1,291						1,291	1,291	1,291
New Renewables NPV	$471						471	471	471
Net Infrastructure Equity							1,518	1,632	1,746
Net Infrastructure Equity Per Share							$2.08	$2.10	$2.39
Parent	2022 EPS								
NMC (Saudi Chemical JV)	$0.05	11.0x		-6.0x	12.0x	13.0x	$0.55	$0.60	$0.65
Parent Interest attributed to utility - 50%	-$0.53	19.1x		0.0x	18.1x	17.1x	-$5.03	-$4.77	-$4.50
Parent Debt- 50%	-$20,702						-$13.34	-$13.34	-$13.34
Total Equity Value							-$17.82	-$17.50	-$17.19
Shares Outstanding								776	
Total Equity Value							$81.00	$87.00	$93.00
Current Share Price							$82.40	$82.40	$82.40
NTM Dividend Yield								4.65%	
Total Return								10.23%	

Source: BofA Global Research estimates, company report, Bloomberg

DTE Energy

We forecast 2Q20 adjusted EPS of $1.27 vs. $0.99 in 2Q19 and $1.13 consensus. We expect that unlike Q1, Q2 will receive a boost from weather in particular with a higher incidence of CDDs in Q2 relative to last year and normal patterns – with Q2 typically a shoulder quarter we do expect some uplift from weather impact particularly as it appears that CDDs in June were 30%+ higher than normal. We estimate that Covid impact on electric sales will be felt most acutely in Q2 given the pace of phased reopening in DTE's MI territory, and we expect approximately half of DTE mgmt.'s forecast $40m decline in sales on an annualized basis to fall in the quarter.

- **Key Drivers:** Primary drivers include weather which is an 18 cent uplift at the electric utility reflecting normalization of 2019 (7 cents) and an estimated 9 cent boost from warmer-than-normal weather during Q2, weighted toward June. We also note that with at least partial stay-at-home orders in place for much of the quarter, the weather boost may be greater than in a 'normal' year. We continue to incorporate the impact of new electric rates which went into effect in May 2019, as well as a partial quarter impact of the new rate increase effective this year, along with correspondingly higher D&A and interest expense. While DTE mgmt. has flagged its previous expectation to utilize financial contingency to mitigate impacts of weather on its utility results, we expect a partial offset via O&M. In the non-reg business we see the biggest jump in the midstream GSP segment as we reflect our higher y/y operating earnings as the company incorporates the contribution of its acquired Haynesville assets.

- **Unknown:** Precise weather-related impacts are difficult to estimate – Q2 2020 CDDs reported *above normal by ~2x the amount below normal in 2019*, leading to our 13 cent estimate – though we highlight some upside to estimates as weather effects may be higher in the quarter due to Covid. We expect the majority of lost sales and additional expenses related to Covid to impact in Q2, with a total 16 cent drag at the electric utility. The Energy Trading business is difficult to forecast owing to the opaque nature of its operations – given significant volatility across most asset classes in the quarter there is potential for an above/below normal quarter, although we do not incorporate this into our estimates.

Table 20: DTE Q2 2020 earnings walk: upside vs. Street despite Covid

DTE Energy 2Q20 Earnings Walk	EPS
Adjusted EPS 2Q19	$0.99
Utility	$0.16
Electric	
Weather - return to normal	$0.07
Weather - 2Q20	$0.09
2019 GRC - $273mn effective 5/2/2019	$0.12
2020 GRC - $188mn effective 5/8/2020	$0.10
D&A, Interest, Other expenses	($0.13)
O&M savings vs. last year	$0.02
Sales impact - Covid	($0.08)
Additional costs - Covid	($0.03)
OID benefit	$0.02
Gas	
Weather - return to normal	($0.02)
Weather - 2Q20	$0.03
D&A, Interest, Other expenses	($0.04)
O&M	$0.02
Sales impact	($0.01)
Non-utility business	$0.16
GSP	0.10
P&IP	0.01
ET	0.04
Corp & Other	0.01
Dilution	($0.04)
2Q20E Adjusted EPS	$1.27
2Q20E Consensus	1.13
2020E BofAe EPS	$6.62
2020E Consensus	6.59
2020 Guidance Midpoint	6.47-6.75
Shares Outstanding 2Q19	184
Shares Outstanding 2Q20	192

Source: BofA Global Research Estimates, company report, Bloomberg

Covid impact on load – Q2 seen most affected

We expect mgmt. of DTE to provide an update on sales in its service territory on the Q2 call. Recall that mgmt. has mapped out two scenarios for returning from mandated shut down orders: May start scenario contemplates most C&I customers beginning a staggered reopening in May with a return to universities and K-12 schools under the regular fall schedule, and a Slow Start scenario with industrial customers remaining idle until late summer and schools and nonessential offices remaining closed until year-end. We note that the company has indicated that the pace of reopening in its service area so far has tracked with the May reopening scenario, though the reopening of schools and universities in the fall remains uncertain given Covid upticks across much of the country. Recall that Michigan reported one of the higher declines in Industrial activity with sales falling by 43% in April at the outset of shut down orders, though we note that based on company sensitivities Residential sales have 15x the earnings impact, making the reported 10.5% increase in sales in April 3x more meaningful from an earnings standpoint.

Table 21: Estimated earnings impact from April reported sales

April reported impact

Customer type	+1% annual impact	Impact (%)	Annual earnings impact ($m)
Residential	15	10.5%	39
Commercial	6	-17.0%	(26)
Industrial	1	-43.0%	(11)
Other	2	0.0%	-
Total			3
2020 guide midpoint		1,270	
Decline impact		0.2%	

Source: BofA Global Research Estimates, company report

Below we present illustrative earnings impact (annual) for a 1% drop in sales across all customer classes based on DTE sensitivities, along with the potential impact on Q2 from a +5%, -15%, -15% drop across the three major customer classes, respectively. We also highlight that our recent work on load trends across the US supports anecdotal reports of sales bottoming out in April and beginning a gradual and uneven recovery. Uncertainty around the reopening of schools and universities in the fall will continue to weigh on forecasts for electricity demand across customer classes.

Table 22: DTE electric demand impact

Flat 1% annual impact

Customer type	Sensitivity (%)	Annual earnings impact ($m)
Residential	-1.0%	15
Commercial	-1.0%	6
Industrial	-1.0%	1
Other	-1.0%	2
Total		24
2020 guide midpoint		1,270
Decline impact		-1.9%

Q2 demand shock illustrative

Customer type	Sensitivity (%)	Annual earnings impact ($m)
Residential	5.0%	19
Commercial	-15.0%	(23)
Industrial	-15.0%	(4)
Other	-15.0%	(8)
Total		(15)
2020 guide midpoint		1,270
Decline impact		-1.2%

Source: BofA Global Research Estimates, company report, Bloomberg

Electric rate case pushed, River Rouge acc. to '21

The Michigan Public Service Commission (MPSC) **approved** DTE Electric's petition to accelerate amortization the $108m portion of its $1.4B accumulated deferred income tax (ADIT) balance associated with the 2017 tax reform law, with the accelerated timeframe requiring DTE to fully amortize by the end of 2021 instead of the end of 2033. Critically, the change in amortization will allow DTE Electric to defer its next electric rate case filing from July 2020 to at least Mar 2021 which will in effect keep customer rates flat through 2022. Yet again, de-risking DTE's utility risk profile through 2020 as far as we're concerned and reiterating our confidence in the MI regulatory backdrop. DTE's application noted that its rate filing would have sought to recover Covid-related costs – recall that per an MPSC order, uncollectibles related to Covid are subject to deferral for future recovery, while a separate docket is pending at the MPSC that will determine whether direct expenses are recoverable as well. Note that DTE mgmt. intends to offset its lost sales and direct expenses via its financial contingency, which we estimate has improved over Q1 given strong weather tailwind at the utilities. We note this is a constructive order for DTE, as ADIT flowback is typically offset by a revenue reduction (since it is normally included in a rate case) though this interim order comes with no adjustment to revenues as it is between rate cases.

In the same order, the MPSC approved early retirement of the River Rouge 3 coal plant, accelerating retirement to May 2021 from previously-scheduled 2022. DTE is required to file a transition plan by Sep 30 that will address the plant retirement and solicit feedback from the community and other stakeholders – note the MPSC order states that the plan to be filed by DTE is not subject to commission approval. As part of the plant retirement, DTE will file for securitization of the undepreciated plant (estimated at

$70m based on filings) along with approximately $120m related to spending on tree trimming. Given the ADIT flowback is typically a cash-negative event we see the concurrent securitization as mitigating most of the cash impact.

The MPSC also approved DTE Electric's amended renewable energy plan, including approvals of new renewable generation to be added to rate base and sourced via PPAs. The commission approved DTE's Meridien Wind project including all engineering and construction – the project is expected to provide 225 MW of generation when it goes in service in late 2021. The MPSC also approved solar PPAs between DTE Electric and two generation stations operated by Ranger Power for 25 year terms, totaling 128 MW of energy. The aggregate additions will bring DTE's renewable generation to the 15% by 2021 requirement set by the state.

Gas rate case – decision expected by Sept

We continue to forecast an authorized ROE reduction of 9.9% for DTE Gas (from the current 10.0%) which is in line with the decision for DTE Electric from earlier this year. Based on PSC staff recommendation of 9.6% (which is in line with the ALJ) and company request for a 10.5%, we see 9.9% as a reasonable level which would be in keeping with the Michigan PSC's history of not making drastic reductions to ROEs and taking a more gradual approach, along with recognizing the lower rate environment. We expect DTE to continue to earn its authorized ROE through the forecast period and to hit the long-term mgmt. guidance CAGR of 9.0% over the 2020-24 period. Bottom line: we expect that DTE's utilities will under-earn their authorized ROEs somewhat in 2020 as a result of sales impacts but recover in 2021 with DTE Electric achieving its authorized 9.9%, while we expect DTE Gas to receive a ~9.9% in its pending rate case.

Table 23: ROE forecast

ROEs							
Authorized	2018A	2019A	2020E	2021E	2022E	2023E	2024E
DTE Electric	10.0%	10.0%	9.9%	9.9%	9.9%	9.9%	9.9%
DTE Gas	10.0%	10.0%	10.0%	9.9%	9.9%	9.9%	9.9%
Earned							
DTE Electric	9.8%	10.0%	9.8%	9.9%	9.9%	9.9%	9.9%
DTE Gas	9.5%	10.5%	9.8%	9.9%	9.9%	9.9%	9.9%

Source: BofA Global Research Estimates

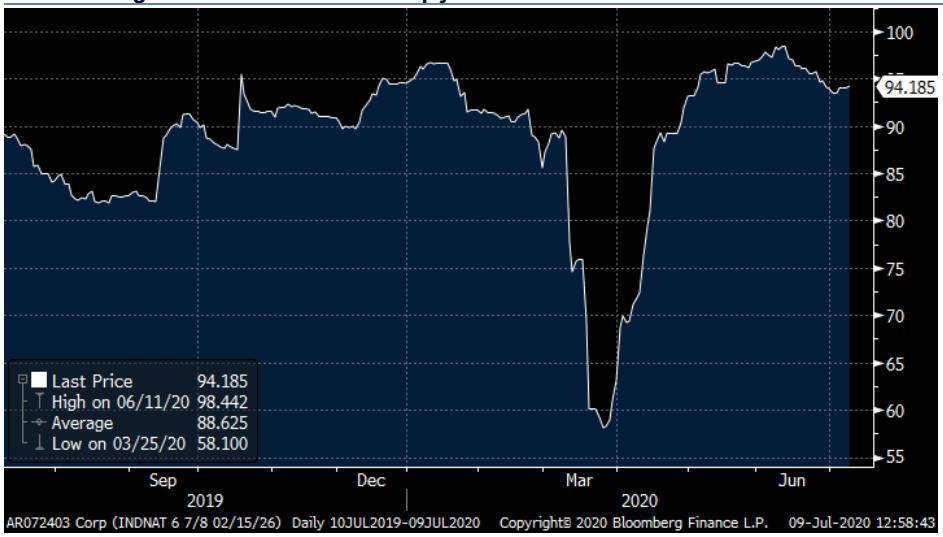
Midstream: read thru from D asset sale

We are forecasting a solid Q2 for DTE's Gas Storage & Pipeline (GSP) biz at approx. $70m operating income, a step-up from the same period last year. The major driver of improved midstream performance is the Haynesville Blue Union/Leap acquisition which is in its first year as part of DTE's midstream business, along with expansions at NEXUS and contributions from the Generation pipeline acquisition. While DTE's midstream business came sharply in focus during the late-March crude oil price collapse as investors ascertained the relative strength of its midstream counterparties, we sense investors have largely grown comfortable with DTE's position – especially in light of an improving natural gas supply/demand outlook given potential exit of producers of low-cost associated gas throughout US basins. Key Haynesville counterparty Indigo has seen its bonds recover substantially – and in fact trade higher than pre-crisis levels – see our recent Upgrade to Buy for more detail.

Following the D sale of its midstream assets to Berkshire *we sense a growing interest among investors in potential further M&A in the midstream space* – while DTE made its most recent acquisition less than 12 months ago, company mgmt. has stated that it continues to evaluate its portfolio on a regular basis and would be open to potentially monetizing assets in the right circumstance; were DTE to divest midstream assets we would expect it to be a fully-developed (with compression) pipeline or storage asset, rather than under-development projects such as LEAP or Generation. We continue to largely expect a status quo outlook for the company given its focus on growth; depending on the ultimate success in Dominion re-rating higher on a stand-alone strategy (or really CMS too), this could drive a further re-think strategically. Moreover,

given focus on growth at this segment only select assets would make sense to divest given need to maintain congruence of growth assets to maximize earned returns.

Exhibit 5: Indigo bonds have rebounded sharply from March lows



Source: Bloomberg

EPS Estimates

We raise our electric utility estimates on the expectation of warmer-than-normal weather enabling a rebuild of DTE's financial contingency. Our updated ests are now 1 cent above the midpoint of mgmt.'s 2020 range at $6.62 and 3 cents above Street consensus – we see upside to 2020 as well as Q2 estimates. We expect that warm weather should provide a tailwind to electric utility results following a warmer-than-normal Q2 and strong start to the key Q3: note that a higher incidence of customers remaining at home during Q3 may well contribute *more to weather impact than a normal year*, though the precise amount is difficult to estimate given uncertain path of state reopening measures. Bottom line: following DTE's reaffirmation of its 2020 guidance range on its Q1 call and commitment to re-establishing financial contingency, we expect company mgmt. will continue to project confidence on non-Covid financial mgmt. including O&M reductions intended to offset sales impacts, with a tailwind from weather in Q2 and early parts of Q3.

Table 24: DTE updated estimates: *getting above Street on '20 and '21*

Earnings Contribution	2018A	2019A	2020E	2021E	2022E	2023E	2024E
DTE Electric	3.70	3.87	3.98	4.27	4.52	4.56	4.83
DTE Gas	0.88	0.98	0.97	1.04	1.17	1.22	1.30
Total utility	4.57	4.85	4.94	5.31	5.69	5.79	6.13
Non-utility segment							
Gas Storage & Pipeline	1.29	1.15	1.49	1.59	1.91	1.91	1.97
Power & Ind. Products	0.90	0.72	0.72	0.79	0.45	0.53	0.63
Energy Trading	0.22	0.16	0.16	0.13	0.15	0.16	0.16
Corp & Eliminations	(0.67)	(0.58)	(0.62)	(0.69)	(0.72)	(0.65)	(0.65)
% of total	*-11%*	*-9%*	*-9%*	*-10%*	*-10%*	*-8%*	*-8%*
Total non-utility	1.73	1.45	1.74	1.82	1.79	1.95	2.11
DTE Consolidated	6.30	6.31	6.62	7.12	7.46	7.72	8.23
Guidance	*0.00*	*6.02-6.38*	*6.47-6.75*				
Prior Estimates		*6.31*	*6.56*	*7.18*	*7.34*	*7.63*	*8.19*
Consensus		6.24	6.59	7.08	7.47	7.78	
			5.0%				
DTE Guidance 6% CAGR ('20-24)			6.61	7.01	7.43	7.87	8.34
Low End				6.94	7.29	7.65	8.03
High End				7.07	7.57	8.10	8.66
BofAe CAGR '20-'24e		5.6%					
Shares outstanding	*181*	*185*	*192*	*194*	*197*	*208*	*209*

Source: BofA Global Research, Bloomberg

PO to $115; Reiterate Buy

We update our PO to $115 following mtm of electric and gas peer group multiples to 16.5x and 15.6x, respectively (17.2x and 17.4x prior). We continue to value midstream assets using a base EV/EBITDA multiple of 9.0x and adjust accordingly for in-progress Haynesville assets. We note that non-equity value of DTE's midstream and other non-reg assets has rebounded from March lows which implied minimal value (low single digits), principally as investor confidence in the outlook for the midstream sector has bounced back. We reiterate our Buy rating following the MPSC constructive decision on electric rate case timing and River Rouge securitization and resulting upward tweak in '20 ests.

Table 25: DTE SOTP

DTE Energy Segments	2022 EPS	Premium /(Discount)	Group Multiple	Applied Multiple	Value
Utility					
Group Peer Multiple - Electric			16.5x		
Group EPS '18-'22 CAGR - Electric			5.00%		
DTE Electric (Distribution)	$4.52	2.0x	17.3x	19.3x	$87.26
Group Peer Multiple - Gas			15.6x		
Group EPS '18-'22 CAGR - Gas			5.10%		
DTE Gas	$1.17	2.0x	16.4x	18.4x	$21.52
Utility Debt Adjustment (20% of non reg debt)	-				
50% interest expense	($0.15)		16.9x		($2.47)
Subtract 50% of holdco debt adjustment	($828)				($4.19)
Utility Equity Value per Share					$102.12

Non-Utility	2022 EBITDA	Premium /(Discount)	Group Multiple	Applied Multiple	
P&I					
Cogen + Legacy Coke Batteries	79	-2.0x	8.0x	6x	$477
NPV of RNG Development	$558		Implied Multiple ---->	6.8x	$558
REF Tax Credit Value (DCF), 2020-2023 @ 6%	198				$198
Energy Trading	44	0.0x	6.0x	6x	$263
Midstream (GSP)	904	-0.3x	9.0x	9x	$7,834
Allocated EBITDA	599	0.0x	9.0x	9x	$5,394
Momentum Midstream	$305	-1.0x	9.0x	8x	$2,440
Holding Company Borrowings					
Consolidated Projected B/S					20,119
(-) Unallocated GSP Project Debt					-
(-) DTE Gas / DTE Electric Debt					(11,839)
(-) Holdco debt adjustment (20%)					(1,656)
Net Non-Utility Net Debt					6,624
Non-Utility Equity Value					$2,705
Shares Outstanding					197
Non-Utility Equity Value per Share					$13.70

	2022 EPS	Premium /(Discount)	Group Multiple	Applied Multiple	
Corp & Other (ex-Interest Expense)	(0.05)	0.0x	19.1x	19.1x	($0.96)
Utility Equity Value per Share					($0.96)
12 Month Price Objective					$115
Implied Consolidated P/E					18.2x
Dividend Yield NTMe					3.8%
Estimated Total Potential Return					10.8%

Source: BofA Global Research, Bloomberg

Edison International (EIX)

With EIX's upcoming 2Q call we expect a miss on EPS, although comparability continues to remain outside of reach given still lack of recovery on O&M memo account items as we await an outcome with the 2021 GRC. Meanwhile, we continue to assume a 20% gross up to the low-end of $4.9bn liability range assumed by mgmt. as we expect an additional $670mn in equity issuance in the outer years (w/ the $1.95bn net imputed on the balance sheet). We note that the Bellwether trial for the Thomas fire is scheduled at the end of the year while there has been no date set for the Woolsey fire. That is not to say that mgmt. cannot reach a settlement with individual claimants prior to that date. While there are thousands of individual lawsuits, if mgmt. can garner meaningful settlements, we would expect the company to update its current charge of $4.9bn, although continue to perceive the bias is to the upside in terms of total liability assumed. With upcoming fire season and focus from the company on PSPS (although still needs permission from CAISO on transmission lines) and new technology deployed by the state (Blackhawks, fire retardants, etc.), execution will be critical to watch. We now move to a 4x discount (from 3x) to capture execution risk into this fire season (equivalent to ~50% prob. of triggering the liability cap with 46% earnings at risk). Still with shares trading at a ~30% discount vs. the broader utility group, we see an opportunity for a re-rating on fire execution and more clarity on the balance sheet.

EIX 2Q20 EPS walk

We forecast 2Q20 EPS of $0.95 compared to 1Q19 results of $1.58 and consensus estimates of $1.17.

- **Key drivers**: Positive YoY drivers include increase FERC and CPUC core contribution (+$0.16), and SCE financial and other benefit variances (+$0.08). Offsetting our estimates is the reversal of CPUC true-up from the GRC (-$0.20) negative variance from O&M expenses (-$0.30), higher D&A (-$0.04), wildfire mitigation costs (not earning ROE) and interest expense on contribution to fund (-$0.07), additional parent drag given HoldCo debt (-$0.07), and share dilution (-$0.20)
- **Unknowns**: We highlight uncertainty with O&M expenses as it continues to be somewhat challenging to handicap given the company will defer costs that are over and above the authorized limit; we expect a negative variance in 2Q20, similar to 1Q20.

Table 26: EIX 2Q20 EPS walk : mild results despite decoupling

Edison International 2Q20 Earnings Walk	EPS
Edison Electric 2Q19 Adjusted EPS	$1.58
SCE	($0.37)
FERC ROE & RB Growth	($0.00)
CPUC RB Growth and 52% Equity Cap	$0.16
CPUC Test year true-up reversal	($0.20)
O&M Effect	($0.30)
Depreciation	($0.04)
Property Taxes	$0.00
Energy Efficiency	$0.00
Wildfire Mitigation Costs	($0.04)
Interest expense for fund contribution	($0.03)
Financial and Other benefits	$0.08
EIX Parent and Other	($0.26)
HoldCo Drag	($0.07)
Dilution	($0.20)
2Q20E Adjusted EPS	$0.95
2Q20 Consensus	$1.17
2020 BAML EPS	$4.46
2020 Consensus	$4.42
2020 Guidance	4.32-4.62
2Q20 Shares Outstanding	373
2Q19 Shares Outstanding	327

Source: BofA Global Research estimates, company report, Bloomberg

Assumptions for remaining '17/18 wildfire exposure

We continue to assume a 20% gross up to the $4.9bn low-end of the '17/18 wildfire liability range, with the net remaining exposure of just $670mn after adjusting for the $1.9bn imputed from rating agencies on the balance sheet. We include this equity issuance in our 2021 share count to provide a fully-diluted EPS outlook. We note that the Bellwether trial for the Thomas fire is scheduled at the end of the year while there has been no date set for the Woolsey fire. That is not to say that mgmt. cannot reach a settlement with individual claimants prior to that dated. While there are thousands of individual lawsuits, if mgmt. can garner meaningful settlements, we would expect the company to update its current charge of $4.9bn that is assuming. We continue to perceive the bias is to the upside in terms of total liability assumed.

Table 27: EIX estimated remaining equity needs for '17/18 wildfires – 20% gross up of low-end

EIX Estimated Remaining Equity		
Current Charge: 2017 Thomas, Mudslides, Woolsey Fires: Low End of Range		-4,900
Gross Up Factor	20%	-5,880
Insurance Receivable		2,000
Wildfire Liability Incl Insurance Offset		-3,880
FERC Allocation ~5%	5%	194
Net Exposure		-3,686
Post Tax Net Exposure	28%	-2,654
Amount imputed from rating agencies ($1.9bn net flows through CFI)		1,984
Remaining Exposure		-670

Source: BofA Global Research estimates, company report

Managing the upcoming wildfire season will be critical

Communication with local authorities and the state is crucial given the need to focus on investments to harden the grid ahead of the upcoming wildfire season while at the same time procuring generators for its most critical customers. We see prioritization of wildfire mitigation and communication with the market as critical, especially ahead of the upcoming wildfire season. Public Safety Power Shutoffs (PSPS) efforts are likely to continue into the '20 season; and while weather conditions similar to last year would result in less shut-offs, mgmt. is going to continue covered conductors in the riskiest areas (1K circuit miles) and re-inspect structures in more than 50% of high-fire risk areas in order to raise the wind threshold and have an overall smaller impact on customers. Recent efforts by the state to deploy Blackhawk helicopters, new retardant technologies to drive more effective suppression, and focus on wildfire mitigation (increased state budget by $90mn), should help to some extent. While utilities continue to focus on PSPS, we remind investors that to shut-off transmission lines, the company will need permission from CAISO first. At the end of the day, fire risk into 2020 will be a binary event.

Just how much exposure is there?

We estimate the T&D cap for EIX is ~$3bn ($2.1bn net of tax) as the maximum amount over a 3year period (3yr rolling average); said another way just $720mn for EIX in 2020. We note that the company would first have to eat through the $1bn insurance deductible and then go through its cap; the company had $1.2bn of insurance through June 30, 2020 and is in the process of procuring the additional amount from July 1, 2020 – June 2021. The cap represents ~46% of EIX earnings that are exposed in addition to amounts of insurance less than $1bn in any given year (subject to a prudency review).

Table 28: EIX Max Liability Cap represents ~46% of earnings on an ongoing basis

Max Liability Cap	2019A	2020E	2021E	2022E	2023E	2024E	2025E
CPUC rate base	24,600	26,760	28,848	30,870	33,270	35,770	38,156
FERC Rate Base	6,200	6,600	6,773	7,033	7,082	7,104	7,099
Total Rate Base	30,800	33,360	35,620	37,903	40,352	42,874	45,255
Less: Generation	1,000	1,000	1,000	1,000	1,000	1,000	1,000
Total T&D Rate Base	29,800	32,360	34,620	36,903	39,352	41,874	44,255
Equity Cap	48%	52%	52%	52%	52%	52%	52%
AB1054 Cap	20%	20%	20%	20%	20%	20%	20%
Total T&D Rate Base	2,861	3,365	3,601	3,838	4,093	4,355	4,602
3 -Year Rolling Average		2,942	3,276	3,601	3,844	4,095	4,350
Tax Effective @ 27%		2,148	2,391	2,629	2,806	2,989	3,176
Amount per year over 3yr period		716	797	876	935	996	1,059
BofA Earnings Estimates		1,654	1,713	1,873	2,051	2,207	2,255
% of Earnings		43%	47%	47%	46%	45%	47%

Source: BofA Global Research estimates, company report

Tracking the memo recovery: critical to limit equity

Mgmt. filed its Fire Memorandum Account (FMA) update, which initiated track 2 of the 2021 General Rate Case (GRC) proceeding. The company is seeking recovery of $509mn of O&M related expenses and $302mn of capital spending. This is considered track 2 of its memo recovery request with a decision not expected until 1Q21 with the GRC. The other items pertain to a decision with Wildfire Memorandum Expense Account (WEMA) for higher insurance cost vs. those approved (requesting $505mn in recovery) with a decision expected in Aug. 2020 and the (Catastrophic Event Memorandum Account) CEMA with a decision in March 2021 (for $88mn request). We now include an estimate for 2020 costs that mgmt. will file at YE20 w/ a decision in '22 (potentially growing by $400-500mn).

Mgmt. will defer these cost (once it consumes amount as prescribed in the GRC), although it's not getting any cash recovery, hence the impacts to credit metrics. We continue to see uncertainty around these items and look for more clarity in the coming months to understand the totality of equity needs as mgmt. has its own internal planning assumptions around recovery. Bottom line, recovery clarity could still take some time and we continue to see some risks on recovery given agencies assume this will be recovered.

Table 29: EIX Wildfire Memorandum Accounts

Memorandum Account	Capital Expenditure	O&M Spent	Total Request	Timeline
Wildfire Mitigation Plan	302	304		PD 1Q21
Fire Hazard Prevention		198		PD 1Q21
Fire Risk Mitigation		8		PD 1Q21
Total 2018-2019 FMA	302	510	500	
Track 2: Wildfire Expense Memo Account	-	341	505	PD Aug 2020
Catastrophic Event Memo Account	57	79	88	PD March 2021
Track 3: 2020 wildfire O&M assumption		~400	400	File YE20; 2022
Total Other Wildfire-related Memo Accounts	57	820	993	
Grand Total	778	1482	1,493	

Source: BofA Global Research estimates, company report

EPS Estimates

We provide our latest EPS estimates for EIX below, moving slightly higher on assumed forward looking share price issuance. Our estimates below are based on a fully diluted assumption with $670mn of incremental equity in 2021and $100mn of ongoing equity needs thereafter. We also continue to assume a constructive outcome in the 2021 GRC in that the company will be able to accrue cost savings over-time (similar to SRE) where we see a 10cent benefit in 2022.

Table 30: EIX EPS estimates and Mini-model

EIX Mini-Model	2018A	2019A	2020E	2021E	2022E	2023E	2024E	2025E
Authorized Capital Structure								
Authorized Equity Capital %	48%	48%	52%	52%	52%	52%	52%	52%
Authorized CPUC ROE	10.30%	10.30%	10.30%	10.30%	10.30%	10.30%	10.30%	10.30%
FERC ROE Build								
FERC Base Rate	9.92%							
CAISO (RTO Participation Adder)	0.50%							
Avg Project Incentive Adder	0.78%							
Assumed Equity Capital %			47.5%	48%	48%	48%	48%	48%
Authorized FERC ROE Build	11.2%	11.2%	10.3%	10.3%	10.3%	10.3%	10.3%	10.3%
Ratebase Growth								
Ratebase - Including Adjustments Below (Avg)	28,601	30,913	33,360	35,620	37,903	40,352	42,874	45,255
Guidance Low ($Bn) (Ex. ~$1.6Bn of fire risk mitigation from AB 1054)			33,300	35,100	37,000	39,200		
Guidance Mid ($Bn) (Ex. ~$1.6Bn of fire risk mitigation from AB 1054)	28,500	30,800	33,350	35,500	37,600	40,100		
Guidance High ($Bn) (Ex. ~$1.6Bn of fire risk mitigation from AB 1054)			33,400	35,900	38,200	41,000		
Breakdown:								
CPUC Ratebase (Avg)	22,107	24,038	26,519	28,934	31,001	33,295	35,781	38,153
FERC Ratebase (Avg)	6,144	6,875	6,841	6,686	6,903	7,058	7,093	7,102
Ratebase Growth	9.4%	8.1%	7.9%	6.8%	6.4%	6.5%	6.2%	5.6%
% FERC	23%	22%	19%	18%	18%	17%	16%	19%
Shares (Basic)	326	342	378	392	393	395	397	397
Shares (Diluted)	326	340	370	387	394	396	398	400
Ratebase-Only EPS	4.37	4.59	4.74	4.85	5.06	5.37	5.69	5.98
Additions/Subtractions to Spend								
Storage Upside (included in base CaEx			0.00	0.00	0.00	0.00	0.00	0.00
Transmission project - pending potential rejection (~$100 Mn capex)			-0.01	-0.01	-0.01	-0.01	-0.01	-0.01
Wildfire mitigation spend (~$1.6bn excluded from earning ROE)			-0.10	-0.08				
Charge Ready II ($561Mn of Capital)			0.02	0.04	0.06	0.08	0.08	0.08
Changes to Capital Structure and ROE Adjustments				New Rate Case Cycle @ 4 years				*Restart*
Cost Savings (ex-Debt Cost Savings) -> Tied to Rate Case Cycle	0.00	0.02	0.20	0.05	0.10	0.20	0.25	0.05
Interest expense from Wildfire Contribution Debt (~$1.2bn) - Opco Non-recoverable		0.00	-0.11	-0.11	-0.10	-0.10	-0.10	-0.10
Energy Efficiency	0.03	0.05	0.04	0.04	0.04	0.04	0.04	0.04
AFUDC Benefits		0.24	0.25	0.25	0.25	0.25	0.25	0.25
Corp Donations and Executive Comp *(Offsets largely AFUDC)*			-0.25	-0.25	-0.25	-0.25	-0.25	-0.25
Parent Drag & Edison Energy								
Edison Energy Group (EEG) --> Breakeven into '20 & Beyond?	-0.04	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Parent and Other	-0.23	-0.33	-0.31	-0.35	-0.39	-0.39	-0.39	-0.39
Toal Parent & Other Drag (Incl EEG)	-0.27	-0.33	-0.31	-0.35	-0.39	-0.39	-0.39	-0.39
Total EPS (Basic)	4.14	4.67	4.38	4.37	4.76	5.19	5.56	5.68
Total EPS (Diluted)	4.14	4.70	4.46	4.43	4.75	5.18	5.54	5.64
Previous estimate		4.70	4.45	4.42	4.73	5.16	5.52	5.62
Consensus		4.77	4.42	4.58	4.83	5.13		
Guidance		4.70-4.90	4.32-4.62					

Source: BofA Global Research estimates, company report

Valuation: $65

We move our PO to $65 based on peer multiples of 17.1x (from 17.6x) and now apply a 4x discount to our EPS assumptions (from 3x) to capture execution risk into this fire season (equivalent to ~50% prob. of triggering the liability cap with 46% earnings at risk). Still with shares trading at a ~30% discount vs. the broader utility group, we see an opportunity for a re-rating on fire execution and more clarity on the balance sheet.

Exhibit 6: EIX SOTP Analysis

EIX SOTP							
SCE Components	% SCE	Authorized ROE Reflected	2022 Earnings	2022 EPS	Peer Multiple	Premium/Discount	Value per Share
Group Peer Multiple - Electric					17.1x		
Group EPS '18-'22 CAGR - Electric					5.00%		
CPUC - Core	82%	10.30%	1,660	$4.21	18.0x	-4.0x	$58.74
CPUC/FERC - Further Capital	1%		30	$0.08	18.0x	-4.0x	$1.07
FERC	17%	10.30%	338	$0.86	18.0x	-4.0x	$11.95
Edison Energy			0	0.00	10.0x	0.0x	$0.00
Parent/Other			-155	-0.39	18.0x	-4.0x	($5.49)
Total EPS				$4.75			
Ongoing contribution to Wildfire Fund				$Mn	EPS	Multiple	
NPV of Ongoing Wildfire Contribution ($945mn over 10yrs)				($664)			($1.68)
Total Equity Value ($/sh)							$65
Price Appreciation							15.3%
NTM Yield							4.5%
Total Return							19.85%
Shares	*394*						

Source: BofA Global Research estimates, company report

Essential Utilities (WTRG)

With a largely resi customer composition and the shoulder season of gas, we see WTRG as well positioned to navigate the evolving COVID crisis. Execution on their capital plans remains largely intact despite modest setbacks ($30Mn) earlier this year, and we would anticipate some further tailwinds from acceleration in muni deals during a recovery period. Meanwhile, we further continue to await developments around the catch up component of repairs tax implementation as additional upside to the recently rolled out guidance with a filing expected imminently. We reiterate our Neutral rating on shares of WTRG, seeing risk/reward as fairly balanced at the current valuation.

WTRG 2Q20 Earnings Walk

We forecast 2Q20 adjusted EPS of $0.24 compared to 2Q19 adjusted results of $0.37 and consensus of $0.22.

- **Key Drivers:** The primary driver of the quarter is the dilution from the Peoples Gas acquisition. This should be somewhat offset by growth in the legacy water business: partial quarter benefit of new rates in PA along with favorable weather should help mitigate COVID related headwinds.

Table 31: WTRG 2Q20 Walk

WTRG 2Q20 Earnings Walk		EPS
WTRG 2Q19 EPS	$	0.37
Aqua		0.01
Peoples Gas		-0.03
Dilution		-0.11
1Q20 BofAe Adjusted EPS	$	0.24
Consensus		$0.22
WTRG Guidance		$1.53-$1.58
2020 Consensus		$1.53

Source: BofA Global Research, Bloomberg

Weather & Commission Help Should Mitigate COVID Impacts

WTRG has guided to 2020 earnings of $1.53-$1.58 and a 5-7% EPS CAGR through '22. The largely residential profile of the water biz provides some protection against load degradation while the gas biz remains in shoulder season, and we expect some benefit from favorable weather at least in 2Q. While early action was taken to maintain a more conservative amount of liquidity, bad debt has been our primary concern. That said, the May order in PA helps to de-risk this given their particularly large presence in the state: recall the PA PUC issued a letter directing utilities to track COVID expenses and authorized regulatory assets for uncollectible expenses incurred above those embedded in rates since the PUC's March 13, 2020 Emergency Order - any regulatory asset created under the authorization contained in the Secretary's Letter will ultimately be subject to review by the PUC in future proceedings. While this won't provide immediate help to cash flow, it should help limit degradation to P&L in the nearer term.

DELCORA Dilemna? Consolidation Prospects Remain Strong

The latest economic pressures are likely to further accelerate consolidation in the industry as muni budgets are further flex'd from the crisis - and any further resulting acquisitions would be upside to mgmt.'s latest reaffirmed targets. States we are watching in the near term include TX & OH following the passage of FMV legislation in the states early last year and VA passing the legislation more recently. While we perceive TX bids as likely more competitive, WTRG is currently the only large water utility in the state of OH - and we see particular opportunities as likely to emerge following the Campbell acquisition. We see NC as another state to watch given the new commission dynamic, albeit muni acquisitions there seem less clear cut relative to the more challenged munis in PA and IN.

Overall, we remain particularly bullish prospects for further consolidation for the water industry going forward shy of any infrastructure bill of magnitude materializing.

Meanwhile, watch developments around their pending DELCORA acquisition after the the independent authority filed an injunction to stop the county from dissolving the authority. That said, we don't see meaningful risk to the deal and it remains upside to estimates over time from the currently laid out plan.

Catch Up Filing Imminent

After closing on the Peoples Gas acquisition in Mid-March, the company elected the current component of repairs tax, reducing income tax by $5.9Bn for the quarter with expectations to drive $0.08-$0.12 worth of contribution for the year. This should limit any risk from rate cases in the state while further driving earnings upside. Meanwhile, the only rate case in North Carolina continues to progress with their request for $7Mn in additional revenue. So overall, we don't see strong reliance on rate cases to hit their targets, albeit watch timing of new rates for any acquisition upside.

Latest discussions suggested a filing for the catch up component imminently with the process taking six to nine months. We see this as the critical debate driving shares with another opportunity in the hundreds of millions over time.

Under implementation for the water biz, seven years of a ten year amortization went to the shareholder while three went to the ratepayer under a particularly constructive outcome. While it remains to be seen how the commission will rule this time around, a constructive outcome would give upside to their numbers.

We maintain our Neutral rating on shares, seeing risk/reward as balanced.

EPS Estimates

The exhibit below reflects our current EPS estimates ahead of the upcoming quarter. We see limited risk to NT numbers and continue to model to the high end of their LT CAGR guidance.

Table 32: EPS Estimates

EPS Estimates	2020E	2021E	2022E
PA	$0.73	$0.80	$0.86
OH	$0.07	$0.07	$0.08
IL	$0.07	$0.08	$0.08
TX	$0.06	$0.07	$0.07
NC	$0.04	$0.04	$0.05
Other States	$0.07	$0.07	$0.08
Water Utility	1.04	1.13	1.21
Peoples Gas	0.62	0.67	0.72
Parent & Other	*-0.10*	*-0.11*	*-0.14*
EPS	1.56	1.69	1.80
YoY Growth	*6%*	*9%*	*6%*
Guidance	1.53-1.58		
Fully Diluted Shares O/S	*254*	*254*	*254*
Previous EPS	*$1.56*	*$1.69*	*$1.80*
Consensus	1.53	1.66	1.79
DPS	0.99	1.06	1.13
Payout Ratio	*63%*	*62%*	*63%*
Guidance	*60-65%*		
Share Count	238	238	250

Source: BofA Global Research, Bloomberg

Valuation

The exhibit below reflects our latest SOTP after applying the current peer multiples to our valuation: 26.9x for water and 15.9x for gas (vs. 26.3x for water and 17.6x for gas previously). Our PO remains unchanged at $49 and we maintain our Neutral rating seeing risk/reward as balanced at the current valuation.

Table 33: SOTP

Water Utilities	2022 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*26.9x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		29.1x							
Water Utilities									
States	2022E EPS	ROE embedded							
PA	$0.86	10.0%	2.0x	30.1x	31.1x	32.1x	$26	$27	$28
OH	$0.08	9.4%	2.0x	30.1x	31.1x	32.1x	$2	$2	$2
IL	$0.08	9.1%	3.0x	31.1x	32.1x	33.1x	$3	$3	$3
TX	$0.07	10.0%	0.0x	28.1x	29.1x	30.1x	$2	$2	$2
NC	$0.05	9.2%	1.0x	29.1x	30.1x	31.1x	$1	$1	$1
Other (including acquisitions)	$0.08	9.2%	0.0x	28.1x	29.1x	30.1x	$2	$2	$2
Water utilities total (ex-Peoples)	$1.21			*29.9x*	*30.9x*	*31.9x*	$36	$38	$39
Gas Utilities									
Peer Gas P/E		*15.9x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		16.8x							
	2022E EPS	ROE embedded							
Peoples Gas	$0.72	12.1%	2.0x	17.8x	18.8x	19.8x	$13	$14	$14
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			-1165	50%			($582)	($582)	($582)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($531)	($492)	($576)
50/50 Weighted Drag from HoldCo Drag							($1,113)	($1,074)	($1,158)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							$45.00	$47.00	$48.00
Current Price								$43.88	
Dividend Yield								2.2%	
Total Return								9.36%	

Source: BofA Global Research, Bloomberg

Evergy Inc. (EVRG)

We forecast 2Q20 adjusted EPS of $0.70 vs. consensus of $0.68 and pro-forma 2Q19 results of $0.58. Our full-year forecast for EVRG of $3.06/sh reflects our expectation of drag resulting from Covid-related slowdowns – though we note EVRG remains one of the few companies in our coverage not to provide interim reporting during Q2, a decision related to the company's ongoing strategic process. We expect mgmt. will report a rebound in load across its service territory through Q2, largely in-line with utility peers, though we note EVRG remains exposed to key aerospace industrial customers in KS, with potential for a slower rebound across that sector.

- **Key Drivers:** Weather is expected to provide an uplift of $0.14/sh as we normalize for the negative effects of 2Q19 (4 cents) and account for milder weather in 2Q20 that increased the number of CDDs in EVRG's service area, particularly in KS. O&M savings including merger synergies are expected to provide an uplift of 6 cents as the company continues to look for ways to cut costs in order to realize full merger synergies, offset Sibley and Jeffery rulings from 2019 (1.5 cent drag in aggregate), and offset potential Covid-related drag on demand. We additionally see 4 cents of accretion from a lower share count in Q2 2020 following EVRG's share buyback program, but note that as this program has been suspended following the Elliott agreement this effect will abate in future quarters.

- **Unknowns:** Weather was warmer than normal in Q2 2020, particularly across EVRG's KS jurisdiction where June CDDs were well above normal. Given the greater importance of June CDDs in the shoulder Q2 quarter we expect a tailwind on results though we note the deviation from normal was more modest across MO. Weather impact on utility results is driven not just by the aggregate number of HDDs but also in the timing of deviations from norm (Jun CDDs worth more than April), and as such the precise weather impact is difficult to gauge. The Covid effect will likely be highest in Q2 as shut-in rules in EVRG's service territory were implemented in a staggered approach at the end of Q1 – we estimate a 7 cent drag.

Table 34: EVRG Q2 EPS walk

Earnings Walk	Notes	EPS
2Q19 EPS		0.58
Weather normal	Reverse favorable effect in Q2 2019	0.04
Weather 2Q20	CDD +19% vs norm; HDDs +13%	0.10
Other	Effect of COVID on load	(0.07)
2Q20 drivers:		
O&M	Cost savings, includes merger synergies	0.06
D&A expense		(0.01)
Interest expense	Incremental KCPL debt, holdco debt	(0.05)
COLI	Based on 2020 guidance	0.02
Jeffrey & Sibley	3 cent drag / annum for each, did not recognize in 2Q19	(0.02)
Accretion		0.04
2Q20E BofAe EPS		$0.70
2Q20 Consensus		$0.68
2020E BofAe EPS		$3.06
2020 Consensus		$3.05
2Q19 Share count		243
2Q20 Share count		227

Source: BofA Global Research Estimates, company report, Bloomberg

Stock trading dynamics

Shares of EVRG are back to trading near a relative high post-Covid, measured on a relative fwd 2Y PE compared to the IXU. Despite being a non-decoupled utility with exposure to two state jurisdictions, we sense investors are looking through near-term Covid impact and focusing on the potential for a constructive outcome from the ongoing strategic process. Recall that when we upgraded EVRG to Buy following the announcement of the formation of the Strategic Review and Operations Committee (SROC) on Mar 2, we applied a 2.0x premium to our electric utility peer multiple for valuation purposes after previously applying a discount to reflect EVRG's regulatory overhang and below-peer growth trajectory. With shares trading at a premium to the IXU of late we note investors remain focused on potential for a constructive SROC outcome, thought the company has not provided interim updates – we highlight the upcoming Jul 30 deadline for SROC recommendation to the board as the next key milestone, and remain Buy-rated.

Exhibit 7: EVRG relative chart

Source: Bloomberg

Covid: KS approves deferral, MO remains pending

In early July the KCC approved EVRG's petition for an Accounting Authority Order (AAO) to track and defer extraordinary costs (net of cost decreases) as well as lost revenues associated with the Covid pandemic. The AAO approval is not a finding that tracked costs and revenues will be recovered, rather that the items will be included in a future rate filing – recall that EVRG is under a rate stayout in KS until 2022 as part of its 2018 merger agreement. EVRG will be required to submit quarterly reports on the amounts tracked – including any federal or state assistance received. In its May filing, EVRG stated that several of its large industrial customers in KS – including Spirit AeroSystems, Textron Aviation, Hallmark Cards, and Goodyear – were forced to furlough employees or temporarily close facilities in its service territory. The AAO petition was supported by KCC staff in an earlier filing, nonetheless the KCC order is a constructive step for EVRG as it continues to deal with the pandemic and reflects a positive fact pattern toward eventual recovery of costs and lost revenues.

Separately, EVRG has filed testimony in its MO petition for an AAO all extraordinary costs and financial impacts that directly result from the Covid pandemic. The financial impacts include additional bad debt expense in excess of amounts recovered in rates and lost revenues, net of cost savings. As in its KS filing, EVRG disclosed that many of its large industrial customers - including a Ford plant – as well as commercial customers including casinos and the Kansas City Royals, were forced to curtail or suspend their

regular business activities, though the public filing does not detail lost sales resulting from the pandemic. The EVRG testimony proposes annual progress reports to track its Covid-related items for recovery, though given the KS ruling and evolving nature of the pandemic we expect the order to be for quarterly filings, should the AAO be approved.

Recapping a busy strategic quarter & looking ahead

Below we highlight some key takeaways from a series of developments during EVRG's strategic review that took place in Q2, and look ahead to the approaching milestones during the summer months which should bring clarity to the direction of the process – whether the company will contemplate M&A or an acceleration of rate base growth via a standalone plan.

KCC moves to get involved early in strategic process

The KCC approved a staff is petition for an order initiating an investigation into the ongoing EVRG strategic review. Staff's filing flagged a high degree of concern that Elliott's focus on increasing shareholder value will come at risk of ratepayers – forcing them to pay higher prices or have to suffer less reliable service in order to maximize shareholder value. Such a result is in direct opposition to EVRG obligations under a 2018 docket and the state's goal of making rates more competitive pursuant to SB 69 according to the filing. Staff did not ask the commission to take affirmative steps, referring to its inquiry as informational in nature. Staff will also petition for a new docket should EVRG elect for a standalone plan, given impact on potential core elements of the prior merger agreement under docket 18-095. Among the specific provisions of the 2018 merger agreement, staff calls out the items below as requiring particular scrutiny in the ongoing SROC review:

- 5-year Kansas rate moratorium following the 2018 rate cases.
- Earnings sharing plan to share merger synergies with shareholders/ratepayers.
- Upfront payments and bill credits.
- Recognition of $30m of merger savings in 2018 rate cases.
- Zero involuntary terminations in KS and maintain HQ in Topeka for 10 years.

New KCC appointment brings Industrials experience

On the same day as the KCC petition filing, Gov. Laura Kelley announced the appointment of Andrew French to the KCC seat being vacated by the expiration of Shari Feist Albrecht's term. French has most recently been employed as counsel at Smythyman & Zakoura, a Topeka-based law firm where he represented large industrial and commercial customers in utility-based litigation matters. With several years of experience litigating on behalf of large utility customers French brings highly relevant experience to the KCC's review of the SROC process and EVRG's retail rates.

Missouri: Focus on jobs, legislation path less clear

In contrast to the Kansas commission which just appointed Andrew French, an experienced litigator who has previously represented large industrial customers at the commission, the MPSC's five members are seen as more open to negotiation on individual issues, without a discernible ideological bent. Stakeholders see potential for progress on a number of issues including securitization and closure of aging coal plants – though this will require legislative action. The most recent appointed commissioner is seen as a proponent of renewable energy which may further accelerate the momentum for coal retirements. Commission staff are seen as key subject matter experts on issues such as authorized holdco equity layers, with commissioners largely relying on the analysis of staff to inform their decisions on such technical topics. The incumbent Missouri governor is largely expected to not seek an additional term if reelected this

November, having taken over from the predecessor halfway into the current term. In the event that the incumbent were to lose the election a new governor would take time to replace members of the MPSC, potentially slowing approval of any deal. With commissioners not ideologically opposed to a deal, a merger proposal that includes an additional rate stayout beyond the current one which runs through 2022 would be seen as most likely to garner support.

SROC milestones approaching in coming weeks

EVRG's Strategic Review & Operations Committee (SROC) created in EVRG's agreement with Elliott outlines specific dates by which proposals must be submitted, voted on, and presented publicly. Two of the four members of the SROC are the new directors selected by Elliott - industry vets Paul Keglevic and Kirk Andrews - giving the activist manager even representation with incumbent directors. Unsurprisingly, given intense focus by utility mgmt. teams and state utility regulators (not limited to EVRG) on maintaining ongoing service amid the Covid emergency, the SROC issued an updated time frame pushing back its most significant deliverables further into the year. We view the revised timeframe below as merely reflecting the practical realities of evaluating a complex transaction amid work-from-home restrictions and market volatility and remain constructive on the overall direction of the review.

- **SROC recommendation to Board due Jul 30.** The original timeline called for the committee to present to the Board its recommendation of a transaction or standalone strategy by May 30 - note that the specific recommendation will also determine the level of public disclosure, as we detailed previously.

- **Board announcement by August 17.** Previously June 17, giving the Board the same number of days to evaluate as under the previous timeframe. We note some nuance in the language of the agreement that allows members of the SROC to publicize both recommendations in the event of a tie vote and *both Elliott-appointed directors voting for the same recommendation*, in which case the external directors are permitted to discuss their vote publicly within 5 days of the earlier Jul 30 deadline.

- **Modified standalone plan by Oct 14 if selected.** Originally the deadline was Sep 4, so the time frame for a presentation of a potential standalone plan has been pushed back by six weeks. We continue to view this as the less likely option given specific wording of the SROC agreement and note that logistics around presenting such a plan may require rethinking in the wake of Covid. Note this deadline now also impacts EVRG's reporting to the KCC that is required pursuant to the commission's recent order, which is required to answer a set of questions about the committee's decision and process.

Updated estimates

We maintain our EVRG estimates at $3.06/sh for 2020 as we had previously reduced our forecast to account for Covid-related impacts and resulting company response via additional cost-cutting (mgmt. announced an additional 1% of cuts on the Q1 call). Our estimates are 1 penny above Street in 2020 after consensus forecasts were revised down to reflect the 2020 sales outlook. Looking ahead, we make tweaks and maintain our long-term EPS growth forecast which is based on rate base growth of 3-4% based on the most recent rolled-forward capex forecast presented by mgmt. on is Q4 call. While rate base and earnings growth is certainly below the peer group, we sense investors remain focused on the outcome of the strategic review principally, with organic growth considerations currently seen as less urgent by most investors.

Table 35: EVRG estimates

Evergy, Inc. Dashboard

EPS Estimates by Subsidiary	2018A	2019A	2020E	2021E	2022E	2023E	2024E
Evergy Metro	$0.76	$1.06	$1.07	$1.13	$1.17	$1.20	$1.23
Evergy Missouri West	$0.35	$0.37	$0.44	$0.47	$0.49	$0.51	$0.52
Kansas Central	$1.58	$1.43	$1.67	$1.78	$1.88	$1.92	$1.95
Parent/Other	($0.19)	($0.08)	($0.11)	($0.11)	($0.11)	($0.13)	($0.16)
GAAP EPS	$2.50	$2.79	$3.06	$3.28	$3.44	$3.50	$3.53
Y/Y EPS Growth %		*11.6%*	*9.7%*	*7.1%*	*4.7%*	*1.9%*	*1.0%*
Prior estimates	$2.50	$2.89	$3.06	$3.27	$3.40	$3.47	$3.50
Consensus (BBG)		$2.92	$3.05	$3.22	$3.38	$3.54	nm
DPS	$1.84	$1.95	$2.07	$2.19	$2.30	$2.42	$2.54
Dividend Payout (60-70%)	73.5%	69.8%	67.5%	66.8%	66.9%	69.0%	71.8%

Source: BofA Global Research, Bloomberg

Valuation

We update our PO to $68 reflecting an updated electric utility peer group multiple of 17.1x (17.6x previously). Our valuation is largely unaffected by the near-term drag on our estimates related to milder weather and Covid as both are expected to normalize by 2022. Shares have re-rated vs the peer group since our upgrade to Buy though we still perceive upside to the current share price amid ongoing strategic review.

Table 36: ERG SOTP

Evergy Sum-of-the-Parts Valuation	2022 EPS	P/E Multiple					Equity Value/Sh		
		Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric			17.1x						
Group EPS '18-'22 CAGR - Electric			5.00%						
			18.0x						
Evergy Metro	$1.17	19.0x		2.0x	20.0x	21.0x	$22.24	$23.42	$24.59
Evergy Missouri West	$0.49	19.0x		2.0x	20.0x	21.0x	$9.32	$9.82	$10.31
Evergy Kansas Central	$1.88	19.0x		2.0x	20.0x	21.0x	$35.58	$37.45	$39.33
Parent & Other	-$0.11	19.0x		2.0x	20.0x	21.0x	-$2.00	-$2.10	-$2.21
EVRG consolidated '22 EPS	$3.44				*20.1x*		$65.00	$69.00	$72.00

	After-tax amount $m	$/sh	Probability				
Deferral of Sibley return + D&A	23	-$0.10	50%			-$1.99	-$0.99	$0.00
Shares outstanding (Average 2022)	227							
Shares outstanding (Y/E 2022)	227							
EVRG Price Objective						$63.00	$68.00	$72.00
Implied Return							7.68%	
EVRG Standalone NTM Dividend Yield							3.47%	
Total Return							11.15%	

Source: BofA Global Research, Bloomberg

FirstEnergy (FE)

We anticipate a quiet second quarter call approaching. We again expect to see the Street focus on New Jersey given it's the only regulatory rate case the company is in right now. For FERC, interim rates already took effect with a ruling on its 10.8% ROE request outstanding, and for distribution, the schedule is still outstanding. The lack of regulatory activity outside of this until 2023 is a positive in our eyes. FE is somewhat shielded from COVID impacts as Ohio is decoupled, it has a low portion of revenue that is tied industrial sales (just 7%), just 10% of industrial revenue is volumetric-based, and FE recovers uncollectible expenses in OH / NJ through a rider and in PA / WV / MD through base rates. We look for commentary on the company's $3bn per year of capex trajectory – particularly as mgmt. has noted perhaps +$400mn of additional opps. We also look for hints towards the West Virginia IRP scheduled for later this year (given FE indicated it expects it will show need for capacity), and updates on credit rating agency discussions. We forecast a 2Q20 estimate of $0.54/sh – just 1c lower than Consensus.

2Q20 EPS Walk

We forecast a 2Q20 of $0.54/sh versus a Consensus of $0.55/sh and last year's 2Q19 estimate of $0.61/sh.

- **Drivers**: We anticipate 2c of riders and decoupling along with -6c of losing the OH DMR as key drivers for the quarter.
- **Other**: 2Q is generally not a large driver for the year given it is a shoulder month; as 2Q20 saw a hotter than normal June and colder than normal April, we factor in +1c. 2Q19 was slightly mild versus normal, we assume +1c in reversing last year's impact. We also factor in -2c of D&A, lower intr exp from refinancing maturities at lower interest rates that are balanced by higher distribution & transmission interest, and a flat parent with balancing tax implications.
- **Wildcard**: We only factor in -1c of Covid impact based on the four weeks of data provided on the last earnings call (i.e. -13% in C&I and +6% in resi). We anticipate O&M savings of +1c largely offset this.

Table 37: FE 2Q20 EPS Walk

FirstEnergy 2Q20 Earnings Walk	EPS
2Q19E Adjusted EPS	0.61
Regulated Distribution	-0.04
Weather Vs normal in 2Q19	0.01
Weather Vs normal in 2Q20	0.01
Distribution sales growth / Covid impact	-0.01
Riders: Including Ohio Grid Mod, Ohio decoupling, PA LTIIP, OH DCR	0.02
OH: DMR (stopped recognizing earnings benefit)	-0.06
FE Tomorrow	0.00
O&M: Pension & OPEB	0.01
D&A and taxes	-0.02
Debt maturities	0.00
Regulated Transmission	0.01
Revenues (net of D&A and taxes): higher ratebase	0.01
Parent and Other	-0.02
Tax rate benefit	-0.02
Timing of taxes	-0.02
2Q20E Adjusted EPS	0.54
2Q20E BofAe EPS	0.61
2Q20 Consensus	0.55
2Q Guidance	0.48-0.58
2020 BofAe EPS	2.46
2020 Consensus	2.48
2020 Guidance	2.40-2.60

Source: BofA Global Research estimates, company report, Bloomberg

Key topics for 2Q20

- **Capex**: Reiterated comments made around capex during fireside chat.

- succession planning and CEO turnover are likely a 2021 item- albeit as part of an entirely regulatory path. OH is likely to continue under PUCO leadership of Sam Randazzo and with ~2.5 years of the current admin left, there remains ample time for legislation or reg reform that establishes stability

FFO/debt, Balance sheet, credit rating

FE's Balance Sheet is improving with expectations of improving credit metrics translating at first with an upgrade from S&P and subsequently Moody's, albeit still largely in the 12% FFO/debt range for our reconciliation. We' expect a positive outlook from S&P first – as early as later this year. Mgmt. has acknowledged it is discussing its credit metrics with rating agencies, with potential positive news to come from S&P considering the agency lowered its FFO/debt threshold to 12%. Moody's upgrade threshold is 14% however, so the process may be a little more protracted - but there is potential opportunity for Moody's to bring down its upgrade threshold to 13% (note Fortis' is 11-13% and FE noted it sees its companies in line with theirs in terms of credit and risk). We could expect to see FE approach a 13% FFO/debt in the next few years, particularly as FE has plans for incremental equity starting in '22 and the years after (could be up to $600mn/yr). With its FES business disposition resolved, we perceive few angles to meaningfully shift its balance sheet outlook so look to '22-'23 when the potential Moody's upgrade could be.

Rate cases

FE is one of the least exposed amongst peers to lower authorized returns given the company re-affirmed limited regulatory activity thru the forecast outlook with capex largely recovered thru riders rather than litigated cases. We suspect this limited rate case risk profile will increasingly resonate with investors keen to pursue a less volatile & overall noisy profile. Outside its NJ cases, FE is not planning to file elsewhere for several years - specifically noting for at least three years without a case. The pandemic is not expected to have an impact on timing.

We are still awaiting outcomes in NJ. For distribution, FE awaits a rate case schedule from the ALJ. NJ is just 13% of our modeled '22 EPS and that the distribution case was never included in FE's 2020 guidance. FE noted previously it expects an opportunity to settle (at the earliest later this year), and updated timing for a full case to a result in '21. Recall NJ is already FE's lowest allowed ROE at 9.6%, and we model 9-9.5% earned in the next few years. This remains among the principle (small gyrations) in outlook still.

Sustainable capex

Mgmt. continued to reiterate that it has a strong ability to execute on its ~$3bn/yr capex plans (+/- ~$400mn/yr - more likely a +). Further, the company has flexibility in its size and geographic diversity that allows it to proactively shift where it deploys capex. Mgmt. again noted that it is leaning towards not pursuing a second round of IIP at JCP&L because it currently sees itself as having accomplished reliability projects in the state, while also having enough investments in other states. The West Virginia IRP this fall is likely to drive new generation needs, improving opportunities but unclear if this will see an aggregate uptick in capex levels; we would expect a generation outlook is more likely in 2H.

Succession

The company announced plans to search for a candidate internally, we would expect any succession to take place next year at the earliest (if not longer). We see a discussion of mgmt incentives around change in control as meriting some attention. We see governance and exec comp as having improved in recent years under its regulated strategy.

Estimates

We provide our latest EPS estimates below.

Table 38: FE EPS Estimates

EPS	2016A	2017A	2018A	2019E	2020E	2021E	2022E	2023E	2024E	2025E
Ohio Utilities	0.50	1.03	1.23	0.92	0.82	0.83	0.85	0.88	0.91	0.94
Ohio Edison (Inc PennPower)	0.35	0.59	0.64	0.50	0.48	0.49	0.51	0.53	0.55	0.57
CEI	0.09	0.27	0.39	0.26	0.20	0.20	0.20	0.21	0.21	0.22
TE	0.06	0.17	0.20	0.15	0.14	0.14	0.14	0.15	0.15	0.15
West Virginia										
MonPower	0.15	0.16	0.25	0.21	0.21	0.22	0.23	0.23	0.23	0.25
Maryland										
Potomac	0.14	0.10	0.10	0.10	0.12	0.14	0.16	0.18	0.20	0.22
New Jersey										
JCP&L	0.19	0.26	0.32	0.32	0.33	0.35	0.35	0.37	0.39	0.41
Pennsylvania	0.73	0.76	0.93	0.92	0.92	0.94	0.94	0.95	0.98	1.02
PennPower (already included in OE)	0.05	0.07	0.07	0.08	0.08	0.08	0.08	0.08	0.08	0.09
Penelec	0.21	0.22	0.32	0.29	0.29	0.30	0.30	0.31	0.32	0.33
WPP	0.27	0.25	0.23	0.24	0.24	0.23	0.23	0.24	0.25	0.26
MetEd	0.21	0.22	0.31	0.31	0.32	0.32	0.32	0.32	0.33	0.34
Regulated Utilities (Inc Transmission)	*1.66*	*2.23*	*2.75*	*2.40*	*2.33*	*2.40*	*2.45*	*2.53*	*2.63*	*2.75*
Regulated Distribution	-0.55	2.32	2.31	2.26	2.15	2.20	2.23	2.27	2.35	2.45
Guidance	2.60-2.70	2.27-2.31	2.34-2.40	2.20-2.26	2.13-2.27					
FET	0.45	0.62	0.58	0.66	0.69	0.75	0.82	0.89	0.95	1.02
Intrastate	0.28	0.13	0.21	0.16	0.18	0.20	0.22	0.25	0.27	0.30
Transmission	0.73	0.83	0.74	0.83	0.89	0.95	1.04	1.14	1.22	1.32
Guidance		.82-.84	.74-.76	.83-.84	.85-.89					
Competitive Energy Svcs.	0.60	0.46	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Guidance		0.42-0.46								
Corporate (reduced by pref)	-0.55	-0.53	-0.56	-0.51	-0.57	-0.55	-0.56	-0.55	-0.55	-0.55
Guidance		-0.51	(.58)-(.56)	(.53)-(.50)	(.58)-(.56)					
Eliminations		0.16	0.13	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Consolidated EPS	2.61	3.07	2.59	2.58	2.46	2.59	2.71	2.86	3.03	3.20
Guidance		3.00-3.10	2.50-2.60	2.50-2.60	2.40-2.60					
Previous EPS		3.07	2.59	2.58	2.46	2.59	2.71	2.86	3.03	3.20
Consensus EPS		3.05	2.54	2.53	2.48	2.63	2.76	2.89	3.02	
EPS CAGR off 2.15 (2018)					7.03%	6.47%	5.95%	5.85%	5.88%	5.83%
EPS CAGR off 2.43 ('19 2.55 Midpt less 0.12 DMR)					1.35%	3.34%	3.69%	4.13%	4.51%	4.68%
EPS CAGR off 2020						5.37%	4.89%	5.08%	5.31%	5.36%
EPS CAGR off 2021							4.40%	4.93%	5.29%	5.36%
Ex CES EPS	2.02	2.61	2.59	2.58	2.46	2.59	2.71	2.86	3.03	3.20
YoY Growth Rate Excl CEC EPS				0%	-4%	5%	4%	5%	6%	6%
Sum of the subs		3.24	2.49	2.58	2.48	2.59	2.71	2.86	3.03	3.22
Bottom - 5%			2.15	2.26	2.37	2.49	2.61	2.74	2.88	3.03
Top - 7%				2.30	2.46	2.63	2.82	3.02	3.23	3.45
Shares	429	444	538	539	543	543	549	561	572	583

Source: BofA Global Research estimates

Valuation

We provide our latest SOTP valuation below. We maintain our Buy rating and $45.50/sh SOTP valuation, tweaking our regulated peer ute multiple slightly higher to 17.1x (17.0x previously).

Exhibit 8: FE SOTP Valuation

FirstEnergy SOP Valuation									
	Metric	P/E Multiple					Equity Value ($/sh)		
	2022 EPS	Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric			17.1x						
Group EPS '18-'22 CAGR - Electric			5.00%						
Electric Utilities			18.0x						
FE Utilities: OH Utility (CEI, Ohio Edison, TE), Ex-DMR, Ex-PP	$0.78	16.0x		-1.0x	17.0x	18.0x	$12	$13	$14
FE Utilities: PA Utility (MetEd, WPP, PenElec, Penn Power) - WPP T Incl	$0.94	17.0x		0.0x	18.0x	19.0x	$16	$17	$18
FE Utilities: NJ Utility (JCP&L) - T&D	$0.35	17.0x		0.0x	18.0x	19.0x	$6	$6	$7
FE Utilities: Other Utility (MonPower, Potomac Ed) - T&D	$0.38	17.0x		0.0x	18.0x	19.0x	$7	$7	$7
Less: Intrastate Transmission embedded above	-$0.22	17.0x		0.0x	18.0x	19.0x	-$4	-$4	-$4
FE Utilities: Transmission (FET + Intrastate)	$1.04	17.0x		0.0x	18.0x	19.0x	$18	$19	$20
Total T & D 'Regulated' Utility EPS	$3.27				17.7x		$55	$58	$61
BAMLe Utility + Parent	$2.71								
Holding Company Liabilities & Earnings Drag									
FE: HoldCo Drag	-$0.56	16.7x		0.0x	17.7x	18.7x	-$9.4	-$10.0	-$10.6
Add Back: Interest Expense drag @ 50%	$0.22	16.7x		0.0x	17.7x	18.7x	$7.4	$3.9	$4.1
Holding Company Debt								$Mn	
Short Term Holdco Debt								$750	
Unsecured LT Debt								$6,100	
Total Debt								-$6,850	
Total Debt @ 50% Split								-$3,425	
$/Sh - Equity value in valuation								-$6.2	
Total Debt at Parent (per share)								*-$12.48*	
Other Liabilities	Liability	Probability					Low	Base	High
Shares Outstanding (2022e)								549	
Total Equity Value							$40.00	$45.50	$49.00
2020 Dividend								$1.57	
Current Yield								3.7%	
Price Return							-5%	8.0%	16%
Total Return							-1%	12%	20%

Source: BofA Global Research estimates

Pinnacle West (PNW)

We expect Q2 Operating EPS of $1.55/sh as compared to $1.34/sh Street estimates and $1.28/sh in 2019. Weather is expected to be the largest single driver as we normalize for the effects of a significantly below-normal 2019 and add further tailwind from 2020 CDDs. We further note that PNW had increased its bad debt expense target for 2020 given last year's disconnect moratorium, suggesting it may be better able to withstand an increase in delinquent accounts than peers. We see additional impact from COVID-19 on sales – though this impact appears to have largely abated as the quarter developed resulting in company-reported flat weather-normalized level of sales for a trailing 33-day period ending in June. However, given the uptick in cases of COVID-19 in the state of Arizona, we acknowledge that C&I sales may fluctuate through the coming quarter. Finally, PNW's most important earnings quarter is Q3, with potential upside to results from increased residential usage given that customer segment's higher margin contribution. While visibility around the near-term outlook appears to be improving (and for the better), we continue to see substantial risks around the pending rate case (and potential for ACC turnover), with upcoming staff testimony the next significant milestone to watch for – due Aug 3.

2Q20 Walk

We forecast 2Q20 adjusted EPS of $1.55 vs. $1.28 in 1Q19 and $1.34 Street consensus. We expect substantial upward revisions to Street estimates over the coming weeks.

- **Key Drivers:** Weather normalization will be a significant driver in Q2 as 2019 was a below-average weather quarter, with an uplift of 31 cents. In addition, we see 14 cents uplift from weather in 2020 as service territory CDDs were meaningfully above normal (14% above normal). We see COVID-19-related impacts on EPS of -15 cents, which is in-line with company provided disclosures during Q2. While PNW realized significant Q1 savings in O&M – near levels suggested by its full year 2020 guidance – we assume an additional one cent of savings in the quarter as mgmt. seeks additional offsets to drag resulting from lost sales. Finally, we see two cents of drag related to pension/OPEB given the six cent gains reported in Q1 relative to full-year company guidance.

- **Unknowns:** Weather and COVID-19 sales fluctuations are the two key wildcards in Q2, with both playing meaningful and opposite roles. Unlike Q1 where both weather and COVID-19 provided a drag on utility earnings, we see the two factors as largely offsetting in Q2. Our 14 cent weather uplift estimate is based on CDDs 14% above normal as reported by PNW, compared with 27% below normal in 2019. Our COVID-19 impact of 15 cents is based on an earlier intra quarter update by the company which disclosed an EPS impact of -$0.14/sh for the period of Mar 13 – May 26, and the expectation that drag from lost sales *abated slightly during June* given the state's reopening schedule, though we acknowledge some uncertainty here given: 1) relative weighting of warmer-month earnings, and 2) uptick in COVID-19 cases and resulting impacts on business and consumer behavior.

Table 39: PNW Q2 earnings walk

PNW 2Q20E Earnings Walk	EPS
2Q19 Adjusted EPS	$1.28
Weather return to normal	$0.31
Weather effect vs norm	$0.14
COVID-19 sales impact	($0.15)
Gross margin	$0.02
O&M	$0.01
D&A	($0.04)
Interest Expense	($0.01)
TEAM	$0.01
Other Opex - pension and OPEB	($0.02)
Dilution	($0.00)

Table 39: PNW Q2 earnings walk

PNW 2Q20E Earnings Walk	EPS
2Q20E Adjusted EPS	$1.55
2Q20E Consensus	$1.34
2020E Adjusted EPS	$4.80
2020E Consensus	$4.83
2020 Guidance	$4.75-4.95

2Q19 Shares Outstanding	113
2Q20 Shares Outstanding	113

Source: BofA Global Research estimates, Bloomberg

COVID-19 disclosures trending in the *right direction*

We estimate a 15 cent impact from COVID-19-related sales disruptions in Q2. PNW's early June update reported a 14 cent EPS drag from Mar 13 to May 26, which we assume is heavily weighted toward April-May when the full impact of state closures took effect. With sales impacts abating per the most recent disclosures which cover the period running through mid-June, we expect that the weather-normalized impact on sales in the month of June was not as intense as in the prior periods reported. Below we include the weather-normalized sales trends by customer class for several periods as reported by the company as well as trailing-period EPS impacts. While most of the figures below are reported by PNW in its interim updates, the $0.15/sh EPS drag for Q2 in the rightmost column is our estimate based on prior-reported figures.

Table 40: PNW COVID-19 sales and EPS impact

			Mar 13 - Apr 30		May 1 - May 26		May 13 - June 16	
Sensitivities	Sales	Annual EPS Impact	Sales	EPS impact 3/13 - 4/30	Sales	EPS Impact 3/13 - 5/26	Sales	EPS Impact Q2 (BofA estimate)
Residential	1%	$0.09	7%		4%		4%	
Commercial	1%	$0.05	-14%		-8%		-4%	
Industrial	1%	$0.01	-14%		-8%		-4%	
Total		$0.16-0.20	-7%	($0.10)	-4%	($0.14)	0%	($0.15)

Source: BofA Global Research estimates, company reports

Catching up with mgmt. on key topics

Below we review the key issues surrounding PNW after catching up with its management team on our recent fireside chat. We saw this as an opportune time to discuss the company's broader strategic vision and strategy for improving regulatory relationships. A recap of key topics follows.

- **Don't expect a settlement of the APS rate case.** Mgmt. sees little pathway to a settlement of the current APS rate case given the procedural and election schedules coming up in the second half of the year. Upcoming milestones in the rate case include filing of staff/intervener testimony on Aug 3 and the beginning of the Hearing on Sep 30. At this point in the calendar, PNW mgmt. expects that *even if a settlement agreement were reached with key counterparties, procedurally it would need to be approved by the next commission which will be seated in 2021.* Recall that 3 of 5 commissioner seats are up for election in Nov, with a minimum of 2 guaranteed to be replaced as Chair Bob Burns is termed out and Boyd Dunn is barred from running after forging signatures. Given these dynamics, mgmt. indicated the difficulty in reaching general consensus on key issues including revenue requirement, ROE, and equity layer with stakeholders and then seeking subsequent approval of a settlement agreement from a commission with 40% new members in 2021. Despite some earlier indications that a settlement may be possible (in order to give the current ACC an opportunity to decide APS' rates), all indications now point to a fully litigated outcome.

Table 41: APS case schedule

Event / Item Due	Original	Updated
Staff & Intervenor Testimony w/o Rate Schedules	5/20/2020	8/3/2020
Staff & Intervenor Testimony w/ Rate Schedules	5/27/2020	8/10/2020
APS Rebuttal Testimony	6/18/2020	9/1/2020
Prehearing Conference	7/13/2020	9/26/2020
Hearing Begins	7/17/2020	9/30/2020
Hearing Ends (30 day)	8/31/2020	11/11/2020
Transcripts Filed	9/11/2020	tbd
Briefs Due w/ Final Schedules	9/16/2020	tbd
Response Briefs Due	9/25/2020	tbd
Recommended Opinion and Order	11/25/2020	tbd
Exception Period Ends	12/16/2020	tbd
Open Meeting	12/17/2020	tbd
Deadline for Final Decision (AZ rule)	2/21/2021	tbd

Source: ACC docket #19-0236

Two other utilities (FTS and SWX) currently have rate cases pending before the ACC that are further advanced. FTS expects a fully litigated resolution to its case *prior to ACC turnover*, leaving APS in the unique position of having its case process straddle two ACC benches. *We perceive the protracted processes with these to suggest a case potentially delayed well into '21 with a new ACC composition.*

- **Pivot to clean generation is ongoing, expect mix of PPA and owned buildout.** Mgmt. expects to continue its pivot to a greater share of clean generation, as outlined in its decarbonization plan published earlier this year and recently-updated IRP filing. With 40% of its announced '21-22 capex plan allocated to clean generation, PNW is moving forward with a combination of owned and PPA renewable generation projects, and while the company intends to move forward with an ambitious Energy Storage buildout (750 MW through 2024 per the IRP), plans are currently on hold pending the outcome of the ongoing McMicken investigation. The company currently has two RFPs out for renewable generation including 150 MW of APS-owned solar and 250 MW of wind that may be owned or under a PPA structure. Critically, mgmt. sees future renewable solicitations as considering both owned and PPA structures given requirements to secure the most economic forms of supply. One potential form of additional PPA generation that was highlighted is a bolt-on addition to an existing renewable generation asset that is already contracted with APS, owing to the existence of already-built infrastructure that would reduce total costs to ratepayers.

- **Ratemaking and customer education are priorities – *but how to fix?*** *We see this as among the stickiest issues management has yet to resolve with its stakeholders.* Mgmt. highlighted its continuing efforts to rebuild relationships with regulators, as evidenced by frequent appearances at ACC open meetings to participate in direct dialogue with commissioners and the public – while efforts have yet to bear tangible outcomes, mgmt. indicated its intention to maintain the dialogue with stakeholders on the numerous issues in front of the ACC. We note the rate design question discussed in detail at a recent open meeting remains unanswered: given the requirement of the previous case settlement to encourage customers to opt-in to the "most economical plan", the company reported that a meaningful percentage of customers did not elect to do so, citing difficulty in getting customer engagement. Regarding future rate design, APS has proposed a flat bill option where the utility manages customers' thermostat settings though this proposal is opposed by some interveners for failing to send a price signal to customers.

- **No equity in '20, $300-400m coming *before* next case filing.** PNW does not expect to issue block equity until it is contemplating its next rate case filing. Company mgmt. has previously flagged some flexibility around APS' equity layer (rate case request of 54.7% has historically not been a negotiated term) with an

intention to true-up prior to its next filing. Consistent with prior statements, mgmt. does not expect to issue equity in order to preserve its credit rating. Our base case expectation is for a rate case filing in 2022, and we see an issuance of $350m, in line with the midpoint of mgmt. expectations, and a concurrent equity injection by PNW to APS in the same year. Additionally, while we forecast PNW's consolidated debt metrics to remain above the Moody's downgrade threshold through '22, we forecast the ratio dropping to ~18% by 2025 – consistent with mgmt. statements of some latitude on this front (not managing to a credit ratio).

Table 42: APS ROE and Equity forecast

Earned ROE - GAAP calculation	2018A	2019E	2020E	2021E	2022E	2023E	2024E
Average Equity Method - GAAP	10.45%	9.80%	9.51%	9.58%	9.19%	9.17%	9.65%
APS Earned ROE - GAAP	0.52%	9.80%	9.51%	9.58%	9.19%	9.17%	9.65%
Authorized Equity Layer	*55.80%*	*55.80%*	*55.80%*	*54.70%*			
Book equity (GAAP) %	*54.69%*	*53.13%*	*52.02%*	*52.07%*	*54.73%*	*53.19%*	*52.26%*
Equity Injection			5	260	625	10	10

Source: BofA Global Research estimates, company report

- **Renewable buildout is the path to greater cooperation with ACC.** PNW intends to shift its generation mix to 65% clean energy by 2030 (note this includes Palo Verde) by continuing its buildout of owned wind, solar, and storage and retiring Cholla in 2025. As part of its 2020-24 plan, the company intends to add 962 MW of renewable energy and 750 MW of storage, with the balance of the 2,900 MW in the plan consisting of Demand Side Mgmt, Demand Response, and Distributed Generation. *We look for whether management will be able to recover these in a rider treatment akin to its earlier AZ Sun program through the course of the pending rate case; we perceive this as increasingly key to rate case timeline and implicitly capex clarity too but don't perceive a need for pre-approval/CPCN for any of its renewables regardless. Meanwhile we anticipate a large chunk of its future renewable procurement to still be done on a PPA (rather than ownership) basis.*

- **Coal plans still key to de-risk in the rate case.** Given the uncertain treatment of the Four Corners scrubbers as part of the current rate case, mgmt. highlighted that previous dockets have laid out an evidentiary record for the need to invest in scrubbing technology and support for recovery in rates. While the rate case ask stands out for being one of the few among our coverage that actively seeks to *increase coal rate base,* PNW mgmt. stresses that Four Corners remains a key part of the company's generation mix today and expects to utilize the plant until its scheduled retirement in 2031 (itself pushed up from 2038 previously). We further note that the plant is a key employer in the Navajo Nation territory, making a potential early retirement thorny from a regulatory and political angle. PNW highlights that it sees its clean gen pivot as a key part of its strategy for enhanced cooperation with stakeholders and the ACC, noting significant support for renewables across the state.

Updated estimates

We update our PNW estimates as per below, as we increase our 2020 forecast from the low end of 2020 guidance to $4.80/sh, driven principally by the above-normal weather contribution in Q2. Our estimates are now three cents below Street consensus which itself is two cents below the midpoint of mgmt.'s guidance range. While PNW gave a relatively soft reaffirmation of 2020 guidance on its Q1 update, we see likelihood of a more confident tone on the upcoming call as a tailwind from warm Q2 weather and abating COVID-19 sales impacts has improved the near-term outlook of late, though we flag Q3 as critically important for the company's full year prospects given the importance of the peak cooling season. Looking ahead, we see an EPS CAGR of 3-4% through 2023 based on company-provided capex disclosures and assumptions around rate case filing

cadence and impacts on earned ROEs at APS. Upside to the current forecast is tempered somewhat by PNW mgmt. comments that the company intends to pursue PPA as well as utility-owned solutions for its future renewable procurement.

Capex updates

We perceive less confidence on long-dated further acceleration of current clean energy capex beyond '22, but rather more sustainable levels of investment. Meanwhile, we are critically focused on the 2Q call around the composition of just *what is reflected in its clean energy outlook.* As a reminder, the company has yet to clarify *what* specific projects are contemplated within its '21 guidance as far as clean energy investments go. We anticipate some level of details and/or risk of delay if not – but bias towards the former.

Table 43: PNW updated estimates

PNW EPS Estimates	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E	2025E
EPS From Continuing Operations	$4.55	$4.71	$4.95	$4.98	$5.30	$5.38	$5.76	$6.31	$6.34
Net Income (Loss) Attributable to Noncontrolling Interests	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17	$0.17
Income From Discontinued Operations	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
Accounting Changes/Non Operating Adjustments	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00
Linked to model - EPS	$4.37	$4.54	$4.77	$4.80	$5.12	$5.21	$5.60	$6.14	$6.18
APS - EPS From Continuing Operations	$4.66	$5.24	$5.19	$5.22	$5.55	$5.70	$6.13	$6.69	$6.72
Parent - EPS From Continuing Operations	($0.11)	($0.53)	($0.24)	($0.24)	($0.26)	($0.33)	($0.37)	($0.38)	($0.38)
Net Income (Loss) Attributable to Noncontrolling Interests	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)	($0.17)
EPS From Cont Ops Attributable to Common Shareholders	$4.37	$4.54	$4.77	$4.80	$5.12	$5.21	$5.60	$6.14	$6.18
Previous Estimates	*$4.37*	*$4.54*	*$4.77*	*$4.75*	*$5.12*	*$5.21*	*$5.60*	*$6.14*	*$6.18*
Guidance	4.15-4.30	4.35-4.55	4.75-4.95	4.75-4.95					
Consensus				$4.83	$5.07	$5.29			
Delta vs Consensus				($0.02)	$0.05	($0.07)			
EPS CAGR off 2019A				0.7%	3.6%	3.0%	4.1%	5.2%	4.4%
Street CAGR				3.1%	3.8%	3.9%			

Source: BofA Global Research estimates, Bloomberg

Valuation: PO to $78

We update our PO to $78 based on marking-to-market the electric utility peer multiple to 16.6x, from 15.6x previously. We continue to apply a -2.5x discount to PNW's consolidated '22 earnings, reflecting the unique set of regulatory risks facing the company in its sole AZ jurisdiction, notably timing of the current rate case whereby a settlement increasingly looks as if it is not an option and a *new* slate of commissioners will decide the pending proceeding – a decidedly uncertain prospect given Nov elections. Reiterate our Neutral rating as we see only modest return potential to shares at current levels.

Table 44: PNW updated SOTP

Price Objective $78	
PNW Valuation: P/E Based on 2022E EPS	
	Price Objective
2022 EPS	$5.21
Group Peer Multiple - Electric	16.6x
Group EPS '18-'22 CAGR - Electric	5.00%
P/E Multiple - Utility Average	17.4x
Premium	-2.5x
Price Objective	$78
2020 Dividend	$3.16
Dividend Yield	4.0%
Total Return (%)	1.6%

Source: BofA Global Research estimates, Bloomberg

PPL Corporation (PPL)

We remain Neutral rated on shares of PPL into the quarter. While shares have meaningfully underperformed this year, FX remains volatile with current forwards remaining at the low end of mgmt.'s assumptions (already lowered earlier this year) and we critically watch load impacts after mgmt. elected to keep guidance unchanged last quarter. While the UK is decoupled, volumes are only trued up on a two year basis and mitigating impacts in the jurisdiction could be critical to keeping guide intact. Meanwhile, we await any developments around a formal decision for a rate case in KY - which we continue to see as unlikely against the protracted pandemic and latest ROE backdrop – along with the RIIO-ED2 consultation from Ofgem expected later this month: LT ROEs in the UK remain a lingering uncertainty after latest pressure suggested by T&G drafts. Bottom line, we ultimately see risk/reward as balanced at the current valuation.

PPL 2Q20 Earnings Walk

We forecast 2Q20 adjusted EPS of $0.54 compared to $0.58 in 2Q19 & $0.56 consensus.

- **Key Drivers:** We expect COVID challenges in the UK and dilution to weigh on the quarter and offset currency tailwinds and O&M savings.

Table 45: PPL 2Q20 Walk

PPL 2Q20 Earnings Walk	EPS
2Q19 EPS	$0.58
WPD	
Rates & Loads	($0.05)
Pension Headwinds	($0.01)
FX Tailwinds	$0.05
Kentucky	
Reversal of Tax Benefit in 2Q19	($0.02)
New Base rates & Weather Against COVID Challenges	$0.00
PPL PA	
Growth & Covid Challenges	$0.01
Corp & Other	
Dilution	($0.03)
Depreciation	($0.02)
Interest	($0.01)
O&M Savings	$0.04
2Q20 BofAe Adjusted EPS	$0.54
2Q20 Consensus	$0.56
BofAe 2020E EPS	$2.45
2020 Consensus	$2.43
2020 Guidance	$2.40-2.60

Source: BofA Global Research, Bloomberg

Contemplating COVID Implications

After electing to keep guidance unchanged last quarter, we critically watch developments on load. Recall the company noted $0.03-$0.04 monthly impact in April primarily from lower electric sales in the UK and KY (2/3rds from the UK). Full disclosures noted specific early load observations and sensitivities in April: UK - +1-3% resi & (20-25%) C&I with a 1% change translating to a penny of EPS for each; PA - +6-8% resi & (15-20%) C&I with a 1% change translating to $0.005 for resi and no impact for C&I; KY - +5-7% resi and (15-20%). Given the extents of unknowns and a seemingly lack of conviction around full year guilde with 1Q results, we wouldn't be surprised for an expectation reset – albeit our estimates remain at the lower end but within their current guide.

FX Outlook: Forwards Remain Near Low End of Guide

After lowering embedded assumptions with an earlier update, FX rates and forecasts remain at the low end of the range. While the company is 86% hedged for the remainder of 2020 at an average rate of $1.55, it is only 8% hedged in 2021 at $1.32 and

completely exposed in outer years. On an open basis, every 1c in the exchange rate equates to about $0.01/sh of EPS for the company.

OFGEM Prospects: Contemplating Future UK Returns

Earlier this month, Offgem released its RIIO-2 draft proposals on price controls for the '21-26 period for transmission and gas distribution. The draft reflected a reduction of the base equity returns to 3.95% (post tax real, CPIH basis) for GT & GD, and 3.7% for ET vs. a previous 4.3% indication. The difference would appear principally driven by a change in lower interest rates reflected (and could yet change into the final decision).

While the draft proposals on Totex are 20-40% lower than business plans, the regulator indicated allowances to be considered on project by project basis instead of upfront considerations, and actual allowances could potentially be much higher than business plans. Ofgem's current base return proposal still includes a contentious -25bps adjustment justified by "information asymmetry" compared to -50bps adjustment previously included.

Shares of PPL underperformed on the news as we viewed the proposals more stringent than anticipated and as investors try to get a read-through to future returns for ED – a more protracted process that will shake out over the next couple of years. That said, the ED2 specific methodology expected later this month should provide some color around ED specific thoughts. We ultimately expect nuances between ED2 and the gas/transmission framework given different risk profiles. However, we see a desire from Ofgem to maintain incentives and give the best performing companies an ability to overearn, particularly as distribution networks will be a key enabler of the net-zero carbon target. Any developments out of the COVID crisis will also be critical in terms of nuances around their thought process for UK utilities longer term. *Our model assumes a base equity return of 3.95%, with up to 300bps of incentives.*

EPS Estimates

The table below reflects our latest EPS estimates after reflecting the latest currency forwards and on-going developments, and we see limited growth ahead given pension headwinds and questions around longer term UK returns, particularly without meaningful FX improvement.

Table 46: PPL EPS Estimates

PPL EPS Estimates	2020E	2021E	2022E	2023E
Regulated Utilities				
International Regulated	$1.39	$1.30	$1.29	$1.15
Pennsylvania Regulated	$0.62	$0.65	$0.68	$0.71
Kentucky Regulated	$0.55	$0.62	$0.68	$0.71
Domestic Utilities	*$1.18*	*$1.27*	*$1.36*	*$1.42*
Parent/Other	($0.13)	($0.12)	($0.12)	($0.10)
Consolidated EPS	$2.44	$2.44	$2.53	$2.47
Prior Estimates	*$2.45*	*$2.45*	*$2.52*	*$2.48*
Consolidated Growth CAGR off 2018 ($2.30 midpoint)	2.99%	2.04%	2.40%	1.41%
Consensus	$2.43	$2.45	$2.59	$2.76
Guidance	$2.40-2.60	$2.40-2.60		
DPS	1.66	1.68	1.69	1.71
DPS Growth (%)	*0.61%*	*1.00%*	*1.00%*	*1.00%*
DPS Payout	68.05%	68.61%	66.96%	69.33%
FFO (CFO pre-W/C) / Total Debt	15.02%	15.17%	15.51%	15.45%

Source: BofA Global Research, Bloomberg

Valuation: Risk/Reward Remains Balanced

The table below reflects our latest valuation based on a SOTP approach. On our latest estimates, we apply the current peer multiple of 17.1x (vs. 16.5x previously) for both PPL Electric and PPL Kentucky. Meanwhile, we ascribe a 25% premium to RAV for the UK biz.

Our PO ultimately remains unchanged at $27, and we continue to see risk/reward as balanced: Maintain Neutral.

Table 47: PPL SOTP

PPL Sum-of-the-Parts	EPS	Lower	Peer	Prem/ Disc.	Base	High	Equity Value Low	Base	High
RAV Approach	C2021 RAV								
WPD RAV	11,058	0.8x	1.0x	0.25x	1.3x	1.8x	$8,293	$13,822	$19,351
Less: WPD leverage (80% Gearing)							($8,846)	($8,846)	($8,846)
							($553)	$4,976	$10,505
UK Equity Value							($553)	$4,976	$10,505
Implied Valuation / Share							*-0.71*	*6.41*	*13.54*
Domestic: Regulated Utilities			2022 P/E Multiples						
Group Peer Multiple - Electric			17.1x						
Group EPS '18-'22 CAGR - Electric			5.00%						
		Base Multiple	18.0x						
PPL Electric Utilities	$0.68	17.0x		0.0x	18.0x	19.0x	$8,904	$9,429	$9,954
PPL Kentucky (KU/LG&A)	$0.68	17.0x		0.0x	18.0x	19.0x	$8,941	$9,469	$9,996
Parent/Int Expense	($0.12)	17.0x		0.0x	18.0x	19.0x	($1,526)	($1,616)	($1,706)
			50% Weighting						
PPL Cap Funding Debt	4,530		2,265				-2,265	-2,265	-2,265
Parent Interest Expense (Tax effected @ 21%)	142		71				1,204	1,276	1,347
--> Add back 50% of EPS drag above							-1,061	-989	-918
PPL Equity Value ($/Sh) Unrounded							$18.95	$27.41	$35.87
Shares Outstanding	2022 EPS						776	776	776
Total PPL Equity Value Per Share	$2.53						$19.00	$27.00	$36.00
Implied P/E							7.5x	10.7x	14.2x
Total Return Calculation									
Current Stock Price								$25.85	
Price Objective								$27.00	
Upside/Downside (%)								4.45%	
Dividend								$1.66	
Dividend Yield								6.42%	
Total Return								10.87%	

Source: BofA Global Research, Bloomberg

WEC Energy (WEC)

We expect WEC to hit the high end of its increased Q2 EPS guidance range of $0.67-0.69 for the quarter. WEC stood out as among the stronger 2020 guidance reaffirmations following Q1 reporting, with the company flagging ongoing O&M reductions above its original 2-3% forecast as an offset to an expected $70-80m gross margin drag due to sales lost resulting from Covid. The company provided an intra-quarter update where it flagged sales trending above its revised forecast, but it remains unclear whether the improving sales is due to faster-than-expected resumption of economic activity or to a higher incidence of Cooling Degree Days (CDDs) driven by unseasonably warm weather. Nonetheless, we perceive incrementally less pressure on mgmt. going into the Q2 print following the latest reaffirmation, and see the high end of 2020 guidance as well within reach.

WEC 2Q20 Earnings Walk

We forecast 2Q20 adjusted EPS of $0.69 compared to 2Q19 results of $0.74, consensus estimates of $0.67, and guidance of $0.67-0.69.

- **Key Drivers:** Weather is expected to be a key positive driver in Q2 with +3 cents from normalizing for below-normal temps in 2019 and an additional 5 cent uplift from warmer weather in 2019. While WEC has stated that Q2 sales have developed ahead of prior forecasts, we note it is unclear whether this is due to a faster reopening or to weather, accordingly we estimate an 8 cent quarterly drag from Covid lost sales based on company-provided sensitivities. American Transmission Co's (ATC) 3 cent uplift is driven by the Federal Energy Regulatory Commission's (FERC) Midcontinent Independent System Operator (MISO) order of 10.02% authorized ROE, recognizing benefits to 2015. Finally, in 2020 WEC realized the full benefits of its fuel cost recovery rider in Q1, resulting in a 2 cent drag in Q2 as compared to the prior year.

- **Unknowns**: Weather and Covid-linked shutdowns are both expected to have a disproportional impact on sales in Q2 and estimating the precise impact of both line items is difficult –warm weather along with a higher incidence of CDDs has coincided with the most acute period of lockdowns, largely mitigating the loss on our estimates. WEC maintains a Rabbi Trust to offset future legacy compensation obligations – while the trust tends to create Other Income in periods of strong market performance (as seen during Q2), the positive contribution tends to be offset in the O&M line, accordingly we do not estimate it in our walk below.

Table 48: WEC Q2 earnings walk

WEC 2Q20 Earnings Walk	EPS
2Q19 Adjusted EPS	$0.74
Weather - 2Q19 normalized	$0.03
Weather - 2Q20	$0.05
Covid impact	
Electric	($0.07)
Gas	($0.01)
Fuel cost recovery - all realized in Q1	($0.02)
Interest Expense - re-financing	($0.03)
D&A	($0.05)
O&M	$0.01
Storm expense	$0.00
ATC	$0.03
Infrastructure	$0.01
Dilution	($0.00)
Other income	$0.00
2Q20 Adjusted EPS	$0.69
2Q20 Consensus	$0.67
2Q20 Guidance	$0.67-0.69
2020 BofAe	$3.75
2020 Consensus	$3.73

Table 48: WEC Q2 earnings walk

WEC 2Q20 Earnings Walk	EPS
2020 Guidance	3.71-3.75
Share Count	
2Q19	317
2Q20	317

Source: BofA Global Research estimates, company report

Covid update and outlook

WEC last provided an update on Q2 sales expectations on its Q1 call, with the forecast below for the quarter and full-year results. An inter-quarter update from WEC disclosed that weather-normalized sales are trending above the current quarter outlook, which the full-year assumptions remain unchanged, following the lifting of state lockdown orders and resumption of business and commercial activity in a phased approach. Note that relative to 2019 normalized sales, mgmt.'s forecast calls for an annualized drop in total retail sales ex iron ore of 4.6%, with a modest 1.4% increase in residential sales offset by an 11.9% drop in C&I. While the WI Public Service Commission (WPSC) was one of the first commissions in the US to issue an order on deferral of Covid-related extraordinary items, we note the order includes bad debt and additional direct costs related to the pandemic and does not include lost revenues – we look to the Q2 update on cost cutting (where mgmt. flagged confidence) as well as weather contribution from higher than normal cooling days to provide the offset to lost revenues and allow mgmt. to hit the high end of its guidance range.

Table 49: WEC reported and forecast 2020 sales

	2020 Original	Q1 Actual	Q2 Forecast	2020 Revised
Residential	-0.2%	-4.6%	4.0%	1.4%
Small C&I	-0.3%	-2.6%	-8.0%	-4.6%
Large C&I	-1.0%	-3.1%	-18.0%	-10.5%
Total C&I	-1.2%	-2.5%		-11.9%
Total Retail	-0.6%	-3.2%		-5.3%
Total Retail ex iron ore	-0.5%	-3.4%		-4.6%

Source: Company report

Mgmt.'s Q1 announcement of an acceleration in cost cuts was predicated on offsetting an anticipated $70-80m in gross margin drag stemming from Covid. With additional Q2 data points now suggesting a meaningful weather tailwind, a key question remains whether mgmt. will continue to pursue aggressive cost reductions as originally planned, or whether an improving margin outlook will make less stringent cuts palatable. While some O&M reductions are a natural extension of telework and a reduced ability to travel, we perceive latitude to avoid certain discretionary cuts driven by better-than-expected contribution from weather during the quarter. Below we include our original estimate of O&M reductions aimed at offsetting the $70-80m of gross margin drag originally forecast from Covid-related shutdowns.

Table 50: Potential additional O&M savings; good historical success, but *where to now?*

	2016	2017	2018	2019	2020
Day to Day O&M	1,342	1,281	1,234	1,143	
y/y % chg		*-4.5%*	*-3.7%*	*-7.4%*	*-2-3%*
Addt'l O&M Cuts					
Pre-tax					75
Post-tax					63
PF Day-to-day O&M					1,052
y/y % chg					*-8.0%*

Source: BofA Global Research, company report

Infrastructure update: modest delay to Badger Hollow II

Though not particularly surprising following the announced delay of the Badger Hollow I solar facility, Badger Hollow II announced a project delay with an updated in-service date of year-end 2022 vs. year-end 2021 previously. WEC's contribution of $130m to the project is modest relative to its projected $1.8B spend during the forecast period. Given the delays are linked to Covid and staging of work crews in rural WI, we do not see the delays as indicative of further slippage or lack of execution on future projects.

Reflecting an NPV valuation across the infra segment

We update our valuation methodology for WEC. While we had previously continued to use a P/E based approach for valuing WEC's planned investment other than announced projects, we now update our approach to reflect this across the segment. We see a DCF approach as increasingly relevant given the reflection of asset lives of wind projects as well as varying risk profiles by asset type.

Table 51: Allocated and unallocated infra investment – NPV approach

Project Name	Investment	Unlevered NPV	Unlevered IRR	Capacity	In Service
Upstream Wind	307	115	8.8%	180	Jan-19
Bishop Hill III Wind	166	72	8.9%	119	May-18
Coyote Ridge Wind	145	63	8.7%	78	YE 2019
Thunderhead Wind	381	174	8.9%	270	YE 2020
Blooming Grove	389	192	8.9%	225	YE 2020
Total	1,388	616		871	
Shares		317			
Equity value per share		1.94			

Summary of unallocated CAPEX

Project Name	Investment	Unlevered NPV	Unlevered IRR	Capacity	In Service
2021 Capex	100	45	8.8%	67	YE 2021
2022 Capex	315	140	8.8%	210	YE 2022
2023 Capex	315	139	8.8%	210	YE 2023
2024 Capex	308	135	8.8%	205	YE 2024
Total	1,038	460		692	
Shares		317			
Equity value per share		1.45			

Source: BofA Global Research estimates,

Estimates: Moving to high end of '20 guidance

We update our consolidated WEC ests to reflect the high end of mgmt.'s $3.71-3.75/sh 2020 guidance range. Given the degree of confidence reflected by WEC mgmt. in the company's ability to meet its guidance following its Q1 reporting – indeed before the Q2 weather impact was fully known and before raising its quarterly guidance range – we feel comfortable at the high end of the range, even given the backdrop of continuing pressure on sales from Covid. We also tweak our ATC numbers slightly to reflect the updated FERC ROE of 10.02% plus 50 bps adder, though this has a modest impact on our numbers. Bottom line: we continue to see earnings growth near the high end of mgmt.'s 5-7% long-term guidance range through the forecast period.

Table 52: WEC updated SOTP

WEC EPS Estimates	2018A	2019A	2020E	2021E	2022E	2023E	2024E
WI Electric	$1.13	$1.15	$1.25	$1.26	$1.30	$1.34	$1.37
WPS	$0.55	$0.59	$0.56	$0.59	$0.64	$0.68	$0.71
WI Gas	$0.24	$0.26	$0.39	$0.48	$0.58	$0.67	$0.75
Peoples Gas	$0.42	$0.50	$0.44	$0.49	$0.55	$0.60	$0.65
North Shore Gas	$0.05	$0.05	$0.05	$0.05	$0.06	$0.06	$0.06
ATC	$0.36	$0.39	$0.42	$0.44	$0.47	$0.50	$0.51
We Power (PTF) + Non utility infrastructure	$0.70	$0.76	$0.77	$0.89	$0.91	$0.97	$1.03
MERC/MGU	$0.14	$0.15	$0.13	$0.14	$0.15	$0.16	$0.16
Parent & Int Expense	(0.23)	(0.24)	(0.26)	(0.38)	(0.41)	(0.43)	(0.43)
BofA Estimate	$3.34	$3.60	$3.75	$3.98	$4.25	$4.52	$4.81
Company Guidance			$3.71 -$3.75				
Prior Estimates			*$3.71*	*$3.96*	*$4.24*	*$4.51*	*$4.78*
BofA CAGR (off 2019 estimate of $3.50)			*7.24%*	*6.59%*	*6.70%*	*6.63%*	*6.56%*
Consensus			$3.73	$3.98	$4.26	$4.54	
Consensus CAGR			*6.5%*	*6.6%*	*6.7%*	*6.7%*	
Mgmt. Guidance 5-7% off $3.50 in 2019							
Low		$3.48	$3.71	$3.86	$4.05	$4.25	$4.47
Mid		$3.50	$3.73	$3.93	$4.17	$4.42	$4.69
High		$3.52	$3.75	$4.01	$4.29	$4.59	$4.91

Source: BofA Global Research, Bloomberg

Valuation

We update our valuation to reflect mark to market of electric and gas peer group multiples to 16.7x and 15.7x respectively. We additionally tweak our valuation premium applied to WI utilities to 4.0x to reflect the strong regulatory backdrop and long-term opportunity to invest in more rate base renewables. We also shift or Energy Infrastructure methodology to applying an NPV valuation to both announced as well as growth projects – recall that we had previously updated our valuation to reflect an NPV value for announced renewable projects. While execution by the mgmt remains strong and data points on sales remain constructive, we believe valuation is expensive with WEC shares trading at an implied P/E of 19.5x vs. electric/gas peer P/E of 17.5x/16.5x, respectively, reflecting 6-7% growth vs. mgmt.'s 5-7% guidance range even after the recent pullback that narrowed the premium between WEC and peers. We reiterate Underperform.

Table 53: WEC updated SOTP: raising our relative premium on WI to +4x and Bluewater to +2x; keeping renewables on DCF & IL at +1x. PTF also at +1x too.

Regulated Utilities	2022 EPS	2022 Net Income	P/E Multiple					Equity Value		
			Low	Peer	Prem/ Discount	Base	High	Low	Base	High
Group Peer Multiple - Electric				16.7x						
Group EPS '18-'22 CAGR - Electric				5.00%						
Group Peer Multiple - Gas				15.7x						
Group EPS '18-'22 CAGR - Gas				5.10%						
Applied Multiple				Electric 17.5x Gas 16.5x						
WI Electric	$1.30	413	20.5x		4.0x	21.5x	22.5x	$8,487	$8,901	$9,314
WPS	$0.64	202	20.5x		4.0x	21.5x	22.5x	$4,152	$4,354	$4,556
WI Gas	$0.58	184	19.5x		4.0x	20.5x	21.5x	$3,582	$3,765	$3,949
Peoples Gas	$0.55	173	16.5x		1.0x	17.5x	18.5x	$2,860	$3,034	$3,207
North Shore Gas	$0.06	18	16.5x		1.0x	17.5x	18.5x	$291	$308	$326
ATC	$0.47	149	18.5x		2.0x	19.5x	20.5x	$2,768	$2,917	$3,066
We Power (PTF)	$0.61	193	17.5x		1.0x	18.5x	19.5x	$3,386	$3,579	$3,772
MERC/MGU	$0.15	48	16.5x		1.0x	17.5x	18.5x	$790	$838	$886
Parent & Int Expense	-$0.41	(129)	17.5x		1.0x	18.5x	19.5x	($2,268)	($2,397)	($2,527)
Total Implied Utilities	$4.25	1,251				20.2x		$24,048	$25,299	$26,550
Non Utility Energy Infrastructure								$1,292	$1,304	$1,315
Wind projects - announced	NPV value							$616	$616	$616
Wind projects - growth	NPV value							$460	$460	$460
Bluewater	$0.04	12	18.5x		2.0x	19.5x	20.5x	$217	$229	$240
Implied Valuation Multiple					19.5x				$4.12	
HoldCo Debt Adjustment										
Add Back: 50% of Interest Expense	$0.13	40	19.2x			20.2x	21.2x	$774	$815	$855
Subtract: HoldCo Debt (Net out 50%)	2,550	(1,275)						($1,275)	($1,275)	($1,275)
Total Equity Value								$24,839	$26,143	$27,446
Valuation								$78.00	$83.00	$87.00
Price Objective									$83.00	
Upside/Downside									-5.8%	
NTM Div Yield									3.0%	
Total Return									-2.8%	

Source: BofA Global Research, Bloomberg

Xcel Energy (XEL)

Below we find 2Q20 EPS of $0.43/sh, versus a $0.48/sh Consensus and a 2Q19 estimate of $0.46/sh.

- **Drivers**: We see Covid impacting sales about -5c, associated with a 6% sales drop; note our view that 2Q was impacted less than initially anticipated, but we expect the 'base case' for Covid to remain roughly around the same (or maybe just shy of the 'up to 17c EPS impact') as we think more impact could come later this year (e.g. if there is another shut-down or delay of openings). We expect this is balanced by +3c of O&M savings; while XEL communicated a 4-5% decrease YoY in O&M, we expect these to be more back-end loaded.

- **Others**: Rate changes in Minnesota (+4c), Colorado (+2c), and one month of NM (+0c) are not to be ignored. AFUDC was adjusted to $25-35mn annually (+1c) and capital rider revenue continues to add +2c. Interest expense (-2c) is in line with annual $50-60mn guidance, increase in D&A expense (-4c) is back end loaded, and property tax (-1c) is in line with annual $35-45mn guidance.

- **Unkown:**: Weather's return to normal was -1.4c and we expect another -1c of mild weather this quarter (which could be a wild card).

Table 54: XEL EPS Walk 2Q20

Xcel Energy 2Q20 Earnings Walk	EPS
Ongoing EPS 2Q19	$0.46
Weather	
Return to normal (1.4c of adverse impact)	($0.01)
Current quarter	($0.01)
Rate Changes	
NSPM Minnesota Electric Interim sales true up & Nuke decommissioning ($122mn, Jan 2020)	$0.04
PSCo Colorado - Electric rates ($35mn, Feb 25 2020)	$0.02
SPS New Mexico - Electric rates ($31mn, 1 month in 2Q20)	$0.00
SPS Texas - Electric rates (requested $136mn, 3Q20)	$0.00
Capital rider revenue	$0.02
AFUDC	$0.01
Other	
Interest Expense increase	($0.02)
Increase in D&A expense	($0.04)
O&M (we assume 4-5% decrease, but more back-end loaded)	$0.03
Property taxes	($0.01)
COVID 2Q impact (up to -17c '20 impact in base case)	($0.05)
Bad debt (would be considered in O&M)	*$0.00*
Dilution (settled)	($0.00)
2Q20E Adjusted EPS	$0.43
2Q20E BofA Securities Estimate	0.43
2Q20 Consensus	0.48
2020 BofA Securities EPS	$2.78
2020 Consensus	2.77
2020 Guidance	2.73-2.83
Shares Outstanding 2Q19	516
Shares Outstanding 2Q20	525
Tax rate	25%

Source: BofA Global Research estimates, company report, Bloomberg

Adj capex to incl. 50% Minnesota stimulus

Adjusting incremental capex into our numbers: 50% probability weighting

Of the $3bn capex proposed with XEL's MN stimulus filing, roughly half is intended to accelerate capex already planned in later years of the 5-year outlook (e.g. distribution and natural gas spend). The other half is for newly proposed projects (e.g. wind repowering presumably under latest PTC extension, solar, and electric vehicle spend).

Capex opportunities likely include $1-1.4bn of wind repowering ('21-23), $650mn of solar ('23-25), and $100-150mn of EV infrastructure ('anytime' but we would expect '21-'25). It is unclear to us how the accelerated capex for already planned distribution and nat gas spend would re-arrange existing capex plans.

We provide details on how we include in our numbers below. We factor in a 50% probability weighting that the incremental capex is added in full, and we take an average of the assumed capex ranges per item. For example, wind repowering's $1-1.4bn capex opportunity averages to $1.2bn; with a 50% probability, we factor in $600mn of additional capex to the years '21-'23 – or $200mn each year in '21-'23. The same applies for solar ($108mn each year in '23-25) and EV infra ($12.5mn in '21-'25).

Bottom line, we see this as a net positive datapoint to shares and highlighting an emerging angle to capex. Moreover, we see the capex step-up as among the only such increases thus far in the sector; expect financing update discussion with 2Q as well pending success of filing. This critically drives cumulative gross EPS of ~$0.10 by 2025, or net of equity, ~$0.07 upside on our probability weighted basis. Upside to our ests below do not *directly* tie to this given other model refinements.

Table 55: Incremental capex factored into our Minnesota capex

Incremental capex associated with Minnesota stimulus (keeping the remaining 'accelerated' as is)						Prob. weight:	50%
Type	Details	2021	2022	2023	2024	2025	Total
Wind repowering	$1-1.4bn in '21-23	200	200	200			600
Solar	$650mn '23-'35			108	108	108	325
EV infrastructure	$100-150mn anytime	12.5	12.5	12.5	12.5	12.5	63
Total	$1.75-$2.20bn	213	213	321	121	121	988

Source: BofA Global Research estimates, company report

Below, we reflect how our capex numbers have been adjusted in our model. We leave existing capex as is (i.e. don't pull forward Minnesota capex associated with accelerated distribution and natural gas proposed spend) and we add in the incremental capex associated with wind renewables above.

Table 56: BofA modeled capex for XEL

Subsidiary	2015A	2016A	2017A	2018A	2019A	2020E	2021E	2022E	2023E	2024E	2025E
NSPM	1,855	1,205	1,017	1,150	1,417	2,025	1,793	1,883	2,121	1,966	1,966
SPS	600	513	560	1,021	844	1,025	530	700	750	800	800
PSCo	996	1,114	1,476	1,577	1,691	1,415	1,445	1,720	1,565	1,530	1,530
NSPW	252	204	219	227	212	250	320	345	350	425	425
Parent	(18)	220	48	(17)	61	(85)	(65)	10	10	10	10
Consolidated	3,683	3,256	3,319	3,957	4,225	4,630	4,023	4,658	8,726	4,731	10,368

Source: BofA Global Research estimates, company report

Recovery and commission procedures

We would anticipate the company looks to recover spend for wind repowering and solar incremental investments through its renewable rider, and spend for advanced grid through its transmission rider. Note the wind repowers would likely qualify for the 60% production tax credit (PTC) if equipment is safe-harbored this year in 2020. We expect the rest to fall under a sought after enhanced recovery mechanism that will be determined by the Commission. We also await developments on a wider effort to delay its rate case altogether and see the formal indication of such in this filing as a positive step.

More details on the capex positive: MN is first to stimulus program

As noted in our first take here, Xcel's Northern States Power Company Minnesota (MN) biz recently filed a proposal for $3bn accelerated and additional capex in the state. This will likely create new jobs in an effort to counter-balance 400,000 unemployment filings in MN from Covid and the economic shut-down. This is the first proposal of its kind nationally for a return to infrastructure 'stimulus' programs (akin to efforts in the 2008 GFC). Likely the first of several others – both in terms of peers following suit and XEL's other jurisdictions as well.

Fate of the docket: We see positively and giving rise to more

The filing seems likely to gain key support for two reasons. 1) It was made in response to the MN Public Utilities Commission (PUC) request from May to examine what utilities can do to spur jobs and economic development. 2) It will be in line with labor goals. We expect an update by later this year from the MN PUC as creating jobs amid a pandemic is a timely item, and we would also expect XEL to consider opportunities like this in other jurisdictions - particularly CO.

Next key datapoint: What happens with rate cases?

In its filing, the company expressed it would be open to staying out of a rate case in MN this year – in line with mgmt. commentary. Recall XEL was expected to file at the end of 2019 but was able to stay-out, meaning this would be the second stay-out. Whether this is possible will not be determined through this docket but rather was expressed by XEL as one way it could keep customer rates down. We expect to see discussion in the coming months of what XEL would need to file to pursue another stay-out. We would expect XEL to look similarly to CO as well – and that in both states it will expect to recover spend through existing trackers.

Estimates

We include our latest estimates below, highlighting capex changes made to the model as well as our assumption that 30% of this incremental capex (i.e. nearly $300mn) is funded with incremental equity. We include this additional equity need into our assumptions and find the EPS CAGR to be above midpoint of the 5-7% guide starting in '21 and beyond. Note that the our '20 estimates are the same as prior assumptions, given that while there was less Covid impact in 2Q than originally anticipated (just -5c we forecast associated with a 6% sales drop), there could be more impact on demand later this year given resurfacing concerns. XEL's base case includes 'up to 17c' of Covid impact for '20.

Table 57: XEL EPS Estimates

Subsidiary	2016A	2017A	2018A	2019E	2020E	2021E	2022E	2023E	2024E
Northern States Power Minnesota (NSPM)	0.96	1.01	0.96	1.05	1.11	1.28	1.39	1.46	1.53
Southwestern Public Service (SPS)	0.30	0.30	0.42	0.51	0.59	0.60	0.63	0.65	0.67
Public Service Colorado (PSCo)	0.91	0.94	1.08	1.11	1.07	1.11	1.17	1.24	1.32
Northern States Power Wisconsin (NSPW)	0.14	0.16	0.19	0.15	0.16	0.18	0.20	0.21	0.23
Parent (Excl Mankato)	(0.10)	(0.12)	(0.18)	(0.17)	(0.16)	(0.16)	(0.18)	(0.20)	(0.21)
Consolidated	2.21	2.29	2.47	2.64	2.78	3.00	3.20	3.36	3.55
EPS Growth (%)			*8%*	*7%*	*5%*	*8%*	*7%*	*5%*	*6%*
Prior Estimates			*2.47*	*2.64*	*2.76*	*2.94*	*3.14*	*3.33*	*3.51*
Guidance (Excl Mankato)	2.17-2.22	2.25-2.35	2.45-2.49	2.60-2.65	2.73-2.83				
Consensus			2.46	2.62	2.77	2.96	3.13	3.32	3.44
Mgmt EPS CAGR: 5-7% off 2018 base ($2.43)	2.21	2.29	2.47	2.60	2.78	2.95	3.12	3.31	3.51
		low	*2.43*	*2.55*	*2.73*	*2.87*	*3.01*	*3.16*	*3.32*
		high	*2.43*	*2.65*	*2.83*	*3.03*	*3.24*	*3.47*	*3.71*
BofAe CAGR '18-'23e (off $2.43)	6.7%								
BofAe CAGR '18-'24e (off $2.43)	6.5%								
Target FFO/Debt			17%	18%	17%	17%	17%		
BofAe FFO/Debt		22%	19%	19%	17%	18%	17%	17%	

Source: BofA Global Research estimates, company report, Bloomberg

Valuation

We MtM our peer multiple to 16.3x from 16.7x before. We maintain our PO of $62.50/sh (unch vs prior) and we reiterate our Neutral rating as we factor in our 50% probability weighted Minnesota capex opp'y to the model. We note this still needs regulatory approval.

Table 58: XEL SOTP

2022E SotP Analysis - BofA All figures in USD millions except per share										
Regulated Utilities	2022 Net Income	EPS	P/E Multiple					Equity Value		
			Bear	Peer	Prem/ Discount	Base	Bull	Bear	Base	Bull
Group Peer Multiple - Electric				16.3x						-
Group EPS '18-'22 CAGR - Electric				5.00%						-
										-
Relative Utility Group P/E Multiple				17.1x						
Northern States Power Minnesota (NSPM)	$748	$1.39	19.1x	17.1x	3.0x	20.1x	21.1x	$26.54	$27.93	$29.32
Southwestern Public Service (SPS)	$339	$0.63	19.1x	17.1x	3.0x	20.1x	21.1x	$12.04	$12.67	$13.30
Northern States Power Wisconsin (NSPW)	$106	$0.20	19.1x	17.1x	3.0x	20.1x	21.1x	$3.76	$3.95	$4.15
Public Service Colorado (PSCo)	$630	$1.17	19.1x	17.1x	3.0x	20.1x	23.1x	$22.35	$23.52	$27.03
Total/Average Utility Earnings (excl Mankato)	$1,824	$3.38			3.0x					
Parent/Unallocated (excl Mankato)	-$99	-$0.18	19.1x	17.1x	3.0x	20.1x	21.1x	-$3.50	-$3.69	-$3.87
Add back 50% of HoldCo interest	$70	$0.13	19.1x	17.1x	3.0x	20.1x	21.1x	$2.50	$2.63	$2.76
Less: 50% of HoldCo Debt	-$2,462							-$4.57	-$4.57	-$4.57
Total	$1,725	$3.20						$59.11	$62.44	$68.11
Shares Outstanding (2022e)									*539*	
Total Equity Value Per Share								$59.00	$62.50	$68.00
Dividend FY20									1.72	
Dividend Yield									2.7%	
Total Potential Return Projected								-5%	1.0%	10%

Source: BofA Global Research estimates, company report, Bloomberg

Table 59: Stocks Mentioned

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
LNT	LNT US	Alliant Energy Corp	US$ 49.99	A-1-7
AEE	AEE US	Ameren Corp	US$ 73.24	A-1-7
AEP	AEP US	American Elec Power	US$ 82.91	A-1-7
AWK	AWK US	American Water	US$ 126.46	A-3-7
ED	ED US	Consolidated Edison	US$ 85.47	A-2-7
DTE	DTE US	DTE Energy	US$ 100.76	A-2-7
DUK	DUK US	Duke Energy	US$ 86.65	A-2-7
EIX	EIX US	Edison Intl	US$ 60.01	B-2-8
ETR	ETR US	Entergy Corp.	US$ 96.45	A-1-7
WTRG	WTRG US	Essential Utilities	US$ 42.24	A-2-7
EVRG	EVRG US	Evergy	US$ 59.12	A-1-7
ES	ES US	Eversource Energy	US$ 87.77	A-3-7
FE	FE US	FirstEnergy	US$ 44.49	A-1-7
PNW	PNW US	Pinnacle West Capit	US$ 76.60	A-2-7
PPL	PPL US	PPL Corp.	US$ 25.25	B-2-8
WEC	WEC US	WEC Energy Group Inc	US$ 95.88	A-3-7
XEL	XEL US	Xcel Energy	US$ 64.35	A-2-7

Source: BofA Global Research, Bloomberg

Price objective basis & risk

Alliant Energy Corporation (LNT)
Our $54.5 PO is based on a sum of the parts analysis employing relative premium and discounts to the large cap regulated peer multiple of 17.1x 2022E P/E. While our PO is on a 1 year basis we note the 2022 P/E multiple reflects a discount back to 2019. We note that electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. We apply a 2.0x P/E premium on IPL as we see the ratecase overhang being resolved. We apply a 3.0x P/E premium on Eastern Wisconsin Electric Company reflecting 1) low risk investment nature of the state, 2) above average ROEs, 3) higher than average growth runway for investments, and 4) bad debt deferral. At ATC, we reflect a 2.0 x P/E premium on LNT's 16% share in the transmission company. Growth expectations for this segment are high, paired with above average ROEs that we believe face less downward pressure vs. regulated state distribution ROEs. We apply an in line multiple at the parent to account for the blend of numerous businesses some which benefit from long term stable PPAs via intercompany generation. Risks to our price objective are: 1) adverse rate case outcomes, 2) further equity dilution beyond our estimates, 3) interest rate risk, 4) natural disasters, and 5) lower allowed ROEs.

Ameren Corporation (AEE)
Our $79 price objective is predicated on a P/E based sum of the parts, valuing each business subsidiary relative to the 2022E ratebase weighted peer multiple of 16.3x for electric. We apply a 2.0x premium to peers at AEE Missouri to account for the improving prospects of capital spend, supplemented by a regulatory jurisdiction becoming more favorable - but lack of decoupling. We apply a 3.0x premium to peers at AEE Illinois to account for decoupling on the distribution business which aids in earnings predictability. The overall business is expected to grow at a more meaningful clip than that of peers - we see a 10% EPS CAGR at IL 2020-2024. At ATXI, we apply a 0x premium to peers to reflect the latest potential step down in FERC ROEs. At the Parent, we assume an in line multiple given the healthy debt metrics with FFO/Debt at 17%+. Electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector.

The upside (downside) risks to our price objective are the utilities earning their allowed returns or better (worse), a significant increase (decrease) in 30-year U.S. Treasury bond yields, and positive (adverse) regulatory outcomes that could impact mgmt's ability to earn its allowed return

American Electric Power (AEP)
Our price objective of $88 is based on SOTP analysis. We ascribe a peer forward P/E multiple (17.1x) with a 1.0x premium for its transmission-only Utilities segments, a 1.0x premium for its T&D utilities, and a 0x premium for regulated utilities as well as 2x for Kentucky Power. We note that electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. We assume 100% likelihood of the North Central wind project and assign it a 0x premium under the reg utes as well.

Downside risks to our price objective are 1) regulatory outcomes are less favorable than expected, which could result in reduced ROE, 2) large capital intensive are subject to delays or cost overruns, which can change the return profile, 3) natural disasters or catastrophic events can affect system reliability and are subject to regulatory cost recovery risk, 4) utilities are subject to interest rate risk to fund their business, which affects cost of capital, 5) commodity risk affects the generation business margins and indirectly affects the regulated business as a pass through cost, 6) consumer advocates are focused on bill inflation, which can affect regulatory outcomes, 7) non-regulated businesses are inherently more risky and subject to execution risk and commodity variation.

American Water Works (AWK)
Our PO for American Water Works is $135. We apply the sector average 26.9x (vs. 26.3x) to American Water's 2022E earnings based on the water peer multiple and a 8.1% group EPS CAGR for '18-'23E. We think this multiple is justified as in our view AWK largely drives the peer multiple as the largest publicly traded water utility. We ascribe a 3x premium for NJ, PA, and IL, and a -3x discount to the military biz. Meanwhile, we ascribe a 12x multiple to the non-regulated Retail biz. Also a -1x P/E for Cali utility. no prem/discount for 'Other' segment with smaller state exposures.

Risks to the downside are increase in market interest rates, potential impact of tax reform on utilities, operational errors, changes in valuation levels for water utilities. Risks to the upside are accelerating muni acquisitions, multiple expansion, and constructive legislation in regulatory jurisdictions

Consolidated Edison (ED)
Our $86 PO is based on a sum-of-the-parts analysis applying premiums and discounts to the regulated group multiples (16.8x/15.8x for electric/gas respectively) with a 1.0x premium to reflect defensive nature of the stock, and -1.0x discount on Steam to reflect lack of decoupling / weather risk. We note that both electric and gas peer P/E multiples are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We applied inline peer regulated multiple at CECONY despite its rate certainty for conservatism as our higher capex expectations are reflected in our EPS outlook. We apply a discounted PE for infrastructure projects given the lack of clarity around the capital structure. We further apply an EV/EBITDA approach on 2022E EBITDA to the CEB business using a 10.0x multiple for both the legacy portfolio and the renewables portfolio seeing it as having higher quality returns.

Downside risks: ED, like all utility stocks, is also sensitive to changes in the market level of interest rates. Utilities historically underperform if bond yields rise, and outperform when they fall. Further downside risks are the inability to recontract storage, adverse regulatory outcomes, a deteriorating regulatory environment, or unforeseen disasters such as the Harlem gas explosion, the SRE transaction not being completed. Customer inflation is also a downside risk. PCG related counterparty exposure is among the nearest exposures to watch.

DTE Energy (DTE)
We value DTE Energy at $115 using a SOTP approach.
We value the utility segment on a 2022E forward P/E multiple basis and the non-utility seg. on a 2022E forward EV/EBITDA multiple basis. For the utility segment we apply a 2x premium to our both reg. electric and gas utility peer multiple of (16.5x and 15.6x respectively). Both electric and gas peer P/E multiples are grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We subtract out Corp & Other expense excl. interest rate.
For GSP we use a midstream peer group multiple of 9x, with a -1x discount for Momentum. P&I, we apply an 8x EV/EBITDA multiple, despite the lower equality of these earnings and opaque disclosures, as mgmt has been able to execute on new project origination. We value the reduced emissions fuel (REF) tax credits separately using a DCF methodology at 6% discount rate.

Upside risks to our PO are capex expansions, higher authorized ROEs, and strong performance in the ET segment. Downside risks are interest rate hikes, execution risk on organic growth initiatives at the nonregulated business, and less favorable regulatory environment.

Duke Energy (DUK)
Our $87 PO is derived from a sum-of-the-parts valuation. We value the Electric and Gas utilities using peer 2022E P/E multiples. We apply a 1.0x multiple premium to Duke's

operations in FL/IN to reflect more favorable regulatory environments. We apply an in-line multiple to the Carolinas given risk ahead. We value the other regulated electric utilities at 17.1x and the gas utilities at peer group multiples of 15.9x 2022E P/E, respectively. Both electric and gas peer P/E multiples are grossed up by 5% for the groups CAGR to reflect capital appreciation across the sector. The commercial midstream, and transmission are valued on a 2022E EV/EBITDA basis. We use a 9.0x multiple for midstream and transmission segment. We add the net present value of renewable segment using an 8% discount rate. We subtract out the impact of commercial debt, and add back for the renewable debt.

Upside risks: constructive rate case results, higher capital expenditure additions vs our assumptions, lower interest rates. Downside risks: poor rate case results, operating errors, and negative changes in the regulatory environment, Macro risks: Increases in interest rates and decreases in equity market valuations.

Edison International (EIX)
Our $65 PO is based on SOTP, applying a 4x disc to the FERC and CPUC jurisdictional subsidiaries, and the parent/other segment 17.1x on 2022E (grossed up by 5% to reflect capital appreciation across the sector). The disc reflects CA ongoing wildfire risk despite the improved construct through AB1054. We apply 10x 2022E P/E to the Edison Energy segment to reflect uncertainty in the nascent biz. We net out ongoing contribution to the fund on an NPV basis.

Downside risks: 1) Regulatory outcomes less favorable than expected. 2) Natural disasters or catastrophic events can affect system reliability and are subject to regulatory cost recovery risk. 3) Interest rate risk. 4) Non-reg businesses are inherently more risky and subject to both execution risk and commodity variation. 5) CA has specific risks given the differentiated regulatory regime. 6) CA wildfires.
Upside risks: rate case outcome above what's embedded in companies' guidance and BofA estimates, lower interest rates, more constructive regulatory / legislative outcomes to address wildfire risk

Essential Utilities (WTRG)
Our price objective is $47 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. We apply a 2.0x premium to Peoples Gas given the organic growth opportunities.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Risks to the upside include upward revisions to street estimates and further accretion from implementation of the Repairs Tax Benefit.

Evergy, Inc (EVRG)
Our $68 price objective for EVRG shares is based on sum of the parts valuation, applying an in-line utility peer 2022E P/E of 17.1x. Electric peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We further apply a +2.0x turn discount across all jurisdictions based on our perception of improving regulatory relationships and possibility of further stakeholder engagement.

Downside risks to our price objective are adverse regulatory outcomes in rate cases, higher interest rate environments, adverse and unexpected risks associated with operating a nuclear facility, the possibility that the strategic review committee does not result in a transaction recommendation and that a modified standalone plan disappoints in rate base and earnings growth when presented later in 2020.

Upside risks to our price objective are favorable regulatory outcomes in rate cases, lower interest rate environments, higher than anticipated O&M benefits and merger synergies, ability to recover capital tied to retired coal plant.

FirstEnergy (FE)
Our PO of $45.5 is based on a SOTP: Multiples are driven by relative P/E premiums/discounts to the 2022 regulated peer multiple of 17x (previously 16.9x) . Electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. As for premiums/discounts, we view NJ as in-line given a generally constructive commission, PA as in-line as we view our more punitive ests already account for industrial load sensitivity incl O&G royalties, and others as in-line. In OH, we apply a -1x P/E discount multiple, We argue this accounts for overearning risk. Finally, we apply a 0x P/E premium to peers 2022E multiple to the Transmission business given some limited ability to invest and FERC ROE difficulties. We removed impact of DMR payments. We subtract out the holding co debt given the high parent lev. We net out potential liabilities from a potential FES bankruptcy by assuming all known 'extra' potential liabilities.

Downside risks: 1) Reg outcomes may improve/deteriorate, 2) legislative solutions may materialize for challenged parts of biz or FE could lose/fail to gain legislative support in key states, 3) int rates positively/negatively affect cost of cap, 4) reg staff or cons advocates may focus on issues beneficial/detrimental to ROEs, 5) exit from comp power biz may or may not have substantive liabilities accrued to equity holders.

Pinnacle West (PNW)
Our price objective of $78 is based on a peer utility 2022E P/E multiple of 16.6x with a -2.5x discount to account for PNW's risk around its pending rate case as well as headline risk related to disconnect policy review. Electric and gas peer P/E mult is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We ascribe an in-line premium despite clear renewable capex backdrop given ongoing regulatory risk associated with the company's upcoming rate filing and 2020 election risk.

Upside risks: 1) Regulatory relationships/outcomes could improve, including changes at the elected commission 2) load growth in territory above expectations 3) Riders and capital trackers could help achieve ROE 4) positive weather helps earnings 5) interest rate risk changes cost of capital - lower rates could improve 6) Consumer advocates or utility staff could become focused on issues that improve ROE

Downside risks: 1) Regulatory relationships/outcomes could decline, including changes at the elected commission 2) load growth in territory below expectations 3) Riders and capital trackers could hurt ROE 4) negative weather hurts earnings 5) interest rate risk changes cost of capital - higher rates could worsen 6) Consumer advocates or utility staff could become focused on issues that hurt ROE 7) Solar advocates in the state have engaged in public confrontations with the utility, which could change public relations in the future.

PPL Corporation (PPL)
Our $27 price objective is based on a sum of the parts methodology applying respective premium/discounts to the 2022E peer group multiple of 16.5x. Electric peer P/E multiple is grossed up by 5% to reflect capital appreciation across the sector. We apply a 1.25x RAV multiple in our base case for our Western Power Distribution (WPD) RAV approach, seeing the higher ROEs relative to other distribution networks commanding a premium valuation.

Downside risk to our price objective is exposure to FX rates. Since the UK segment represents a significant portion of PPL's earnings, a Federal Reserve decision to raise interest rates could produce a fall in the GBP/USD currency rate that would adversely

affect our estimates and valuation for PPL. Also, like all utility stocks, PPL has historically underperformed if bond yields rise. Upside risks are a rising $/pound (GBP) price, positive regulatory outcomes, and decreasing treasury yields.

WEC Energy Group Inc (WEC)
Our $83 PO is based on a 2022E SoTP analysis, based on the large cap electric group multiple of 16.7x and the gas regulated multiple of 15.7x. Both electric and gas peer P/E multiples are grossed up for a year to reflect capital appreciation across the sector.

We apply a 4.0x premium to WEC's WI electric & gas subs to compensate for surety in earnings growth for the next two years following the Commissions affirmation of the recent settlement on above average ROE's of 10%+. We apply a 1x premium to the gas utilities, incl IL's Peoples Gas and North Shore Gas with the Gas System Modernization Program (GSMP) and capex forecasts de-risked following the ICC order. We ascribe a 2x premium vs. the group at ATC to account for the steady nature of earnings growth as well as above average ROE's that are set at a federal level by FERC. We give Power the Future (PTF) a 1.0x premium multiple given the ROE is set indefinitely on historical and new investments. We ascribe an in line multiple for the parent accounting for the interest expense which finances overall utility operations. For the HoldCo adjustment to debt, we net out 50% of HoldCo debt from equity valuation and adjust to add back the parent drag on interest exp.

Upside risks are stronger than expected execution and accelerating capital oppt'y.

Downside risks are inability to achieve historical track record on cost cutting and ability to cont. to scale regulated investments given growing portion from contracted renewables.

Xcel Energy Inc (XEL)
Our PO is $62.5. We value Xcel Energy using a sum of the parts (SOTP) approach. Given the difference in geography, earnings strength, growth opportunity and risk profile, we divide the segments by subsidiary.

We use 2022E forward P/E multiples to derive a value for the different business segments, including the parent segment. We use a peer multiple of 16.3x . Electric peer P/E multiple is then grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector. We apply a 3x premium to subsidiaries. We see this multiple as appropriate as the company has growth opportunities, resolving regulatory drag and resolving uncertainty around rate cases. We stripped Mankato as a non-reg asset in our SOTP due to the sale. We also net back 50% of the parent interest expense and instead subtract out 50% of parent debt to more accurately reflect HoldCo leverage.

Downside risks are interest rate increases, regulatory risk such as lower authorized ROEs or less favorable riders/trackers for renewables and transmission, interest rate risk, execution delays, and weather anomalies.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AES	AES	AES US	Julien Dumoulin-Smith
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
NEUTRAL				
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	El Paso Electric Company	EE	EE US	Julien Dumoulin-Smith
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith

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Important Disclosures

Equity Investment Rating Distribution: Utilities Group (as of 30 Jun 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	76	51.01%	Buy	56	73.68%
Hold	33	22.15%	Hold	22	66.67%
Sell	40	26.85%	Sell	29	72.50%

Equity Investment Rating Distribution: Global Group (as of 30 Jun 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1632	52.21%	Buy	1031	63.17%
Hold	711	22.74%	Hold	444	62.45%
Sell	783	25.05%	Sell	407	51.98%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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Essential Utilities

All Aboard: Upgrading to Buy as WTRG Plan More than Just Holds Water

Rating Change: BUY | PO: 52.00 USD | Price: 47.27 USD

Execution Remains Strong Despite Pandemic Backdrop

Following a strong 2Q and mgmt. affirmation of guide, we are jumping back in to WTRG and upgrading from Neutral to Buy. We see shares as poised to outperform with consistent quarterly execution to drive EPS of $1.53-$1.58 this year and the 5-7% EPS CAGR through '22, and stress incremental upside opportunities as acquisitions continue to materialize across their water footprint (we stress sharp contrast vs. peer AWK who already reflects acquisitions in guide). With favorable transaction legislation now enacted in all eight of their Aqua jurisdictions, we expect water rate base to grow well in excess of the 6-7% outlined through '22: the further municipal budget strain from the ongoing pandemic will likely accelerate consolidation in the industry at an even faster pace - and we expect additional developments over the next several months (after closing two deals already in '20 with four add'l signed agreements translating to ~$300Mn of rate base & ~$15Mn of earnings). Meanwhile, the 2,700 miles of pipe replacement at the recently acquired Peoples Gas segment will help drive 8-10% organic rate base through '22 and beyond - while mgmt. benefits from repairs tax treatment at the sub in PA to drive returns without the need for a rate case (with the repairs tax catch up component filed with the commission last Thurs providing even more latitude). With a growing focus on ESG – and mgmt.'s proactive action around PFAs – we see this an underappreciated angle not reflected at the current valuation (particularly vs. peer AWK with an elevated premium). Bottom line, we see shares as poised to re-rate higher given consistent execution, elevated growth prospects, and increasing appreciation for clean quality stories.

Upgrading to Buy

While our estimates are largely unchanged, we have increasing conviction in mgmt.'s ability to consistently deliver and see the company as a prime beneficiary of further consolidation across the water industry - while the latest filing for the catch up component of Repairs Tax treatment in PA should provide further latitude to stay out of rate cases for the gas segment. After applying slightly higher premiums and marking to market for the latest water and gas multiples (28.1x and 16.3 vs. 26.9x and 15.9x previously), our PO ultimately shifts to $52 (from $47 previously). Upgrade to Buy.

Estimates (Dec)

(US$)	2018A	2019A	2020E	2021E	2022E
EPS	1.41	1.47	1.56	1.69	1.80
GAAP EPS	1.41	1.47	1.56	1.69	1.83
EPS Change (YoY)	3.7%	4.3%	6.1%	8.3%	6.5%
Consensus EPS (Bloomberg)			1.53	1.66	1.79
DPS	0.86	0.92	0.99	1.06	1.13

Valuation (Dec)

	2018A	2019A	2020E	2021E	2022E
P/E	33.5x	32.2x	30.3x	28.0x	26.3x
GAAP P/E	33.5x	32.2x	30.3x	28.0x	25.8x
Dividend Yield	1.8%	2.0%	2.1%	2.2%	2.4%
EV / EBITDA*	9.5x	36.6x	20.1x	18.5x	17.2x
Free Cash Flow Yield*	-1.1%	-1.8%	-3.7%	-2.6%	-2.1%

* For full definitions of *iQmethod℠* measures, see page 8.

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Refer to important disclosures on page 9 to 11. Analyst Certification on page 6. Price Objective Basis/Risk on page 6. 12177433

Timestamp: 10 August 2020 08:04AM EDT

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10 August 2020

Equity

Key Changes

(US$)	Previous	Current
Inv. Opinion	B-2-7	B-1-7
Inv. Rating	NEUTRAL	BUY
Price Obj.	47.00	52.00

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Stock Data

Price	47.27 USD
Price Objective	52.00 USD
Date Established	10-Aug-2020
Investment Opinion	B-1-7
52-Week Range	30.40 USD - 54.52 USD
Mrkt Val (mn) / Shares Out (mn)	11,588 USD / 245.2
Average Daily Value (mn)	42.81 USD
BofA Ticker / Exchange	WTRG / NAS
Bloomberg / Reuters	WTRG US / WTRG.N
ROE (2020E)	8.6%
Net Dbt to Eqty (Dec-2019A)	31.1%

ESG: Environmental Social Governance

PFA: Perfluoroalkoxy Polymer-Chemical Compound

iQprofile℠ Essential Utilities

*iQ*method℠ – Bus Performance*

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Return on Capital Employed	3.9%	3.5%	5.3%	5.0%	5.1%
Return on Equity	9.7%	8.9%	8.6%	8.2%	8.9%
Operating Margin	38.7%	38.4%	64.5%	66.5%	68.3%
Free Cash Flow	(127)	(212)	(428)	(304)	(246)

*iQ*method℠ – Quality of Earnings*

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Cash Realization Ratio	1.9x	1.3x	1.7x	1.8x	1.7x
Asset Replacement Ratio	3.4x	3.5x	3.1x	2.8x	2.5x
Tax Rate	NM	NM	10.0%	10.0%	10.0%
Net Debt-to-Equity Ratio	127.1%	31.1%	98.4%	106.0%	112.7%
Interest Cover	2.8x	3.1x	3.4x	3.4x	3.4x

Income Statement Data (Dec)

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Sales	835	886	955	1,005	1,053
% Change	3.7%	6.2%	7.7%	5.3%	4.8%
Gross Profit	838	890	1,551	1,656	1,752
% Change	3.5%	6.2%	74.3%	6.8%	5.8%
EBITDA	1,941	504	916	997	1,074
% Change	-86.4%	-74.1%	81.8%	8.8%	7.8%
Net Interest & Other Income	(99)	(100)	(181)	(195)	(215)
Net Income (Adjusted)	192	263	371	402	450
% Change	-19.9%	36.9%	41.2%	8.3%	12.0%

Free Cash Flow Data (Dec)

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Net Income from Cont Operations (GAAP)	192	225	397	431	457
Depreciation & Amortization	147	156	338	371	402
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	(15)	(10)	(75)	(75)	(75)
Other Adjustments, Net	45	(32)	(38)	(6)	(5)
Capital Expenditure	(496)	(550)	(1,050)	(1,025)	(1,025)
Free Cash Flow	-127	-212	-428	-304	-246
% Change	-31.5%	-66.5%	-102.1%	28.9%	19.2%

Balance Sheet Data (Dec)

(US$ Millions)	2018A	2019A	2020E	2021E	2022E
Cash & Equivalents	4	1,869	6	6	7
Trade Receivables	101	108	188	200	212
Other Current Assets	42	36	50	52	54
Property, Plant & Equipment	5,930	6,346	10,657	11,312	11,935
Other Non-Current Assets	887	1,003	1,003	1,003	1,003
Total Assets	6,964	9,362	11,904	12,574	13,211
Short-Term Debt	160	131	126	141	155
Other Current Liabilities	239	188	244	253	261
Long-Term Debt	2,398	2,943	4,597	5,138	5,653
Other Non-Current Liabilities	2,158	2,219	2,144	2,069	1,994
Total Liabilities	4,955	5,481	7,111	7,601	8,063
Total Equity	2,009	3,881	4,793	4,973	5,148
Total Equity & Liabilities	6,964	9,362	11,904	12,574	13,211

* For full definitions of *iQmethod*℠ measures, see page 8.

Company Sector

Water Utilities

Company Description

Essential Utilities is a regulated water/gas providing water or wastewater services to 3M customers in the states of PA, OH, TX, IL, NC, NJ, IN, and WV, with PA segment being the largest contributor to the NI - along with a natural gas presence through the recently acquired Peoples Gas providing distribution services to 740,000 customers in PA, WV, and KY.

Investment Rationale

We are Buy rated on shares of WTRG, seeing shares as poised to re-rate higher given consistent execution, acquisition upside, and increasing conviction around the premium story.

Stock Data

Average Daily Volume	905,604

Quarterly Earnings Estimates

	2019	2020
Q1	NA	NA
Q2	NA	NA
Q3	NA	NA
Q4	NA	NA

Why We're More Constructive Again

We are upgrading shares of WTRG following another consistent quarter of execution by management. Following a large 2Q beat, mgmt. reaffirmed their 2020 EPS of $1.53-$1.58 (while peer AWK revised down on COVID impact) and a 5-7% EPS CAGR through '22. We have increasing conviction around mgmt.'s ability to consistently deliver and see upside risk from further acceleration in muni acquisitions (excluded from guidance while already contemplated in the growth plan for AWK). In the near term, resi strength of their portfolio and constructive regulatory treatment (with the March order from the PA PUC boding particularly favorable given their large presence in the state) position the company to navigate pandemic challenges while the growing pipeline of municipal opportunities should provide a long term tailwind for the water biz; meanwhile after electing to implement Repairs Tax for the gas biz in PA (and a catch up filing to amortize capital already spent filed last week), we see a clear runway to drive earned returns for the next several years (Mgmt. noted expectations for the initial filing to drive $0.08-$0.12 worth of contribution for the year).

Following the adoption of Fair Market Value legislation in TX and VA, the company now has the constructive legislation in all eight states of their water footprint. We expect this to help further accelerate consolidation in the industry as muni budgets are further flex'd from the crisis - and any further resulting acquisitions would be upside to mgmt.'s latest reaffirmed targets. Despite the more recent adoption in the state, WTRG already announced their first acquisition in TX under the legislation and we perceive more and more acquisitions of muni's to materialize over the next several months across their footprint. Meanwhile, we are less concerned around recent media headlines around the DELCORA acquisition: we don't see meaningful risk to the deal and it remains upside to estimates over time from the currently laid out plan. With the PUC fully accepting the application last week, mgmt. noted expectations to close the transaction in early '21. Overall, we stress $300Mn+ in rate base opportunities from signed APAs expected to generate ~$15Mn in earnings that are all upside to the currently laid out plan.

Bottom line, we see upside to the plan given the more conservative approach to guide, and expect shares to rerate higher relative to AWK as investors continue to appreciate the premium story amid consistent management execution.

EPS Estimates

The exhibit below reflects our latest EPS Estimates. In addition to limited risk to NT numbers (despite some dilution from the expected equity offering) given the defensive nature of their portfolio and constructive regulatory treatment, we see the company as poised to deliver on their 5-7% EPS CAGR – with upside from a likely acceleration in industry consolidation. We continue to model towards the high end of their 5-7% EPS CAGR through '22. With consistency the metrics many in the industry continue to pursue as part of further re-rating opportunities, we see the relative *lack* of outperformance of late despite its track record and its relatively attractive ESG profile make it among the more compelling investments. With prospective EPS growth likely more consistent than earlier trajectory (which proved more 'lumpy' we perceive the outlook as ever more appealing for those seeking a de-risked outlook).

Table 1: EPS Estimates

EPS Estimates	2020E	2021E	2022E
PA	$0.73	$0.80	$0.86
OH	$0.07	$0.07	$0.08
IL	$0.07	$0.08	$0.08
TX	$0.06	$0.07	$0.07
NC	$0.04	$0.04	$0.05
Other States	$0.07	$0.07	$0.08
Water Utility	1.04	1.13	1.21
Peoples Gas	0.62	0.67	0.72
Parent & Other	*-0.10*	*-0.11*	*-0.14*
EPS	1.56	1.69	1.80
YoY Growth	*6%*	*9%*	*6%*
Guidance	1.53-1.58		
Fully Diluted Shares O/S	*254*	*254*	*254*
Previous EPS	*$1.56*	*$1.69*	*$1.80*
Consensus	1.53	1.66	1.79
DPS	0.99	1.06	1.13
Payout Ratio	*63%*	*62%*	*63%*

Source: BofA Global Research estimates

Valuation: Upgrading to Buy with $52 PO

The exhibit below reflects our latest SOTP after applying the current peer multiples to our valuation: 26.9x for water and 15.9x for gas (vs. 26.9x for water and 15.9x for gas previously). We raise our premiums across the board given particular confidence in management and their consistent ability to deliver, strong municipal acquisition prospects, and an underappreciated ESG angle. Our PO shifts to $52 (from $49 previously) and we are upgrading to Buy.

We note shares have notably lagged AWK, which has also consistently executed. We attribute some of this to WTRG's ownership of gas utility: ultimately we view this as quite value accretive and EPS accretive given sharp discrepancy in valuations. The question remains whether investors will value the consolidated entity for a clean(er) story with a carbon profile driven by a gas utility. We already substantially discount the gas utility: we perceive comps for the gas utility itself could well include the likes of ATO among other higher quality avenues.

We perceive management to be exceptionally consistent and focused on executing across a range of opportunities. Numerous acquisition avenues yet to be discovered.

Table 2: SOTP

Water Utilities	2022 EPS		P/E Multiple				Equity Value		
		Peer	Prem/Disc	Low	Base	High	Low	Base	High
Peer Water P/E		*28.1x*							
Group EPS '18-'22 CAGR		*8.30%*							
1-year forward group Water multiple		30.4x							
Water Utilities									
States	2022E EPS	ROE embedded							
PA	$0.86	10.0%	4.0x	33.4x	34.4x	35.4x	$29	$29	$30
OH	$0.08	9.4%	2.0x	31.4x	32.4x	33.4x	$2	$3	$3
IL	$0.08	9.1%	3.0x	32.4x	33.4x	34.4x	$3	$3	$3
TX	$0.07	10.0%	2.0x	31.4x	32.4x	33.4x	$2	$2	$2
NC	$0.05	9.2%	2.0x	31.4x	32.4x	33.4x	$1	$2	$2
Other (including acquisitions)	$0.08	9.2%	0.0x	29.4x	30.4x	31.4x	$2	$2	$2
Water utilities total (ex-Peoples)	$1.21			*32.8x*	*33.8x*	*34.8x*	$40	$41	$42
Gas Utilities									
Peer Gas P/E		*16.3x*							
Group EPS '18-'22 CAGR		*5.80%*							
Peoples Gas Multiple		17.2x							
	2022E EPS	ROE embedded							
Peoples Gas	$0.72	12.1%	3.0x	19.2x	20.2x	21.2x	$14	$15	$15
HoldCo Debt									
(50% Netting out Debt) @ Aqua Parent			-1165	50%			($582)	($582)	($582)
'(50% P/E multiple on Interest Exp)			4.3%	50%			($553)	($511)	($598)
50/50 Weighted Drag from HoldCo Drag							($1,135)	($1,094)	($1,180)
Fully Diluted Shares Outstanding							*254*	*254*	*254*
PO							$49.00	$52.00	$53.00
Current Price								$47.27	
Dividend Yield								2.1%	
Total Potential Return								12.09%	

Source: BofA Global Research, Bloomberg

Price objective basis & risk

Essential Utilities (WTRG)
Our price objective is $52 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. These peer multiples are 28.1x and 16.3 vs. 26.9x and 15.9x, respectively, previously. We apply a 3.0x premium to Peoples Gas given the organic growth opportunities, while applying a variety of premiums to its water (2x previously) subsidiaries: +4x to PA, +3x to IL, +2x to OH, +2x for TX, +2x for OH, and no premium for balance of biz.We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AES	AES	AES US	Julien Dumoulin-Smith
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	Atlantica Yield	AY	AY US	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	PNM Resources Inc.	PNM	PNM US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
NEUTRAL				
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith
RSTR				
	Vivint Solar	VSLR	VSLR US	Julien Dumoulin-Smith

iQmethod℠ **Measures Definitions**

Business Performance	Numerator	Denominator
Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Other LT Liabilities	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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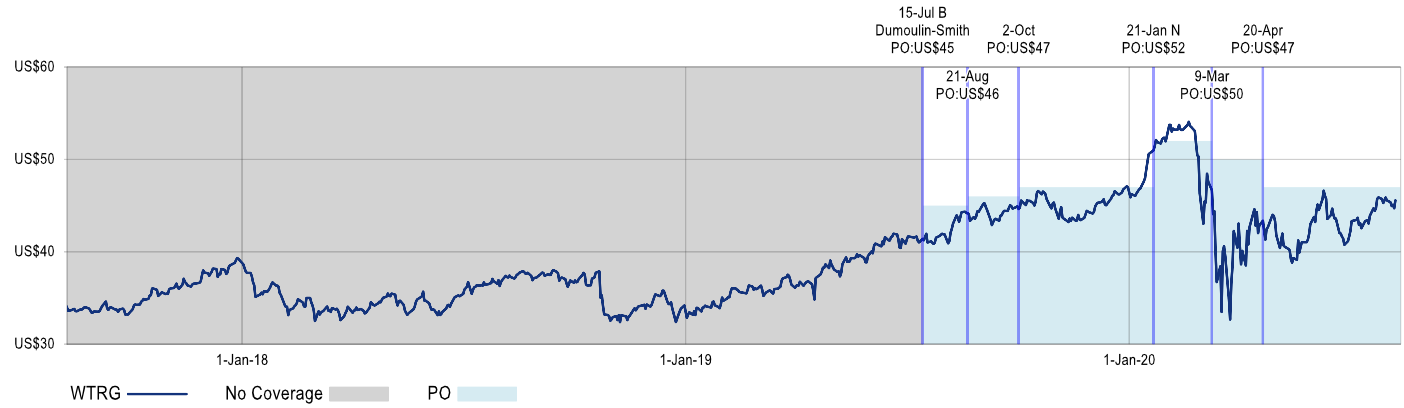
Essential Utilities (WTRG) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Utilities Group (as of 30 Jun 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	76	51.01%	Buy	56	73.68%
Hold	33	22.15%	Hold	22	66.67%
Sell	40	26.85%	Sell	29	72.50%

Equity Investment Rating Distribution: Global Group (as of 30 Jun 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1632	52.21%	Buy	1031	63.17%
Hold	711	22.74%	Hold	444	62.45%
Sell	783	25.05%	Sell	407	51.98%

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
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Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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North American Electric Utilities

EEI: The Final Day of our Virtual Exploration Tour

Price Objective Change

12 November 2020

Equity
North America
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So big surprises? No; but datapoints, plenty.

As we close out this year's EEI we appreciate that few companies provided material updates. That said numerous companies provided substantive incremental datapoints on their trajectories – and overall large-cap companies did well in de-risking their outlooks including D, DUK, SO, and NEE. While large-caps have done relatively well already this year, we perceive support for each of these discrete stories to bolster sector prospects. By contrast, among the lone more cautious updates was AEP's '21 EPS guidance release & 5-yr view, which painted a slowing view vs earlier elevated expectations. Among other companies offering more cautious updates on their prospects included FE and EVRG albeit both are already at substantial discounts. We perceive persistent confidence in CNP on its subsequent roll forward (with details on both ENBL and LDC strategy), and a positive clear read-thru to NI. We suspect both will continue to trend well. With LDCs in focus, we perceive BKH as warranting greater attention given initiation of an EPS CAGR & yet further positive capex revisions. Other smids such as IDA and POR offered confidence inducing updates on their prospects – with expectations still relatively lower for POR, we flag this as particularly compelling. Finally, with DTE among the most controversial equities into the EEI conference we see mgmt's ability to add cnofidenc to reaching the high end of '21 affirmed that lingering doubts on spin could drive yet a further pos re-rating. Meanwhile on rate case developments, PNW offered among the single updates for a constructive new rider to limit renewable lag but ACC acceptance is still key. See earlier write-ups from Day 1, Day 2 and Day 3 here.

So who were our latest meetings? Wednesdays Slate

We met with AY, ED, ES, HE, LNT, MGEE & WTRG yesterday to close out the conference. AY appears poised to provide substantial 4Q updates, likely slowing its DPS growth to a mid-single digit (see table below), from 8-10%. That said, buyout opportunities of partners and expansions at existing sites provide a rare opportunity for higher return opportunities for YieldCo. We stress its focus on smaller acquisitions too also lend themselves to sustained higher returns too. ED's new CEO was indeed impressive & thoughtful on expanding ED increasingly into renewables; its challenges in NY remain real with pressures on '21 EPS. ES was indeed positive – and whether it raises its outlook for a 6-8% EPS CAGR (or not), we see a clear bias to argue this company will achieve a 7% EPS CAGR through '25 when disclosed on 4Q call (formally rolling in transmission, CMA accretion, and smaller South Fork offshore wind project). With expectations higher, these developments appear largely appreciated by the market. Rather, more importantly, we perceive near-term confidence around draft net metering decision and forthcoming affirmation on BOEM permitting process as all boding relatively well for shares. As for LNT, we perceive confidence on substantial cost reductions & emphasize this aspect as a key point to enable yet further T&D spending (that was otherwise displaced with its 3Q updates with renewables taking its 'place' in its 5-year capex budget). On balance, our favorite defensive utility still. MGEE was indeed constructive on just how further coal retirements could meaningfully shift its outlook from cost structure – enabling yet larger capex program and potentially protracted rate case stayouts. Our ES PO shifts to $95 (vs. $90) on group multiples.

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Alliant Energy (LNT)

Alliant mgmt. highlighted the meaningful rate of change ahead in the composition of its generation portfolio, with an estimated 14% of its 2020 rate base allocated to coal generation forecast to shift to 7% by 2030 following the retirement of Lansing, conversion to gas of Burlington, and in-servicing of currently planned renewables (1000 MW WI solar, 400 MW IA solar). Among the operational improvements driven by the evolving generation portfolio are meaningful reductions in O&M, with mgmt. targeting cuts of 3-5%/yr, among the more impressive cost cutting targets across our coverage. Maintain Buy on LNT as remains our favorite defensive utility idea.

Driving 3-5% O&M reduction through renewables build

With 1400 MW of solar scheduled to come on line in coming years along with pending retirements of Edgewater (414 MW in 2022), Lansing (275 MW in 2022), and conversion of Burlington (2021), LNT mgmt. flagged an impressive outlook for O&M reductions of 3-5% per annum through 2024 as high fixed cost generation is swapped for renewables. The majority of savings are expected to come from lower overhead associated with no longer operating coal generation (including lower headcount) as well as additional investments in technology and automation across the enterprise. We note that the overall trajectory of O&M reduction implies ~15% aggregate savings over the course of the forecast period, one of the more impressive cost reduction trajectories across our coverage. Following the latest announcements of coal retirements and conversions in Iowa, mgmt. continues to evaluate the rest of its coal burning fleet to determine if and when an accelerated retirement is appropriate (coal rate base expected to fall from 14% to 7% of total through the decade). We note that MGEE mgmt. has been discussing potentially accelerating the retirement of Columbia generating (which is co-owned by LNT, MGEE, and WEC) though LNT mgmt. has stressed that it continues to evaluate plant productivity with needed future investments in deciding whether or not to accelerate a retirement.

Cash tax runway until 2024, steady balance sheet improvement seen

LNT mgmt. sees itself as not paying cash taxes based on its current appetite and tax credit profile until 2024. Mgmt. is not currently making any assumptions about potential monetization of investment tax credits in the event that such a provision were passed as part of a stimulus bill – the expectation remains that the federal government is reluctant to pick winners in terms of fuel type when crafting tax policy as it pertains to renewable generation. In terms of the balance sheet, LNT sees its FFO metrics improving over the course of the forecast period with current levels in the 'mid teens' (our forecast sees a range from 16-18% through 2024).

Clear path to 5-7% through 2024

While we attribute some of LNT shares' underperformance in the week following the Q3 announcement to lingering expectations of a capex increase at the roll-forward, we now sense that investors have largely come to appreciate that the composition of spending is weighted toward renewables in the near part of the forecast period, with a corresponding shift toward more distribution spend in later years. With no block equity in the current forecast and robust O&M reductions targeted, we continue to see LNT as one of the best-positioned Midwest utilities looking ahead.

Atlantica Sustainable Infrastructure (AY)

We continue to question the yieldco ESG re-rating trend, given the level of growth prospects that has been priced into shares across the sector. With AY expected to announce '21 guidance and a LT growth CAGR next quarter, we remain skeptical around ability to maintain 8-10% DPS growth. That said, mgmt expects AY's valuation to be supported by $200-$300mn of annual investment, at high-single-digit to low-double-digit returns, and an 80% payout; if achievable, this could admittedly help support div growth. The critical question will be whether the opportunities exist. In European markets, we note several administrations pushing for infrastructure programs with renewable components. The U.S., similarly, may provide a supportive environment for renewable development. The other question will be the level of support received from AY's sponsor AQN, given their own current issues. We would expect less support from AQN near-term, although in the longer term this may change. Maintain Neutral.

How to justify the yieldco re-rating trend?

Our meeting focused firstly on the latest yieldco re-rating trend, with questions on being able to justify current valuations in the sector. Mgmt expects AY's valuation to be supported by growth, with $200-$300mn of investments annually, including in 2020 thus far. Finding opportunities with an adequate return profile will be the key challenge, given declining returns across the renewables space. Mgmt did note that while returns have seen compression over the last couple of years, the recent declines in interest rates have helped to make returns somewhat more justifiable. A higher share price should further help to reduce dilutive impact of dropdowns partially funded with equity issuance. Assuming a high-single-digits levered return on equity investment and an 80% payout on ~$250mn annual investment and employing 3.3x CAFD/Debt, we perceive AY could potentially stand to grow at **~4% annual DPS**; suspect a substantially moderated growth rate from 8-10% given reduced usage of HoldCo debt. We note the $200-300 Mn is a placeholder but mgmt. appears abundantly confidence it can execute at this scale with its current employee base. However, the critical question will be whether sufficient opportunities exist today to generate this level of investment at adequate returns.

Exhibit 1: Placeholder drop down math

Drop Down Math			
		HoldCo Debt	74.25
Share Price	30	Debt/CAFD	3.3x
Midpoint of CAFD	250	Shares Issued (ex-Debt)	5.86
CAFD	22.5	Dilution (% Shares)	5.74%
CAFD Yield	9%	DPS Dilution =>	0.10
80% DPS Payout	18	Interest Expense	0.03
DPS Upside	0.176471	Debt Coupon	5%
Current Div	1.68	Financing Costs (EPS Terms)	*0.12*
Div % Inc (Pre-Financing)	0.105042	DPS Upside	0.05
		DPS Accretion @ 80%	3%
		DPS Accretion @ 100% payou	6%

Source: BofA Global Research, Bloomberg

Growth prospects and return expectations across geographies: watch for expansions & buyouts of partners *to continue*

In the U.S., Atlantica targets high single digit returns, while in international markets, the target is in the low double digits in certain geographies. In European markets, we see several administrations pushing infrastructure programs with renewable components which could drive growth for AY (given strong Spanish base with solar asset portfolio). In the U.S., as well, a potential Biden administration could boost growth prospects through improved returns and opportunities. We note AY's continued expansion in North American markets with its first investment in Canada, a $20mn district heating

investment. Separately, we highlight room for several more "niche opportunities" akin to the recent Solana tax equity investor buyout (we note peers including CWEN have also entered this area with re-powerings of existing projects).

Growth: Dropdowns vs. third-party partnerships vs. M&A

Atlantica noted several avenues through which to pursue growth, including investments to develop existing assets, partnerships with developers and construction companies (e.g. Algonquin, etc.), and third-party M&A through competitive deals. While AY expects that partnerships may comprise a smaller portion of growth in the short term (as partners are still developing their portfolios), longer term they are expected to make up a greater portion of the overall development pipeline.

Consolidated Edison (ED)

Con Ed's incoming CEO presented his vision for the company that largely builds on the strategic direction of the utility and non-reg business to date. At the regulated utilities the near term challenge remains managing the financial and operational impacts of Covid which are expected to persist into 2021 (and led to the recent '20 guidance cut). At the Clean Energy Business, the company continues to target investments of $400m/yr with an expectation to pivot to greater reliance on tax equity given its $800m backlog of accumulated tax credits as well as pursuing develop-build-flip projects that are less capital intensive. Incremental renewable investment opportunities were laid out for the regulated business as well, though the EV 'make ready' initiative had been previously known and battery storage potential remains in early days. Maintain Neutral on ED; we were impressed by the incoming CEO's eloquent description of future strategy – and efforts to expand renewable mandate but perceive pressures as likely to persist into 2021. We see question as still pending around future gas strategy, pressures from lost fees persisting into '21, and a regulatory backdrop that remains at an elevated risk (into 1Q21 O&R rate case filing). On balance, we perceive challenges ahead prior already reflected in its discount to peers.

2021 drivers: deferring bad debt, uncertain on foregone fees

We expect that per its usual schedule ED will provide forward guidance for 2021 with its Q4 update next Feb. Company mgmt. Among the key updates in the company's Q3 results is the deferral of Covid-linked bad debt expense – the uptick in expense reached $46m at the Con Ed Co of NY (CECONY), surpassing the materiality threshold of $20m that is part of ED's rate plans and allowing full deferral of the expense item to be considered in the next rate case filing (2022). Mgmt. indicated that it expects to defer these expenses in '21 as well, not surprising given the q/q uptick of $30m in bad debt expense as of Q3. Less obvious is whether foregone fees will be deferred in 2021 given the uncertain duration of the prohibition on charging fees to residential customers affected by Covid – recall this was the change in law (Cuomo exec orders) that drove the deferral of bad debt expense. ED estimates that it is losing $6.4m in fees *per month* during the pandemic, with an estimated half of that attributed to residential customers (though not clear how many of those are directly attributable to Covid). As we previously indicated in our updated estimates, we expect 6 months' of lost fee revenue and direct Covid expenses to impact ED by -7c, with an additional -7c due to lower Steam demand (TTM earned ROE at the Steam business is 5.6% as of Q3).

Table 1: EPS forecast

ED 2021 EPS Walk	EPS	Note
Start: 8.8% earned ROE	4.54	Based on CECONY earning full authorized
Less: foregone fees 6 months	(0.04)	6 months' impact, $6.4m revenue per month
Less: direct Covid expenses	(0.03)	Q2 impact was ($0.06)
Less: higher bad debt expense	-	Now deferred
Less: Steam lower demand	(0.07)	
BofA 2021 EPS estimate	4.40	

Source: BofA Global Research estimates

Renewable opportunities: EV station build out, still early on utility-scale storage

Incoming management flagged the opportunity to add to rate base meaningfully over the coming years via a number of renewable energy initiatives that are not fully captured in the current rate base forecast. We previously incorporated the EV 'Make Ready' charging station program into our forecasts, with an estimated EPS impact ranging from $0.02-0.04/yr based on ED's $314m of capex allocated to the program.

Table 2: Make-Ready Spend Detail

	State total	CECONY	O&R	ED Total	Central Hudson	NYSEG	Niagara Mohawk	RG&E
Level 2 Plugs	95	42	16	58	18	51	87	23
DC Fast Charger	386	192	4	195	3	13	25	8
Incentive	480	234	19	253	21	64	112	31
Futureproofing	38	19	2	20	2	5	9	2
Implementation	72	35	3	38	3	10	17	5
Transit Authority	10	3		3			5	2
Total	601	290	24	314	26	78	143	40

Source: BofA Global Research estimates

Near-term upside from spending opportunities on utility-scale storage is less obvious though mgmt. reports high-level discussions with state regulators including the New York State Energy Research and Development Authority (NYSERDA). Among the structures under consideration is a partnership with private developers whereby battery storage is developed and utility-owned for a period of 7-10 years after which ownership would revert to the developer, with initial procurement estimated in the 300 MW range in ED's service territory. We note that conversations around this remain in early stages without a formal proposal, though we do expect acceleration of renewable and storage solicitations (ED estimates ~2.5 GW of renewables needed annually to reach state interim decarb goals by 2030).

Essential Utilities (WTRG)

Management Successfully Navigating COVID & Peoples Integration

Following their positive 3Q report last week in which management reaffirmed full year guidance of $1.53-$1.58 - noting expectations to be at the top end of the range and affirmation of their 5-7% EPS growth through '22 - latest discussions with management stressed confidence around execution of their strategy with the company successfully navigating the pandemic while integrating their Peoples Gas acquisition. Recall the company has elected to use Repairs Tax accounting treatment and has effectively implemented the last several months – with guidance of $0.08-$0.12 benefit annually. We await developments around the regulatory process of the catch up component after the earlier filing, with resolution expected early in April of 2021. Rather than drive incremental upside to their 5-7% EPS CAGR, the filing seeks to extend the growth without a need for a rate case. As opposed to going in for new rates in 2023 to take effect in 2024, a constructive outcome from the catch up filing would benefit '23, with incremental benefits in '24, and '25 to help drive earned returns for the segment in outer years without any rate relief until 2026. Bottom line, the repairs tax debate boils down to Peoples Gas ROE lag in '23, likely to a modest degree. Focus on EPS growth roll-forward to '23 (presumably with 4Q) will be of importance. Given the uncertainties in the outlook mgmt. intends to limit its roll forward to a 3-year outlook in spite of peers having a 5-year outlook. On balance we feel comfortable in mgmt's ability to manage lag around its ROEs at core water utilities including PA into a potential water filing next year.

Muni Pipeline Remains Strong amid pending DELCORA developments

With FMV legislation now in all eight water & wastewater states in WTRG's footprint following the passage in Virginia earlier this year, the company continues to execute on tuck in acquisitions and discussions continue to highlight a robust pipeline of opportunities. The company has already closed on Campbell, East Norriton, and Rockwell Utilities this year, with another ~353Mn of rate base opportunities from signed APAs expected to generate an additional ~$18Mn of earnings potential. Meanwhile, the company is actively pursuing acquisition opportunities across all of their water geographies, with ~360K customers identified, the majority being wastewater. We expect more firm announcements in coming weeks.

We see the latest pressures put on munis from the ongoing pandemic as likely to only further accelerate consolidation in the industry. Meanwhile, a further environmental push under a Biden administration could provide additional capital opportunities as compliance costs with PFAs and water quality concerns have already started contributing to the push away from muni owned water systems.

Management remains confident on the DELCORA process, with a regulatory approval expected in mid-March. This would put the company on track to potentially close the transaction in April or May after the 30 day appeal window. Meanwhile, a hearing is scheduled for early December regarding the litigation around the trust with a ruling expected from the judge within 60 days. Recall the company has until August to pull on the ~$300Mn equity forward to be used for DELCORA and other acquisitions.

We reiterate our Buy rating, seeing upside risk in the event of better than expected execution on their long-term growth rate.

Eversource Energy (ES)

Poised to Extend with Upcoming Roll Forward: Q'n is Just How Much Upside?

Following their 3Q report last week in which ES management reaffirmed full year guidance of $3.60-$3.70 (excluding full year costs related to the recently completed acquisition of Columbia Gas of Massachusetts) and its long-term EPS growth rate from its core regulated business of 5-7%, latest discussions with management continued to stress confidence around the trajectory of the company. While still unclear if it will formally raise to 6-8% trajectory, it is clear mgmt. will pivot to high end of its EPS growth rate by 4Q with inclusion of both smaller offshore (South Fork) likely alongside inclusion of CMA and potentially modest capex. We see a positive near-term tailwind between offshore wind trends and otherwise constructive updates. Management plans to roll forward their five year outlook through 2025 with full year results, with inclusion of Columbia Gas and some added capex from annual updates across their businesses including some transmission projects incremental to the plan. We perceive another ~$50Mn in transmission spend vs. what was previously contemplated; meanwhile, new MA legislation allowing the expansion of utility-owned solar generation is awaiting conference committee after being enacted in the House: this would allow utilities to own up to 10% of solar amount on its system, suggesting 230MW permitted for NSTAR Electric that would be incremental to the plan. We don't necessarily anticipate offshore wind or AMI to be firmly included with the update given a lack of clarity around approvals and timing, but nonetheless could see management point to a higher range from just the CMA accretion given the low acquisition price of 1x rate base. Expectations are for CMA alone to be accretive this quarter with further incremental accretion each year. It remains unclear if management would formally shift up guidance as opposed to pointing to the higher end given additional opportunities not yet formally included.

Offshore Protracted, but Upside Here too Quite Possible

After early commentary from Orsted around offshore delays, ES indicated changes in expectations around most recent in service dates of end of 2023 for South Fork wind (vs. End of 2022 previously), that it is unlikely to achieve end of '23 in-service date previously alluded to for Revolution Wind, and that it is unlikely to achieve the end of '24 in-service date for Sunrise Wind. Following the BOEM review schedule for South Fork Wind, the COP decision is due in January 2022 while the BOEM review schedule for Revolution Wind is now expected in early '21 (vs. late this year previously). After filing the COP application for Sunrise wind, the BOEM review schedule is expected in 2021. We see 2026 as entirely possible – and therefore outside of the 5-year window for the 2021-2025 CAGR roll forward. Management expects news from BOEM around Vineyard Wind shortly to help provide further clarity on their projects.

That said, a growing consideration is improvements to the economics of the projects: commentary from management highlighted that delays have provided latitude for better tech and we see improving O&M as another interesting nuance. It remains to be seen how prospects can further improve under a Biden administration given his support for offshore wind. We could yet see extensions for tax credits & inclusions for offshore wind and we perceive potential appetite for ITCs through 2025.

While current projects face delays on the margin, the company has capacity to build 4GW (with the JV representing 1.7GW) as they look to optimize their local expertise, and Orsted and ES announced their joint proposal to develop Sunrise Wind 2 (a new offshore wind farm for New York State). We perceive there may have only been three bidders for the project and quite possible multiple bids are awarded.

We see near-term resolution around low income rates in CT and storm response as key to enabling re-rating of shares higher. While we could yet see penalties accrue around Isaias, we stress the watered down Take Back our Grid Act in Connecticut was ultimately much less punitive than initially feared. We raise the PO from $90 to $95 on higher

group electric/gas multiples (17.3x/15.3x) vs. prior (16.5x/13.8x) Maintain Neutral given we see balanced risk/reward.

That said, we look for resolution around potential latest proposed decision in net metering tariff adjustment that would reduce rates in CT. Management remained confident in its ability to recover lost revenues from NEM in final order. Watch this in coming weeks to drive shares given $16Mn+ impact.

Hawaiian Electric Industries (HE)

Sustained cost reductions remains a key focus area ahead

With discussions, mgmt focused on sustaining cost reductions into '21+. Mgmt expressed a focus on sustained cost savings with the PUC mgmt audit. Among key cost levers expressed include strategic sourcing (renegotiating supply agreements with vendors, etc), work force reduction strategy (reduced overtime and improved scheduling coordination), process improvements, and other cost efficiency to lower cost of services.

That being said, in terms of O&M reductions to date, mgmt acknowledges meaningful portion (half of 3Q) associated with delayed but needed generation overhauls and station maintenance work, effectively timing shifts into 4Q and 1Q21 with FY20 utility guidance remaining at the bottom half of the range despite YTD performance. On a forward basis, mgmt express ability to keep O&M at or below inflation as key to forward performance beyond commitments of $25mn in annual cost reductions.

On balance a constructive meeting when considering both O&M tailwinds discussed from latest cost cuts pursued as well as potentially bottoming out on ASB. That said, clear pressures exist into '21 to drive EPS pressures vs Street. We maintain our Underperform pending clarity on critical PBR reforms ahead in coming weeks – this will be the single most important datapoint for shares in years.

PBR key focus on potential to reduce structural lag towards 9.0%

Among notable commentary, mgmt expressed potential opportunity to improve earned ROEs towards 9.0% (relative to authorized ROE of 9.5%) following the conclusion of PBR through the reduction of structural lag. While LTM ROE stands at 8.4% (with structural lag comprising ~120bps), mgmt expressed near-term O&M levels as an exception given push-out benefit with negative impact to 4Q/1Q21 ahead. As such, mgmt expects PBR resolution of structural lag potentially supporting towards a 9.0% earned ROE relative to a lower than 3Q normalized baseline ROE.

In terms of PBR discussions, mgmt expressed positives as support for earning sharing mechanisms (ESM) including both positive and negative, potentially with sharing in under-earning as well. Additionally, mgmt expressed focus on incentive PIMs with a range being established. Accelerating the annual accrual date for RAM to Jan 1 annually from June 1 also helps with structural lag. That said, 'day-1 savings' will likely be a focus as well, with Consumer Advocate proposing 4x cumulative value of accelerated RAM accrual relative to HE proposing the already committed $25mn by 2022 reduction.

Mgmt continues to expect a final PUC decision for PBR Phase II in Dec. That said, mgmt emphasizes specific rate tariffs will be established to implement new and gauged mechanisms after the order, as a new step by the PUC. As such, the timeline to reduce structural lag remains unclear. With potentially multi-year targets, mgmt expressed the extent of which under-earning can be mitigated in 2021 remains contingent on PBR results. Nonetheless, we perceive potential upside relative to earned ROE reflected in the low 8% range in our forecast but emphasize need for execution.

ASB remains cautious with yet further NIM compression likely ahead

On the other hand, ASB discussions remained cautious. With continued NIM compression into 3Q already at 3.12% (vs. 2Q/1Q NIM of 3.21%/3.72%), mgmt expressed further pressure ahead relative to already below-expectation 3Q levels. This is primarily driven

by the spread between higher rate existing loans rolling off and being replaced by new customer loan agreements at lower rates, with mgmt expressing a slow but gradual continued decline in NIMs likely as long as interest rates are lower relative to a year prior. With rates expected to remain low through the near-term, we expect continued pressure at the ASB segment. While, mgmt did not explicitly guide expectations for lower NIM relative to 3.12% in 3Q into 2021, noting variables including potential for higher margin mix as well, downward pressure on existing vs. new pricing remains.

For loan loss provision, mgmt continues to express uncertainty, though noting it exercises conservatism in projecting potential loan losses. If actual net charge offs are ultimately less than what is provisioned for ASB could see some provision come back. Mgmt expresses YTD provision largely in-line with its expectations. However, mgmt notes this could worsen if additional lockdown and economic pressures worsen (with economic impact with sustained tourism reopening uncertain).

MGE Energy (MGEE)

MGEE mgmt. expressed confidence in its near-term regulatory outlook with the pending decision of its WI rate case settlement expected before the end of the year. While capex shifted incrementally during the 2020-22 period it still remains elevated as MGEE works to complete its utility scale solar build at Badger Hollow and Two Creeks. Ahead of the roll-forward of its 3-year capex plan to be rolled out with the Q4 results, we look ahead to potential updates on further generation spend (particularly given WEC's confirmation of the exercise of its West Riverside option) though see these as mid-2020s items. Maintain Underperform on MGEE.

Generation investment needed by mid-decade

MGEE is in the process of completing 170 MW of utility scale solar at its Badger Hollow, Two Creeks, and O'Brien facilities with all targeted for completion by 2022. Unlike WEC, which confirmed its intention to exercise the option it holds to purchase an incremental 200 MW of generation capacity at LNT's recently opened West Riverside facility for total capex of $180m, MGEE did not confirm its plans with the option it holds for 50 MW (with option good until 2025). While the *specific* generation addition plans remain to be determined, MGEE mgmt. reiterated that it does see investment opportunities in new generation by the mid-2020s with expected upcoming retirements of gas combustion turbines (75 MW), Blount Generating (94 MW), and expiring PPAs (50 MW). We perceive that MGEE mgmt. is holding off on making fuel type decisions for its future generation fleet until necessary investments are required, rather than committing to a specific fuel now (such as gas as a bridge to renewables). While we do see a step-down in capex in the 2023+ timeframe following the placement in service of the current crop of renewables, we note there is mid-decade upside from the next tranche of generation spend, as well as incremental opportunities such as deployment of advanced meters.

Looking constructive on WI rate settlement

The Wisconsin electric 2021 rate settlement remains pending with the commission, though mgmt. indicates confidence in achieving a final order before year-end. Under the proposal rates would remain flat at the electric utility along with a 4% increase in gas rates, with a tightening of the fuel cost bandwidth to 1% from 2%, with an expected continuation of the ROE and authorized equity layer. With the majority of stakeholders in the proceeding signing off on the proposed settlement, we see a constructive outcome as more likely than not.

Storage co-investment opportunities with WEC, others

Following fellow WI utility WEC's update which is targeting 600 MW of rate base storage rollout through its forecast period, MGEE sees opportunities for co-investment, in particular in storage attached to co-owned projects (Badger Hollow, Two Creeks). Intriguingly, the opportunity extends beyond pairing storage with generation assets to the distribution system as well, though specific projects and investment sizes were not included in MGEE's update. As with additional generation investment, we see storage co-investment as a potential area to watch though likely in the 2022+ timeframe (beyond the current capex forecast).

Stocks mentioned

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
LNT	LNT US	Alliant Energy Corp	US$ 57.42	B-1-7
AY	AY US	Atlantica Sustain	US$ 33.87	B-2-7
ED	ED US	Consolidated Edison	US$ 81.72	A-2-7
WTRG	WTRG US	Essential Utilities	US$ 46.37	B-1-7
ES	ES US	Eversource Energy	US$ 94.42	C-2-8
HE	HE US	Hawaiian Electric	US$ 37.05	A-3-7
MGEE	MGEE US	MGE Energy	US$ 72.16	A-3-7

Source: BofA Global Research

Price objective basis & risk

Alliant Energy Corporation (LNT)
Our $61 PO is based on a sum of the parts analysis employing relative premium and discounts to the large cap regulated peer multiple of 16.8x 2023E P/E. We note that electric peer P/E multiple is grossed up for a year by 5% to reflect capital appreciation across the sector. We apply a 3.0x P/E premium on IPL as we see the rate case overhang being resolved. We apply a 4.0x P/E premium on Eastern Wisconsin Electric Company reflecting 1) low risk investment nature of the state, 2) above average ROEs, 3) higher than average growth runway for investments, and 4) bad debt deferral. At ATC, we reflect a 2.0 x P/E premium on LNT's 16% share in the transmission company. Growth expectations for this segment are high, paired with above average ROEs that we believe face less downward pressure vs. regulated state distribution ROEs. We apply an in line multiple at the parent to account for the blend of numerous businesses some which benefit from long term stable PPAs via intercompany generation. Risks to our price objective are: 1) adverse rate case outcomes, 2) further equity dilution beyond our estimates, 3) interest rate risk, 4) natural disasters, and 5) lower allowed ROEs.

Atlantica Sustainable Infrastructure (AY)
Our $33/sh PO is based 50% on a DCF valuation and 50% on our Growth approach. Our Growth value is $36 (weighted 50%). Our DCF value is $29.00 (weighted 50%).

Assumptions in our DCF valuation are:
- A 7.0% discount rate based on a CAPM methodology assuming a 0.6% risk free rate and a 5.5% equity risk premium
- 2% annual escalator in corporate expenses

Main assumptions in our Growth valuation are:
- Run-rate CAFD generated by the current portfolio of $213 Mn
- 750 MW of future drop downs
- A target payout ratio of 80%

Downside risks are 1) the company may not be able to access capital markets at favorable terms, 2) the company may not be able to make accretive acquisition opportunities to fuel growth, 3) the company may not be able to grow DPS at the targeted growth rate, 4) the company may not be able to sustain its current dividend levels, and dividend yield could increase.5) PCG related counterparty exposure is among the nearest exposures to watch.

Consolidated Edison (ED)
Our $82 PO is based on a sum-of-the-parts analysis applying premiums and discounts to the regulated group multiples (16.6x/14.0x for electric/gas respectively) with a -1.0x discount on both Steam & Electric to reflect Covid recovery overhang. Steam for lack of decoupling. Both electric and gas peer P/E multiples are grossed up for a year to 2021 by 5% to reflect capital appreciation across the sector. We applied inline peer regulated multiple at CECONY despite its rate certainty for conservatism as our higher capex expectations are reflected in our EPS outlook. We apply a discounted PE for infrastructure projects given the lack of clarity around the capital structure. We further apply an EV/EBITDA approach on 2023E EBITDA to the CEB business using a 10.0x multiple for both the legacy portfolio and the renewables portfolio seeing it as having higher quality returns.

Downside risks: ED, like all utility stocks, is also sensitive to changes in the market level of interest rates. Utilities historically underperform if bond yields rise, and outperform when they fall. Further downside risks are the inability to recontract storage, adverse regulatory outcomes, a deteriorating regulatory environment, or unforeseen disasters such as the Harlem gas explosion, the SRE transaction not being completed. Customer

inflation is also a downside risk. PCG related counterparty exposure is among the nearest exposures to watch.

Essential Utilities (WTRG)
Our price objective is $51 based on our SOTP approach, applying a peer multiple to the water utility and gas utility, respectively and accounting for expected growth for each sector. These peer multiples are 25.5x and 13.9x. We apply a 3.0x premium to Peoples Gas given the organic growth opportunities, while applying a variety of premiums to its water (2x previously) subsidiaries: +4x to PA, +3x to IL, +2x to OH, +2x for TX, +2x for OH, and no premium for balance of biz. We net out parent debt and parent interest expense associated with parent debt 50/50 weighed basis.

Risks to the downside are acquisition risk, deteriorating regulatory outcomes, and risks from a lower rerating following the diversification into gas.

Eversource Energy (ES)
Our sum of the parts based price objective of $95 uses P/E multiples on 2023E earnings. For electric utilities, we attribute a 4x premium NSTAR, and 3x premium to PSNH and CL&P to peer 17.3x multiple, reflecting future potential positive revisions to capex and earnings. For gas, we apply a 3x premium to the peer 15.3x multiple, given capex upside particularly in MA and a 2x for Columbia Gas. Both electric and gas peer P/E multiples are grossed up by 5% to reflect capital appreciation across the sector. We value Aquarion at a 1x premium to the 27.5x water multiple. We reflect ES's 50% ownership in Revolution and South Fork offshore wind sites on an NPV basis. We take out 50% of parent debt, and 50% of interest to accurately reflect parent leverage.

Upside risks to our price objective are additional capex announcements on the T&D side, as well as success in offshore wind RFPs.

Downside risks are reduction in authorized ROEs, inability to meet earned ROE expectations, as well as failure to receive permitting on incremental capex opportunities

Hawaiian Electric Industries (HE)
Our PO of $34 for Hawaiian Electric Industries is based on a sum of the parts approach. We apply: 1) a 2023E forward P/E multiple in line with electric utility peer multiple of 16.9x. We see this as justified given ongoing issues in the regulatory environment need to be resolved and the earnings gap vs what is required to achieve authorized ROEs across all three of the jurisdictions. Electric utility peer P/E multiple is grossed up for a year to 2020 by 5% to reflect capital appreciation across the sector, 2) a 2021E forward price to tangible book value of 1.50x to the banking subsidiary, a 0.5x premium to smid cap regional peers (0.96x), in-line with Hawaiian banks peers due to outperformance. We then take into account parent overhead by applying the same multiple here as to the utility segment to 50% of parent interest and subtracting the per share value of the remaining 50% of the debt. Downside risks are delays on capital expenditures, weakening regulatory environment, PUC denial of new capital investments or lower authorized ROEs. Upside risks are expansion of capital expenditure plan, significant improvements in earned and/or authorized ROEs

MGE Energy (MGEE)
Our $62 PO is based on a sum-of-the-parts analysis applying premiums and discounts to the regulated group multiples (16.5x/13.9x for electric/gas respectively) with a 4.0x premium on WI regulated gas and electric to reflect the constructive regulatory mechanism, and a 2.0x premium on Transmission assets. We note that both electric and gas peer P/E multiples are grossed up for a year to 2021 by 5% to reflect capital appreciation across the sector. We apply utility premiums to the non-regulated Elm Road and West Campus assets as these are leased under long-term contractual arrangements. Downside risks: MGEE, like all utility stocks, is sensitive to changes in the market level of

interest rates. Utilities historically underperform if bond yields rise, and outperform when they fall. Further downside risks are the inability to secure further renewable rate base investments, adverse regulatory outcomes, a deteriorating regulatory environment, or adverse weather leading to less consumption of electricity and gas. Upside risks are acceleration of renewable gen investment, legacy coal asset early retirement, and enactment of further pro-renewable state policies.

Analyst Certification

I, Julien Dumoulin-Smith, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AES	AES	AES US	Julien Dumoulin-Smith
	Alliant Energy Corporation	LNT	LNT US	Julien Dumoulin-Smith
	AltaGas	YALA	ALA CN	Julien Dumoulin-Smith
	Atmos Energy Corporation	ATO	ATO US	Richard Ciciarelli, CFA
	Clearway Energy	CWENA	CWEN/A US	Julien Dumoulin-Smith
	Clearway Energy	CWEN	CWEN US	Julien Dumoulin-Smith
	CMS Energy	CMS	CMS US	Julien Dumoulin-Smith
	DTE Energy	DTE	DTE US	Julien Dumoulin-Smith
	Duke Energy	DUK	DUK US	Julien Dumoulin-Smith
	Edison International	EIX	EIX US	Julien Dumoulin-Smith
	Emera Inc	YEMA	EMA CN	Julien Dumoulin-Smith
	Enphase Energy	ENPH	ENPH US	Aric Li
	Entergy	ETR	ETR US	Julien Dumoulin-Smith
	Essential Utilities	WTRG	WTRG US	Julien Dumoulin-Smith
	Evergy, Inc	EVRG	EVRG US	Julien Dumoulin-Smith
	FirstEnergy	FE	FE US	Julien Dumoulin-Smith
	Hydro One	YH	H CN	Julien Dumoulin-Smith
	Idacorp	IDA	IDA US	Julien Dumoulin-Smith
	NextEra Energy	NEE	NEE US	Julien Dumoulin-Smith
	NiSource Inc	NI	NI US	Julien Dumoulin-Smith
	NRG Energy	NRG	NRG US	Julien Dumoulin-Smith
	OGE Energy Corp	OGE	OGE US	Julien Dumoulin-Smith
	PG&E Corporation	PCG	PCG US	Julien Dumoulin-Smith
	Portland General Electric Company	POR	POR US	Julien Dumoulin-Smith
	PPL Corporation	PPL	PPL US	Julien Dumoulin-Smith
	Public Service Enterprise Group	PEG	PEG US	Julien Dumoulin-Smith
	Sempra Energy	SRE	SRE US	Julien Dumoulin-Smith
	Spire	SR	SR US	Richard Ciciarelli, CFA
	Sunnova Energy	NOVA	NOVA US	Julien Dumoulin-Smith
	SunRun	RUN	RUN US	Julien Dumoulin-Smith
	Vistra Energy	VST	VST US	Julien Dumoulin-Smith
NEUTRAL				
	Ameren Corporation	AEE	AEE US	Julien Dumoulin-Smith
	American Electric Power	AEP	AEP US	Julien Dumoulin-Smith
	Atlantica Sustainable Infrastructure	AY	AY US	Julien Dumoulin-Smith
	Avista	AVA	AVA US	Richard Ciciarelli, CFA
	Black Hills Corporation	BKH	BKH US	Julien Dumoulin-Smith
	CenterPoint Energy	CNP	CNP US	Julien Dumoulin-Smith
	Cheniere Energy Inc	LNG	LNG US	Julien Dumoulin-Smith
	Consolidated Edison	ED	ED US	Julien Dumoulin-Smith
	Dominion Energy	D	D US	Julien Dumoulin-Smith
	Eversource Energy	ES	ES US	Julien Dumoulin-Smith
	First Solar, Inc.	FSLR	FSLR US	Julien Dumoulin-Smith
	Hannon Armstrong	HASI	HASI US	Julien Dumoulin-Smith
	NextDecade	NEXT	NEXT US	Julien Dumoulin-Smith
	NextEra Energy Partners	NEP	NEP US	Julien Dumoulin-Smith
	ONE Gas, Inc.	OGS	OGS US	Richard Ciciarelli, CFA
	Southern Company	SO	SO US	Julien Dumoulin-Smith
	Southwest Gas Holdings	SWX	SWX US	Richard Ciciarelli, CFA
	Tellurian Inc	TELL	TELL US	Julien Dumoulin-Smith
	TransAlta Renewables Inc.	YRNW	RNW CN	Julien Dumoulin-Smith
	Unitil Corporation	UTL	UTL US	Julien Dumoulin-Smith
	Xcel Energy Inc	XEL	XEL US	Julien Dumoulin-Smith
UNDERPERFORM				
	Algonquin Power & Utilities Corp	AQN	AQN US	Julien Dumoulin-Smith
	Algonquin Power & Utilities Corp	YAQN	AQN CN	Julien Dumoulin-Smith
	American Water Works	AWK	AWK US	Julien Dumoulin-Smith
	Avangrid	AGR	AGR US	Julien Dumoulin-Smith
	Bloom Energy	BE	BE US	Julien Dumoulin-Smith
	Exelon	EXC	EXC US	Julien Dumoulin-Smith
	Fortis	YFTS	FTS CN	Julien Dumoulin-Smith
	Fortis Inc	FTS	FTS US	Julien Dumoulin-Smith
	Hawaiian Electric Industries	HE	HE US	Julien Dumoulin-Smith
	MGE Energy	MGEE	MGEE US	Julien Dumoulin-Smith

North American Utilities, Alternative Energy & LNG Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	New Jersey Resources Corp	NJR	NJR US	Richard Ciciarelli, CFA
	Northwest Natural Holdings	NWN	NWN US	Richard Ciciarelli, CFA
	NorthWestern Corporation	NWE	NWE US	Julien Dumoulin-Smith
	Pinnacle West	PNW	PNW US	Julien Dumoulin-Smith
	South Jersey Industries	SJI	SJI US	Richard Ciciarelli, CFA
	SunPower Corp.	SPWR	SPWR US	Julien Dumoulin-Smith
	WEC Energy Group Inc	WEC	WEC US	Julien Dumoulin-Smith

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Utilities Group (as of 30 Sep 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	79	51.63%	Buy	59	74.68%
Hold	36	23.53%	Hold	24	66.67%
Sell	38	24.84%	Sell	25	65.79%

Equity Investment Rating Distribution: Global Group (as of 30 Sep 2020)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1749	54.79%	Buy	1114	63.69%
Hold	677	21.21%	Hold	415	61.30%
Sell	766	24.00%	Sell	386	50.39%

* Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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January 11, 2021

Research Flash Update

Essential Utilities, Inc.
(WTRG/NYSE)

Rating/Risk:	Outperform/Moderate
Price:	$48.72
Target Price ($US):	$54.00
Market Cap ($US millions):	$11,950
ADTV (US$ millions):	$61.0

Target Price and Rating are for 12 months.

Estimates	EPS		Revenue (Net)		
	B&S	Cons.	B&S	Cons.	P/E
2018A	$1.08	-	$838.1	-	45.1x
2019A	$1.00	-	$889.7	-	48.7x
2020E*	$1.15	$1.59	$1,396	$1,639	42.5x
2021E	$1.68	$1.67	$1,625	$1,819	29.0x

FYE 12/30; Revenue in USD millions.

All historical EPS and B&S EPS estimates GAAP.

*Guidance: $1.53-$1.58 ("adjusted") reflects full year of Peoples.

Source: Capital IQ, B&S Estimates

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2021 guidance in-line, muni acquisition program remains on-track with key DELCORA court win.

Essential Utilities issued initial 2021 EPS guidance of $1.64-$1.69, bracketing incoming consensus of $1.67 (2020E: $1.59), highlighting the steady growth story of the regulated utility business. At the mid-point, the 2021 guidance represents year/year EPS growth of 5%, a solid figure in what remains a highly uncertain macro environment. We reiterate our Outperform rating for shares of WTRG, which are among our current top ideas in the water/environmental sector.

Key Guidance/Outlook Highlights:

- Diluted EPS: $1.64-$1.69 (midpoint $1.665)
- 3-year EPS CAGR: 5% to 7% (through 2023)
- 3-year Capex Target: $3 billion (Water + Gas)
- 3-year Rate Base CAGR – Water: 6% to 7%
- 3-year Rate Base CAGR – Gas: 8% to 10%
- Water Customer Growth: 2% to 3% (organic + acquisitions)

Discussing the municipal acquisition pipeline, Essential says that it currently has purchase agreements in place representing 225,000 customer connections and $420 million in rate base. This is up from 212,000 connections at the end of 3Q despite the tabling (for now) of the Norristown (PA) opportunity, reflecting in part the recent addition of Bourbonnais (IL) and underscoring the depth and cadence of the municipal M&A market in the fair market value era.

The $276 million purchase of DELCORA is the biggest deal pending, and we believe recent developments bode well for the transaction. A legal challenge brought by Delaware County politicians received a major setback when the Delaware Court of Common Pleas ruled in Essential's/Aqua's favor. Attention now turns to the PUC, where the deal must be approved before moving on to closing. We see the DelCo ruling as a key win for Aqua and would be very surprised if the PUC does not approve the deal. We anticipate a 2Q21 close.

WTRG and its regulated utility peers have performed respectably of late on a risk-adjusted basis (WTRG +5% TTM), but have lagged the broader bull market (S&P 500 +17% TTM) and in particular the huge gains in the water industrial sector (peer group average +33% TTM). We believe WTRG shares offer a compelling reward/risk equation, and reiterate our Outperform rating. Our price target of $54 reflects a P/E of 32times, in-line with the water utility peer group.

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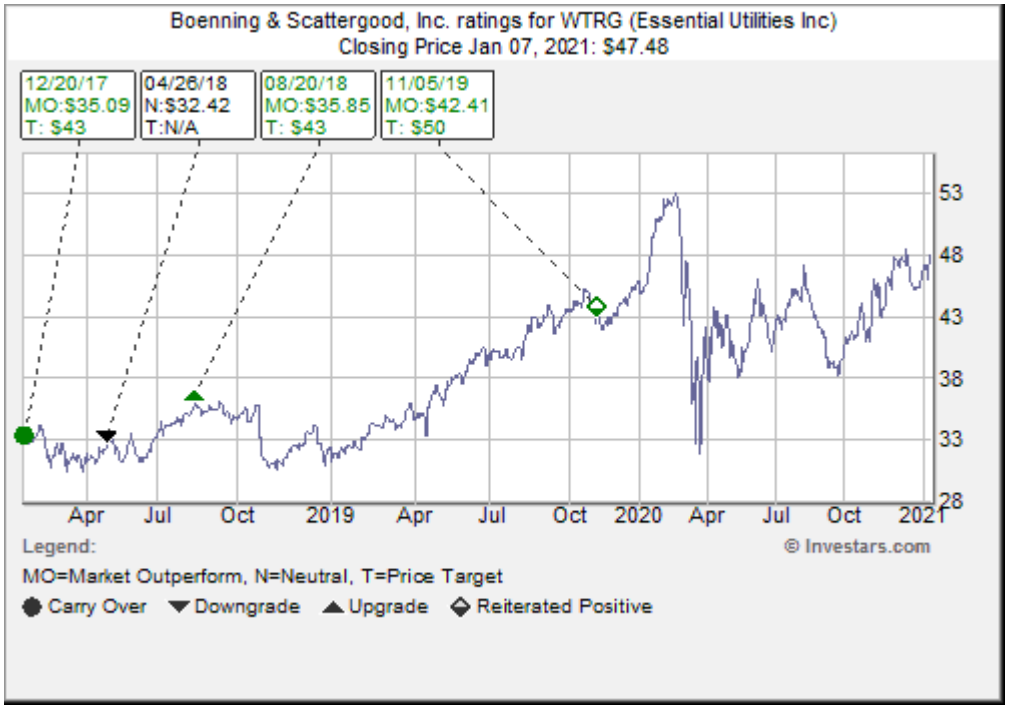
Disclosure Appendix

Rating and Price Target History:



Risk Factors

The realization of any or all of the following risk factors, among others, may adversely affect the company's stock price and prevent it from reaching our price target: the economic cycle, concentration in energy sector, foreign currency exposure, and client concentration.

Analyst Certification:

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Boenning & Scattergood received compensation for investment banking services from the subject company within the past 12 months.

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Boenning & Scattergood's Ratings System:

Our three-tier investment ratings are based on a stock's return potential relative to a broad market index:

- ***Outperform (Buy):*** The security's total return over the year or longer is expected to exceed the total return of the S&P 500™ over the identical period.
- ***Neutral (Hold):*** The security's total return over the next year or longer is expected to be roughly equivalent to the total return of the S&P 500™ over the identical period.
- ***Underperform (Sell):*** The security's total return over the next year or longer is expected to be less than the total return of the S&P 500™ over the identical period.

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- ***Low:*** The security has higher-than-average fundamental predictability and/or lower-than-average price volatility.
- ***Moderate:*** The security has average fundamental predictability and/or average price volatility.
- ***High:*** The security has lower-than-average fundamental predictability and/or higher-than-average price volatility.
- ***Speculative:*** The security has very inconsistent fundamental predictability and/or very high relative price volatility.

Ratings Distribution (9/30/20):

Coverage Universe (a)	% of Universe
Outperform (Buy)	32%
Neutral (Hold)	46%
Underperform (Sell)	1%
Not Rated	20%

Investment Banking Clients (b)	% of Rating Group
Outperform (Buy)	21%
Neutral (Hold)	9%
Underperform (Sell)	100%
Not Rated	7%

(a) Related to services provided within the past 12 months.

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August 14th, 2019

Coker Palmer Institutional

Equity Research
Water & Sustainable Infrastructure

Aqua America, Inc.

WTR - NYSE

Recent Px: $43.65

Company Update:

Company Delivers Favorable Q2 Results & Outlook; Advise Buying Dips

Investment Summary: *Aqua reported solid Q2 results as the company beat our non-GAAP diluted EPS estimate. Many developments transpired during the quarter that are imperative to our model, including a timing discrepancy in the P&L recognition of the Pennsylvania rate case, a delay in the close of the Peoples acquisition, and approval of the large Peoples rate case. As a result, WTR was short of our Q2 top-line estimate, and we were forced to meaningfully modify our model. However, the revision positively affects the model by swinging our 2019 diluted EPS estimate to the top-end of the guidance range from the bottom, and for 2020 and 2021, diluted EPS estimates are essentially the same. On top of these factors, the long U.S. Government bond yield fell over the course of Q2, as well as the five-year WTR beta (according to FactSet). In turn, the stronger 2019 estimated Aqua fundamentals, together with the lower long yield and beta, drive up the valuation multiple, and with our 2020 diluted EPS estimate unchanged, our fair value rises due to the valuation multiple increase. Accordingly, we view the Q2 report and resultant outlook favorably. Still, the stock run-up (along with top water utility peers) the past two weeks on trade tensions, and a falling risk-free rate, is pressing shares against our revised fair value that is at Street-high. Plus, we see the emergence of chatter around Fed rate cutting, and/or a trade truce, contracting the valuation multiple. As such, we see strong potential for a lid to be placed on shares, and for pullback and volatility. That said, our desire to recommend accumulating shares on the solid Q2 report and attractive outlook is offset by valuation. With this in mind, we encourage investors to take a year-end 2020 investment horizon with Aqua and buy dips, because once valuation rolls to 2021 estimates, it becomes compelling once again, and WTR is armed with many catalysts to power the stock to the next year fair value that currently stands at $51/sh according to our model.*

- **Aqua delivers Q2 bottom-line beat.** Q2 non-GAAP diluted EPS of $0.37 was $0.03 higher than our estimate. Revenue of $218.9m was $7.8m beneath our $226.7m estimate. The sales difference was a function of timing discrepancy in the model around incorporating the Pennsylvania rate case versus when the rate case went into effect. For simplicity, we plugged an April 1st rate case impact start into the model, yet the rate relief began May 24th. Had we forecasted a one-month recognition of the rate case in the model for Q2, our sales estimate would have matched the Q2 report. On that note, bottom-line outperformance stemmed from better-than-expected other income lines below the line.
- **Flow-through on model revision strengthens 2019 to 2021 earnings estimates and the financial condition.** During Q219, Aqua announced it anticipates closing the Peoples acquisition this fall instead of this summer. Moreover, WTR announced a Peoples rate case outcome of $59.5m. Going into Q2, we modeled Aqua and Peoples to begin operating as one company in Q319, and we estimated a $54.1m positive top-line impact, starting in Q419, from the Peoples rate case. Owed to the Peoples developments, we push out the close of the Peoples deal, in our model, by one quarter to Q419, which cuts our Q319 estimates, and we bump up our Q419-start Peoples rate case estimate to $59.5m to mirror the outcome. We also adjust the Aqua Pennsylvania rate case inclusion in the model to more accurately reflect timing. The model flow-through from these changes, and the update for actual Q2 figures, causes our 2019 non-GAAP diluted EPS estimate to climb by $0.06 to $1.50 (top of the $1.45 to $1.50 2019 guidance range), strengthening cash generation to a degree that reduces net debt estimates while lifting dividend estimates. Due to the greater 2019 non-GAAP diluted EPS estimate, lower net debt forecast, and higher dividend projection, our target P/E valuation multiple swells. For 2020 and 2021, the model flow-through leads to non-GAAP diluted EPS estimates for each year staying the same. This translates into YoY non-GAAP diluted EPS growth of ~6.5% for each year over the 2019 to 2021 period, implying to us our earnings estimates are on track when considering the Aqua rate base, and consolidated company breakdown, guidance for the Peoples and WTR combined entity.
- **We see stock pullbacks creating investment opportunity.** With our 2019 dividend and non-GAAP diluted EPS estimates rising to $0.91/sh from $0.90/sh, and $1.50 from $1.44, respectively, combined with the drop in the year-end 2019 consensus 30-year U.S. Government bond yield estimate to 2.5% from 3.0%, and the WTR five-year beta fall to 0.63 from 0.65 (FactSet), our target P/E valuation multiple amplifies to 28.2x from 26.4x. As a result, our fair value increases by $3 to $45. We support our valuation with the justified P/B multiple and justified dividend yield approaches that point to fair values of $45 and $47, respectively, based on a multiple and yield of 3.2x and 1.95%, respectively. Peeking into next year, our model suggests P/E multiple expansion to 29.9x, and when applied to our 2021 non-GAAP diluted EPS estimate of $1.70, the 29.9x multiple implies 2021 year-end fair value is $51/sh. Bearing this in mind, upside to the $51 mark from the present trading level stands at 16.8%, yet, accumulating shares at the current price sets up for the risk of pullback on current year (2020-based) valuation. Furthermore, we see potential for pullback on the back of easing trade tensions and discussion of Fed rate cuts. To these points, we advise investors to accumulate shares on dips with an investment horizon through 2020 year-end, and as Aqua catalysts come to fruition, we see value in the stock being unleased to ultimately drive it to the $51 fair value by end of next year.

Ticker	WTR
Last Price	$43.65

Valuation Parameters	
Risk-Reward	0.9x
Upside	$49
Fair Value	$45
Downside	$38

Market Capitalization	
Market Cap ($m)	9,419
Cash ($m) (2018A)	4
Debt ($m) (2018A)	2,398
Enterprise Value ($m)	11,814

Financial Estimates

	2018	2019E	2020E	2021E
Rate Base ($m)	4,500	7,073	7,657	8,246
EBITDA ($m)	470	576	881	940
EPS	$1.41	$1.50	$1.59	$1.70
DPS	$0.84	$0.91	$0.98	$1.06

Valuation

	2018	2019E	2020E	2021E
P/E	31.0x	29.1x	27.4x	25.7x
Dividend Yield	1.9%	2.1%	2.2%	2.4%
EV/EBITDA	25.1x	20.5x	13.4x	12.6x

Market Stats	
Shares, FD (2018A)	178m
Short Interest, % Float	530%
Beta	0.63
52 Wk High	$44
52 Wk Low	$32
Average Daily Volume (90-Day)	1,051k

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Please see full disclosures in the Appendix of this report.

Exhibit 1: Base Case P&L

Aqua America, Inc.
Income Statement
(in millions except per share data)

Coker Palmer Institutional
Richard Verdi; 646.827.9586

December Fiscal Year	FY 2016	FY 2017	FY 2018					FY 2019E					FY 2020E	FY 2021E
Non-GAAP	Year	Year	1Q18	2Q18	3Q18	4Q18	Year	1Q19	2Q19	3Q19E	4Q19E	Year	Year	Year
Revenue	**$819.9**	**$809.5**	**$194.3**	**$211.9**	**$226.1**	**$205.7**	**$838.1**	**$201.1**	**$218.9**	**$244.7**	**$473.4**	**$1,138.2**	**$1,944.9**	**$2,015.9**
Operating & Maintenance	304.9	287.2	73.9	73.5	68.6	92.4	308.5	79.3	86.4	92.3	239.2	497.2	985.4	995.2
Depreciation	131.0	136.3	36.0	36.6	37.5	36.0	146.0	39.1	39.6	40.1	61.8	180.5	253.7	262.9
Amortization	2.0	0.4	0.1	0.1	0.2	0.2	0.6	0.3	(2.9)	0.2	0.2	(2.2)	0.9	0.9
Non-Income Taxes	56.4	56.6	15.0	14.8	15.6	14.4	59.8	15.0	14.9	16.0	18.8	64.7	78.6	80.6
Operating Income	**325.6**	**329.0**	**69.3**	**86.8**	**104.3**	**62.8**	**323.2**	**67.4**	**80.9**	**96.1**	**153.4**	**397.9**	**626.4**	**676.3**
Interest Expense, Net	(80.6)	(88.3)	(23.5)	(23.7)	(25.4)	(26.3)	(98.9)	(27.9)	(28.9)	(29.8)	(48.6)	(135.2)	(213.5)	(234.2)
Allow. for Funds for Construction	8.8	15.2	2.9	2.6	3.1	4.5	13.0	4.1	3.6	3.9	5.6	17.1	25.1	24.5
Gain on Sale of Other Assets & Other	0.4	0.5	0.2	0.1	0.3	14.3	14.9	6.0	10.9	8.4	8.4	33.7	20.0	20.0
Equity Earnings in JV	1.0	0.3	(0.2)	0.5	(0.1)	(0.1)	0.1	0.5	1.2	0.6	0.3	2.7	1.9	1.5
Income Before Taxes	255.2	256.7	48.7	66.2	82.2	55.2	252.3	50.2	67.8	79.2	119.1	316.3	459.9	488.1
Income Taxes	21.0	16.9	(2.1)	(0.4)	3.9	0.0	1.5	0.5	0.9	1.7	13.2	16.3	51.1	54.2
Net Income (Continuing Operations)	**234.2**	**239.7**	**50.8**	**66.6**	**78.2**	**55.2**	**250.8**	**49.7**	**66.8**	**77.5**	**105.9**	**299.9**	**408.8**	**433.9**
Diluted EPS	**$1.32**	**$1.35**	**$0.29**	**$0.37**	**$0.44**	**$0.31**	**$1.41**	**$0.28**	**$0.37**	**$0.43**	**$0.42**	**$1.50**	**$1.59**	**$1.70**
Diluted Shares Outstanding	177.8	177.2	178.2	178.3	178.4	178.4	178.4	178.6	178.7	178.8	254.3	197.6	254.9	255.9
Margin Analysis														
Operating & Maintenance	37.2%	35.5%	38.0%	34.7%	30.3%	44.9%	36.8%	39.4%	39.5%	37.7%	50.5%	43.7%	50.7%	49.4%
Depreciation	16.0%	16.8%	18.5%	17.3%	16.6%	17.5%	17.4%	19.4%	18.1%	16.4%	13.1%	15.9%	13.0%	13.0%
Amortization	0.2%	0.1%	0.1%	0.1%	0.1%	0.1%	0.1%	0.2%	-1.3%	0.1%	0.0%	-0.2%	0.0%	0.0%
Non-Income Taxes	6.9%	7.0%	7.7%	7.0%	6.9%	7.0%	7.1%	7.4%	6.8%	6.6%	4.0%	5.7%	4.0%	4.0%
Operating Income	39.7%	40.6%	35.7%	40.9%	46.1%	30.5%	38.6%	33.5%	37.0%	39.3%	32.4%	35.0%	32.2%	33.5%
Income Before Taxes	31.1%	31.7%	25.1%	31.3%	36.3%	26.8%	30.1%	24.9%	31.0%	32.4%	25.2%	27.8%	23.6%	24.2%
Income Taxes	8.2%	6.6%	-4.4%	-0.6%	4.8%	0.0%	0.6%	0.9%	1.4%	2.1%	11.1%	5.2%	11.1%	11.1%
Net Income	28.6%	29.6%	26.2%	31.4%	34.6%	26.8%	29.9%	24.7%	30.5%	31.7%	22.4%	26.4%	21.0%	21.5%
Growth Rates yr/yr														
Revenue	0.7%	-1.3%	3.5%	4.2%	5.2%	1.2%	3.5%	3.5%	3.3%	8.2%	130.1%	35.8%	70.9%	3.7%
Operating Income	1.4%	1.0%	-0.8%	2.5%	7.0%	-18.4%	-1.8%	-2.7%	-6.7%	-7.8%	144.3%	23.1%	57.4%	8.0%
Income Before Taxes	7.1%	0.6%	-6.3%	-0.5%	3.2%	-5.6%	-1.7%	3.0%	2.3%	-3.6%	115.8%	25.4%	45.4%	6.1%
Net Income	4.9%	2.4%	3.6%	9.2%	2.6%	3.2%	4.6%	-2.2%	0.3%	-0.9%	91.9%	19.6%	36.3%	6.1%
Diluted EPS	4.5%	2.3%	3.4%	9.1%	2.5%	3.1%	4.5%	-2.4%	0.1%	-1.1%	34.6%	6.5%	6.4%	6.4%

Source: Aqua America, Coker Palmer Institutional Equity Research Estimates

Required Disclosures:

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Coker Palmer Institutional Ratings Distribution * as of 6 | 25 | 2019			Ratings Distribution of IB Clients ** as of 6 | 25 | 2019		
Category	Count	Percent	Category	Count	Percent
Buy	NA	NA	Buy	0	0%
Hold	NA	NA	Hold	0	0%
Sell	NA	NA	Sell	0	0%
No Rating	34	100%	No Rating	4	12%

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** Coker & Palmer (C&P) acted as a Co-Manager for a Gulfport Energy (GPOR) and Halcon (HK) and a HighPoint Resources (HPR) fixed income offering over the past six months, or more. C&P also received consulting fees for work associated with Goodrich Petroleum (GDP).

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Oilfield Services (OFS) business is inherently risky. OFS investors should be fully aware of these risks, which include, but are not limited to, volatile natural gas, NGL's and crude oil prices, demand for and competition for a company's product and/or service, asset quality, customer risks, changes in operating costs, company capital structures, operating and working capital needs and ability to raise both debt and equity capital to fund operations. We value OFS equities on many different metrics, including but not limited to, our subjective view as to the quality of management, discounted cash flows, net asset values, enterprise value to EBITDA or cash flow multiples, price to earnings or cash flow multiples, reinvestment risk and full cycle economics. These factors are uncertain and our outlook is subject to change, sometimes quite quickly. Any changes in the above factors can impede achievement of our valuation assessments.

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Energy | Power & Utilities

May 19, 2020

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AGA Meeting Takeaways

In this note, we briefly summarize takeaways from each of our AGA meetings over the past two days.

Ameren Corp. (AEE), Outperform rating, $84 price target

- **IL Downstate Clean Energy Act:** AEE feels good about bill passage this year given bipartisan support / job creation potential. Whether it is addressed during the current legislative session ending 5/31, in a special session or the veto session remains to be seen. Recall that the Act would increase the adder on the ROE formula from 580 to 680 bps above the 30-YR treasury. It would also create the opportunity for solar/storage/EV investment in a state where AEE is purely T&D.
- **MISO ROE decision possible this Thursday:** AEE is hopeful that FERC will revise the methodology/raise the base ROE given consensus that it is based on a flawed methodology and the fact that transmission investment is more risky than distribution.
- **Next rate case in MO**: The primary factors determining timing of the next rate case are the wind projects slated to go into service late this year and early next year, and COVID-related issues. The only restriction on filing in MO is a 60-day notice. AEE expects to earn its allowed ROE in MO (recently increased from 9.2-9.7% to 9.4-9.8%) with help from PISA accounting and RESRAM riders.
- **O&M savings**: As AEE stated on the Q1 call, it expects to deliver within its 2020 EPS guidance by offsetting COVID-related impacts with reduced O&M. The reductions fall into several buckets, including reduced hiring, travel, consultants, etc.

See inside for our takeaways on 11 more companies.

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Avangrid (AGR), In Line Rating, $46 price target

- **Vineyard Wind:** AGR still expect BOEM to release draft cumulative impact statement on June 12 and for final EIS to come in November in line with BOEM's most recent schedule. AGR noted they have been in constant contact with BOEM, giving us more confidence that this schedule will hold. As a reminder, the cumulative impact statement will have impacts on other projects in the area, such as ES and Orsted's Revolution Wind.
- **NECEC**: The ME Department of Environment Protection issued a permit last week, so they now have all state permits. They are still waiting for Army Core of Engineers and a Presidential permit. YE'22 in-service still targeted but could see delay of a few months depending on remaining permits.
- **Analyst Day**: AGR expects to hold this event in coordination with Iberdrola in 4Q and will likely include disclosures on par with prior years (LT growth rate through 2024, rate base and capex, capacity factor forecasts for the renewables business, etc.)
- **CEO Succession plan:** The board is considering both internal and external candidates we would expect a successor to be name prior to current CEO Jim Torgerson's departure in June.

CenterPoint Energy (CNP), In Line rating, $18 price target

- **COVID update:** All of the states in CNP's service territory are in the process of reopening, giving confidence in the expected U-shaped recovery by September. Notably, the Toyota plant in Indiana is reopening.
- **2020 and long-term EPS guidance**: assumes earnings at or near allowed returns across the utilities and a continuation of 2% customer growth at Houston Electric. CNP does not expect ROEs in rate cases to be pushed much lower than current levels.
- **CEO search**: as CNP highlighted on the Q1 call, it is currently in the back end of the process.
- **Business Review and Evaluation Committee will pick up soon**. CNP said its Board always considers both corporate and asset-specific M&A, including as it relates to ENBL, though the tax basis still an issue with that. The company will publicly share any updates that it has after the Committee's recommendation to the Board in October and potentially before the Analyst Day in 1Q21.
- **Credit metrics**: as CNP stated on the Q1 call, it expects higher than 14.5% FFO to debt this year, providing some cushion for COVID with respect to company's 14% target long term. CenterPoint anticipates that rating agencies will revisit outlooks after the CES divestitures closes in Q2. Recall that CNP is currently on negative outlook at both Moody's and S&P, which were last updated prior to the $1.4Bn equity investment.

CMS Energy (CMS), In Line Rating, $63 price target

- **Covid sales impacts:** CMS indicated they see the $0.03-$0.04/sh per month hit to EPS quoted on the 1Q call as likely being the trough in terms of impacts. With reopening's starting in Michigan, they are already seeing signs that ultimate monthly impacts will be less.
- **Seeking approval to defer certain Covid costs:** Michigan has already authorized utilities to defer bad debt expense and has opened the door for consideration of other cost deferrals. In April, CMS also sought approval to defer other Covid-19 costs related to sequestering labor for 14 days at power plants and compression stations, keeping certain labor at home in home reserve status, incremental cleaning, and new technology for employees to work from home. All together these costs could total $2.2M to $15.3M per month.
- **Covid mitigation plans:** On the 1Q call, CMS noted that they have reduced expenses by $0.10-$0.15 in a given year in response to weak load or other unexpected negatives. At AGA, they reminded us that this was just to show what they have done in the past and was not meant to be considered a ceiling.
- **Enerbank:** CMS sounded relatively upbeat on Enerbank's positioning noting that while originations slowed in March they did see a nice recovery in April.
- **M&A Strategy**: CMS is focused on its organic growth plan and executing their capex backlog, while like any other prudent management team they consider M&A but view such transactions as having a high hurdle rate.

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Consolidated Edison (ED), In Line rating, $85 price target

- **Long-term EPS growth rate**: Items causing the reduction to 2020 EPS guidance is not expected to be carried forward into 2021 and beyond. Con Ed's 3-5% EPS CAGR through 2024 off of the original (higher) 2020 guidance remains intact.
- **COVID impacts:** Con Ed does not expect to recover lost revenue from suspension of late fees and connect / disconnect fees. Some incentives in the CECONY rate plan are harder to achieve in the COVID environment; these include work that is customer-facing, such as selling energy efficiency, connecting distributed energy resources, etc. While the incentives are not based on cumulative results, a ramp-up in 2021 could be required to recover lost ground.
- **O&M**: expected to be lower in 2020 than original plan due to acceleration of cuts that were originally planned for 2021 and 2022, as per the CECONY rate agreement. The bulk of the cuts are expected to be sustainable.
- **Equity issuance plans:** ED entered a bank loan agreement at the parent on April 6th that gave it the ability to borrow $750mm on a 364-day basis. It is designed to provide liquidity that the equity offering would have provided, so it gives ED flexibility to find a more opportune time to issue equity but still expected this year. Recall that the company has guided to up to $600mm this year and $1.1Bn in 2021/22. Con Ed typically issues equity to target a regulatory cap structure rather than an FFO to debt credit metric.
- **Pipeline update**: Sponsors still see a narrow path for a Mountain Valley Pipeline in-service date by YE'20. It is thought possible that the project will be delayed again given a federal judge's (in Montana) ruling in a case involving Keystone crude pipeline that the US Army Corps of Engineers did not comply with the Endangered Species Act. Last week, the judge refused to limit his decision to Keystone, prompting the US Justice Department to ask the 9th Circuit Court of Appeals to stay the lower court's ruling. Separately, Stagecoach does not fit into ED's long term plans in a decarbonized world, but the company is not in a hurry to reduce its ownership.

DTE Energy (DTE), In Line rating, $120 price target

- **Covid sales impacts**: Due to AMI, DTE is seeing real time impacts of reopening's in MI and is seeing load improve a little bit more than their assumptions discussed on the 1Q call.
- **Michigan regulatory environment**: Continue to be pleased with relationship in MI noting that the recent electric rate order was constructive.
- **Power & Industrials segment**: DTE noted that their industrial energy services business benefits from long-term contracts and is well insulated during Covid 19. The RNG business is also holding up well as pricing for RNG in California remains strong and there is still demand for new RNG projects.
- **Gas Storage and Pipelines segment**. The business (both in Appalachian and Haynesville basins) continues to deliver ahead of plan into 2Q in part driven by higher gas futures due to reduced associated gas supply.

Duke Energy (DUK), In Line rating, $90 price target

- **Covid sales impacts**: Load trajectories appear to be relatively consistent with what DUK had expected at the time of the 1Q call.
- **Rate cases:** No material updates in either the NC cases or in IN. They are awaiting a response in NC to the motion to consolidate hearings in the DEP and DEC cases and expect a rate order in IN around mid-year.
- **ACP:** The court order on Nationwide Permit 12 could be impactful on ACP. The Army Corp has already filed an appeal in the 9th Circuit Court and we could see a decision this month on their request for a stay of the application of the court order on the use of the nationwide permitting process. The appeal itself will likely play out through the rest of this year. They also await a decision on the Appalachian Trail crossing from the Supreme Court and a revised Biological Opinion from the US Fish and Wildlife Service. Michigan regulatory environment:
- **Credit Metrics**: An announced cost reduction puts them in targeted 15% FFO/Debt range for this year. No change to 2020 financing plan.

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Sempra Energy (SRE), Outperform rating, $138 price target

- **Chile:** SRE still expect to close the sale of its Chilean business by the end of the month. The last step before closing is getting workers from State Grid International, a Chinese company, into the country, which has of course been complicated by Covid-19. As we understand it, the workers might also need to be quarantined for 14 days before closing.
- **LNG:** Announced production at Cameron 3 during conference. They continue to expect to make a final investment decision on the ECA project in Mexico this quarter. The project still needs an export permit from Mexico –also complicated by Covid- before a decision can be made.
- **2020 EPS Guidance**: SRE continued to sound optimistic on their positioning in 2020 despite Covid, reiterating plans to deliver in the upper end of their current guidance as discussed on the 1Q call.
- **Covid exposure**: SRE's utilities are well positioned for Covid given decoupling and tracking mechanisms in California and still strong demand in Texas.
- **Credit Ratings**: We believe SRE's comments suggest they will be more likely to accept a credit rating downgrade (they are rated Baa1 by Moody's, so a credit downgrade is still high rated IG) at Moody's, which placed them on an outlook for downgrade earlier this year, than to issue incremental equity

Southern Company (SO), In Line rating, $59 price target

- **Covid sales impacts:** SO indicated that load in April was pretty consistent with what they expected at the time of the 1Q call and with their guidance for Covid to negatively impact revenues in the $250m-$400m range.
- **Mitigation plans:** SO is hopeful they might get some help from weather this summer but also noted that they still feel well positioned to offset Covid-related sales impacts with cuts to O&M. They will also benefit from the ability to defer Covid-related costs, like bad debt expense, in GA and MS now**.**
- **Doing more with less at Vogtle:** SO continues to adjust the Vogtle construction site in the wake of the labor force reduction last month. They have seen Cost performance Index (CPI) improve and are now focused on getting earned hours back to where they were. While they expect monthly completion in May at Unit 3 to hover around 1-1.5%, in line with what they delivered in April, they are hopeful that they will ramp back up to 2% in June even with around 2,000 fewer laborers on site.

WEC Energy (WEC), In Line rating, $93 price target

- **Covid sales impacts:** Recent sales trends have been consistent with the revised forecasts issued on the 1Q call.
- **Customer arrears/bad debt expense:** WEC has been pleasantly surprised by trends so far in terms of customer arrears but they will have a better idea of impacts as time goes on.
- **M&A:** WEC's message was relatively consistent in terms of how they think about M&A. They were willing to comment specifically on EVRG, however, noting that they were not interested in participating in any formal auction and also highlighted concerns with the Sibley coal plant disallowance in particular**.**

Essential Utilities (WTRG), In Line rating, $42 price target

- **PA Commission order on uncollectible expense:** In a letter dated 05/13/20 the PA commission directed state utilities to create a regulatory asset for any incremental uncollectible expenses incurred above those embedded in rates since the issuance of the Emergency Order.
- **M&A:** COVID has impacted the pace of discussions on M&A/tuck in opportunities but WTRG is in discussions with several municipalities and has line of sight to sizable water/wastewater acquisitions.
- **Delcora:** Still expected to close by year end but may get pushed into early next year. $300MM in equity issuance still anticipated late this year or early next.

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- **Peoples Gas repairs catch up:** There could be further potential earnings upside if the commission allows favorable treatment of the legacy tax balance ($0.05 - $0.10 annual EPS uplift not in our forecast). WTRG is expected to file with the PA commission in summer this year, timing on a final decision is unknown.

Xcel Energy (XEL), In Line rating, $65 price target

- **XEL is very comfortable in delivering 2020 EPS guidance**. The company believes there is opportunity to cut O&M more than 4-5% if the COVID impact is worse than their base case assumptions. So far, it has been better.
- **COVID expenses**: Minnesota is the latest state where XEL received a COVID expense deferral order, with a decision last week. Xcel has had some discussions in various states about tracking savings as well, but nothing has been finalized.
- **Long-term capex opportunities**: incremental capex could be driven by electric vehicle infrastructure, Minnesota renewables (could be highlighted in upcoming IRP) and PPA buyouts. These can be thought of as extending the five-year 5-7% growth rate rather than increasing it.
- **Rate case update**: Xcel is pleased with the recent modifications (resulting in an $11mm revenue increase) that came out of the reconsideration of the Colorado electric rate case. The company is generally pleased with the recent testimony in the Colorado gas rate case, especially as it pertains to the strong cap structure recommended by Staff and the Office of Consumer Council.. XEL is also having discussions in rate cases about how it can help the economy (i.e. workforce) by putting private capital back to work. This could also benefit them by allowing for more capex and/or acceleration of capex and also remove political pressure associated with a rate case.

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Coverage Universe			**Investment Banking Services I Past 12 Months**		
Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	368	48	Buy	98	27
Hold	305	40	Hold	48	16
Sell	53	7	Sell	4	8
Coverage Suspended	32	4	Coverage Suspended	10	31
Rating Suspended	12	2	Rating Suspended	2	17

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August 08, 2019

Aqua America

WTR | $42.06

In Line | TARGET PRICE: $37.00

Commentary

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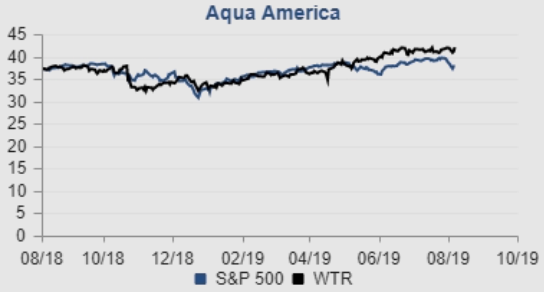
Company Statistics

Market Capitalization (M)	$9,074
Shares Outstanding (M)	216
Dividend	0.91
Dividend Yield	2.2%
Payout Ratio	61.2%
Expected Total Return	(9.9)%
Fiscal Year End	Dec

Earnings Summary

	2019E	2020E	2021E
EPS	**$1.48**	**$1.56**	**$1.64**
P/E	**28.4**	**26.9**	**25.7**
EPS vs Consensus	**6.9%**	**(0.6)%**	**(1.9)%**
Consensus EPS	**$1.38**	**$1.57**	**$1.67**
Consensus P/E	**30.4**	**26.7**	**25.2**

1 Year Price History



Source: FactSet

In Line Quarter; Eyes On The Prize

WTR reported a largely in line 2Q19. FOUR key items worth highlighting are: 1) The Peoples Gas acquisition is still expected to close in fall of this year; 2) Potential acquisition of a PA-based wastewater operator DELCORA (~$300mm rate base and ~$0.03 EPS uplift by our estimate); 3) Repair tax pass-through may be pursued next year; and 4) Long-term guidance is expected to be issued in December. We use a sum-of-the-parts approach to value WTR using a blend of water and gas multiples. At this current juncture, we think the stock trades above our bull-base valuation and we see limited near-term upside; **our rating remains In Line.**

Earnings notes. 2Q19 adjusted EPS of $0.37 was flat to prior year. EPS growth from rate cases and customer growth (acquisitions/ organic) was offset by higher depreciation, lower consumption, and impact of repairs tax. 2019 capex is still expected to be ~$550mm and the company reaffirmed its $1.4bn capex plan through '21, which supports 7% rate base growth in their legacy water business. The Y/Y customer growth rate is still expected to be between 2-3% for '19 (from both organic growth and acquisitions).

Peoples Gas update. Aqua still targets to close the Peoples Gas acquisition in fall of this year. A settlement agreement has been filed with the administrative law judge with a recommended decision expected later this month, and a final PA commission order is expected in the fall. On the rate case front, a settlement agreement seeking $59.5mm in rate increase is awaiting commission approval. New rates are expected to go into effect in October 2019.

Repairs tax election at Peoples could be up to $0.10 EPS accretive ($2/sh or 5% valuation uplift). In 2012, Aqua changed its tax method of accounting for qualifying utility asset repairs in PA. The tax accounting method was changed to permit the expensing of certain utility asset repairs/maintenance costs that were previously being capitalized and depreciated for tax purposes. The company used flow-through accounting for the tax benefits of the repair tax accounting change per the Pennsylvania rate order from June 2012. The flow-through accounting implementation resulted in a reduction in the company's effective income tax rate, which in turn lowered income tax expense and increased net income. WTR's effective tax rate was materially lower than the statuary tax rate at (7.7%) / 6.6% / 8.2% for the years '18 / '17 / '16 respectively. Higher earnings power supported higher returns on equity, which allowed Aqua to invest over $2bn of capital on system improvements over the past seven years without having to go in for rate cases in PA. If regulators approve a similar tax treatment at Peoples, it could be up to $0.10 accretive to EPS and $2/sh accretive to value by our math. We will look for additional color at the Analyst Day in December this year.

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DELCORA opportunity. On the call management announced that the Delaware County Regional Water Authority (DELCORA) had signed a letter of intent with the company committing to exclusive discussions, which could result in a potential combination. DELCORA is a wastewater conveyance and treatment authority that serves approximately 500,000 people in 42 municipalities in Delaware and Chester Counties in southeastern Pennsylvania. We estimate that this could be a potential ~$300mm rate base ($0.03 EPS) uplift, assuming 50%/50% debt/equity financing if they were to move forward.

We are maintaining our $37 price target for WTR; our rating remains In Line. Our $37 target price is based on a sum-of-the-parts valuation where we assign 23.0x '21 P/E to the earnings contribution from the legacy water business and ~21.0x to earnings from the gas segment. The 23.0x water P/E is in line with our water regulated peer average target multiple. The gas multiple of ~21x is also in line with current gas LDC trading valuation multiples. Our bull case valuation of $39 assumes that both the water and gas segment trade at 5% premium to our base case scenario. Our bear case valuation of $33 assumes a 10% discount multiple to our base case scenario for both segments. Please see Exhibit 1 for additional details.

Exhibit 1
WTR Post-Merger Valuation Framework

SOTP Valuation (Base Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.16	23.0x	$27.00
Gas EPS	$0.48	21.5x	$10.00
	$1.65		$37.00

SOTP Valuation (Bull Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.16	24.1x	$28.00
Gas EPS	$0.48	22.6x	$11.00
	$1.65		$39.00

SOTP Valuation (Bear Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.16	20.7x	$24.00
Gas EPS	$0.48	19.4x	$9.00
	$1.65		$33.00

Source: Evercore ISI Research

VALUATION METHODOLOGY

Our $37 target price is based on a SOTP where we assign 23.0x P/E to the earnings contribution from the legacy water business and ~21.0x to earnings from the gas segment. The 23.0x water P/E is in line with our water regulated peer average target multiple. The gas multiple of ~21.0x is also in line with current gas LDC trading valuation multiples.

RISKS

Risks to our thesis include an unfavorable regulatory outcome leading to lower rate base growth and/or lower allowed or earned ROEs in ongoing and future rate cases. Other risks include exposure to unusual weather, impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer, cyber security and water contamination.

COMPANIES UNDER COVERAGE BY AUTHOR

Symbol	Company	Rating	Price (2019-08-08)	Evercore ISI Target
AWK	American Water Works Company, Inc.	Outperform	$118.45	$108.00
AWR	American States Water Company	Underperform	$80.41	$54.00
CTWS	Connecticut Water Service, Inc.	In Line	$69.73	$67.00
CWT	California Water Service Group	In Line	$52.40	$44.00
DCP	DCP Midstream, LP	In Line	$24.66	$34.00
ET	Energy Transfer Partners, L.P.	Outperform	$13.33	$18.00
KMI	Kinder Morgan, Inc.	Outperform	$19.97	$23.00
MPLX	MPLX LP	Outperform	$27.12	$39.00
SJW	SJW Group	In Line	$64.19	$62.00
TRP	TC Energy Corp.	In Line	CAD63.62	CAD60.00
WMB	The Williams Companies Inc.	Outperform	$23.62	$31.00
WTR	Aqua America	In Line	$42.06	$37.00

TIMESTAMP

(Article 3(1)e and Article 7 of MAR)

Time of dissemination: August 08 2019 09:11

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In Line- the total forecasted return is expected to be in line with the expected total return of the analyst's universe
Underperform- the total forecasted return is expected to be less than the expected total return of the analyst's universe
Coverage Suspended- the rating and target price have been removed pursuant to Evercore ISI policy when Evercore is acting in an advisory capacity in a merger or strategic transaction involving this company and in certain other circumstances.*
Rating Suspended- Evercore ISI has suspended the rating and target price for this stock because there is not sufficient fundamental basis for determining, or there are legal, regulatory or policy constraints around publishing, a rating or target price. The previous rating and target price, if any, are no longer in effect for this company and should not be relied upon.*

*Prior to October 10, 2015, the "Coverage Suspended" and "Rating Suspended" categories were included in the category "Suspended."

FINRA requires that members who use a ratings system with terms other than "Buy," "Hold/Neutral" and "Sell" to equate their own ratings to these categories. For this purpose, and in the Evercore ISI ratings distribution below, our Outperform, In Line, and Underperform ratings can be equated to Buy, Hold and Sell, respectively.

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Hold- the total forecasted return is expected to be greater than or equal to 0% and less than or equal to 10%
Sell -the total forecasted return is expected to be less than 0%

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Prior to October 10, 2014, the ratings system of ISI Group and ISI UK which was based on a 12-month risk adjusted total return:

Strong Buy- Return > 20%
Buy- Return 10% to 20%
Neutral - Return 0% to 10%
Cautious- Return -10% to 0%
Sell- Return< -10%

For disclosure purposes, ISI Group and ISI UK ratings were viewed as follows: Strong Buy and Buy equate to Buy, Neutral equates to Hold, and Cautious and Sell equate to Sell.

Evercore Group:

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Overweight- the stock is expected to outperform the average total return of the analyst's coverage universe over the next 12 months.
Equal-Weight- the stock is expected to perform in line with the average total return of the analyst's coverage universe over the next 12 months.
Underweight -the stock is expected to underperform the average total return of the analyst's coverage universe over the next 12 months.
Suspended- the company rating, target price and earnings estimates have been temporarily suspended.

For disclosure purposes, Evercore Group's prior "Overweight," "Equal-Weight" and "Underweight" ratings were viewed as "Buy," "Hold" and "Sell," respectively.

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Short- the stock is a negative holding in the model portfolio; the total forecasted return is expected to be less than 0%.
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Coverage Universe			**Investment Banking Services I Past 12 Months**		
Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	396	51	Buy	268	68
Hold	315	41	Hold	170	54
Sell	39	5	Sell	16	41
Coverage Suspended	18	2	Coverage Suspended	14	78
Rating Suspended	10	1	Rating Suspended	4	40

Issuer-Specific Disclosures (as of August 08, 2019)

Price Charts

Ratings Key

B	Buy	OP	Outperform	L	Long	CS	Coverage Suspended
H	Hold	IL	In Line	NP	No Position	RS	Rating Suspended
S	Sell	UP	Underperform	S	Short		

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Water Utilities Q2 2019 Earnings Recap

The sector continues to look expensive to us on both an absolute and relative basis. Water utilities in our coverage universe are currently trading at a 30x P/E multiple on '21E EPS versus our fair value estimate for the space at 23x (58% / 75% premium to the electric utilities / S&P 500, respectively, versus the 10-year average of ~35% / ~50% based on a one-year forward P/E). 2Q19 earnings results were a mixed bag for the water utilities; see our key takeaways by company below.

AWK ($108PT, Outperform). 2Q19 EPS of $0.94 was a penny higher than consensus.

- The quarter benefitted from ~$0.10 EPS uplift from one-time items (land sales etc) offset by wet weather impact of $0.05.
- FY '19 adjusted EPS guidance range of $3.54-$3.64 was reaffirmed. The long-term EPS CAGR is still projected to be in the top half of the 7-10% range anchored off '17 adjusted EPS of $3.03, with dividends expected to grow at the high end.
- Capex guidance for the year was raised $100mm to $1.9bn, primarily driven by regulated acquisitions.
- We continue to struggle with the valuation for water utilities in our coverage universe. Despite a NTM total return proposition of -9% under our base case scenario (group average is around -11%), we think AWK offers the most attractive risk / reward proposition among our coverage universe over the long term, remain **Outperform**.

AWR ($60PT, Underperform). AWR reported 2Q19 adjusted EPS of $0.64 vs consensus of $0.56.

- Quarterly dividend was increased 10.9% and long term they are now targeting more than 7% compounded annual dividend growth (vs more than 6% previously)
- Company's proposed water rate case settlement was approved by the commission; gross margin is expected to increase by $7mm / $10mm / $12mm in '19 / '20 / '21, respectively.
- The commission issued a proposed decision in the ongoing electric rate case approving the settlement reached between the company and various parties. If approved, the rate increase would be retroactive, beginning 1/1/18.
- Reaffirmed ASUS 2019 EPS guidance range of $0.43 to $0.47, consolidated capex this year is still expected to be in the $115mm to $125mm range.
- We are raising our '19 / '20 / '21 EPS forecast to $2.00 / $2.10 / $2.25, driven by better than expected results YTD.
- Raising target price from $57 to $60, remain **Underperform.**

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CTWS ($70PT, In Line). CTWS reported 2Q19 EPS of $0.48 vs prior year EPS of $0.39.

- The company filed an updated settlement agreement related to the SJW / CTWS merger application in CT. The one key addition to the previous application filed on 4/3/19 was that of rate credits totaling $300k/yr for a period of ten years, starting with the next general rate case (~$0.01 annual EPS impact before offsets). The agreement provides the companies with the opportunity to offset these credits with merger-related cost savings.
- SJW and CTWS expect the transaction to close in the third quarter of 2019, be neutral to slightly dilutive in the first full year, and be high-single-digit EPS accretive in the second full year post-closing.
- We are maintaining our $70 target price and **In Line** rating.

CWT ($46PT, In Line). CWT reported 2Q19 EPS of $0.35 vs consensus of $0.38.

- They are in settlement discussions in their ongoing rate case in CA. Recall they had filed their GRC in CA on 7/2/18, requesting $828.5mm in capital spend from '19-'21. The rate increase application requests $50.7mm / $31.5mm / $33.0mm revenue increases for years '20-'22, respectively. The company expects a final decision by YE '19 with rates effective 1/1/20.
- The company is dealing with a new variable: Public Safety Power Shutoffs (PSPS). Electric companies have been authorized to shut off the grid in addressing wildfire risk. They have redirected staff resources towards internal operational / wildfire readiness training, as well as hardening of their system for wildfires. They expect $2-3mm in equipment leases costs in 2H19 (59 generators for wildfire response)
- CWT's cost of capital filing is due in March next year. Currently they are approved for an equity / debt layer of 53% / 46%, and an ROE / cost of debt of 9.2% / 5.5%, respectively.
- We are maintaining our $46 target price and **In Line** rating.

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SJW ($62PT, In Line). SJW reported 2Q19 EPS of $0.47 vs consensus of $0.56. Excluding one-time items, second quarter adjusted EPS came in at $0.58 versus $0.72 in the prior year.

- The company filed updated settlement agreement related to SJW/CTWS merger application in CT. The one key addition to the previous application filed on 04/03/19 was that of rate credits totaling $300k/yr for a period of ten years, starting with the next general rate case (~$0.01 annual EPS impact before offsets). The agreement provides for the companies' opportunity to offset these credits with merger-related cost savings.
- SJW expects the transaction to close in the third quarter of 2019, be neutral to slightly dilutive in the first full year, and be high-single-digit EPS accretive in the second full year post-closing.
- They settled with the California Public Utilities Commission (CPUC) over past customer billing practices. If approved by the Commission, the company would pay ~$2.1mm in one-time customer credits ($0.06 EPS hit booked in Q2) and invest $5.0mm in utility plant without seeking an investment return or rate recovery (<$0.01 EPS hit).
- In Texas (which represents ~5% of total EPS) legislations SB-700 and HB-3542 will take effect 09/01/19: the former will allow water utilities to recover and earn a return on capex in-between rate cases (similar to DSIC/infrastructure surcharges mechanisms in other states); HB-3542 allows a utility in Texas to value acquired assets at fair market value for ratemaking purposes.
- We are maintaining our $62 target price and **In Line** rating.

WTR ($37PT, In Line). 2Q19 adjusted EPS of $0.37 was largely in line with expectations and flat to prior year.

- The Peoples Gas acquisition is still expected to close in fall of this year. A settlement agreement has been filed with the administrative law judge with a recommended decision expected later this month, and a final PA commission order is expected in the fall. On the rate case front, a settlement agreement seeking $59.5mm in gas rate increase is awaiting commission approval. New rates are expected to go into effect in October 2019.
- Potential acquisition of a PA-based wastewater operator DELCORA may be in the cards (~$300mm rate base and ~$0.03 EPS uplift, by our estimate).
- Repair tax pass-through could be pursued next year, and could be up to $0.10 EPS accretive ($2/sh or 5% valuation uplift).
- Long-term guidance is expected to be issued in December '19; we are maintaining our $37 price target for WTR and **In Line** rating.

Exhibit 1
AWK Valuation Framework

Scenario	EPS CAGR*	'21EPS	'20 P/E	Valuation	Tot. Return
Base Case	7.9%	$4.10	26.5x	$108	-9%
Bull Case	9.3%	$4.32	27.8x	$120	1%
Bear Case	7.0%	$3.97	25.1x	$100	-15%

**17 through '21*

Valuation: Our $108 price target is 26.5x our FY '21 EPS estimate of $4.10/share. That is a ~15% premium to our water utility average target multiple of 23x, due to the company's best-in-class earnings and dividend growth, as well as geographical / regulatory diversity. The latter not only minimizes regulatory risks, but also offers a competitive advantage to capitalize on industry consolidation opportunities, given AWK's presence in 16 states. Our bull case valuation of $120 for AWK assumes growth in the upper half of their targeted 7-10% EPS growth guidance range and a 5% premium to a '21 P/E multiple of 26.5x. Our bear case valuation of $100 assumes AWK can grow earnings at the low end of the targeted 7-10% growth range and we apply a 10% discount to a '21 P/E multiple of 26.5x.

Source: Evercore ISI Research

Exhibit 2
AWR Valuation Framework

Scenario	EPS CAGR*	'21EPS	'20 P/E	Valuation	Tot. Return
Base Case	9.2%	$2.25	26.5x	$60	-27%
Bull Case	10.0%	$2.30	27.8x	$64	-23%
Bear Case	8.2%	$2.19	25.1x	$55	-33%

**18 through '21*

Valuation: Our $60 price target is 26.5x our FY '21 EPS estimate of $2.25/share. That is a ~15% M&A premium to our water regulated target multiple of 23x. Our bull case valuation of $64 for AWR assumes they can grow EPS at 10% through '21 and trade at a 5% premium to our base case '21 P/E multiple of 26.5x. Our bear case valuation of $55 assumes that they grow earnings at 6.5%, 100 bps lower than our base case and trade at 5% discount to our '21 base case P/E multiple of 26.5x.

Source: Evercore ISI Research

Exhibit 3
CTWS Valuation Framework

Scenario	EPS CAGR*	'21EPS	'21 P/E	Valuation	Tot. Return
Base Case	7.1%	$2.75	25.3x	$70	2%
Bull Case	8.1%	$2.83	26.6x	$75	9%
Bear Case	6.1%	$2.67	24.0x	$64	-6%

**18 through '21*

Valuation: Our $70 price target is 25.3x our FY '21 EPS estimate of $2.75/share. That is a ~10% M&A premium to our water regulated target multiple of 23x. Our bull case valuation of $75 for CTWS assumes they can grow EPS at 8.1% 100 bps higher than our base case forecast and trade at a 5% premium to our base case '21 P/E multiple of 25.3x. Our bear case valuation of $64 assumes that they grow earnings at 6.1%, 100 bps lower than our base case and trade at 5% discount to our '21 base case P/E multiple of 25.3x.

Source: Evercore ISI Research

Exhibit 4
CWT Valuation Framework

Scenario	EPS CAGR*	'21EPS	'21 P/E	Valuation	Tot. Return
Base Case	8.7%	$1.75	26.5x	$46	-14%
Bull Case	9.7%	$1.80	27.8x	$50	-6%
Bear Case	7.7%	$1.70	25.1x	$43	-19%

**18 through '21*

Valuation: Our $46 price target is 26.5x our FY '21 EPS estimate of $1.75/share. That is a ~15% M&A premium to our water regulated target multiple of 23x. Our bull case valuation of $50 for CWT assumes they can grow EPS at 9.7% 100 bps higher than our base case forecast and trade at a 5% premium to our base case '21 P/E multiple of 26.5x. Our bear case valuation of $43 assumes that they grow earnings at 7.7%, 100 bps lower than our base case and trade at 5% discount to our '21 base case P/E multiple of 26.5x.

Source: Evercore ISI Research

Exhibit 5
SJW Valuation Framework

Valuation	Post Merger	No Merger	Base Case (a)	Valuation	Bull Case	Bear Case
Consolidated 2021 EPS	**$2.55**	**$2.30**		**Consolidated 2021 EPS**	**$2.55**	**$2.30**
Forward P/E Multiple	25.5x	25.5x		Forward P/E Multiple	26.5x	24.5x
Implied Valuation	**$65.0**	**$59.0**	**$62.0**	**Implied Valuation**	**$68.0**	**$56.0**
Current Stock Price (07/25/19)	$64.3	$64.3	$64.3	Current Stock Price (07/25/19)	$64.3	$64.3
Price Appreciation	**1.1%**	**-8.2%**	**-3.6%**	**Price Appreciation**	**5.8%**	**-12.9%**
Dividend Yield	**1.9%**	**1.9%**	**1.9%**	**Dividend Yield**	**1.9%**	**1.9%**
Total Shareholder Return	**3.0%**	**-6.4%**	**-1.7%**	**Total Shareholder Return**	**7.6%**	**-11.0%**

Valuation: Our base case valuation of $62 is an average of our post-merger and no-merger valuations. Firstly, our $65 post-merger valuation is based on a pro-forma FY '21 EPS estimate of $2.55 and a 25.5x P/E multiple, which represents a ~10% M&A premium to our regulated water target multiple of 23.0x. Secondly, our no-merger valuation of $59 is based on a standalone FY '21 EPS estimate of $2.30 and a 25.5x P/E multiple. In our bull case of $68, we assume that the merger goes through and assign a 1.0x higher P/E multiple vs. the base case. In our bear case valuation of SJW, we assume the merger is not consummated and assign a 1.0x lower P/E multiple vs. the base case.

Source: Evercore ISI Research

Exhibit 6
WTR Valuation Framework

SOTP Valuation (Base Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.16	23.0x	$27.00
Gas EPS	$0.48	21.2x	$10.00
	$1.65		$37.00

SOTP Valuation (Bull Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.16	24.1x	$28.00
Gas EPS	$0.48	22.3x	$11.00
	$1.65		$39.00

SOTP Valuation (Bear Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.16	20.7x	$24.00
Gas EPS	$0.48	19.1x	$9.00
	$1.65		$33.00

Valuation: Our $37 target price is based on a SOTP valuation where we assign 23x P/E to earnings contribution from the legacy water business and ~21x to earnings from the gas segment. The 23x water P/E is in line with our water regulated peer average target multiple .The gas multiple of ~21x is also in line with current gas LDC trading valuation multiples. Our bull case valuation of $39 assumes that both the water and gas segment trade at 5% premium to our base case scenario. Our bear case valuation of $33 assumes 10% discount multiple to our base case scenario for both segments.

Source: Evercore ISI Research

Risks. Risks to our thesis include an unfavorable regulatory outcome leading to lower rate base growth and/or lower allowed or earned ROEs in ongoing and future rate cases. Other risks include exposure to unusual weather, impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer, cyber security and water contamination.

TIMESTAMP

(Article 3(1)e and Article 7 of MAR)

Time of dissemination: August 11 2019 08:52

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Buy- Return 10% to 20%
Neutral - Return 0% to 10%
Cautious- Return -10% to 0%
Sell- Return< -10%

For disclosure purposes, ISI Group and ISI UK ratings were viewed as follows: Strong Buy and Buy equate to Buy, Neutral equates to Hold, and Cautious and Sell equate to Sell.

Evercore Group:

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Overweight- the stock is expected to outperform the average total return of the analyst's coverage universe over the next 12 months.
Equal-Weight- the stock is expected to perform in line with the average total return of the analyst's coverage universe over the next 12 months.
Underweight -the stock is expected to underperform the average total return of the analyst's coverage universe over the next 12 months.
Suspended- the company rating, target price and earnings estimates have been temporarily suspended.

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Stocks included in the model portfolio will be weighted from 0 to 100% for Long and 0 to -100% for Short. A stock's weight in the portfolio reflects the analyst's degree of conviction in the stock's rating relative to other stocks in the portfolio. The model portfolio may also include a cash component. At any given time the aggregate weight of the stocks included in the portfolio and the cash component must equal100%.

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Coverage Universe			**Investment Banking Services I Past 12 Months**		
Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	384	51	Buy	253	66
Hold	295	40	Hold	154	52
Sell	40	5	Sell	15	38
Coverage Suspended	21	3	Coverage Suspended	16	76
Rating Suspended	7	1	Rating Suspended	2	29

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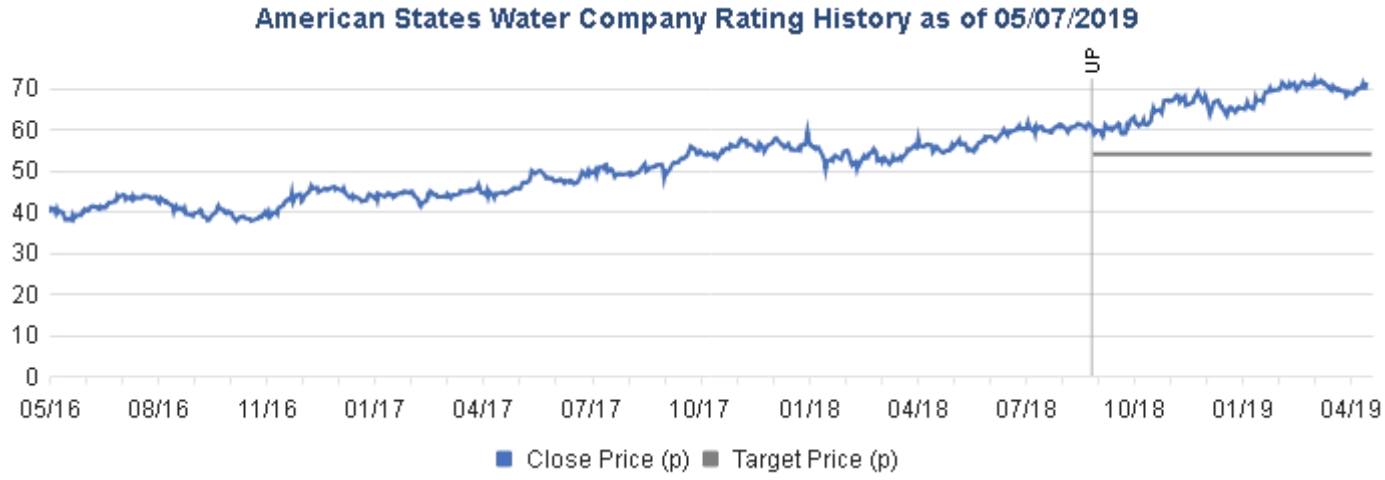

Ratings Key

B	Buy	OP	Outperform	L	Long	CS	Coverage Suspended
H	Hold	IL	In Line	NP	No Position	RS	Rating Suspended
S	Sell	UP	Underperform	S	Short		

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EVERCORE ISI

Energy | Power & Utilities

January 11, 2021

Essential Utilities Inc.

WTRG | $48.31

In Line | TARGET PRICE: $49.00 (from $42.00)

Company Update

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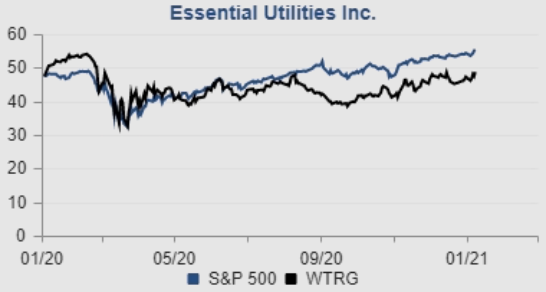
Company Statistics

Market Capitalization (M)	$11,817
Shares Outstanding (M)	245
Dividend	1.03
Dividend Yield	2.1%
Payout Ratio	61.7%
Expected Total Return	3.8%
Fiscal Year End	Dec

Earnings Summary

	2021E	2022E
EPS	**$1.67**	**$1.79**
P/E	**28.9**	**27.0**
EPS vs Consensus	**(0.2)%**	**0.1%**
Consensus EPS	**$1.67**	**$1.79**
Consensus P/E	**28.9**	**27.0**

1 Year Price History



Source: FactSet

Announces '21 EPS Guidance Range, Extends Long-Term Growth Rate Target Through '23

Essential Utilities initiates' 2021 EPS guidance range of $1.64-$1.69, extends 5-7% EPS growth target through 2023. Essential hosted a guidance call earlier today to discuss company's 2021 expected EPS projection and three year outlook. The company initiated 2021 EPS guidance range of $1.64-$1.69 which at the mid-pt of $1.66 is in line with consensus/our estimate of $1.67 and points to year over year growth rate of 7% towards the high end of management targeted 5-7% long term growth rate. WTRG also extended its capex and rate base growth forecast by one year through 2023 and still anticipates water rate base growing by 6-7% (excluding acquisitions) and gas rate base 8-10% on average through that period. Fueling this growth is $3B in expected combined investments from 2020 through 2023. They expect to issue some equity to fund base capex (we model $100MM through 2023), municipal system acquisitions and dividends which are expected to grow in line with earnings. The company also extended its 5-7% EPS growth target through 2023 and introduced 60% emission reduction target by 2035. WTRG anticipates closing the DELCORA acquisition in the second quarter this year and plans on filing a general rate case application in PA later in the year for rate effective in late '21/early '22.

We are introducing '23E of $1.90, raising target price to $49. We are also modestly adjusting our '21/'22 eps estimates to $1.67/$1.79 respectively. Our 23E of $1.90 drives a CAGR of 7% (using 2020 guidance mid-pt of $1.56) which is at the high end of company's targeted 5-7% earnings growth rate. We further note that our EPS forecast could be conservative if WTRG announces more private and municipal water/waste water system acquisitions above their current forecast. Our $49 target price is based on a SOTP where we assign 29.5x P/E to the '23 earnings contribution from the legacy water business and ~ 17.5x to earnings from the gas segment. The 29.5x water P/E is a ~30% premium to our water utility average target multiple of 23x which we think is warranted in this environment given above average residential customer mix which positions them well against COVID related demand headwinds. Majority of their water EPS is derived from PA which is also a relative advantage versus peers. The gas multiple of ~17.5x is also in line with our target Electric/gas utility multiple. We see bull/bear case valuation of $56/$43 respectively, and given the potential upside from municipal water/waste water deals and other complementary growth projects we assign low probability to our bear case scenario, see page 2 of the report.

Q3 2020 Earnings Recap. WTRG reported Q3 '20 Adjusted EPS of $1.01 versus consensus of $1.02. Management Reaffirmed 2020 EPS guidance range of $1.53-$1.58, but expected to be at the top end. WTRG still projects EPS to grow in the range of 5-7% on average from 2019 through 2022. In Q3, company announced offering of 6.7MM shares via an equity forward agreement (~$300MM in proceeds). Proceeds which are expected to be used to fund general corporate purposes, including the acquisition of the Delaware County Regional Water. Quality Control Authority (DELCORA) and other water and wastewater acquisitions in its pipeline.

See inside for detail on the DELCORA opportunity, Repairs Tax Election Uplift, and our price target.

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DELCORA opportunity. In September '19, management had announced a signed purchase agreement with Delaware County Regional Water Authority (DELCORA), following the latter's signing of a letter of intent with Aqua committing to exclusive discussions in August '19. DELCORA is a wastewater conveyance and treatment authority that serves approximately 500,000 people in 42 municipalities in Delaware and Chester Counties in southeastern Pennsylvania. We estimate that this could be a potential ~$300mm rate base / $0.03 EPS annual uplift (included in our forecast), assuming 50%/50% debt/equity financing. WTRG expects to close the transaction in second quarter this year.

Repairs Tax Election Uplift, 8-12c/yr. Essential's 2020 and forward looking EPS guidance includes 8-12c/share annual earnings uplift which is more/less in line with our estimate of ~10c. There may be additional accretion from historical balances pending commission review and final decision. For context, in 2012, Aqua (water utility) changed its tax method of accounting for qualifying utility asset repairs in PA. The tax accounting method was changed to permit the expensing of certain utility asset repairs/maintenance costs that were previously being capitalized and depreciated for tax purposes. The company used flow-through accounting for the tax benefits of the repair tax accounting change per the Pennsylvania rate order from June '12. The flow-through accounting implementation resulted in a reduction in the company's effective income tax rate, which in turn lowered income tax expense and increased net income. WTR's effective tax rate was materially lower than the statuary tax rate at (7.7%) / 6.6% / 8.2% for the years '18 / '17 / '16 respectively. Higher earnings power supported higher returns on equity, which allowed Aqua to invest over $2bn of capital on system improvements over the past seven years without having to go in for rate cases in PA. There could be further earnings upside (~$0.05 annual EPS uplift by our estimate) if the commission allows favorable treatment of the legacy tax balance. WTRG is asking the commission to apply the earnings upside to years 2023 and beyond such that the company can delay its 2023 rate filing by a year.

We are raising our target price to $49; our rating remains In Line. Our $49 target price is based on a SOTP where we now assign 29.5x P/E to the '23 earnings contribution from the legacy water business and ~ 17.5x to earnings from the gas segment. The 29.5x water P/E is a ~30% premium to our water utility average target multiple of 23x which we think is warranted in this environment given above average residential customer mix which positions them well against COVID related demand headwinds. Majority of their water EPS is derived from PA which is also a relative advantage versus peers. The gas multiple of ~17.5x is also in line with our target electric/gas multiple. Our bull case valuation of $56 assumes that they are able to achieve ~$0.06 combined upside from tax repairs, and both the water and gas segment trade at 10% premium to our base case scenario. Our bear case valuation of $43 assumes a 5% discount multiple to our base case scenario for the water segment, current trading multiple of comparable gas LDC's and low end of targeted LT EPS growth. Please see Exhibit 1 for additional details.

Exhibit 1

WTR Valuation Framework

SOTP Valuation (Base Case)	'23E	'23 P/E	Valuation
Legacy WTR EPS	$1.33	29.5x	$39.00
Gas EPS	$0.57	17.5x	$10.00
	$1.90		$49.00

SOTP Valuation (Bull Case)	'23E	'23 P/E	Valuation
Legacy WTR EPS	$1.37	32.5x	$45.00
Gas EPS	$0.59	19.3x	$11.00
	$1.96		$56.00

SOTP Valuation (Bear Case)	'23E	'23 P/E	Valuation
Legacy WTR EPS	$1.26	28.1x	$35.00
Gas EPS	$0.54	14.7x	$8.00
	$1.80		$43.00

Source: Evercore ISI Research

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VALUATION METHODOLOGY

Our $49 target price is based on a SOTP where we now assign 29.5x P/E to the '23 earnings contribution from the legacy water business and ~ 17.5x to earnings from the gas segment. The 29.5x water P/E is a ~30% premium to our water utility average target multiple of 23x which we think is warranted in this environment given above average residential customer mix which positions them well against COVID related demand headwinds. Majority of their water EPS is derived from PA which is also a relative advantage versus peers. The gas multiple of ~17.5x is also in line with our target electric/gas multiple

RISKS

Risks to our thesis include an unfavorable regulatory outcome leading to lower rate base growth and/or lower allowed or earned ROEs in ongoing and future rate cases. Other risks include exposure to unusual weather, impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer, cyber security and water contamination.

COMPANIES UNDER COVERAGE BY AUTHOR

Symbol	Company	Rating	Price (2021-11-01)	Evercore ISI Target
AEE	Ameren Corp.	Outperform	$75.06	$84.00
AEP	American Electric Power	Outperform	$78.78	$95.00
AES	The AES Corporation	Outperform	$25.50	$23.00
AWK	American Water Works Company, Inc.	Outperform	$156.84	$129.00
AWR	American States Water Company	Underperform	$80.61	$60.00
CMS	CMS Energy Corp.	In Line	$57.16	$63.00
CNP	CenterPoint Energy, Inc.	In Line	$20.78	$23.00
CWEN	Clearway Energy	In Line	$34.89	$22.00
CWT	California Water Service Group	In Line	$55.29	$40.00
D	Dominion Energy, Inc	In Line	$72.63	$77.00
DTE	DTE Energy Co.	In Line	$117.73	$121.00
DUK	Duke Energy Corp.	In Line	$89.28	$89.00
ED	Consolidated Edison Inc.	In Line	$68.59	$80.00
EIX	Edison International	In Line	$61.50	$72.00
ES	Eversource Energy	In Line	$89.23	$91.00
ETR	Entergy Corp.	In Line	$94.44	$106.00
EVRG	Evergy	Outperform	$52.55	$62.00
EXC	Exelon Corp.	Outperform	$41.95	$45.00
FE	FirstEnergy Corp.	In Line	$30.36	$41.00
HE	Hawaiian Electric Industries Inc.	Underperform	$34.06	$34.00
NEE	NextEra Energy Inc	In Line	$79.71	$75.00
NI	NiSource Inc	Outperform	$21.82	$26.00
NRG	NRG Energy Inc.	Outperform	$39.69	$40.00
OGE	OGE Energy Corp	Outperform	$31.61	$35.00
PCG	PG&E Corp.	Rating Suspended	$12.17	
PEG	Public Service Enterprise Group	In Line	$56.90	$53.00
PNW	Pinnacle West Capital Corp.	In Line	$76.77	$85.00
PPL	PPL Corp.	In Line	$27.77	$31.00
SJW	SJW Group	In Line	$69.28	$60.00
SO	Southern Co.	In Line	$61.24	$59.00
SRE	Sempra Energy	Outperform	$118.25	$138.00
VST	Vistra Energy Corp	Outperform	$21.27	$27.00
WEC	WEC Energy Group, Inc.	In Line	$86.88	$93.00
WTRG	Essential Utilities Inc.	In Line	$48.31	$49.00
XEL	Xcel Energy Inc.	In Line	$64.37	$65.00

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Time of dissemination: January 11 2021 06:49 PM ET

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Outperform- the total forecasted return is expected to be greater than the expected total return of the analyst's coverage universe
In Line- the total forecasted return is expected to be in line with the expected total return of the analyst's universe
Underperform- the total forecasted return is expected to be less than the expected total return of the analyst's universe
Coverage Suspended- the rating and target price have been removed pursuant to Evercore ISI policy when Evercore is acting in an advisory capacity in a merger or strategic transaction involving this company and in certain other circumstances.*
Rating Suspended- Evercore ISI has suspended the rating and target price for this stock because there is not sufficient fundamental basis for determining, or there are legal, regulatory or policy constraints around publishing, a rating or target price. The previous rating and target price, if any, are no longer in effect for this company and should not be relied upon.*

*Prior to October 10, 2015, the "Coverage Suspended" and "Rating Suspended" categories were included in the category "Suspended."

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Historical Ratings Definitions

Prior to March 2, 2017, Evercore ISI's recommendations were based on a stock's total forecasted return over the next 12 months:

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Buy- the total forecasted return is expected to be greater than 10%
Hold- the total forecasted return is expected to be greater than or equal to 0% and less than or equal to 10%
Sell -the total forecasted return is expected to be less than 0%

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ISI Group and ISI UK:

Prior to October 10, 2014, the ratings system of ISI Group LLC and ISI UK which was based on a 12-month risk adjusted total return:

Strong Buy- Return > 20%
Buy- Return 10% to 20%
Neutral - Return 0% to 10%
Cautious- Return -10% to 0%
Sell- Return< -10%

For disclosure purposes, ISI Group and ISI UK ratings were viewed as follows: Strong Buy and Buy equate to Buy, Neutral equates to Hold, and Cautious and Sell equate to Sell.

Evercore Group:

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Overweight- the stock is expected to outperform the average total return of the analyst's coverage universe over the next 12 months.
Equal-Weight- the stock is expected to perform in line with the average total return of the analyst's coverage universe over the next 12 months.
Underweight -the stock is expected to underperform the average total return of the analyst's coverage universe over the next 12 months.
Suspended- the company rating, target price and earnings estimates have been temporarily suspended.

For disclosure purposes, Evercore Group's prior "Overweight," "Equal-Weight" and "Underweight" ratings were viewed as "Buy," "Hold" and "Sell," respectively.

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Long- the stock is a positive holding in the model portfolio; the total forecasted return is expected to be greater than 0%.
Short- the stock is a negative holding in the model portfolio; the total forecasted return is expected to be less than 0%.
No Position- the stock is not included in the model portfolio.
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Stocks included in the model portfolio will be weighted from 0 to 100% for Long and 0 to -100% for Short. A stock's weight in the portfolio reflects the analyst's degree of conviction in the stock's rating relative to other stocks in the portfolio. The model portfolio may also include a cash component. At any given time the aggregate weight of the stocks included in the portfolio and the cash component must equal100%.

Stocks assigned ratings under the alternative model portfolio-based coverage system cannot also be rated by Evercore ISI's Current Ratings definitions of Outperform, In Line and Underperform.

FINRA requires that members who use a ratings system with terms other than "Buy," "Hold/Neutral" and "Sell," to equate their own ratings to these categories. For this purpose, and in the Evercore ISI ratings distribution below, our Long, No Position and Short ratings can be equated to Buy, Hold and Sell respectively.

Evercore ISI rating (as of 01/11/2021)

Coverage Universe			**Investment Banking Services I Past 12 Months**		
Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	438	55	Buy	98	22
Hold	301	38	Hold	29	10
Sell	28	4	Sell	3	11
Coverage Suspended	13	2	Coverage Suspended	5	38
Rating Suspended	12	2	Rating Suspended	3	25

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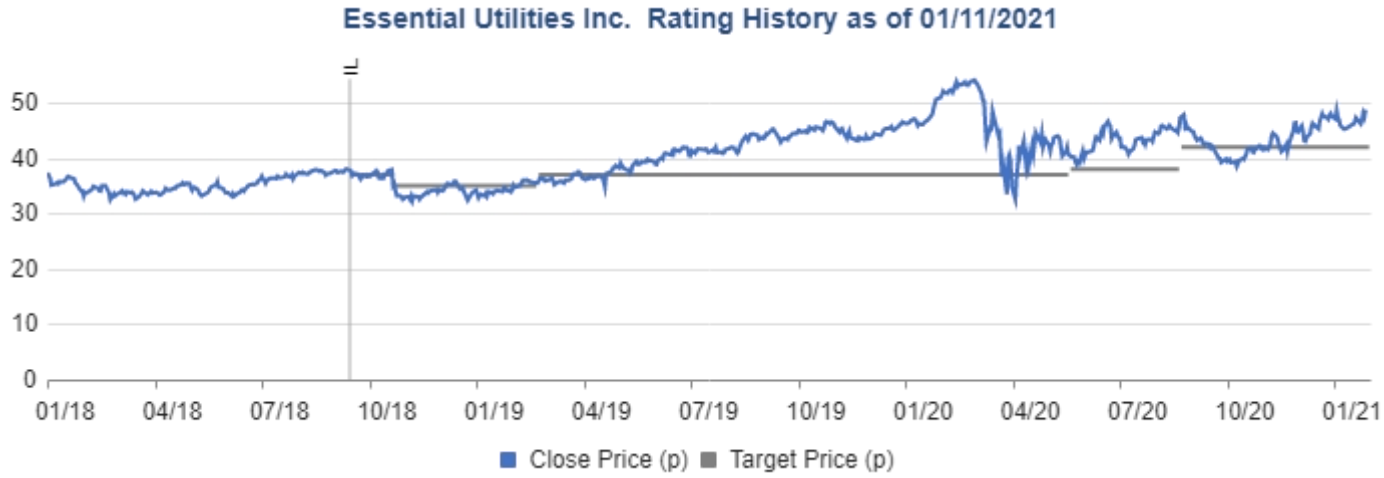

Ratings Key

B	Buy	OP	Outperform	L	Long	CS	Coverage Suspended
H	Hold	IL	In Line	NP	No Position	RS	Rating Suspended
S	Sell	UP	Underperform	S	Short		

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EVERCORE ISI

Energy | Power & Utilities

February 27, 2020

Essential Utilities Inc.

WTRG | $46.96

In Line | TARGET PRICE: $37.00

Company Update

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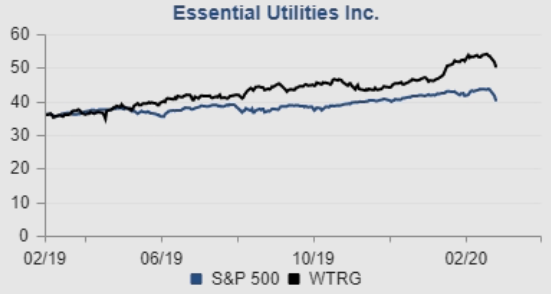
Company Statistics

Market Capitalization (M)	$9,559
Shares Outstanding (M)	216
Dividend	0.91
Dividend Yield	2.0%
Payout Ratio	61.2%
Expected Total Return	(14.4)%
Fiscal Year End	Dec

Earnings Summary

	2019E	2020E	2021E
EPS	**$1.48**	**$1.56**	**$1.64**
P/E	**29.9**	**28.3**	**27.0**
EPS vs Consensus	**1.9%**	**(1.8)%**	**(2.4)%**
Consensus EPS	**$1.45**	**$1.59**	**$1.68**
Consensus P/E	**30.5**	**27.8**	**26.4**

1 Year Price History



Source: FactSet

LT Growth Outlook Below Expectations

WTRG lagged peers today (-8% vs water uts/UTY -6%/-5%) amid a broad market sell off on a weaker than expected LT EPS growth outlook. The company initiated 2020 EPS guidance range of $1.53 - $1.58 and projects earnings to grow in the range of 5-7% on average from 2019 through 2022. Starting with 2019 adjusted EPS of $1.47, 6% EPS growth rate mid-pt would translate into 2021 EPS of $1.65 (includes ~10c repair tax uplift) materially below our bull case scenario of $1.78 which assumes repair election + Delcora accretion, see our last note here. Peoples Gas acquisition is expected to close in March 2020, combined water and gas, Essential expects to invest $2.8B from 2019 through 2022. The abovementioned capex investment (including ~$25MM towards reducing PFOS/PFOA levels) is projected to generate rate base growth of 6-7% in the water business and 8-10% in gas through the forecast period. We will be back with a model update and our '22 EPS projection, see additional details within.

2020 Guidance & LT EPS Growth. As we stated earlier, Essential initiated 2020 EPS guidance range of $1.53-$1.58 and projects EPS to grow in the range of 5-7% on average from 2019 through 2022. Both the guidance and LT earnings growth rate include 8-12c/year EPS uplift from repair tax flow through at Peoples gas. $2.8B in planned investments through 2022 is driving projected 6-7%/8-10% rate base growth at water/gas during that period. Included in the capex plan is $25MM in investment towards reducing PFOS/PFOA (potentially harmful chemicals in the water stream) levels to 13 parts per trillion across their service territory significantly below federal governments health advisory level of 70 parts per trillion. The company pointed to lower future earned ROE's (2019 returns were higher due to repairs flow through in the water business), regulatory lag on municipal acquisitions, and dilution from additional equity units as primary drivers of the lower expected EPS CAGR versus rate base growth.

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Repairs Tax Election Uplift, 8-12c/yr. Essential's 2020 and forward looking EPS guidance includes 8-12c/share annual earnings uplift which is more/less in line with our estimate of ~10c. There may be additional accretion from historical balances pending commission review and final decision. For context, in 2012, Aqua (water utility) changed its tax method of accounting for qualifying utility asset repairs in PA. The tax accounting method was changed to permit the expensing of certain utility asset repairs/maintenance costs that were previously being capitalized and depreciated for tax purposes. The company used flow-through accounting for the tax benefits of the repair tax accounting change per the Pennsylvania rate order from June '12. The flow-through accounting implementation resulted in a reduction in the company's effective income tax rate, which in turn lowered income tax expense and increased net income. WTR's effective tax rate was materially lower than the statuary tax rate at (7.7%) / 6.6% / 8.2% for the years '18 / '17 / '16 respectively. Higher earnings power supported higher returns on equity, which allowed Aqua to invest over $2bn of capital on system improvements over the past seven years without having to go in for rate cases in PA.

DELCORA Acquisition. In September '19, management had announced a signed purchase agreement with Delaware County Regional Water Authority (DELCORA), following DELCORA signing of a letter of intent with Aqua committing to exclusive discussions in August '19. DELCORA is a wastewater conveyance and treatment authority that serves approximately 500,000 people in 42 municipalities in Delaware and Chester Counties in southeastern Pennsylvania. We estimate that this could be a potential ~$300mm rate base / $0.03 EPS uplift in '21 (company expects to close in late '20/early '21), assuming 50%/50% debt/equity financing.

Peoples Gas Update. In March 2019, Essential received regulatory approval for the Peoples transaction from the Kentucky Public Service Commission, followed by approval in Kentucky next month. On 10/28/19 the PA Administrative Law Judge assigned to the case issued a proposed decision approving the Peoples Gas acquisition which was subsequently approved by the Commission in January this year. The company expects to complete the acquisition in March 2020.

2019 EPS. Essential reported FY 2019 adjusted EPS of $1.47 which was more/less in line with our forecast of $1.48. Compare to prior year EPS was $ 0.06 or 4.3% higher driven by rate/surcharges supporting capex +$0.16, customer growth +$0.03, higher expenses -$0.06, and lower usage/other -$0.07.

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VALUATION METHODOLOGY

Our $37 target price is based on a SOTP where we assign 23.0x P/E to the earnings contribution from the legacy water business and ~21.0x to earnings from the gas segment. The 23.0x water P/E is in line with our water regulated peer average target multiple. The gas multiple of ~21.0x is also in line with current gas LDC trading valuation multiples.

RISKS

Risks to our thesis include an unfavorable regulatory outcome leading to lower rate base growth and/or lower allowed or earned ROEs in ongoing and future rate cases. Other risks include exposure to unusual weather, impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer, cyber security and water contamination.

COMPANIES UNDER COVERAGE BY AUTHOR

Symbol	Company	Rating	Price (2020-27-02)	Evercore ISI Target
AWK	American Water Works Company, Inc.	Outperform	$128.81	$118.00
AWR	American States Water Company	Underperform	$82.80	$60.00
CWT	California Water Service Group	In Line	$50.69	$46.00
DCP	DCP Midstream, LP	In Line	$15.52	$29.00
ENB	Enbridge Inc.	In Line	$37.89	$48.00
EPD	Enterprise Products Partners LP	Outperform	$23.00	$32.00
ET	Energy Transfer Partners, L.P.	Outperform	$10.78	$18.00
KMI	Kinder Morgan, Inc.	Outperform	$19.62	$22.00
MMP	Magellan Midstream Partners, L.P.	Outperform	$55.47	$67.00
MPLX	MPLX LP	In Line	$19.15	$34.00
OKE	ONEOK Inc.	In Line	$67.78	$65.00
PAA	Plains All American Pipeline, L.P.	In Line	$13.69	$20.00
PAGP	Plains GP Holdings, L.P.	In Line	$13.83	$25.00
SJW	SJW Group	In Line	$65.23	$65.00
TRGP	Targa Resources Corp	In Line	$32.54	$39.00
TRP	TC Energy Corp.	In Line	CAD71.83	CAD60.00
WMB	The Williams Companies Inc.	Outperform	$19.04	$28.00
WTRG	Essential Utilities Inc.	In Line	$46.96	$37.00

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Underperform- the total forecasted return is expected to be less than the expected total return of the analyst's universe
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Rating Suspended- Evercore ISI has suspended the rating and target price for this stock because there is not sufficient fundamental basis for determining, or there are legal, regulatory or policy constraints around publishing, a rating or target price. The previous rating and target price, if any, are no longer in effect for this company and should not be relied upon.*

*Prior to October 10, 2015, the "Coverage Suspended" and "Rating Suspended" categories were included in the category "Suspended."

FINRA requires that members who use a ratings system with terms other than "Buy," "Hold/Neutral" and "Sell" to equate their own ratings to these categories. For this purpose, and in the Evercore ISI ratings distribution below, our Outperform, In Line, and Underperform ratings can be equated to Buy, Hold and Sell, respectively.

Historical Ratings Definitions

Prior to March 2, 2017, Evercore ISI's recommendations were based on a stock's total forecasted return over the next 12 months:

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Buy- the total forecasted return is expected to be greater than 10%
Hold- the total forecasted return is expected to be greater than or equal to 0% and less than or equal to 10%
Sell -the total forecasted return is expected to be less than 0%

On October 31, 2014, Evercore Partners acquired International Strategy & Investment Group LLC ("ISI Group") and ISI UK (the "Acquisition") and transferred Evercore Group's research, sales and trading businesses to ISI Group. On December 31, 2015, the combined research, sales and trading businesses were transferred back to Evercore Group in an internal reorganization. Since the Acquisition, the combined research, sales and trading businesses have operated under the global marketing brand name Evercore ISI.

ISI Group and ISI UK:

Prior to October 10, 2014, the ratings system of ISI Group LLC and ISI UK which was based on a 12-month risk adjusted total return:

Strong Buy- Return > 20%
Buy- Return 10% to 20%
Neutral - Return 0% to 10%
Cautious- Return -10% to 0%
Sell- Return< -10%

For disclosure purposes, ISI Group and ISI UK ratings were viewed as follows: Strong Buy and Buy equate to Buy, Neutral equates to Hold, and Cautious and Sell equate to Sell.

Evercore Group:

Prior to October 10, 2014, the rating system of Evercore Group was based on a stock's expected total return relative to the analyst's coverage universe over the following 12 months. Stocks under coverage were divided into three categories:

Overweight- the stock is expected to outperform the average total return of the analyst's coverage universe over the next 12 months.
Equal-Weight- the stock is expected to perform in line with the average total return of the analyst's coverage universe over the next 12 months.
Underweight -the stock is expected to underperform the average total return of the analyst's coverage universe over the next 12 months.
Suspended- the company rating, target price and earnings estimates have been temporarily suspended.

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Long- the stock is a positive holding in the model portfolio; the total forecasted return is expected to be greater than 0%.
Short- the stock is a negative holding in the model portfolio; the total forecasted return is expected to be less than 0%.
No Position- the stock is not included in the model portfolio.
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Stocks included in the model portfolio will be weighted from 0 to 100% for Long and 0 to -100% for Short. A stock's weight in the portfolio reflects the analyst's degree of conviction in the stock's rating relative to other stocks in the portfolio. The model portfolio may also include a cash component. At any given time the aggregate weight of the stocks included in the portfolio and the cash component must equal100%.

Stocks assigned ratings under the alternative model portfolio-based coverage system cannot also be rated by Evercore ISI's Current Ratings definitions of Outperform, In Line and Underperform.

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Evercore ISI rating (as of 02/27/2020)

Coverage Universe			**Investment Banking Services I Past 12 Months**		
Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	411	54	Buy	99	24
Hold	276	36	Hold	37	13
Sell	43	6	Sell	6	14
Coverage Suspended	23	3	Coverage Suspended	8	35
Rating Suspended	14	2	Rating Suspended	2	14

Issuer-Specific Disclosures (as of February 27, 2020)

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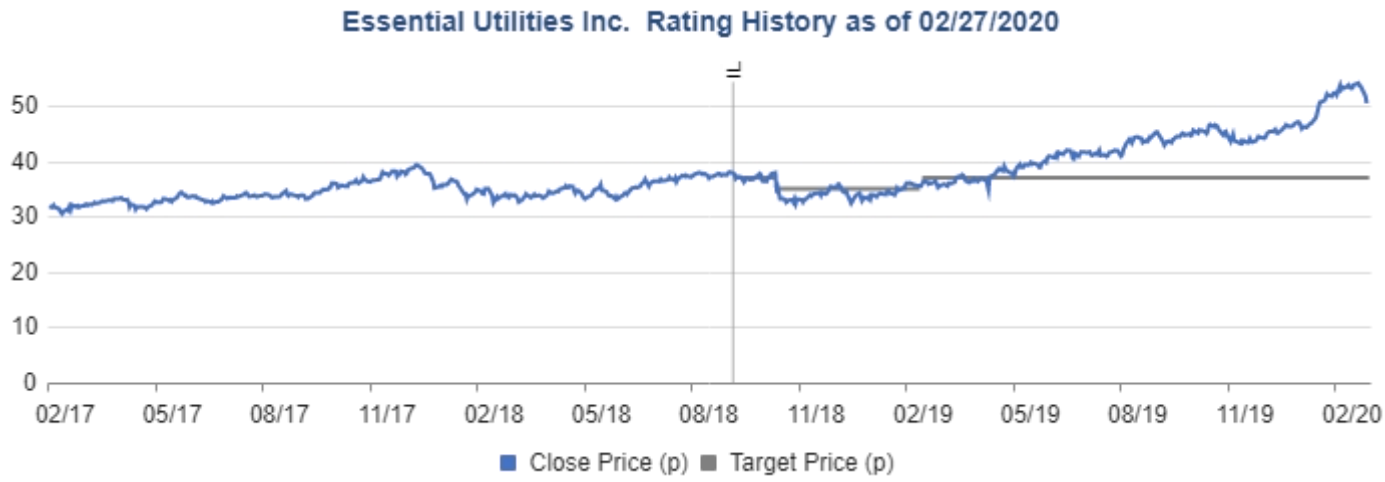
Price Charts



Ratings Key

B	Buy	OP	Outperform	L	Long	CS	Coverage Suspended
H	Hold	IL	In Line	NP	No Position	RS	Rating Suspended
S	Sell	UP	Underperform	S	Short		

GENERAL DISCLOSURES

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In compliance with the European Securities and Markets Authority's Market Abuse Regulation, a list of all Evercore ISI recommendations disseminated in the preceding 12 months for the subject companies herein, may be found at the following site: https://evercoreisi.mediasterling.com/disclosure.

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EVERCORE ISI

Energy | Power & Utilities

May 07, 2020

Essential Utilities Inc.

WTRG | $40.59

In Line | TARGET PRICE: $38.00 (from $37.00)

Earnings Report

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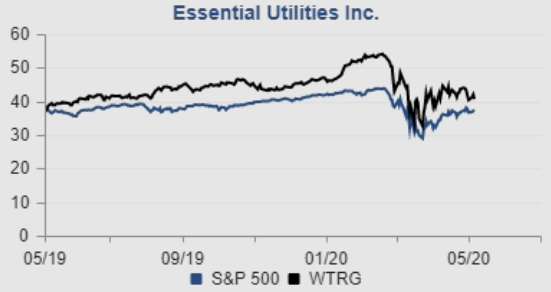
Company Statistics

Market Capitalization (M)	$8,597
Shares Outstanding (M)	223
Dividend	0.95
Dividend Yield	2.5%
Payout Ratio	61.2%
Expected Total Return	1.2%
Fiscal Year End	Dec

Earnings Summary

	2020E	2021E	2022E
EPS	**$1.55**	**$1.65**	**$1.80**
P/E	**24.8**	**23.3**	**21.3**
EPS vs Consensus	**(0.8)%**	**0.2%**	**1.9%**
Consensus EPS	**$1.57**	**$1.65**	**$1.77**
Consensus P/E	**24.6**	**23.3**	**21.8**

1 Year Price History



Source: FactSet

Good quarter, 2020 & LT EPS Targets Reaffirmed

WTRG reported Q1 '20 Adjusted EPS of $0.60 versus consensus of $0.58. The company booked $0.02 EPS uplift from repairs pass-through in the quarter in line with original guidance of $0.08 - $0.12 EPS benefit for the year. There could be further potential earnings upside if the commission allows favorable treatment of the legacy tax balance (not in our forecast). Essential also reaffirmed its 2020 EPS guidance range of $1.53-$1.58 and still projects EPS to grow in the range of 5-7% on average from 2019 through 2022. The company filed for Delcora waste water acquisition approval with the commission in the first quarter and still expects to issue $300MM in equity later this year to finance the deal ($0.03 EPS contribution included in our forecast). They are closely monitoring COVID-related implications on consumption, collections and capital expenditures and based on current available information don't expect a material financial impact to 2020 EPS.

Target Price $38, rating still In Line. We are maintaining our EPS estimates which incorporate company guidance issued at analyst day earlier in the year. Our '20/'21/'22 EPS forecast of $1.55/$1.65/$1.80 drives a '19 through '22 CAGR of ~7% towards the high end of company's targeted EPS growth rate of 5-7%. Our $38 target price is based on a SOTP where we assign 23.0x P/E to the earnings contribution from the legacy water business and ~17x to earnings from the gas segment. The 23.0x water P/E is in line with our water regulated peer average target multiple. The gas multiple of ~17x is also in line with current gas LDC trading valuation multiples. Rating remains In Line

Repairs Tax Election Uplift, 8-12c/yr. Essential's 2020 and forward looking EPS guidance includes 8-12c/share annual earnings uplift which is more/less in line with our estimate of ~10c. There may be additional accretion from historical balances pending commission review and final decision. For context, in 2012, Aqua (water utility) changed its tax method of accounting for qualifying utility asset repairs in PA. The tax accounting method was changed to permit the expensing of certain utility asset repairs/maintenance costs that were previously being capitalized and depreciated for tax purposes. The company used flow-through accounting for the tax benefits of the repair tax accounting change per the Pennsylvania rate order from June '12. The flow-through accounting implementation resulted in a reduction in the company's effective income tax rate, which in turn lowered income tax expense and increased net income. WTR's effective tax rate was materially lower than the statuary tax rate at (7.7%) / 6.6% / 8.2% for the years '18 / '17 / '16 respectively. Higher earnings power supported higher returns on equity, which allowed Aqua to invest over $2bn of capital on system improvements over the past seven years without having to go in for rate cases in PA. There could be further earnings upside (~$0.05 annual EPS uplift by our estimate) if the commission allows favorable treatment of the legacy tax balance.

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VALUATION METHODOLOGY

Our $38 target price is based on a SOTP where we assign 23.0x P/E to the earnings contribution from the legacy water business and ~17x to earnings from the gas segment. The 23.0x water P/E is in line with our water regulated peer average target multiple. The gas multiple of ~17x is also in line with current gas LDC trading valuation multiples.

RISKS

Risks to our thesis include an unfavorable regulatory outcome leading to lower rate base growth and/or lower allowed or earned ROEs in ongoing and future rate cases. Other risks include exposure to unusual weather, impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer, cyber security and water contamination.

COMPANIES UNDER COVERAGE BY AUTHOR

Symbol	Company	Rating	Price (2020-07-05)	Evercore ISI Target
AEE	Ameren Corp.	Outperform	$69.95	$84.00
AEP	American Electric Power	Outperform	$78.79	$95.00
AES	The AES Corporation	Outperform	$12.14	$20.00
AGR	Avangrid Inc	In Line	$41.88	$46.00
AWK	American Water Works Company, Inc.	Outperform	$119.25	$118.00
AWR	American States Water Company	Underperform	$74.17	$60.00
CMS	CMS Energy Corp.	In Line	$54.52	$63.00
CNP	CenterPoint Energy, Inc.	In Line	$17.75	$17.00
CWEN	Clearway Energy	In Line	$20.48	$20.00
CWT	California Water Service Group	In Line	$45.10	$46.00
D	Dominion Energy, Inc	In Line	$78.22	$82.00
DTE	DTE Energy Co.	In Line	$99.18	$120.00
DUK	Duke Energy Corp.	In Line	$80.51	$90.00
ED	Consolidated Edison Inc.	In Line	$74.53	$86.00
EIX	Edison International	In Line	$54.78	$80.00
ES	Eversource Energy	In Line	$77.90	$91.00
ETR	Entergy Corp.	In Line	$93.08	$106.00
EVRG	Evergy	In Line	$56.15	$64.00
EXC	Exelon Corp.	Outperform	$35.07	$49.00
FCFE18-MX	CFE Capital S. de R.L. de C.V.	Outperform	MXN19.30	MXN19.00
FE	FirstEnergy Corp.	Outperform	$40.26	$50.00
HE	Hawaiian Electric Industries Inc.	Underperform	$36.72	$36.00
NEE	NextEra Energy Inc	In Line	$226.04	$249.00
NI	NiSource Inc	Outperform	$22.97	$28.00
NRG	NRG Energy Inc.	Outperform	$32.13	$47.00
OGE	OGE Energy Corp	Outperform	$29.30	$35.00
PCG	PG&E Corp.	Rating Suspended	$11.15	
PEG	Public Service Enterprise Group	In Line	$47.94	$53.00
PNM	PNM Resources, Inc	In Line	$38.39	$44.00
PNW	Pinnacle West Capital Corp.	In Line	$72.05	$85.00
PPL	PPL Corp.	In Line	$24.36	$31.00
SJW	SJW Group	In Line	$58.61	$65.00
SO	Southern Co.	In Line	$54.33	$59.00
SRE	Sempra Energy	Outperform	$123.91	$138.00
VST	Vistra Energy Corp	Outperform	$17.95	$32.00
WEC	WEC Energy Group, Inc.	In Line	$85.36	$93.00
WTRG	Essential Utilities Inc.	In Line	$40.59	$38.00
XEL	Xcel Energy Inc.	In Line	$60.06	$65.00

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TIMESTAMP

(Article 3(1)e and Article 7 of MAR)

Time of dissemination: May 07 2020 08:34 PM ET

ANALYST CERTIFICATION

The analysts, Durgesh Chopra, Tulkin Niyazov, Michael Lonegan, Caroline Bone, primarily responsible for the preparation of this research report attest to the following: (1) that the views and opinions rendered in this research report reflect his or her personal views about the subject companies or issuers; and (2) that no part of the research analyst's compensation was, is, or will be directly related to the specific recommendations or views in this research report.

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Ratings Definitions

Current Ratings Definition

Evercore ISI's recommendations are based on a stock's total forecasted return over the next 12 months. Total forecasted return is equal to the expected percentage price return plus gross dividend yield. We divide our stocks under coverage into three primary ratings categories, with the following return guidelines:

Outperform- the total forecasted return is expected to be greater than the expected total return of the analyst's coverage universe
In Line- the total forecasted return is expected to be in line with the expected total return of the analyst's universe
Underperform- the total forecasted return is expected to be less than the expected total return of the analyst's universe
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Buy- Return 10% to 20%
Neutral - Return 0% to 10%
Cautious- Return -10% to 0%
Sell- Return< -10%

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Evercore ISI rating (as of 05/07/2020)

Coverage Universe			**Investment Banking Services I Past 12 Months**		
Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	366	48	Buy	97	27
Hold	304	39	Hold	49	16
Sell	54	7	Sell	4	7
Coverage Suspended	33	4	Coverage Suspended	11	33
Rating Suspended	13	2	Rating Suspended	2	15

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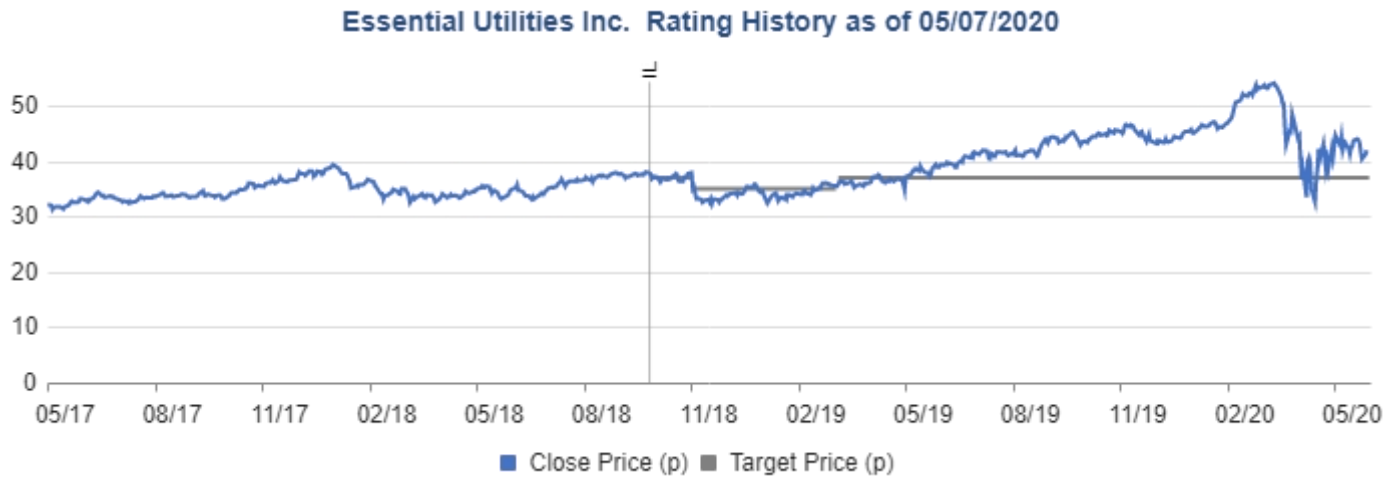
Price Charts



Ratings Key

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H	Hold	IL	In Line	NP	No Position	RS	Rating Suspended
S	Sell	UP	Underperform	S	Short		

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EVERCORE ISI

Energy | Power & Utilities

August 07, 2020

Essential Utilities Inc.

WTRG | $45.56

In Line | TARGET PRICE: $42.00 (from $38.00)

Earnings Report

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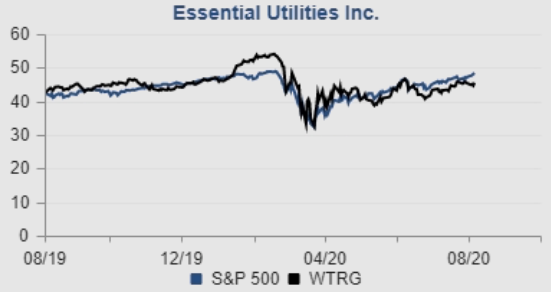
Company Statistics

Market Capitalization (M)	$8,597
Shares Outstanding (M)	223
Dividend	1.03
Dividend Yield	2.7%
Payout Ratio	66.1%
Expected Total Return	11.8%
Fiscal Year End	Dec

Earnings Summary

	2020E	2021E	2022E
EPS	**$1.55**	**$1.65**	**$1.80**
P/E	**24.8**	**23.3**	**21.3**
EPS vs Consensus	**(0.8)%**	**0.2%**	**1.9%**
Consensus EPS	**$1.57**	**$1.65**	**$1.77**
Consensus P/E	**24.6**	**23.3**	**21.8**

1 Year Price History



Source: FactSet

Solid Quarter, LT Outlook Reaffirmed

Essential posted a solid beat in the second quarter reporting EPS of $0.29 versus consensus of $0.23. Helped in part by favorable weather, residential load more the offset decline in Commercial/Industrial usage resulting in no meaningful COVID impact during the quarter. The company filed for repair tax catch-up with the PA Commission (~$0.05 annual EPS uplift if approved our estimate) and advanced Delcora transaction process expected to close early next year. They still expect to issue $300MM in equity later this year to finance the deal ($0.03 EPS contribution included in our forecast). WTRG also reaffirmed its 2020 EPS guidance range of $1.53-$1.58 and still projects EPS to grow in the range of 5-7% on average from 2019 through 2022.

Target Price $42, rating In Line. Our $42 target price is based on a SOTP where we now assign 26.5x P/E to the '22 earnings contribution from the legacy water business and ~ 16.5x to earnings from the gas segment. The 26.5x water P/E is a ~15% premium to our water utility average target multiple of 23x which we think is warranted in this environment given above average residential customer mix which positions them well against COVID related demand headwinds. Majority of their water EPS is derived from PA which is also a relative advantage versus peers. The gas multiple of ~16.5x is also in line with current gas LDC. We see bull/bear case valuation of $48/$38 respectively, and given the potential upside opportunity from tax catch up, municipal water/waste water deals and other complementary growth projects we assign low probability to our bear case scenario, see page 2 of the report.

Repairs Tax Election Uplift, 8-12c/yr. Essential's 2020 and forward looking EPS guidance includes 8-12c/share annual earnings uplift which is more/less in line with our estimate of ~10c. There may be additional accretion from historical balances pending commission review and final decision. For context, in 2012, Aqua (water utility) changed its tax method of accounting for qualifying utility asset repairs in PA. The tax accounting method was changed to permit the expensing of certain utility asset repairs/maintenance costs that were previously being capitalized and depreciated for tax purposes. The company used flow-through accounting for the tax benefits of the repair tax accounting change per the Pennsylvania rate order from June '12. The flow-through accounting implementation resulted in a reduction in the company's effective income tax rate, which in turn lowered income tax expense and increased net income. WTR's effective tax rate was materially lower than the statuary tax rate at (7.7%) / 6.6% / 8.2% for the years '18 / '17 / '16 respectively. Higher earnings power supported higher returns on equity, which allowed Aqua to invest over $2bn of capital on system improvements over the past seven years without having to go in for rate cases in PA. There could be further earnings upside (~$0.05 annual EPS uplift by our estimate) if the commission allows favorable treatment of the legacy tax balance.

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DELCORA opportunity. In September '19, management had announced a signed purchase agreement with Delaware County Regional Water Authority (DELCORA), following the latter's signing of a letter of intent with Aqua committing to exclusive discussions in August '19. DELCORA is a wastewater conveyance and treatment authority that serves approximately 500,000 people in 42 municipalities in Delaware and Chester Counties in southeastern Pennsylvania. We estimate that this could be a potential ~$300mm rate base / $0.03 EPS uplift in '21 (included in our forecast), assuming 50%/50% debt/equity financing.

We are changing our PT to $42 for WTR; our rating remains In Line. Our $42 target price is based on a SOTP where we now assign 26.5x P/E to the '22 earnings contribution from the legacy water business and ~ 16.5x to earnings from the gas segment. The 26.5x water P/E is a ~15% premium to our water utility average target multiple of 23x which we think is warranted in this environment given above average residential customer mix which positions them well against COVID related demand headwinds. Majority of their water EPS is derived from PA which is also a relative advantage versus peers. The gas multiple of ~16.5x is also in line with current gas LDC. Our bull case valuation of $48 assumes that they are able to achieve ~$0.05 combined upside from tax repairs, and both the water and gas segment trade at 10% premium to our base case scenario. Our bear case valuation of $38 assumes a 5% discount multiple to our base case scenario for both segments and low end of targeted LT EPS growth. Please see Exhibit 1 for additional details.

Exhibit 1
WTR Valuation Framework

SOTP Valuation (Base Case)	'22E	'21 P/E	Valuation
Legacy WTR EPS	$1.26	26.4x	$33.00
Gas EPS	$0.54	16.5x	$9.00
	$1.80		$42.00

SOTP Valuation (Bull Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.29	29.0x	$38.00
Gas EPS	$0.55	18.1x	$10.00
	$1.85		$48.00

SOTP Valuation (Bear Case)	'21E	'21 P/E	Valuation
Legacy WTR EPS	$1.19	25.1x	$30.00
Gas EPS	$0.51	15.7x	$8.00
	$1.70		$38.00

Source: Evercore ISI Research

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VALUATION METHODOLOGY

Our $42 target price is based on a SOTP where we now assign 26.5x P/E to the '22 earnings contribution from the legacy water business and ~ 16.5x to earnings from the gas segment. The 26.5x water P/E is a ~15% premium to our water utility average target multiple of 23x which we think is warranted in this environment given above average residential customer mix which positions them well against COVID related demand headwinds.

RISKS

Risks to our thesis include an unfavorable regulatory outcome leading to lower rate base growth and/or lower allowed or earned ROEs in ongoing and future rate cases. Other risks include exposure to unusual weather, impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer, cyber security and water contamination.

COMPANIES UNDER COVERAGE BY AUTHOR

Symbol	Company	Rating	Price (2020-07-08)	Evercore ISI Target
AEE	Ameren Corp.	Outperform	$81.06	$84.00
AEP	American Electric Power	Outperform	$85.37	$95.00
AES	The AES Corporation	Outperform	$16.55	$20.00
AGR	Avangrid Inc	In Line	$48.39	$46.00
AWK	American Water Works Company, Inc.	Outperform	$146.97	$129.00
AWR	American States Water Company	Underperform	$76.65	$60.00
CMS	CMS Energy Corp.	In Line	$61.75	$63.00
CNP	CenterPoint Energy, Inc.	In Line	$20.27	$18.00
CWEN	Clearway Energy	In Line	$25.77	$22.00
CWT	California Water Service Group	In Line	$46.96	$40.00
D	Dominion Energy, Inc	In Line	$79.63	$77.00
DTE	DTE Energy Co.	In Line	$116.94	$120.00
DUK	Duke Energy Corp.	In Line	$84.21	$87.00
ED	Consolidated Edison Inc.	In Line	$73.92	$85.00
EIX	Edison International	In Line	$53.87	$72.00
ES	Eversource Energy	In Line	$88.10	$91.00
ETR	Entergy Corp.	In Line	$102.29	$106.00
EVRG	Evergy	Outperform	$54.75	$62.00
EXC	Exelon Corp.	Outperform	$37.90	$45.00
FCFE18-MX	CFE Capital S. de R.L. de C.V.	Outperform	MXN25.28	MXN19.00
FE	FirstEnergy Corp.	In Line	$29.18	$41.00
HE	Hawaiian Electric Industries Inc.	Underperform	$35.04	$34.00
NEE	NextEra Energy Inc	In Line	$282.81	$277.00
NI	NiSource Inc	Outperform	$24.34	$26.00
NRG	NRG Energy Inc.	Outperform	$33.98	$40.00
OGE	OGE Energy Corp	Outperform	$32.94	$35.00
PCG	PG&E Corp.	Rating Suspended	$9.10	
PEG	Public Service Enterprise Group	In Line	$54.63	$53.00
PNM	PNM Resources, Inc	In Line	$42.84	$44.00
PNW	Pinnacle West Capital Corp.	In Line	$80.79	$85.00
PPL	PPL Corp.	In Line	$26.50	$31.00
SJW	SJW Group	In Line	$64.76	$60.00
SO	Southern Co.	In Line	$53.89	$59.00
SRE	Sempra Energy	Outperform	$128.20	$138.00
VST	Vistra Energy Corp	Outperform	$18.83	$27.00
WEC	WEC Energy Group, Inc.	In Line	$92.99	$93.00
WTRG	Essential Utilities Inc.	In Line	$45.56	$42.00
XEL	Xcel Energy Inc.	In Line	$70.10	$65.00

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Outperform- the total forecasted return is expected to be greater than the expected total return of the analyst's coverage universe
In Line- the total forecasted return is expected to be in line with the expected total return of the analyst's universe
Underperform- the total forecasted return is expected to be less than the expected total return of the analyst's universe
Coverage Suspended- the rating and target price have been removed pursuant to Evercore ISI policy when Evercore is acting in an advisory capacity in a merger or strategic transaction involving this company and in certain other circumstances.*
Rating Suspended- Evercore ISI has suspended the rating and target price for this stock because there is not sufficient fundamental basis for determining, or there are legal, regulatory or policy constraints around publishing, a rating or target price. The previous rating and target price, if any, are no longer in effect for this company and should not be relied upon.*

*Prior to October 10, 2015, the "Coverage Suspended" and "Rating Suspended" categories were included in the category "Suspended."

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Sell -the total forecasted return is expected to be less than 0%

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Strong Buy- Return > 20%
Buy- Return 10% to 20%
Neutral - Return 0% to 10%
Cautious- Return -10% to 0%
Sell- Return< -10%

For disclosure purposes, ISI Group and ISI UK ratings were viewed as follows: Strong Buy and Buy equate to Buy, Neutral equates to Hold, and Cautious and Sell equate to Sell.

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Equal-Weight- the stock is expected to perform in line with the average total return of the analyst's coverage universe over the next 12 months.
Underweight -the stock is expected to underperform the average total return of the analyst's coverage universe over the next 12 months.
Suspended- the company rating, target price and earnings estimates have been temporarily suspended.

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Short- the stock is a negative holding in the model portfolio; the total forecasted return is expected to be less than 0%.
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Stocks included in the model portfolio will be weighted from 0 to 100% for Long and 0 to -100% for Short. A stock's weight in the portfolio reflects the analyst's degree of conviction in the stock's rating relative to other stocks in the portfolio. The model portfolio may also include a cash component. At any given time the aggregate weight of the stocks included in the portfolio and the cash component must equal100%.

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Coverage Universe			**Investment Banking Services I Past 12 Months**		
Ratings	**Count**	**Pct.**	**Ratings**	**Count**	**Pct.**
Buy	377	49	Buy	110	29
Hold	307	40	Hold	49	16
Sell	46	6	Sell	4	9
Coverage Suspended	21	3	Coverage Suspended	6	29
Rating Suspended	15	2	Rating Suspended	3	20

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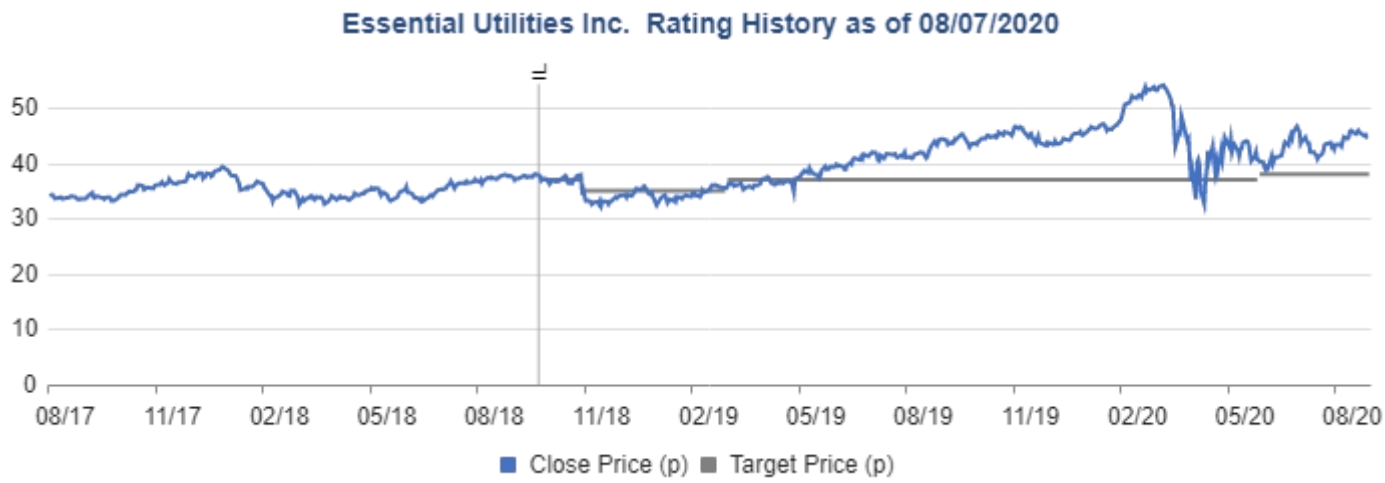

Ratings Key

B	Buy	OP	Outperform	L	Long	CS	Coverage Suspended
H	Hold	IL	In Line	NP	No Position	RS	Rating Suspended
S	Sell	UP	Underperform	S	Short		

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Americas Utilities: Water - infrastructure spend, completed system acquisitions provide LT growth visibility; Buy on AWK, WTRG (on CL)

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Following 4Q2020 earnings, we remain Buy-rated on regulated water utilities American Water (AWK) and Essential Utilities (WTRG, on CL) as we see continued visibility into long-term investment growth from both organic infrastructure modernization and completed municipal system acquisitions, supported by an increasing state/federal focus on water quality and reliability.

Thus far in 2021, in a backdrop where the XLU has underperformed the S&P 500 by 8% driven by rising 10yr bond yields (albeit still at a relatively low ~1.5%), AWK/WTRG shares have declined around 6%/9% on an absolute basis while underperforming the XLU by 1%/4%, respectively. We believe this is driven somewhat by rotation into more value-oriented stocks within our sector, versus anything fundamental to the companies' growth propositions. We view the recent underperformance for both stocks providing a more compelling entry opportunity to gain exposure to these secular winners with a positive ESG footprint, with our $179/$55 price target for AWK/WTRG implying 28%/33% total return, respectively, versus 23% for Regulated Utilities.

WTRG: Water utility expansion, methane reduction strategy fuel growth; remain Buy (on CL)

We stay Buy-rated (on Conviction List) following 4Q2020 earnings on regulated water/gas utility Essential Utilities (WTRG), as we continue to see valuations not fully reflecting the company's primarily water utility exposure, and our expectation for the company to achieve the upper end of its 5-7% EPS CAGR. We believe WTRG's organic/inorganic water growth plans and de-carbonization strategy at its gas utility - as laid out in its January 2021 investor update call - should continue to bolster the case for WTRG as still one of the ESG-friendly stories in our coverage universe. In the near term, we note the pending $276mn DELCORA wastewater system acquisition - with the PA commission decision expected in March - and if completed we expect the Aqua PA utility to file a base rate case later this year. Finally, while WTRG mentioned moderate 1Q21 costs related to their Texas water utilities during the February winter weather event, we note the state represents roughly 6% of total rate base, with management not expecting a net impact to their

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2021 guidance forecast.

We maintain our 2021/2022 estimates while introducing 2023/2024 EPS estimates of $1.93/$2.05, respectively, reflecting a 6.7% CAGR from 2020A-2024E and a 7.1% CAGR from the weather-normal 2020 result of $1.56. We continue to embed issuance of the ~$300mn forward equity in 1Q2021 along with the close of the pending DELCORA municipal acquisition; we also assume $200mn of annual equity to finance future organic/acquisition investments while improving WTRG's FFO/debt from 12% in 2021 to 13% by 2024. Our model reflects the water utilities earning moderately below authorized, along with Peoples Gas ROEs trending down to authorized levels by 2024 (given wind-down of tax repairs and an assumed base rate increase in 2024).

Our $55, 12-month price target (unchanged) is based on a SOTP approach, with 35x/21x P/E applied to our 2022 water/gas utility EPS estimates, and 30x blended P/E on 2022 Other EPS, respectively. Downside risks to our call include: 1) PA regulation turns less constructive, which impacts earnings growth potential given the bulk of WTRG's earnings are derived from the state's water/gas operations, 2) water system acquisitions do not receive necessary approvals for completion, which could impact longer-term water rate base growth outlook barring replacement with other municipal acquisitions, and 3) longer-term growth concerns about the gas utility segment further compresses WTRG's valuation, both on an absolute basis and relative to pure-play water utilities.

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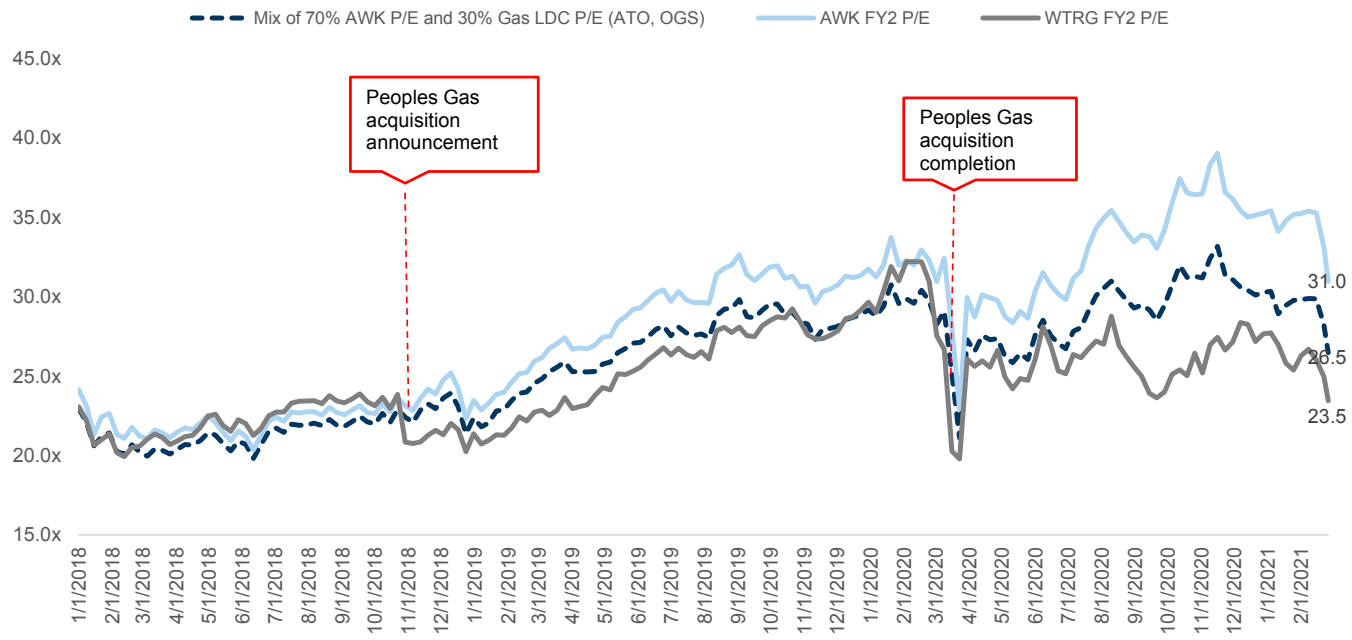
WTRG in Exhibits

Exhibit 1: We continue to see WTRG's valuations not fully reflecting its 70%/30% water/gas profile
FY2 P/E for AWK, WTRG, and an illustrative performance of a 70%/30% water/gas utility



ATO/OGS chosen as illustrative gas utility comps based on company profile, including their status as the two largest gas LDCs by market cap; forward P/Es based on Factset consensus

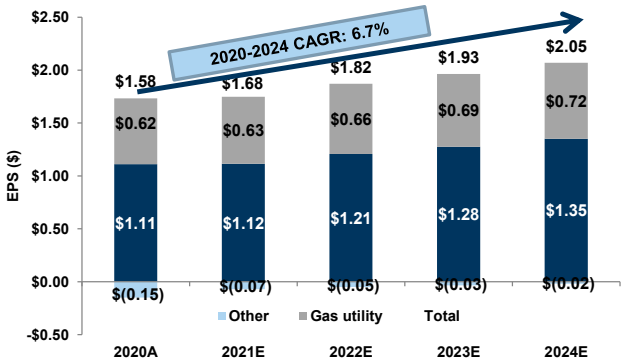
Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 2: We maintain our 2021/2022 estimates, while introducing 2023/2024...
EPS New vs Old vs Consensus

	EPS Estimates			% Difference	
	New	Old	Cons	vs Old	vs Cons
2021E	$1.68	$1.68	$1.67	0%	1%
2022E	$1.82	$1.82	$1.79	0%	2%
2023E	$1.93		$1.89		2%
2024E	$2.05		$2.05		0%

Source: Goldman Sachs Global Investment Research, Thomson Reuters

Exhibit 3: ...implying near-7% EPS CAGR through 2024
EPS CAGR, 2020A-2024E



Source: Company data, Goldman Sachs Global Investment Research

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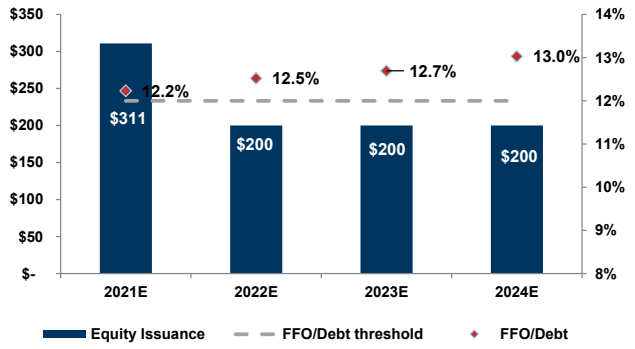
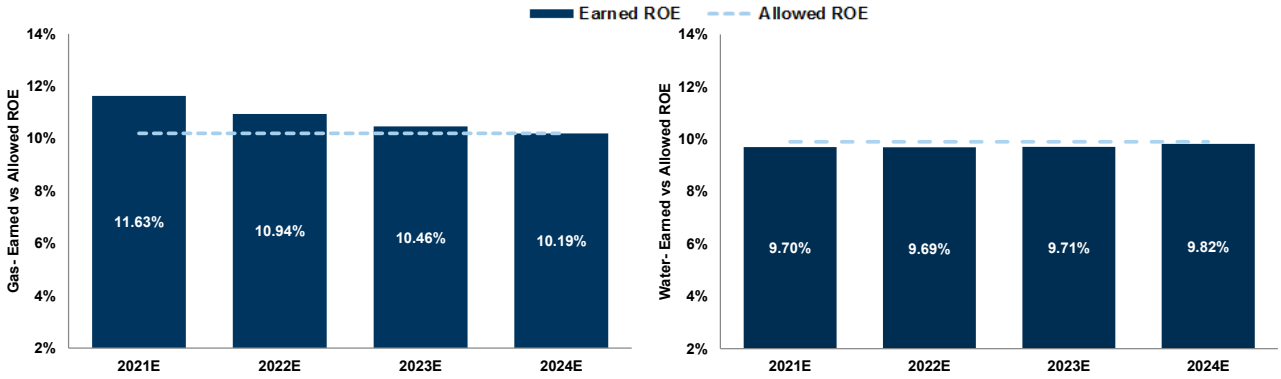
Exhibit 4: We assume annual equity issuances to support organic/inorganic growth while improving the balance sheet
Equity issuance and FFO/debt



Source: Goldman Sachs Global Investment Research

Exhibit 5: We assume the water utilities earn close to their allowed ROEs, while incorporating more robust (but moderating) ROEs for gas utilities given election of repairs tax in PA
Earned vs Allowed ROEs



Source: Company data, Goldman Sachs Global Investment Research

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Exhibit 6: Our SOTP-based $55 price target reflects a 33% total return potential versus 22% on average for our Regulated Utilities
WTRG SOTP Valuation

VALUATION	
Water utility EPS 2022	**1.21**
Water utility multiple	30.00x
Assumed premium	5.00x
Adjusted P/E	35.0x
Water utility valuation	**42.30**
Gas utility EPS 2022	**0.66**
Gas utility multiple	19.00x
Assumed premium	2.00x
Adjusted P/E	21.0x
Gas utility valuation	**13.93**
Valuation - Other	**(0.05)**
2020 Blended multiple	30.04x
Other valuation	**(1.50)**
Total valuation	**55.00**

Source: Goldman Sachs Global Investment Research

AWK: Best-in-class EPS/DPS growth with ESG tailwind; Buy

We stay Buy-rated on AWK post 4Q2020 earnings and Analyst Day given best-in-class EPS and dividend growth. We remain positive on AWK given its status as the only large cap, pure play, publicly traded water utility in the US, as well as its best-in-class ~8.5%+ EPS growth through 2024 driven by robust organic and inorganic water investment opportunities. In addition, we look favorably on the company's increased forecast for water/wastewater municipal system acquisitions that should further support AWK's predominantly regulated utility profile. Finally, we expect the stock to continue to benefit from a scarcity premium and ESG friendly profile that should continue to drive its premium valuation.

We tweak our 2021/2022 EPS estimates while introducing 2023/2024 estimates of $4.98/$5.40, respectively, implying an 8.4% CAGR from 2021A-2024E. Our model assumes $300mn/$200mn/$200mn of equity from 2022-2024, resulting in a 59% net debt/cap ratio and ~17% FFO/debt by 2024, along with earned ROEs of 9.2-9.3% at the Regulated segment versus 9.8% authorized.

Our $179, 12-month price target (unchanged) embeds our water base P/E multiple of 30.0x, as well as a 9x (30%) premium to account for AWK's above-average growth and favorable ESG profile, on our 2022 EPS. Key risks include water quality issues, cost management, regulatory environment, growth at non-regulated segments and reduced

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ESG fund flows.

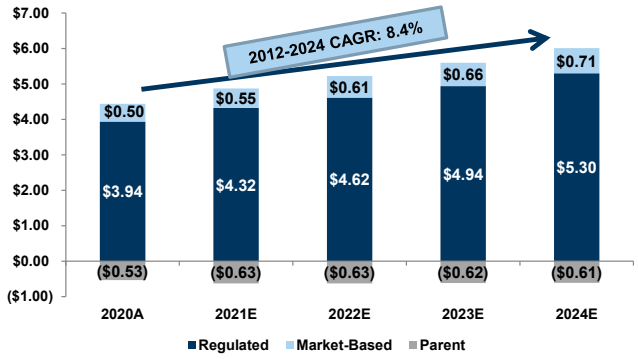
AWK in Exhibits

Exhibit 7: We tweak our 2021/2022 estimates while introducing 2023/2024...
EPS New vs Old vs Consensus

EPS Estimates				% Difference	
	New	Old	Consensus	vs Old	vs Consensus
2021E	$4.24	$4.25	$4.23	0%	0%
2022E	$4.60	$4.59	$4.58	0%	0%
2023E	$4.98		$4.98		0%
2024E	$5.40		$5.46		-1%

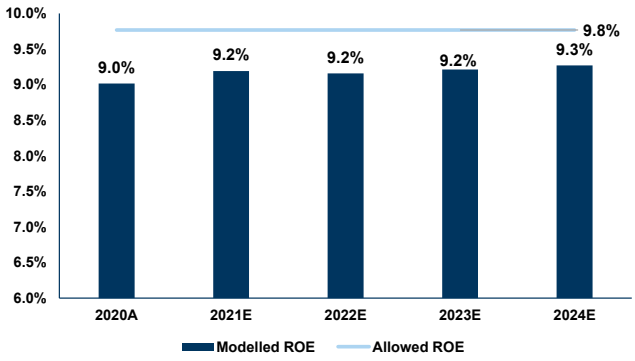
Source: Goldman Sachs Global Investment Research, Thomson Reuters

Exhibit 8: ...which reflect a best-in-class 8.4% EPS CAGR from 2020A-2024E
EPS CAGR, 2020-2024



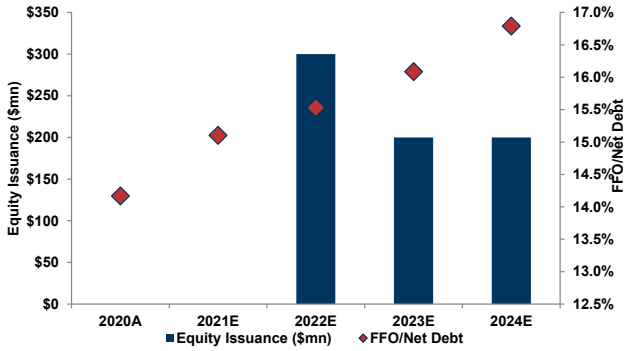
Source: Company data, Goldman Sachs Global Investment Research

Exhibit 9: Our estimates reflect moderate regulatory lag versus authorized ROEs
Authorized versus earned ROEs



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 10: We do assume annual equity issuances from 2022-2024, supporting regulated growth while improving the balance sheet
Equity issuance vs FFO/Net Debt



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 11: Our price target embeds our water base P/E multiple of 30x and a premium to account for AWK's above-average growth and ESG profile
AWK valuation

AWK Valuation	
AWK 2022 EPS	**$4.60**
GS Water Utility Base Multiple	30.0x
Premium / (Discount)	9.0x
Adjusted P/E	**39.0x**
Utility Valuation	**$179**
AWK Valuation	**$179**

Source: Goldman Sachs Global Investment Research

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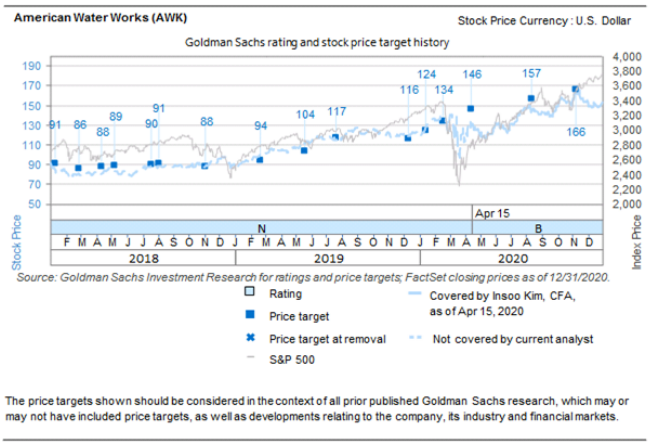

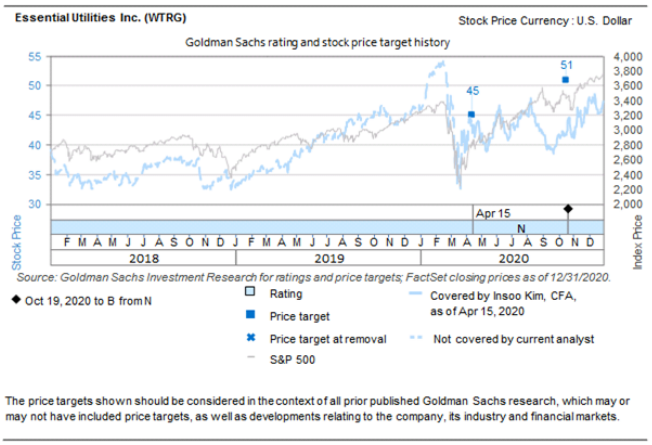

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Americas Energy: GS PUMP Conference: Top ten takeaways from the PUMP Conference panels and dinners

(https://research.gs.com/content/research/themes/power-utilities-mlps-and-pipelines-conference-2019.html)

After hosting this year's GS Power, Utilities, Midstream & Pipeline (PUMP) Conference here in NYC on August 13th, including dinners with FE (Buy), DTE (Buy) and NEE (Buy), we reiterate our top picks, including CL-Buy utilities CNP and SRE, along with NRG within the IPP sector and LNG among midstream stocks.

GS Top Ten Takeaways from Key Panels or Dinners with Company Executives:

1. **FE expects growth to slow after 2021, but from a current elevated rate versus peers of 6%-8%,** as capital spending flattens out and equity financing needs emerge...
2. **...but FE continues to highlight the separation from FES as largely complete.** We note the Nuclear Regulatory Commission's approval of plant ownership licenses - along with bankruptcy court approvals - remain the last steps, expected by 4Q2019.

3. **Substantial regulated renewable development at DTE Electric should support a net income CAGR toward at least the high end of the 7%-8%** operating earnings growth guidance range over the next few years as both the Renewable Energy Plan (REP) and Voluntary Green Program (VGP) spend drives a substantial ramp in renewable capex to meet RPS (renewable portfolio standards) and VGP targets by 2021/2022 - along with the new natural gas power plant in 2022.
4. **Representatives from the credit ratings agencies highlighted** (1) potential does exist, but more time may be needed to prove out the business model, for IPPs to reach investment grade status; (2) changes in oil or especially natural gas production levels could weaken credit metrics for gathering/processing focused midstream companies, but this is not a major 2019 concern yet for the agencies; and (3) offshore wind construction risk emerges now as a credit concern for utility holding companies
5. **NEE views its cost position still as a primary advantage for its FP&L subsidiary** - with costs (per kWh served) at its newly acquired Gulf Power subsidiary almost 2.5x greater than the level at its larger FP&L business, implying ample room for cost management ahead.
6. **More private investment into merchant power likely will occur going forward.** Multiple PE firms highlighted that many conventional merchant generation portfolios deliver double-digit free cash yields - albeit with sizable quarterly volatility - and even after facing new challenges such as subsidized generation (nuclear) in key states like IL, OH, NJ and NY. Funds participating in our conference expect more private capital to come into the space.
7. **WTR highlighted what remains a very attractive M&A landscape for water utilities** as (1) the U.S. has ~40,000+ municipally-owned water systems, and (2) fair market value regulation allows utilities to add goodwill in municipal water utility transactions to rate base.

8. **Capital spending by regulated utilities - as discussed at the conference - will migrate more and more towards distribution** versus spend on other items including large scale transmission.
9. **The Bakken should maintain enough oil/NGL takeaway as new or potential assets come online - more long haul gas pipeline capacity** needs may emerge. In the Bakken, the expansion of the Bakken Pipeline system (DAPL/ETCOP) and startup of OKE's Elk Creek pipeline should provide producers with sufficient long-haul takeaway for both crude oil and natural gas liquids (NGLs). However, there could be additional need for Bakken long-haul natural gas takeaway in the next few years given a reduction in flaring limits and continued growth in gas production.
10. **Along with demand-pull from traditional LNG buyers (including integrated and global utilities), there is growing supply-push from Permian producers** looking to secure flow assurance and end markets for their associated gas production. These producers see new LNG facilities as a way to get their gas to market - and to also reduce flaring levels, assuming pipeline capacity exists to get the gas to the new LNG terminals.

We also highlight a few key insights from panels at the GS PUMP Conference...

Key Trends and Challenges in Midstream Infrastructure in America (Jonathan Stein, CFO, Hess Midstream Partners. Ben Atkins, CFO, NextDecade Corp.)

- NEXT's (Not Covered) Rio Grande LNG project in Brownsville, TX has key competitive advantages over other LNG sites, including proximity to the Permian Basin, and better construction economics given access to labor and an underutilized ship channel.

- A self-funding strategy with minimal leverage remains key to HESM's financing strategy. The partnership is also mitigating its counterparty risk via third-parties - which currently comprise 15% and 30% of HESM's crude oil and natural gas volumes, respectively.

CEO Fireside Chat: The Outlook for Regulated Investment and Growth (Christopher Franklin, Chairman, CEO and President, Aqua America. Charles Jones, President and CEO, FirstEnergy Corp.)

- FE highlighted key types of investment opportunities in a handful of states, including incremental grid modernization in Ohio (i.e., the deployment of ~700,000 smart meters in the state), reliability improvement in Pennsylvania, and renewables as well as energy efficiency in New Jersey (partly driven by the governor's Energy Master Plan).
- WTR noted regulatory encouragement for consolidation across water utilities, as municipalities continue to own the majority of systems in the U.S. Fair market value regulation, allowing acquirers to add goodwill related to water utility M&A in to rate base, has helped make the economics of acquisitions work for IOUs (investor-owned utility).

Merchant and Contracted Power Business Models (Francisco Martinez-Davis, CFO, Atlantica Yield. Brian Vaasjo, President and CEO, Capital Power Corp. Matthew J. O'Connor, Managing Director, Carlyle Power Partners. Darren Olagues, Executive Vice President and CFO, GenOn Energy. Himanshu Saxena, CEO, Starwood Energy Group.)

- The recent delay in the PJM auction was viewed constructively as the correct rules and processes were not in place for a two-step auction. Panelists believe that subsidized assets should not bid in to the same auction as non-subsidized assets, and this will help investors acknowledge/realize the value of competitive assets.

- California's merchant power market structure may create reliability concerns. Current market structure doesn't provide proper compensation for reliability in CA, decreasing interest in incremental baseload generation in the state. In contrast, state policy goals drive significant investment in renewable generation assets. Some panelists believe misaligned incentives and difficulty in forecasting (particularly reliability payments) could create headwinds for CA power investors, but near-term, is supporting elevated RA payments. The GenOn (Not Covered) CFO noted that the NY power market could see a similar uptick in capacity payments as large nuclear assets retire and ambitious renewable goals impact the grid.
- Merchant power (as opposed to contracted power) likely continues to expand globally, with Atlantica Yield's (AY, Not Covered) CFO noting growing levels of comfort with merchant power in other countries -- although not AY's growth strategy. Additionally, panelists highlighted foreign capital searching for yield has driven down financing costs in the U.S., but increased the need for discipline among project developers.

Renewables Ahead, The Role of Natural Gas and The Impact Across the Energy Infrastructure Industries (Peter Oleksiak, Senior Vice President and CFO, DTE Energy. Eric Silagy, President and CEO of FP&L, NextEra Energy)

- NEE highlighted that a combination of customer count and load growth help control the costs of renewables to rate payers, but replacing aging infrastructure continues to provide tailwinds as well. The company noted every $1 of O&M saved creates room for ~$7 of incremental capital spending without impacting customer bills.
- Both NEE and DTE highlighted the cost savings of fleet transformation, with NEE noting $10bn of customer savings since 2001 driven by the heat rate differential between oil and other types of generation. DTE also highlighted the LT savings driven by

fleet rationalization, such as building gas plants near distribution and storage facilities, lower fuel costs, and lower operating and maintenance expenses.

- Within DTE's generation transformation, wind remains the primary source of renewable generation, but DTE expects solar to make headway by the mid-2020s. The company noted (1) it sees significant natural demand from corporates looking to meet internal sustainability goals and (2) its desire to remain in the regulated generation business as it proceeds through fleet transformation - given the value for customers from owning vs PPA'ing a renewable asset as it depreciates.

Generation and Grid Transformation - The Path Ahead (Martin Lyons, Executive Vice President and CFO, Ameren Corporation. Antonio Smyth, Senior Vice President of Transmission, American Electric Power. Rod West, President of Utility Operations, Entergy Corporation.)

- While MO remains a relatively coal-heavy state, AEE expects wind generation capital spending to precede coal plant retirements likely to occur in the next 10-15 years driven by MO's 2035 IRP goals.

The Evolution of State Policies and The Impact on Investment and Opportunity Sets (Stephen Wemple, Director, Consolidated Edison. Maria Pope, President and CEO, Portland General Electric. Steven Rasche, Executive Vice President and CFO, Spire Inc.)

- Panelists highlighted a handful of items on their regulatory wishlists, particularly we flag (1) ED looking for more earnings opportunities from regulatory assets related to renewable projects - as the company cannot own large-scale or customer sited renewables and (2) SR (Not Covered) is looking to replicate Alabama's real-time rate making process in another states.

- POR noted the preference for onshore wind over offshore wind on the West coast continues, driven partly by geographic factors (i.e., wavier waters making the use of buoys to support turbines difficult or the relatively steep nature of the ocean floor) as well as by grid restraints due to the lack of major transmission lines along the coast.

Insights on Power, Utilities and Midstream from the Credit Ratings Agencies (Shalini Mahajan, Managing Director of US Utilities, Fitch Ratings. Peter Molica, Senior Director of US Midstream, Fitch Ratings. James Hempstead, Managing Director of US Utilities, Moody's Investors Service. Elena Nadtotchi, Senior Credit Officer on Oil & Gas, Moody's Investors Service. Michael Grande, Senior Director of Midstream Energy and Refining, S&P Global Ratings. Aneesh Prabhu, Senior Director of Midstream Energy and Refining, S&P Global Ratings.)

- Merchant power can feasibly achieve investment grade credit ratings, but the ratings agencies noted that a limited track record may require more time. The integrated model should in theory work to limit volatility and provide a counter-cyclical business strategy by pairing retail with generation, yet the lack of data around a recession provides little evidence of how it truly holds up under significant stress. Longer-term, the agencies highlighted that there is no fundamental reason why merchant power cannot become IG, given that there is a certain level of debt to EBITDA that would be acceptable and that cash flow volatility has been 17%, lower than some investment grade refiners and with higher cash flow conversion rates.
- Ratings at the holdco level continue to converge to levels around BBB+. With limited benefit to an A credit rating - given tighter spreads - the agencies noted that over the past handful of years, an increasing amount of utility holdcos moved closer to BBB+ and the cash flow to debt metrics for large holding companies declined to about 15% compared to 16% in 2018 and a 2010-2015 average of

about 20%. The agencies highlighted that as utility holdcos give themselves less of a cushion on the credit side, execution risk can become an increasingly large concern over time.

...as well as highlights from our dinners with managements

We hosted a dinner with FE on Tuesday night (8/13) with no new major takeaways, but flag...

- Incremental equity financing will occur to help fund rate base growth and pension requirements - but not likely until 2022+.
- The company views its customer rates as a competitive advantage and does not want to risk losing this edge. FE highlighted its customer bills in key states (NJ, OH, PA, etc.) remain well below peers in those states.
- FE sees limited rate case or regulatory risk - while many investors question earnings levels in OH or PA, the company highlighted that PA earnings levels remain at or below required levels - needing the state's tracker implementation to improve earnings closer to authorized levels.

...while takeaways from our dinner with DTE include...

- Substantial regulated renewable development at DTE Electric should support a net income CAGR toward at least the high end of the 7%-8% operating earnings growth guidance range over the next few years
- Management continues to bake in significant contingencies into DTE's base case guidance. Across the subsidiaries, a level of conservatism makes the 5-7% EPS growth achievable, per management, and DTE highlighted that they often assume mild weather at the regulated segments to determine a starting guidance midpoint, emphasizing the resulting flexibility in their planning.

- Commissioner turnover has continued (with two new commissioners in MI), but DTE believes the key remains providing reliable performance and an open dialogue, understanding the commissioners' goals. Clean energy investments already continue to support significant growth, and the Utility welcomes more opportunities to transform its fleet. In general, following the 2016 energy deal, energy/utility reform does not appear top of mind for state legislators, and they feel comfortable with the current state of regulation.

...and we note a handful of highlights from our dinner with NEE

- The company believes battery storage remains in the very early stages and highlighted expectations to build batteries as part of a wind+solar+battery all-in-one development as well as building batteries in to the distribution and transmission system.
- FP&L highlighted a meaningful difference between its O&M profile relative to the recently acquired Gulf Power. The company noted non-fuel O&M of ~$12/MWh vs Gulf Power's near $30/MWh (near the national average).
- The company remains skeptical of the first wave of offshore wind, highlighting: (1) expectations for massive cost overruns leading to abandoned projects; (2) maintaining and repairing the plants will likely prove more expensive than expected; and (3) believes offshore wind in Europe has advanced largely due to saturation in European power markets.

GS Power & Utilities ratings grid

Exhibit 1: We continue to favor Diversified Utilities over pure-play Regulated Utilities
GS Power & Utilities ratings distribution

	Regulated Utilities	Diversified Utilities	IPPs
Buy	EIX, ES NI	CNP*, DTE ETR, EXC, FE NEE, SRE*	NRG*, NEP
Neutral	AEE, AEP AWK, CMS ED, PNW PPL	AGR, D PEG	CWEN
Sell	DUK, EVRG POR, SO WEC	OGE	

*Part of the Americas Conviction List

Source: Goldman Sachs Global Investment Research

GS Pipelines & MLPs ratings grid

Exhibit 2: LNG remains our top pick, followed by other large caps including ET, EPD and KMI

Pipelines and MLPs rating distribution

	C-Corps	MLPs
Buy	KMI, LNG*	ET, EPD, RTLR
Neutral	TGE, OKE, WMB, ENB, ENB.TO	CQP
Sell	TRP.TO, TRP	TCP

* Denotes Stock is on the Americas Conviction List

Source: Goldman Sachs Global Investment Research

Ratings and PT information

We reiterate our $47, 12-month target price for FE, derived using a SOTP, and remain Buy rated. Key risks for FE include utility regulation, power demand, cost management, and financing.

We remain Neutral rated AEE with a $76, 12-month price target, derived from a 19.75x P/E multiple on 2021E EPS. Key risks for AEE include regulation, project awards, and financing.

We reiterate our $88, 12-month price target for AEP, derived using a sum-of-the-parts, and remain Neutral rated. Key upside/downside risks for AEP include utility regulation, power demand, cost management, and financing.

We remain Buy rated ETR and derive our 12-month target price of $110 using a sum-of-the-parts valuation. Key risks for ETR include utility regulation, demand, and power pricing.

We reiterate our $86, 12-month price target for ED, derived from an 18x P/E multiple on 2021E EPS, and remain Neutral rated. Key risks for ED include CECONY earned RoEs, the ongoing CECONY rate case, CEB contracts, project awards, and financing.

We remain Sell rated with a $50, 12-month target price for POR, derived 85% using a fundamental 18x P/E multiple on 2021E EPS and 15% using a theoretical M&A 21.0x P/E multiple on 2021E EPS. Key risks include utility regulation and demand.

We remain Buy rated on NEE with our $221, 12-month target price, derived using an SOTP. Key risks include utility regulation, renewable development, and cost management.

We remain Buy rated on DTE with our 12 month $136 target price, derived using an SOTP. Key risks include regulatory, legislative, natural gas production, counterparty, transaction, and financing risk.

We remain Buy rated (on the CL) LNG with an $89, 12-month price target, derived with a 12x EV/EBITDA multiple on 2023E EBITDA. Key risks for LNG include construction costs, project financing, operational risk, and global natural gas prices.

We reiterate our $158, 12-month target price for SRE - derived using a sum-of-the-parts - and remain Buy rated (on the CL). Key risks for SRE include construction, utility regulation, and financing.

We remain Buy rated (on the CL) CNP with a $35, 12-month target price, derived using a sum-of-the-parts. Key risks include oil prices, merger synergies, utility regulation, and demand growth.

We remain Buy rated (on the CL) NRG with a $52, 12-month target price. We base our NRG price target 85% on a sum-of-the-parts implying $52/share and 15% on a 9.25x EV/EBITDA M&A multiple implying $54/share. Key risks include power prices, retail margins, cost management, and customer growth.

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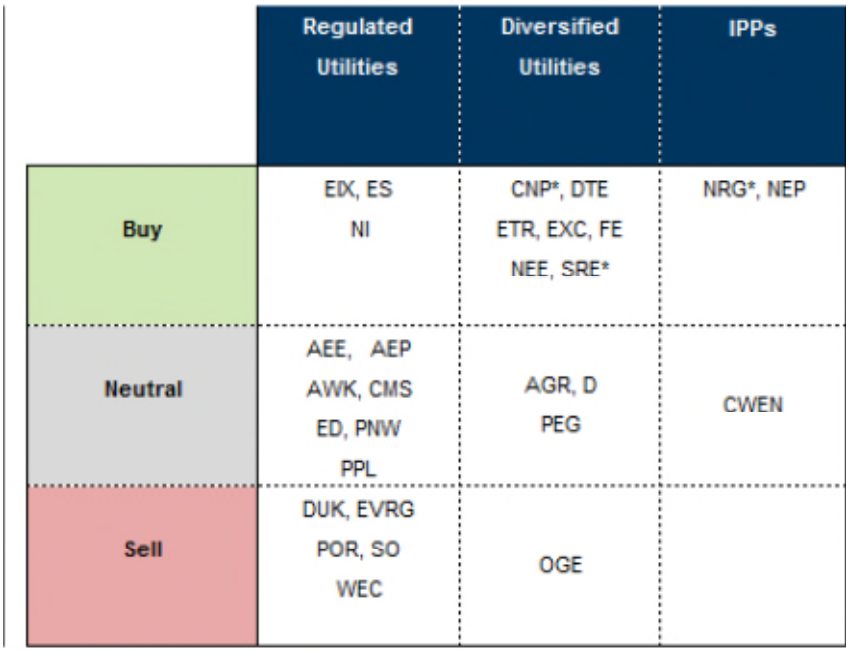

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Regulated water/gas utility Essential Utilities (WTRG, Buy-CL) today introduced 2021 EPS guidance range of $1.64-$1.69 ($1.67 mid-point), relatively in-line with GS/consensus of $1.68/$1.66. The company also extended its 5-7% EPS CAGR forecast through 2023 (versus 2022 prior), using 2020 as the base while reiterating expectations to achieve the upper end of the 2020 guidance range of $1.53-$1.58. In short, we view today's release as largely in-line with our expectations and reaffirming WTRG's focus on water utility expansion and system de-carbonization. We reiterate our Buy rating (on CL), as we continue to see WTRG as a secular winner to benefit from material water infrastructure investment needs in a fragmented market, with valuations not fully reflecting the company's primarily water utility exposure.

We also highlight some key additional disclosures:

- **Extension of 6-7%/8-10% rate base CAGR through 2023 for water/gas utilities,** respectively, using 2019 as the base. We note the water rate base growth excludes rate base additions from municipal acquisitions; inclusive of acquisitions, we calculate the growth rate at between 8-9%. Management also reaffirmed its strategy to maintain at least a 70%/30% water/gas mix by rate base.
- **Expect DELCORA acquisition close by 2Q2021.** With the recently favorable district court decision supporting the asset purchase agreement (APA) between Aqua and DELCORA, management expects the PA commission to provide its decision in March, with the deal close shortly after. We note this wastewater deal represents the largest municipal acquisition done by WTRG, with the ~$310mn forward equity offering already priced in August 2020.
- **WTRG plans to reduce CO2 emissions 60% by 2035** from 2019 levels, both at the gas and water/wastewater segments, via gas infrastructure replacement as well as using renewable electricity for its water operations.

Our $51, 12-month price target (unchanged) is based on a SOTP approach, with 35x/22x P/E applied to our 2021 water/gas utility EPS estimates, respectively. Downside risks to our call include: 1) PA regulation turns less constructive, which impacts earnings growth potential given the bulk of WTRG's earnings are derived from the state's water/gas operations, 2) the proposed DELCORA municipal water

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system acquisition does not receive necessary approvals for completion, which could impact longer-term water rate base growth outlook barring replacement with other municipal acquisitions, and 3) longer-term growth concerns about the gas utility segment further compresses WTRG's valuation, both on an absolute basis and relative to pure-play water utilities.

WTRG	12m Price Target: **$51.00**	Price: **$48.72**	Upside: **4.7%**

Buy CL

Market cap: $12.4bn
Enterprise value: $17.9bn
3m ADTV: $47.4mn
United States
Americas Utilities
M&A Rank: 3
Americas Conviction List

GS Forecast

	12/19	12/20E	12/21E	12/22E
Revenue ($ mn)	889.7	1,571.5	1,998.9	2,125.8
EBITDA ($ mn)	521.4	748.4	1,008.8	1,102.5
EBIT ($ mn)	360.8	492.1	704.9	767.7
EPS ($)	1.47	1.57	1.68	1.82
P/E (X)	27.6	31.0	29.0	26.7
EV/EBITDA (X)	19.1	23.7	18.8	17.7
FCF yield (%)	(2.4)	(1.5)	(1.7)	(0.1)
Dividend yield (%)	2.2	2.0	2.1	2.3
Net debt/EBITDA (X)	2.3	7.4	6.2	6.2

	9/20	12/20E	3/21E	6/21E
EPS ($)	0.23	0.45	0.69	0.31

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 8 Jan 2021 close.

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Disclosure Appendix

Reg AC

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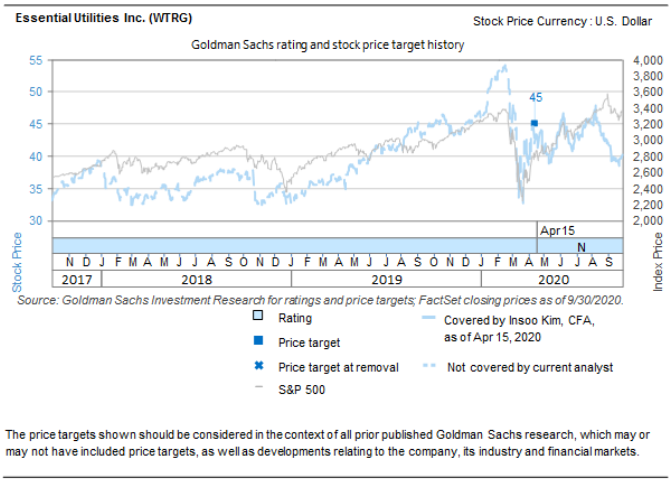

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Americas Utilities: Updating estimates for a few Neutral-rated regulated utilities

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Essential Utilities (WTRG, Neutral)

We tweak down our 2020-2022 EPS estimates to $1.55/$1.63/$1.78 from $1.56/$1.65/$1.78, respectively, to reflect 1) 10-Q update, 2) increased equity dilution in 4Q20 from lower assumed share price, and 3) moderately higher interest expense. We note our 2020 estimate incorporates 1Q20 adjusted EPS of $0.60 as reported by the company, which does not include the mild weather impact on the Peoples Gas segment. We assume relatively flattish gas load growth from 2019A-2022E, while embedding +2%/-1% water customer/usage growth during the same period. We continue to view favorably Essential's heavily residential customer mix for both water/gas businesses that could mitigate the negative COVID-19 related demand impact from commercial/industrial customers. While we estimate a robust 6.4% EPS CAGR from 2019A-2022E, we view WTRG's current valuation as fairly representing the company's water/gas utility mix.

Our $45 12-month price target (unchanged) reflects a 12% total return is based on an SOTP valuation methodology. We apply our 30x base water target P/E multiple to 2021E EPS for the water utility segment, along with a 22x P/E multiple to 2021E EPS for the gas utility segment. Our gas multiple reflects a 10% (or 2x) premium to our 20x base gas target P/E, given our view of the segment's above-average rate base and EPS growth. **Key upside risks** include: 1) Peoples Gas acquisition synergies exceed our expectations, elevating EPS growth profile, 2) tax repairs election for the PA gas utility elevates earned ROEs even above our estimate, and 3) WTRG continues to benefit from ESG fund flows, despite its water/gas utility mix profile on a pro-forma basis. **Key downside risks** include: 1) PA regulation turns less constructive, 2) growth from municipal acquisitions slows, and 3) WTRG credit rating is downgraded.

Eversource Energy (ES, Neutral)

We adjust down our 2020 EPS estimate to $3.63 from $3.66 while our 2021/2022 estimates remain unchanged at $3.89/$4.12, respectively. The lower 2020 estimate stems from a combination of lower expected demand at the New Hampshire electric utility (with no decoupling unlike most of the other ES utility jurisdictions), modestly lower estimates for corporate/other, and partially offset by lower O&M expense (assume -1% CAGR from 2019-2022E). Our model does not incorporate the

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pending $1.1bn acquisition of Nisource's Columbia Gas of Massachusetts (CMA) utility. We view ES with its largely demand decoupled utility portfolio as well positioned to mitigate the current COVID-19 environment while continuing to grow at a robust ~6% EPS CAGR; however, we remain Neutral rated largely on valuation despite acknowledging potential longer-term earnings upside from its investments in offshore wind (mostly in 2024 and beyond).

Our $88 12-month price target (unchanged) implies a 15% total return and is based on a 22.5x P/E applied to our 2021 EPS. **Key upside risks** include improved offshore wind return forecasts, reduced permitting/construction hurdles, indications of additional rate base investments. **Key downside risks** include ineffective cost management, slowing rate base growth, dilutive acquisitions, and delays/cost overruns in ES's offshore wind investments.

Xcel Energy (XEL, Neutral)

We lower our 2020/2021 EPS estimates to $2.75/$2.95 from $2.79/$2.97, while our 2022 estimate remains unchanged at $3.17, implying a 6.3% EPS CAGR from 2019A-2022E. Our adjustments reflect 1) 10-Q update, 2) lower electric demand in 2020/2021 per our GSe forecast, 3) lower O&M expense, and 4) updates related to the recent Texas and New Mexico rate case settlements. Our estimates reflect an 8.6%/8.8%/8.9% earned ROE in 2020-2022, respectively, versus the 9.4% weighted average authorized ROE across the various jurisdictions. We continue to view favorably XEL's revenue decoupling mechanism at its Minnesota and Colorado (residential and small commercial) utilities, which comprise the majority of its consolidated earnings. However, we see the company's ability to implement strong cost controls (-4% to -5% YoY guided by company), especially sustainable cost cuts, as key to achieving its original 2020 EPS guidance range and its 5-7% growth rate. Finally, we view XEL's 7.5% rate base growth as intact, supported by new renewable investments, potential to take ownership of existing PPAs, and ongoing grid modernization efforts.

Our $66 12-month price target (unchanged) reflects a 12% total return and is based on a 2.25x (13%) premium to our baseline 2021E P/E multiple of 20x. Despite our view that XEL could sustain its current ~6.5% EPS growth over the next 10 years given long-term visibility of regulated investment growth, the stock's YTD outperformance - now reflecting a ~3x (15%) premium - makes us incrementally more negative. **Key upside risks** include: 1) Further upward revisions to rate base/EPS growth through increased capital support incremental multiple expansion, 2) XEL realizes higher EPS growth through sustained O&M savings initiatives, and 3) the U.S. government extends federal renewable tax credits, lowering renewable costs and accelerating XEL's capital growth. **Key downside risks** include: 1) negative rate case outcomes impact the utilities' earnings power, 2) XEL realizes less generation into rate base vs. PPA, impacting rate base growth, 3) PPA buyouts do not materialize, stemming incremental rate base growth opportunities, and 4) COVID-19 meaningfully impacts non-decoupled demand in addition to increased cash drag from customer bill non-payment.

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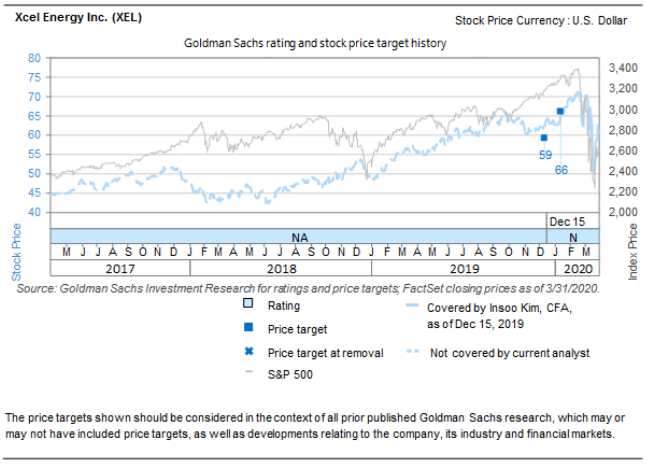

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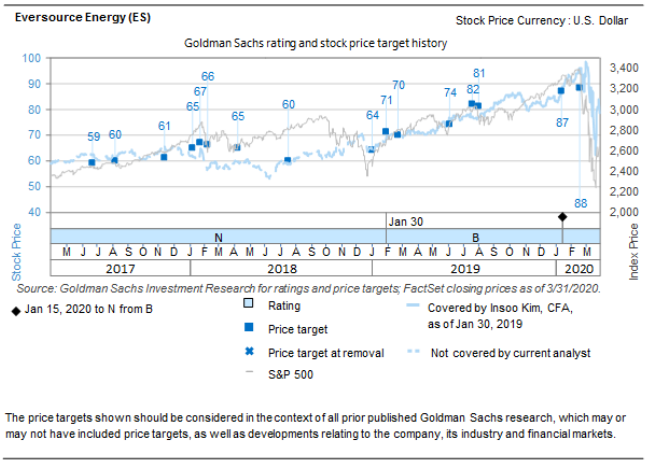

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Americas Utilities: Water: First Takes: AWK, WTRG report solid 2Q20, reiterate guidance

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American Water (**AWK**, Buy) and Essential Utilities (**WTRG**, Neutral) reported quarterly earnings this afternoon. **In short, both companies met or exceeded consensus expectations while reaffirming 2020 guidance, EPS growth, and capital forecasts. We also note that both companies' water demand/margins showed relative resiliency in the current COVID-19 environment, given heavy residential customer exposure**; case in point, WTRG recorded an increase in water usage and margins YoY, as robust residential usage more than offset declines in the other customer classes. We expect shares of both companies to react favorably tomorrow.

American Water Works (AWK, Buy): 2Q2020 results relatively inline, 2020 guidance and EPS growth reiterated

AWK reported 2Q2020 adjusted operating EPS of $0.97, inline with GS and above FactSet estimates of $0.97/$0.96 and versus 2Q2019 of $0.94. The company maintained its 2020 EPS guidance range of $3.79-$3.89 ($3.84 midpoint) versus GS/consensus of $3.85/$3.83, while reiterating the long-term EPS growth CAGR of 7-10%.

Regarding COVID-19, AWK pointed to a -$0.05 EPS for the quarter, driven by a -18%/-12% YoY demand impact for its commercial/industrial segment, partially offset by an 8% increase for residential. We note C&I usage constitutes around 30% of total volumes. At the Homeowner Service segment, AWK noted a -$0.01 of impact due to delayed partner relationships. Total COVID-related impact is expected at between -$0.05 to -$0.08 for the year, while consolidated capital spend expectations remain unchanged at $1.9bn.

Key topics to monitor on AWK's earnings call (8/6 @ 9am ET) include (1) updated thoughts on water/wastewater usage trends for the balance of the year, (2) potential for Homeowner Service revenues could be impacted further given COVID-19, (3) thoughts on potential for increased muni acquisition opportunities over the next 1-2 years above forecast, and (4) potential opportunities/challenges for AWK from potential changes to tax reform and or clean energy/water plans.

Essential Utilities (WTRG, Neutral): 2Q2020 beat GS/consensus, 2020 guidance

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reiterated

WTRG reported 2Q2020 pro-forma EPS of $0.29, vs GS/consensus of $0.17/$0.23, with the beat largely due to quarterly timing of O&M and other expenses, in our view, but also helped by **positive YoY water usage/margins from positive residential demand more than offseting lower C&I usage**. WTRG maintained its 2020 guidance of $1.53 to $1.58, versus GS/consensus of $1.55/$1.56, as well as its 5-7% EPS forecast from 2019A-2022E; we note the 2020 EPS guidance assumes full quarter contribution from the Peoples acquisition. Management also reiterated their 2020 water/gas capex guidance of $550mn/$400mn, as well as $2.8bn of total capex from 2020-2022.

Key topics to monitor on WTRG's earnings call (8/6 @ 11am ET) include (1) assumptions on gas usage trends in 2H2020, (2) latest update on potential revenue/cost synergy levels from integration of Peoples Gas, 3) thoughts on potential for increased muni acquisition opportunities over the next 1-2 years above forecast, and (4) potential opportunities/challenges for WTRG from potential changes to tax reform and or clean energy/water plans.

Price Targets and Key Risks

AWK, Buy: Our $146, 12-month price target is based on a 34.5x P/E multiple on our 2021E EPS. Key risks include water quality issues, cost management, regulatory environment, growth at non-regulated segments, and reduced ESG fund flows.

WTRG, Neutral: Our $45, 12-month price target is based on an SOTP. Key risks include Peoples Gas acquisition synergies, tax repair election in PA, ESG fund flows, PA regulation, growth from municipal acquisitions, and credit rating downgrade.

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Disclosure Appendix

Reg AC

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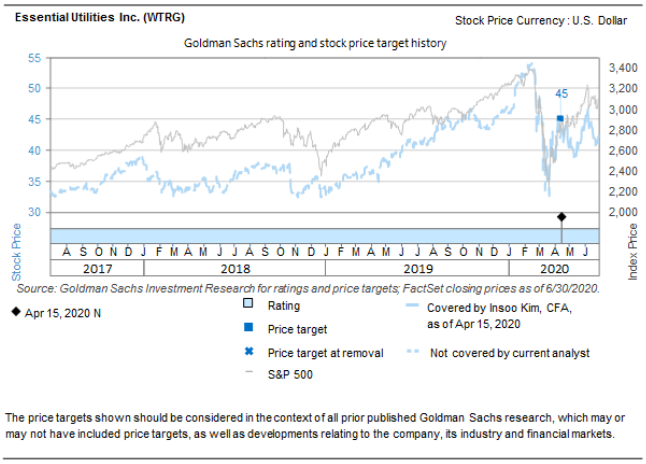

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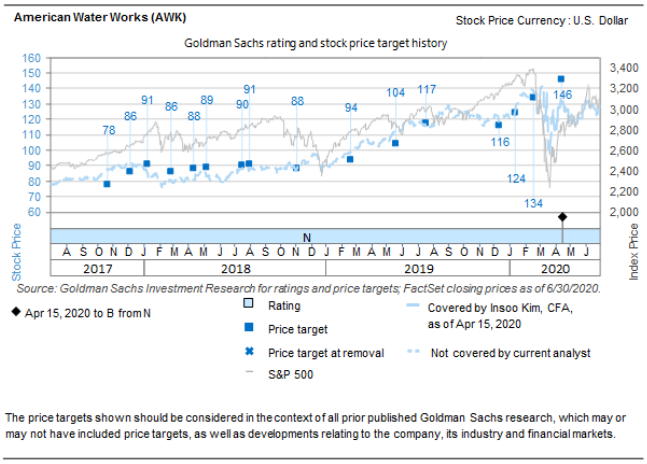

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Buy CL

Essential Utilities Inc. (WTRG)

The under-appreciated water growth opportunity; Upgrade to Buy (add to CL)

WTRG	12m Price Target: **$51.00**	Price: **$41.55**	Upside: **22.7%**

We upgrade regulated water/gas utility Essential Utilities (WTRG) to Buy from Neutral and add to the Conviction List. As one of two large-cap, publicly traded regulated water utilities in the US, we see WTRG as a secular winner to benefit from an estimated $750 billion of water infrastructure investment needs (per the EPA) in a very fragmented market. This represents at least a $7bn opportunity – well above its total current water asset base – excluding any market share gains through municipal and other water utility acquisitions.

After YTD underperformance of 10% versus the XLU, we see current prices reflecting a 7x (20%) P/E discount for the company's water utility segment (comprising ~70% of total earnings) versus the only other large-cap water utility American Water (AWK, Buy); we view this as unwarranted while undervaluing WTRG's normalized EPS growth potential similar to AWK's, representing one of the highest in our coverage universe.

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Key Data

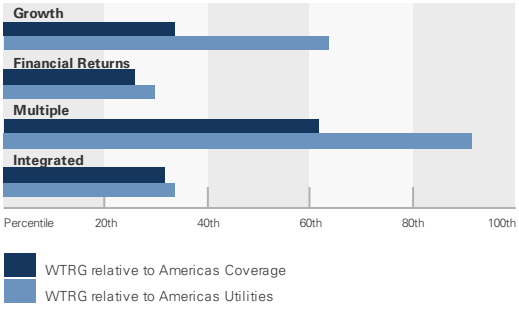
Market cap: $10.6bn
Enterprise value: $16.1bn
3m ADTV: $48.7mn
United States
Americas Utilities
M&A Rank: 3
Americas Conviction List

GS Forecast

	12/19	12/20E	12/21E	12/22E
Revenue ($ mn) New	**889.7**	**1,571.7**	**1,995.4**	**2,113.5**
Revenue ($ mn) Old	889.7	1,571.7	2,032.7	2,165.6
EBITDA ($ mn)	521.4	777.5	1,047.8	1,122.3
EBIT ($ mn)	360.8	525.4	755.5	800.4
EPS ($) New	**1.47**	**1.55**	**1.66**	**1.80**
EPS ($) Old	1.47	1.55	1.65	1.80
P/E (X)	27.6	26.8	25.0	23.1
Dividend yield (%)	2.2	2.3	2.5	2.7
Net debt/EBITDA (X)	2.3	7.2	6.0	6.1

	6/20	9/20E	12/20E	3/21E
EPS ($)	0.29	0.22	0.44	0.69

GS Factor Profile



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Buy CL

Essential Utilities Inc. (WTRG)

Rating since Oct 19, 2020

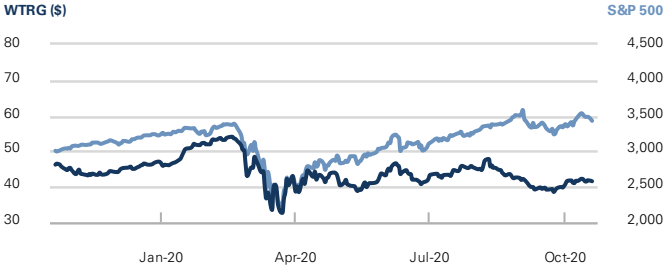
Ratios & Valuation

	12/19	12/20E	12/21E	12/22E
P/E (X)	27.6	26.8	25.0	23.1
EV/EBITDA (X)	19.1	20.5	16.3	15.8
EV/sales (X)	11.2	10.1	8.6	8.4
FCF yield (%)	(2.4)	(1.8)	(1.9)	(0.3)
EV/DACF (X)	19.1	21.0	17.1	16.3
CROCI (%)	6.6	6.9	6.8	6.8
ROE (%)	10.8	9.2	8.8	9.0
Net debt/EBITDA (X)	2.3	7.2	6.0	6.1
Net debt/equity (%)	31.1	118.9	121.6	128.4
Interest cover (X)	–	2.6	3.0	2.9
Inventory days	NM	32.2	25.3	25.3
Receivable days	42.8	30.3	28.0	26.4
Days payable outstanding	NM	156.0	138.3	138.3

Growth & Margins (%)

	12/19	12/20E	12/21E	12/22E
Total revenue growth	6.2	76.7	27.0	5.9
EBITDA growth	23.0	49.1	34.8	7.1
EPS growth	4.2	5.4	7.5	7.9
DPS growth	7.0	7.0	7.0	7.0
Gross margin	100.0	85.2	83.6	84.5
EBIT margin	40.6	33.4	37.9	37.9

Price Performance



	3m	6m	12m
Absolute	(7.1)%	(4.2)%	(10.8)%
Rel. to the S&P 500	(12.6)%	(19.6)%	(22.3)%

Source: FactSet. Price as of 19 Oct 2020 close.

Income Statement ($ mn)

	12/19	12/20E	12/21E	12/22E
Total revenue	889.7	1,571.7	1,995.4	2,113.5
Cost of goods sold	0.0	(232.9)	(327.5)	(327.5)
SG&A	(391.1)	(600.5)	(659.3)	(699.7)
R&D	–	–	–	–
Other operating inc./(exp.)	22.7	39.3	39.2	35.9
EBITDA	**521.4**	**777.5**	**1,047.8**	**1,122.3**
Depreciation & amortization	(160.6)	(252.1)	(292.3)	(321.9)
EBIT	**360.8**	**525.4**	**755.5**	**800.4**
Net interest inc./(exp.)	(125.3)	(201.5)	(249.6)	(274.7)
Income/(loss) from associates	–	–	–	–
Pre-tax profit	**327.9**	**424.5**	**505.9**	**525.7**
Provision for taxes	(10.5)	(30.1)	(71.2)	(56.5)
Minority interest	–	–	–	–
Preferred dividends	–	–	–	–
Net inc. (pre-exceptionals)	**317.4**	**394.4**	**434.7**	**469.1**
Net inc. (post-exceptionals)	**317.4**	**394.4**	**434.7**	**469.1**
EPS (basic, pre-except) ($)	**1.47**	**1.58**	**1.67**	**1.80**
EPS (diluted, pre-except) ($)	**1.47**	**1.55**	**1.66**	**1.80**
EPS (ex-ESO exp., dil.) ($)	**--**	**--**	**--**	**--**
DPS ($)	0.91	0.97	1.04	1.11
Div. payout ratio (%)	61.6	61.4	62.3	61.8
Wtd avg shares out. (basic) (mn)	215.6	249.7	260.9	260.9
Wtd avg shares out. (diluted) (mn)	215.9	254.6	261.1	261.1

Balance Sheet ($ mn)

	12/19	12/20E	12/21E	12/22E
Cash & cash equivalents	1,868.4	110.7	43.4	46.0
Accounts receivable	107.6	152.9	152.9	152.9
Inventory	18.4	22.7	22.7	22.7
Other current assets	18.3	129.7	129.7	129.7
Total current assets	**2,012.7**	**416.0**	**348.6**	**351.2**
Net PP&E	6,345.8	9,389.8	10,625.6	11,427.3
Net intangibles	63.8	2,342.4	2,342.4	2,342.4
Total investments	6.0	5.9	5.9	5.9
Other long-term assets	933.7	1,316.9	1,316.9	1,316.9
Total assets	**9,362.0**	**13,470.9**	**14,639.4**	**15,443.7**
Accounts payable	74.9	124.1	124.1	124.1
Short-term debt	130.8	122.4	147.4	177.4
Current lease liabilities	–	–	–	–
Other current liabilities	113.3	201.7	201.7	201.7
Total current liabilities	**319.0**	**448.2**	**473.2**	**503.2**
Long-term debt	2,943.3	5,548.1	6,160.0	6,710.0
Non-current lease liabilities	–	–	–	–
Other long-term liabilities	2,218.8	2,799.5	2,856.5	2,901.7
Total long-term liabilities	**5,162.2**	**8,347.6**	**9,016.5**	**9,611.8**
Total liabilities	**5,481.1**	**8,795.8**	**9,489.7**	**10,114.9**
Preferred shares	–	–	–	–
Total common equity	**3,880.9**	**4,675.2**	**5,149.7**	**5,328.8**
Minority interest	–	–	–	–
Total liabilities & equity	**9,362.0**	**13,470.9**	**14,639.4**	**15,443.7**
BVPS ($)	18.00	18.73	19.74	20.43

Cash Flow ($ mn)

	12/19	12/20E	12/21E	12/22E
Net income	224.5	293.6	434.7	469.1
D&A add-back	156.5	252.1	292.3	321.9
Minority interest add-back	–	–	–	–
Net (inc)/dec working capital	(62.3)	6.3	–	–
Others	19.3	25.7	57.0	45.2
Cash flow from operations	**338.0**	**577.8**	**784.0**	**836.3**
Capital expenditures	(550.3)	(768.1)	(992.4)	(864.4)
Acquisitions	(59.7)	(3,466.8)	(535.7)	(259.2)
Divestitures	–	–	–	–
Others	5.4	0.0	–	–
Cash flow from investing	**(604.6)**	**(4,234.9)**	**(1,528.2)**	**(1,123.7)**
Dividends paid	(188.5)	(237.2)	(271.0)	(290.0)
Share issuance/(repurchase)	1,947.6	734.1	310.9	–
Inc/(dec) in debt	371.1	1,390.4	636.9	580.0
Others	1.2	11.6	–	–
Cash flow from financing	**2,131.4**	**1,899.0**	**676.8**	**290.0**
Total cash flow	**1,864.8**	**(1,758.1)**	**(67.3)**	**2.6**
Free cash flow	(212.3)	(190.3)	(208.4)	(28.2)
Free cash flow per share (basic) ($)	(0.98)	(0.76)	(0.80)	(0.11)

Source: Company data, Goldman Sachs Research estimates.

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PM Summary

We upgrade regulated water/gas utility Essential Utilities (WTRG) to Buy from Neutral and add to the Conviction List given the following key points:

1. **We see WTRG as a secular winner to benefit from the EPA's estimated $750 billion of water infrastructure investment needs in a very fragmented market.** With the estimates from the Environmental Protection Agency (EPA), and based on WTRG's current 1% market share of US customer connections, this implies at least a $7bn investment opportunity, translating into 15 years of 6-7% organic earnings growth, or ~8% including municipal acquisitions.
2. **WTRG's recent acquisition of PA-based gas utility diluted its pure-play water profile but supports robust growth through de-carbonization.** We view this acquisition as a one-off investment in gas – from a recent conversation with management – given its geographic proximity to water headquarters, along with a robust growth opportunity via aging pipe replacement investments that should reduce 119k tons of CO2 over the next 15 years, equivalent to emissions from 25k cars or 13k homes.
3. **WTRG should benefit from a scarcity premium** as one of two large-cap, publicly traded water utilities in the US that comprise 80% of the sector's total market capitalization, as well as a **renewed ESG focus** given water utilities still comprise 70% of total earnings and management's focus on increasing the exposure.
4. **We view WTRG's multiple compression versus water utilities as overdone,** with current prices reflecting a 7x (20%) discount for the company's water utility segment versus the only other large-cap water utility American Water (AWK, Buy), which we view as unwarranted (Exhibit 4) given comparable long-term growth potential (Exhibit 5). From another angle, we see the market valuing WTRG as a 60% gas utility despite its 70% water earnings composition. Given management's strategy to further increase its water utility exposure over time, we believe WTRG deserves a premium valuation to reflect its high growth, largely ESG-friendly profile.

Our 12-month price target $51 (from $45 prior) reflects a 24% total return versus 13% for Regulated Utilities, with our estimates reflecting a robust 7% EPS/DPS CAGR from 2019A-2022E versus a 5% average for Regulated Utilities.

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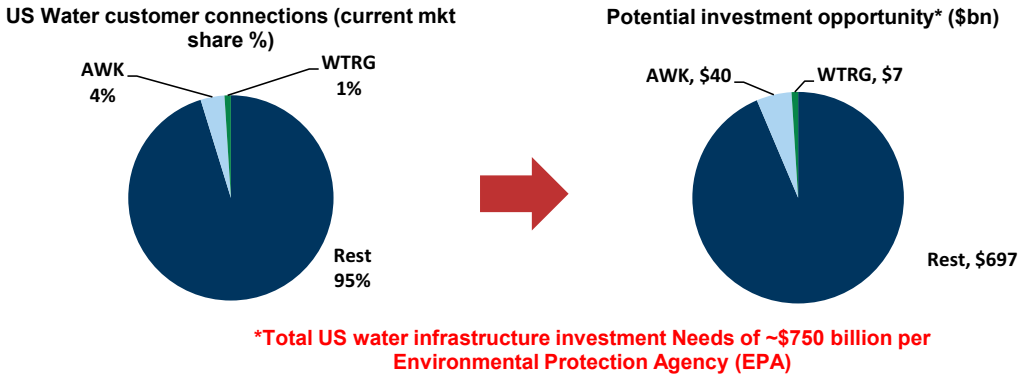
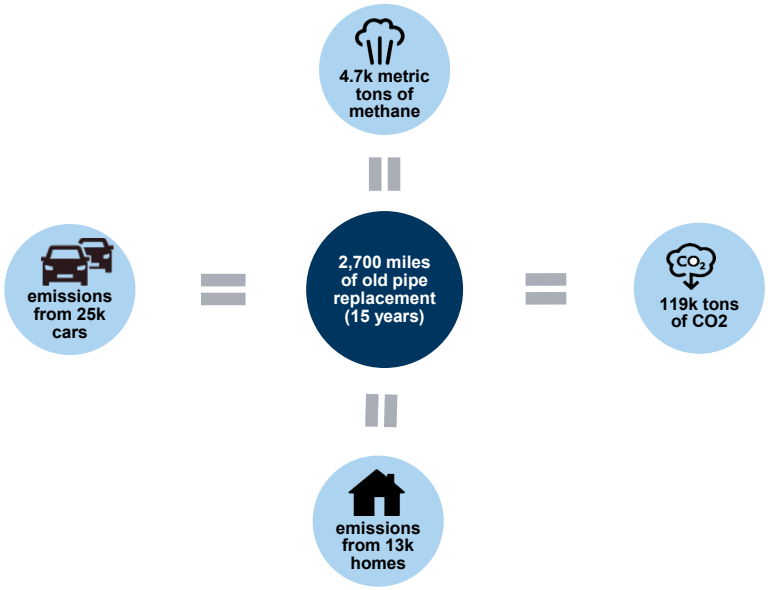
Exhibit 1: With an estimated $750 billion in US water investment needed, WTRG could see at least a $7bn opportunity at current market share, well above its total current water asset base...
US water investment needs, potential opportunity for WTRG/AWK



Source: Company data, Goldman Sachs Global Investment Research, Environmental Protection Agency

Exhibit 2: ...along with aging gas infrastructure replacement that supports de-carbonization
Potential emission reductions from aging gas pipe replacement



Old pipe replacement refers to bare steel and cast iron pipes

Source: Company data, Goldman Sachs Global Investment Research

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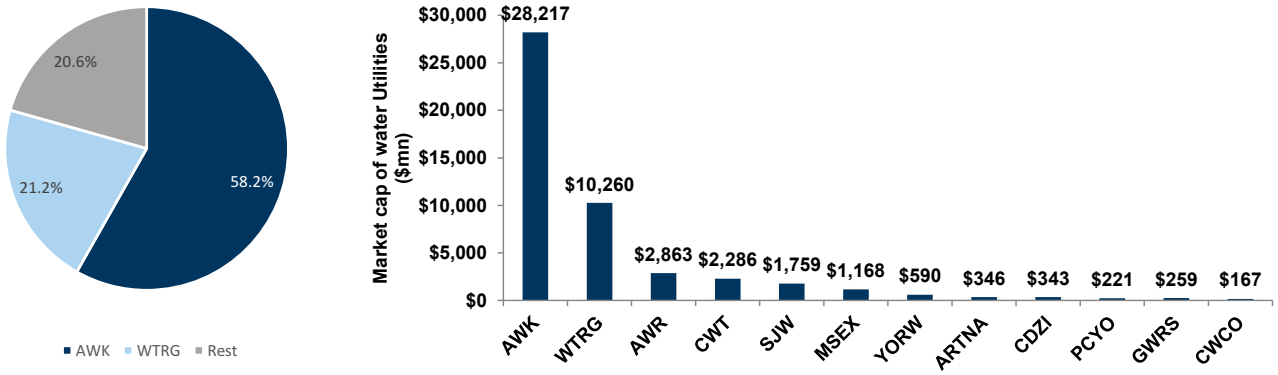
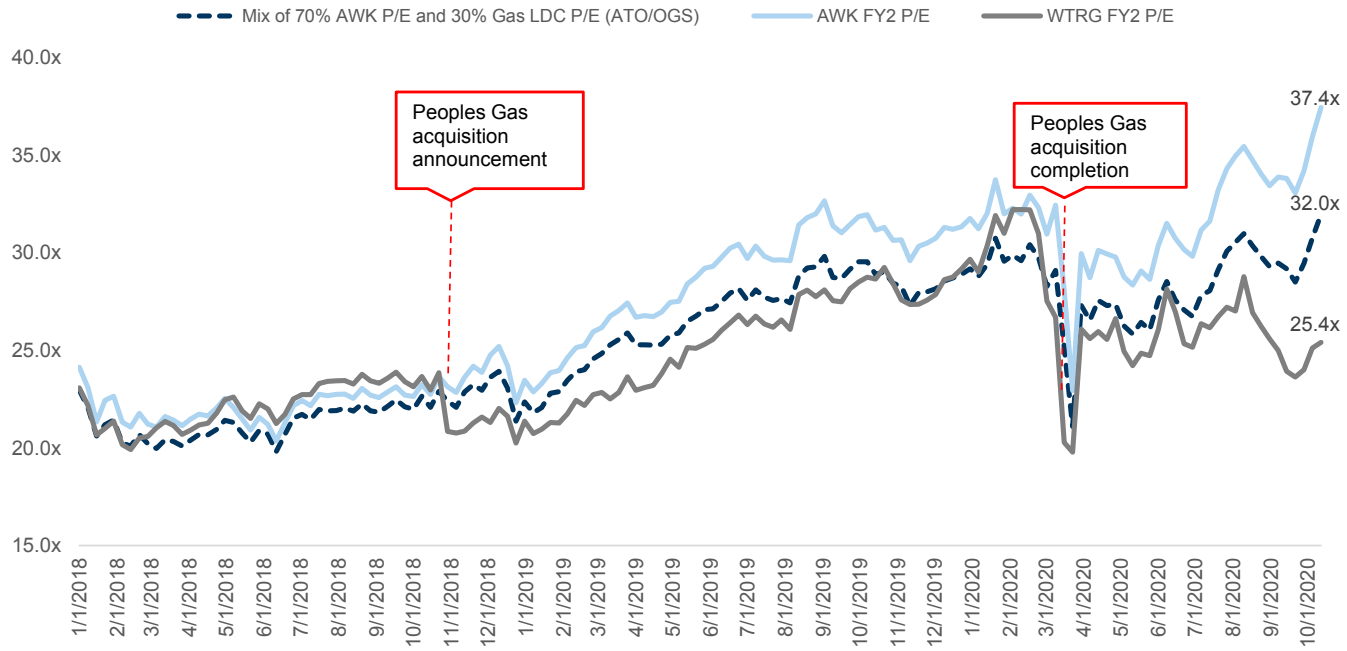
Exhibit 3: WTRG represents one of only two large-cap, publicly traded water utilities in the US, which should support a scarcity premium
Investor-owned water utilities by market cap and by % of total



as of 10/16/20

Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 4: We view WTRG's meaningful relative P/E discount as unwarranted based on its 70%/30% water/gas profile...
FY2 P/E for AWK, WTRG, and an illustrative performance of a 70%/30% water/gas utility



ATO/OGS chosen as illustrative gas utility comps based on company profile, including their status as the two largest gas LDCs by market cap

Source: FactSet, Goldman Sachs Global Investment Research

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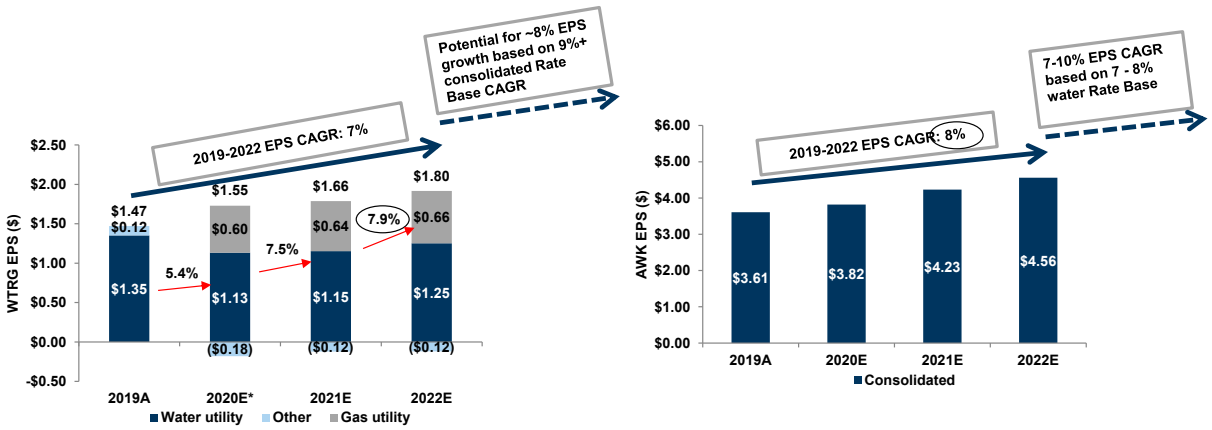
Exhibit 5: ...given we see WTRG's normalized EPS growth potential relatively in-line with that for AWK
WTRG/AWK EPS CAGR, 2019A-2022E; longer-term EPS/rate base growth potential



*Represents AWK's guidance through 2024, with another 1-2% EPS growth contribution expected from its market-based segment. WTRG rate base growth CAGR based on GS estimates.

Source: Company data, Goldman Sachs Global Investment Research

Thesis #1: Material investment needs for US water infrastructure provide secular growth opportunity for WTRG

The $750 billion water proposition. Aging infrastructure and increased regulation in the sector are primary drivers for the need to modernize the country's water and wastewater infrastructure related to water quality and the management of water and wastewater residual discharges. Because pipe assets last a long time, water systems that were built in the latter part of the 19th century and throughout much of the 20th century have not, for the most part, experienced the need for pipe replacement on a large scale. To put this aging infrastructure into context, the Environmental Protection Agency (EPA) estimates almost $750 billion of investment needed to upgrade the country's water systems, both public and private, to meet environmental standards. Based on WTRG's current 1% market share of US customer connections, this implies at least a $7bn investment opportunity, more than the company's current ~$5bn water rate base, supporting visibility to grow rate base at the current 6-7% rate for almost the next 15 years (excluding municipal acquisitions).

The water utility sector is highly fragmented... Of the 50,000/15,000 water/wastewater systems nationwide, only 16%/2% are run by investor-owned utilities (IOUs) and privately held water utilities, making the water industry the most fragmented of the major utility industries (electric, natural gas, water/wastewater). With local municipalities owning and operating the majority of the community water systems, many face challenges associated with their aging, deteriorating water and wastewater assets, do not have the expertise or technical capabilities to continue to comply with ever-increasing environmental regulations or simply want to focus on other community priorities.

...and Fair Market Value (FMV) legislation offers acquisition opportunities for

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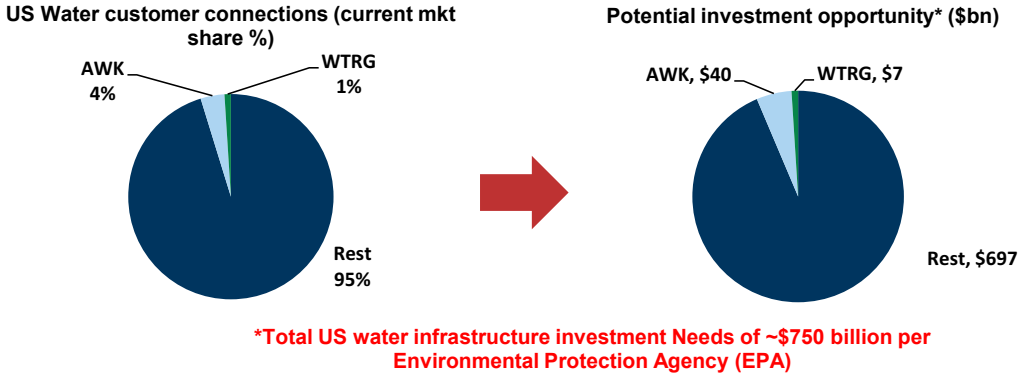
WTRG. The sector has been ripe for consolidation for decades and the largest water utilities have recently altered their strategic growth efforts to focus on buying mid-sized municipal water and wastewater systems fueled by fair market value (or FMV); legislation allows the water utilities to include into rate base the fair market value of the acquired municipal water assets instead of the depreciated original cost of water/wastewater assets. FMV is on the books in all of WTRG's 8 operating jurisdictions, which should allow WTRG to aggressively increase its water utility footprint, per the company's current opportunity set that could increase its customers served by 30% if fully successful. For illustrative purposes, a 1% increase in WTRG's market share by people served could add ~100% of WTRG's 2019A water utility rate base (Exhibit 10), all else equal.

Exhibit 6: We see meaningful water infrastructure replacement opportunities for WTRG that near its current market cap...
US water investment needs, potential opportunity for WTRG/AWK



Source: Company data, Goldman Sachs Global Investment Research, Environmental Protection Agency

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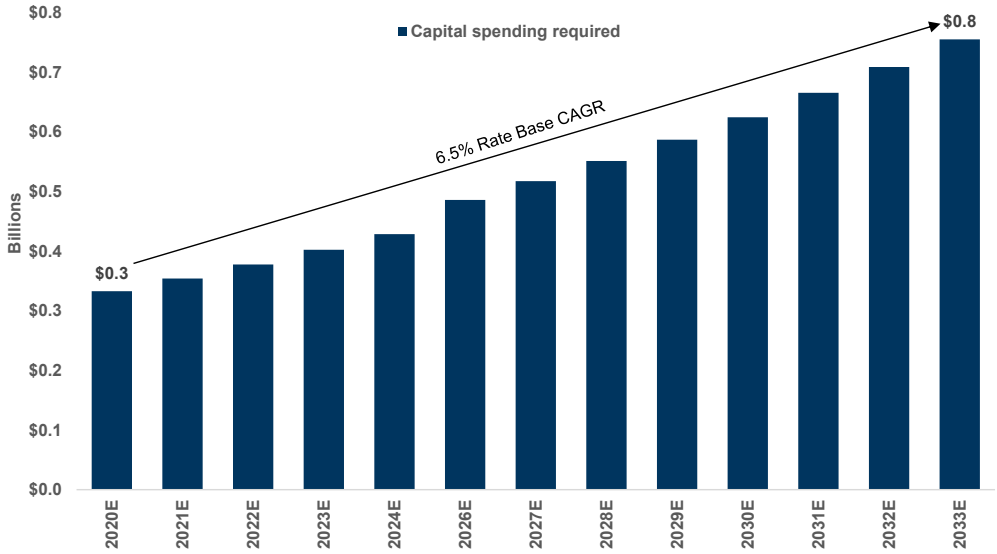
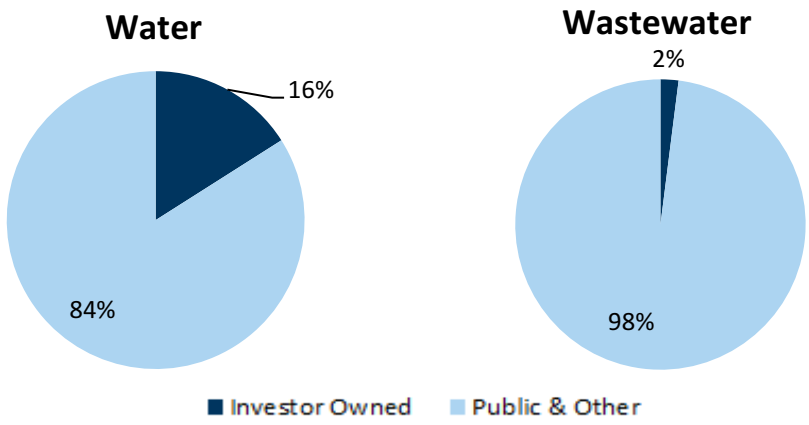
Exhibit 7: ...which could allow WTRG to grow its water rate base at the current 6-7% rate for nearly 15 years (excluding municipal acquisitions that could add an incremental 1-2% growth)
Number of years of 6.5% rate base growth achievable with $7bn of capital spending



Excludes potential rate base additions from municipal system acquisitions

Source: Company data, Goldman Sachs Global Investment Research

Exhibit 8: ...along with consolidation opportunities given IOUs and privately held water utilities operate only a small portion of the US water/wastewater systems
Water Industry- Investor Owned vs Public & Other market share, as of 2019



Source: Company data, Goldman Sachs Global Investment Research

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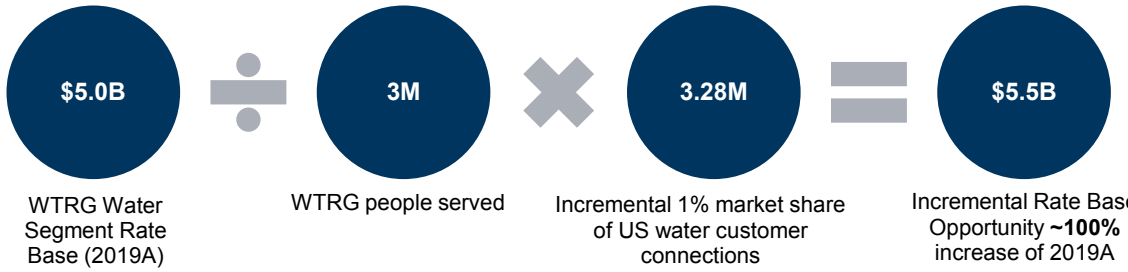
Exhibit 9: FMV legislation provides further impetus for consolidation, with all 8 of WTRG's water utility states passing the law
States with Fair Market Value Legislation for Water Utilities, WTRG states of operations

Source: Company presentation

Exhibit 10: For illustrative purposes, a 1% increase in WTRG's market share by people served could add ~100% of 2019A rate base, all else equal.
Illustrative calculation of incremental rate base from a 1% increase in WTRG's water market share



Source: Company data, AWWA, Goldman Sachs Global Investment Research

Thesis #2: Gas utility infrastructure investments supports robust growth through de-carbonization

We view the recent Peoples Gas acquisition as a one-off investment into gas utilities. WTRG's October 2018 decision to acquire privately held PA-based gas utility Peoples Gas, and the March 2020 completion, created a new asset mix for the company that now comprises 70%/30% water/gas utility by rate base and earnings. While this diluted the company's pure-play water profile supported by ESG-focused investors, in our view, we believe the investment did offer geographic synergy opportunities given WTRG's PA-based headquarters, while adding an under-invested gas system with robust growth opportunities. We note WTRG does not intend to grow its gas utility footprint through other acquisitions, per our recent conversation with management.

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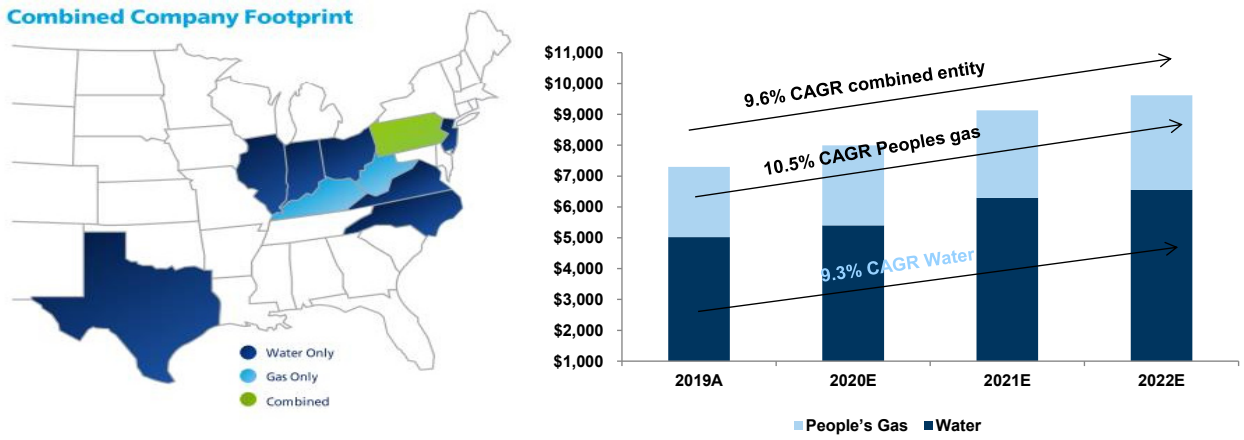
Peoples Gas offers robust growth through aging pipe replacement... We see ~10% rate base growth at Peoples Gas from 2019A-2022E primarily driven by long-term visibility of pipeline replacement projects. We note that Peoples has identified more than 2,700 miles of bare steel and cast iron pipe to be replaced under its Long-term Infrastructure Improvement Plan (LTIIP) by 2034 in its PA service territory, which at ~180-200 miles/year of pipe replacement, implies more than 15 years of increased capital spending to help support visibility of 9% rate base CAGR beyond 2022. We note this growth does not depend on new gas customer connections.

...while achieving de-carbonization. In addition to reliability and safety benefits from aging infrastructure replacement, we highlight that these investments also reduce meaningful methane emissions in the process. Per the company's data, the ~200 miles per year of pipe replacement reduces 9,000 tons of CO2, equivalent to emissions from 1,900 cars or 1,000 homes. Based on the 2,700 miles of identified cast iron/bare steel in the Peoples Gas system, this would equate to 25k cars or 13k homes.

Exhibit 11: We view WTRG's acquisition of Peoples Gas as a one-off gas investment that offers geographic synergies and robust growth...
WTRG operational footpring; rate base ($mn) 2019A-2022E



Water rate base growth includes municipal acquisitions

Source: Company data, Goldman Sachs Global Investment Research

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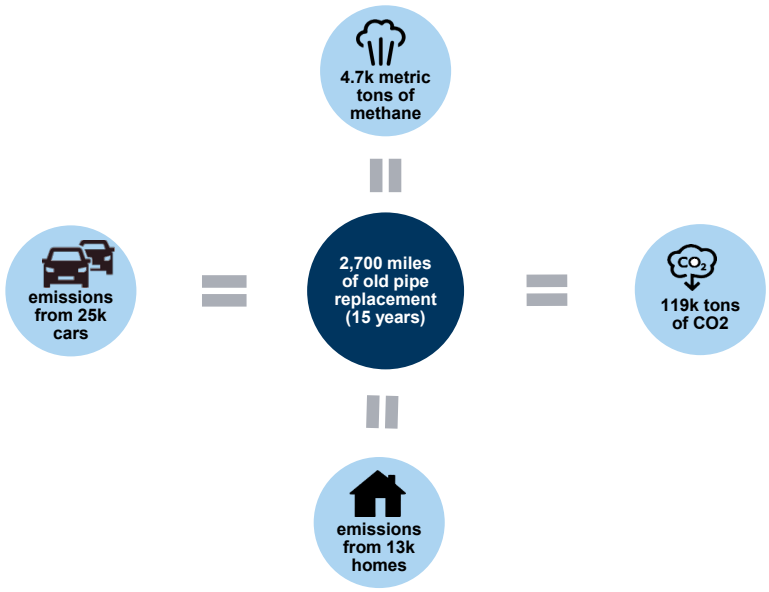
Exhibit 12: ..with aging gas infrastructure replacement that supports de-carbonization
Potential emission reductions from aging gas pipe replacement



Old pipe replacement refers to bare steel and cast iron pipes

Source: Company data, Goldman Sachs Global Investment Research

Thesis #3: WTRG should benefit from a scarcity premium, renewed ESG focus

WTRG is one of only two large-cap, publicly traded water utility in the US. Given the very light trading volumes for the majority of the water IOUs, we believe investors have limited options to invest in water utilities, which should benefit WTRG longer-term. In addition, while the company's recent acquisition of Peoples Gas diluted its status as a pure-play water utility, we see WTRG's 70% earnings mix to water utilities and management's strategy to grow the exposure over time should regain the attention of more ESG-focused investors, given their large overweight position to Water Utilities including WTRG per the recent data and publication from our GS SUSTAIN team (Exhibit 14, Exhibit 16).

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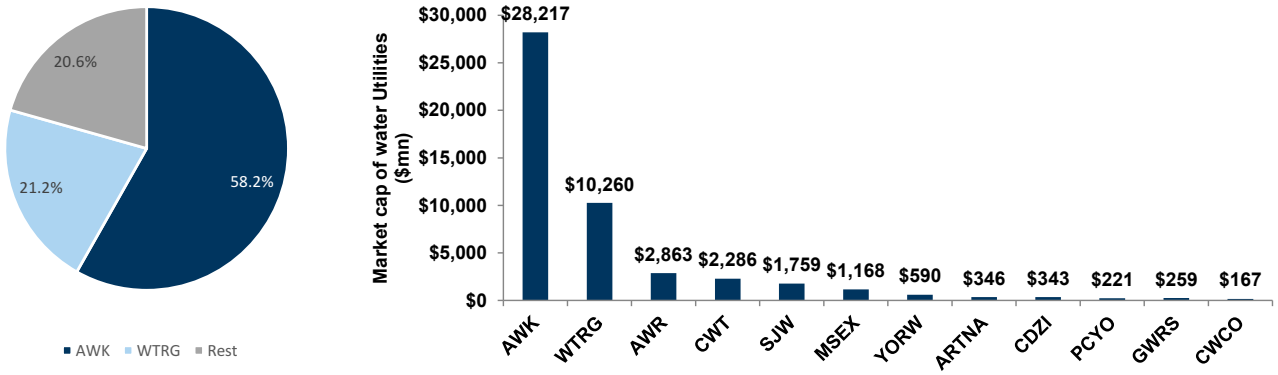
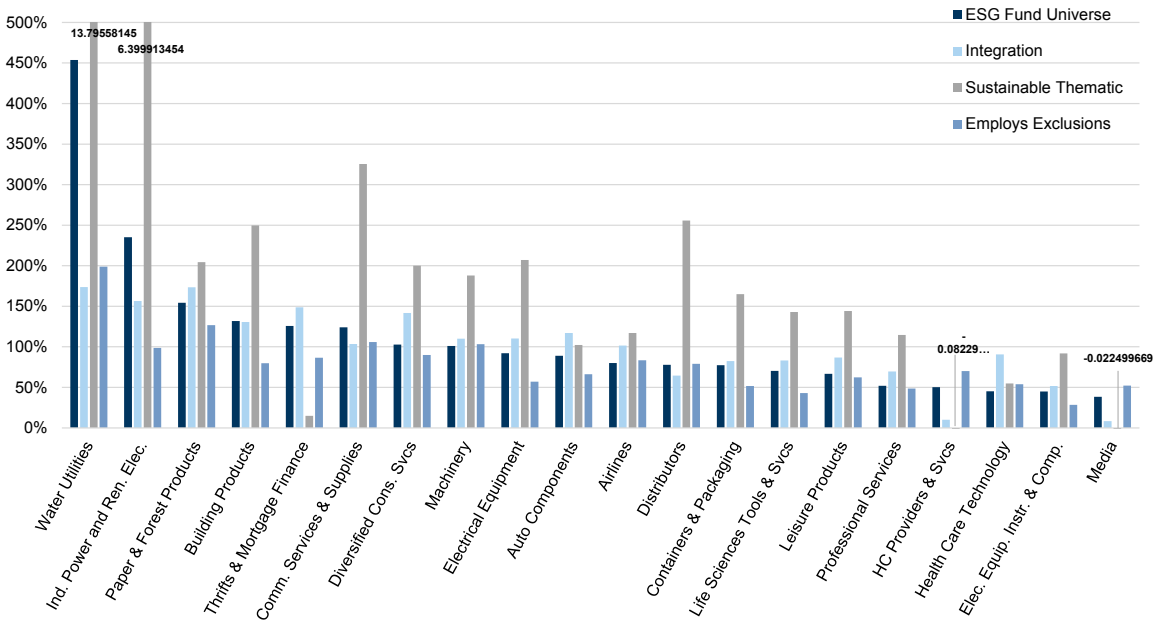
Exhibit 13: WTRG and AWK comprise around 80% of total water IOUs in the US
Investor-owned water utilities by market cap and by % of total



as of 10/16/20

Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 14: Water Utilities are the most overweighted industry by ESG owners
20 most overweighted industries (GICS 3) by ESG-linked equity funds



Source: Morningstar, Thomson Reuters, Goldman Sachs Global Investment Research, GS SUSTAIN

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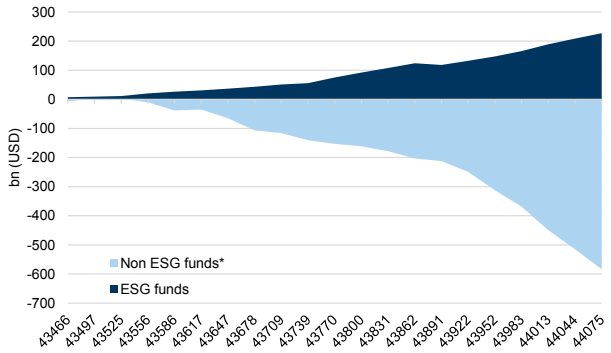
Exhibit 15: ESG fund flows have stood in stark contrast to non-ESG counterparts
Cumulative monthly fund fulows for ESG and non-ESG equity funds (1/2019-9/2020)



Source: Morningstar, Goldman Sachs Global Investment Research, GS SUSTAIN

Exhibit 16: WTRG still ranks as one of the most overweight US companies by ESG funds
Top 10 most relatively overweighted US companies by ESG funds (August 2020)

	Company	Sector
1	First Solar Inc	Info Tech
2	Xylem Inc	Industrials
3	Tetra Tech Inc	Industrials
4	American Water Works	Utilities
5	Sunrun Inc	Industrials
6	Essential Utilities Inc	Utilities
7	IDEX Corp	Industrials
8	Trimble Inc	Info Tech
9	PTC Inc	Info Tech
10	Nuance Communications	Info Tech

Source: Morningstar, Thomson Reuters, Goldman Sachs Global Investment Research, GS SUSTAIN

Thesis #4: WTRG's valuation under-appreciates secular water growth outlook

We view WTRG's multiple compression versus water utilities as overdone, despite its acquisition of privately held PA gas utility Peoples Gas in early 2020 (30% of consolidated earnings) that removed its pure-play water profile and contributed to the underperformance, in our view. Per Exhibit 17, the stock started experiencing P/E multiple compression in October 2018 with the acquisition announcement, with continued pressure following its deal completion in March 2020. The valuation spread versus the other large-cap water utility – American Water (AWK, Buy) – now stands at ~12x P/E on 2021E, versus relatively in-line as of the Peoples Gas acquisition announcement.

We see WTRG's normalized LT EPS growth rate as relatively in-line with that for AWK at around 8% – representing one of the highest growth rates in our coverage universe – given the potential for a 9%+ combined rate base CAGR assuming continued robust municipal acquisitions. We note our estimated 7% EPS CAGR through 2022 reflects certain items including: 1) earnings and financing lag associated with the proposed DELCORA acquisition and timing of inclusion into rate base (1Q2021 equity issuance assumed, rate base inclusion in 2022), 2) the expiration of tax-advantaged rate-making - repairs tax - at the PA water segment and a return to normal rate-making, and 3) the recent election of repairs tax for Peoples Gas and timing of associated earnings benefit.

While we continue to view a discount versus AWK as warranted for WTRG, given our sum-of-the-parts (SOTP) valuation approach for the water/gas businesses versus AWK's pure-play water profile, we see current multiples meaningfully under-valuing the water business (Exhibit 18), based on WTRG's P/E discount versus an illustrative

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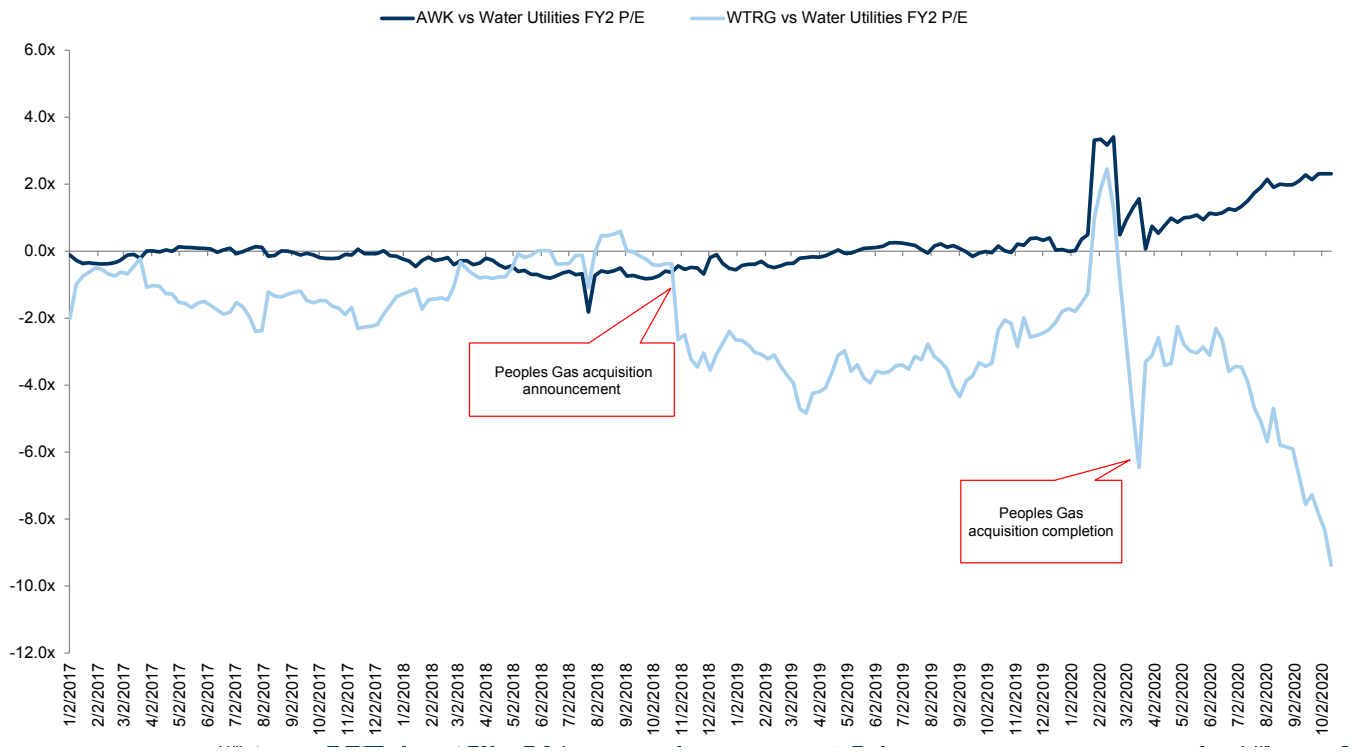
70%/30% water/gas utility mix. In addition, we view management's strategy to increase its water exposure over time as supporting an ESG-friendly profile, which should warrant a premium valuation.

Exhibit 17: WTRG has experienced meaningful relative multiple compression since its announced acquisition of privately held gas utility Peoples Gas

AWK & WTRG vs Water Utilities FY2 P/E (market-cap weighted)



Source: FactSet, Goldman Sachs Global Investment Research

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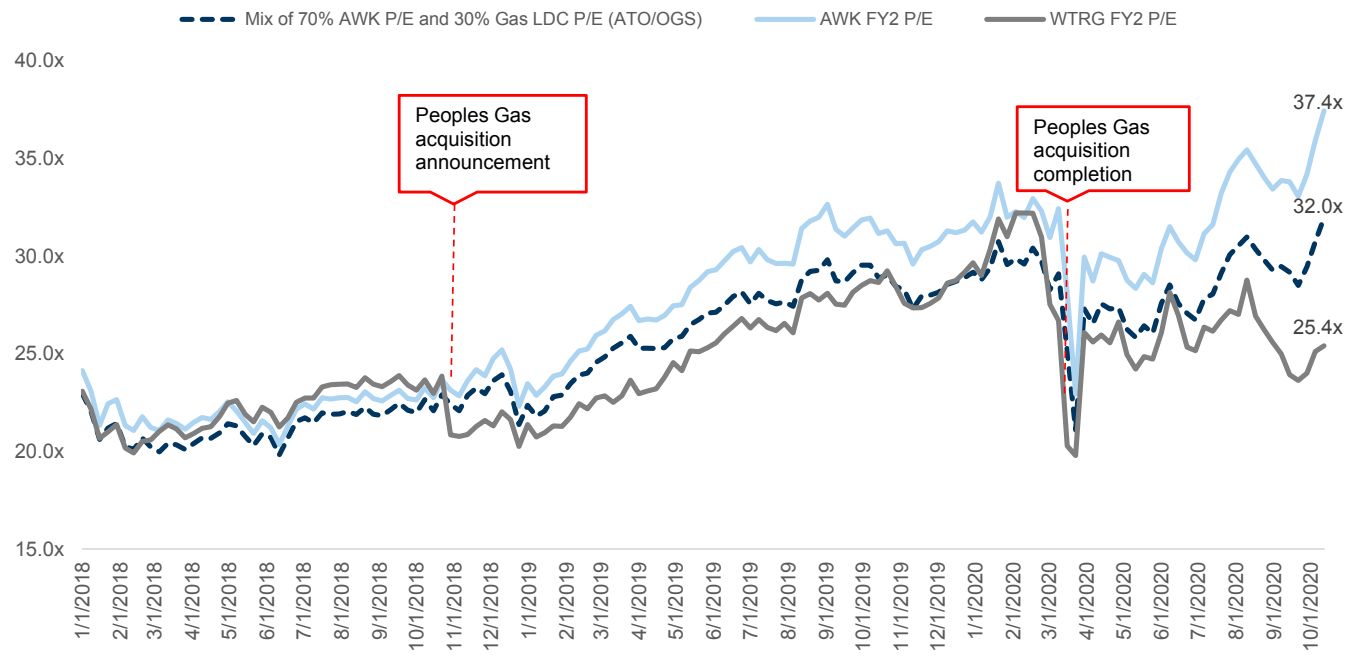
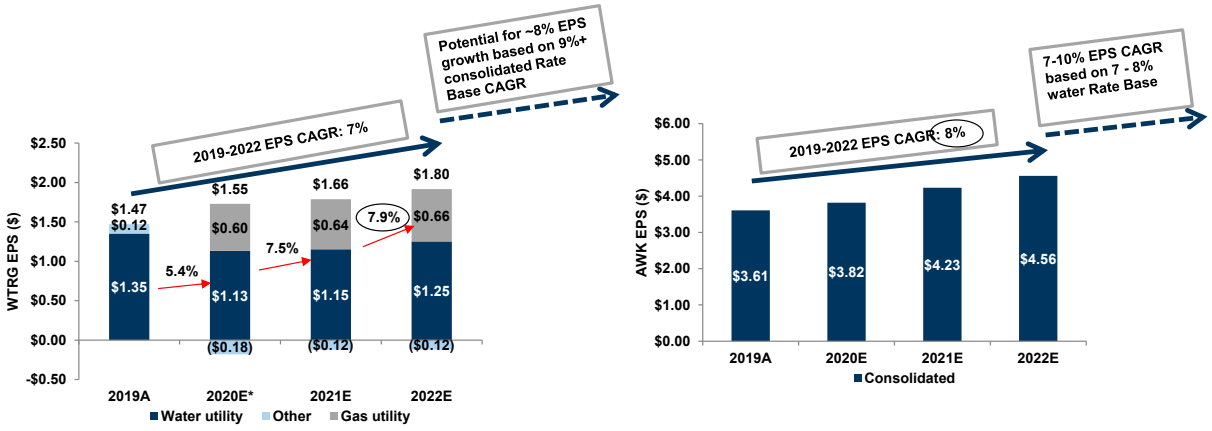
Exhibit 18: We view WTRG's meaningful relative P/E discount as unwarranted based on its 70%/30% water/gas profile...
FY2 P/E for AWK, WTRG, and an illustrative performance of a 70%/30% water/gas utility



ATO/OGS chosen as illustrative gas utility comps based on company profile, including their status as the two largest gas LDCs by market cap

Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 19: ...given we see WTRG's long-term EPS growth potential relatively in-line with that for AWK
WTRG/AWK EPS CAGR, 2019A-2022E; longer-term EPS/rate base growth potential



*Represents AWK's guidance through 2024, with another 1-2% EPS growth contribution expected from its market-based segment. WTRG rate base growth CAGR based on GS estimates.

Source: Company data, Goldman Sachs Global Investment Research

Applying a premium to water segment; upgrade to Buy (add to Conviction List)

Our 2020-2022 EPS estimates remain largely unchanged at $1.55/$1.66/$1.80 – with timing of equity/debt financing the driver of the 2021 estimate from $1.65

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prior - implying a 7% CAGR from 2019A-2022E, along with similar dividend growth during the period. Our 2021 EPS adjustmentWe believe WTRG could achieve a higher growth rate beyond 2022 and closer to its ~9% blended rate base growth, given the more near-term lag from equity financing for the pending DELCORA municipal acquisition, as well as earning on the added rate base.

We raise our 12-month price target to $51 (from $45 prior) based on a SOTP approach, with 35x/22x P/E applied to our 2021 water/gas utility EPS estimates, respectively. We now apply a 5x premium to our base water P/E multiple of 30x to highlight the company's focus on further increasing its water utility exposure that should elevate its ESG-friendly profile, as well as its scarcity premium as one of two large-cap, publicly traded water utilities. Our valuation reflects a 30.6x blended P/E, below our AWK target multiple of 37x, with the relative discount still warranted given WTRG's water/gas business mix. Our new target reflects a 24% total return versus 13% for Regulated Utilities.

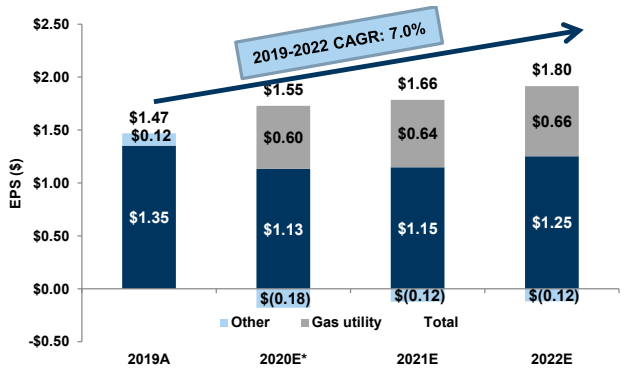
Downside risks to our call include: 1) PA regulation turns less constructive, which impacts earnings growth potential given the bulk of WTRG's earnings are derived from the state's water/gas operations, 2) the proposed DELCORA municipal water system acquisition fails to receive necessary approvals for completion, which could impact longer-term water rate base growth outlook barring replacement with other municipal acquisitions, and 3) longer-term growth concerns about the gas utility segment further compresses WTRG's valuation, both on an absolute basis and relative to pure-play water utilities.

Exhibit 20: Our EPS estimates remain largely in line with consensus through 2022...
GSe vs Consensus

EPS Estimates			% Difference
	GSe	Consensus	vs Consensus
2019A	$1.47	$1.47	0%
2020E	$1.55	$1.56	-1%
2021E	$1.66	$1.66	0%
2022E	$1.80	$1.80	0%

Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 21: ...reflecting a robust 7% EPS CAGR through 2022
EPS 2019A-2022E



*2020 incorporates full-year of Peoples Gas earnings, comparable versus adjusted proforma company guidance. Segment EPS may not add up to consolidated EPS due to rounding.

Source: Company data, Goldman Sachs Global Investment Research

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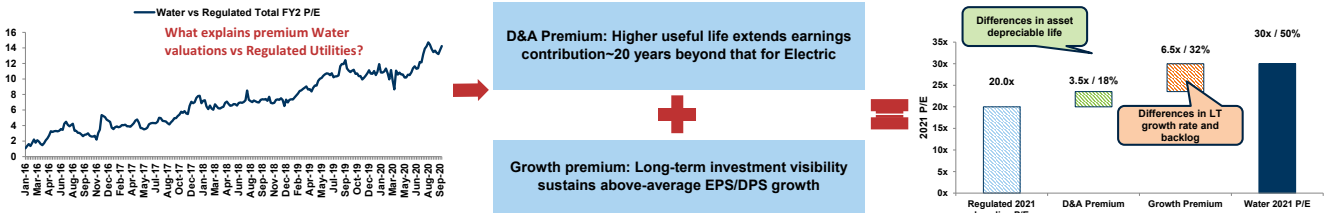
Exhibit 22: Our SOTP-based $51 price target reflects a 25% total return potential
WTRG SOTP Valuation

VALUATION	
Water utility EPS 2021	**1.15**
Water utility multiple	30.00x
Assumed premium	5.00x
Adjusted P/E	35.0x
Water utility valuation	**40.31**
Gas utility EPS 2021	**0.64**
Gas utility multiple	20.00x
Assumed premium	2.00x
Adjusted P/E	22.0x
Gas utility valuation	**13.99**
Valuation - Other	**(0.12)**
2020 Blended multiple	30.37x
Other valuation	**(3.74)**
Total valuation	**51.00**
Current price per share	$41.85
Return potential	**21.86%**
Dividend yield	2.24%
Total return potential	**24%**

Source: Goldman Sachs Global Investment Research

Exhibit 23: Longer useful life and long-term investment visibility largely justify premium water base P/E multiple vs. electric/gas



Source: Goldman Sachs Global Investment Research

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Reg AC

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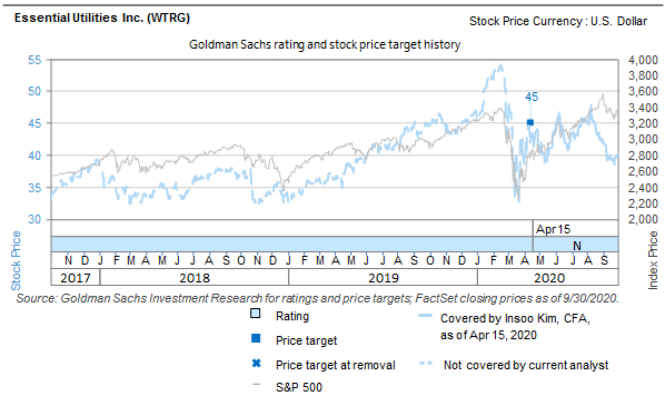

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Essential Utilities Inc. (WTRG): Relative optimism to concerns on asset mix - investor feedback from our upgrade to Buy (add to CL)

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After our October 19 note upgrading regulated water utility WTRG to Buy (on CL), we received a wide range of investor feedback on both sides of the aisle, with some in agreement with the attractive relative valuation and robust long-term growth potential, while others remain concerned about the company's water/gas utility profile from an ESG perspective, along with the market's increasingly negative view on the terminal growth rate for gas demand due to electrification.

We highlight below the main discussion points from our investor conversations on the WTRG upgrade:

1. **Some investors see WTRG as a "show me" story,** despite attractive relative valuations, per their view that the PA-based Peoples Gas utility acquisition diluted its status as a pure-play water utility and did not represent the best strategy for value accretion. That said, they are encouraged by management's commitment to increase its 70% water profile (by earnings) through continued water system acquisitions, which investors view as a higher multiple business that they agree is undervalued at current valuations.
2. **What could improve gas utility valuation multiples?** While investors agreed that WTRG should trade at a discount to pure-play water peers given its exposure to a gas utility, they believe a portion of the company's multiple compression is attributed to the increasingly negative view on gas utilities' terminal growth rate from the electrification theme. They acknowledge that Peoples Gas' majority exposure to gas-friendly Pennsylvania and 10+ year of growth through infrastructure replacement investments (without reliance on new customer connections) should support a premium valuation versus gas LDC peers; however, they remain concerned that continued market pressure on this segment could weigh on WTRG's overall valuation longer than expected.
3. **Investors wonder whether WTRG could continue to maintain its overweight position among ESG funds,** with the stock still ranking as a top 20 relative overweight per our GS SUSTAIN team data. With ESG fund flow continuing to increase, the funds' perception of WTRG's 30% gas exposure remain key to closing the valuation gap versus American Water (AWK, Buy), the only other large-cap water utility that still maintains its pure-play water profile. Some thematic investors did acknowledge the de-carbonization benefit of

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Peoples' gas pipe replacements as a qualifying factor for potential investment; however, others view the elimination of the gas exposure via a spin or sale as the quickest solution to re-capture its clean energy status.

4. **More bearish investors see WTRG un-deserving of a premium P/E multiple,** given their view of the Peoples Gas acquisition as a strategic misstep that may require time to recover. Despite the discount to AWK, they view WTRG's 23-24x P/E on 2022E as not fully capturing the execution and strategic risks, especially versus high-growth, premium electric utilities like Wisconsin Energy (WEC, Sell) or Xcel Energy (XEL, Neutral).

Our $51, 12-month price target (unchanged) is based on a SOTP approach, with 35x/22x P/E applied to our 2021 water/gas utility EPS estimates, respectively. Our valuation reflects a 30.6x blended P/E, below our AWK target multiple of 37x, with the relative discount still warranted given WTRG's water/gas business mix.

Downside risks to our call include: 1) PA regulation turns less constructive, which impacts earnings growth potential given the bulk of WTRG's earnings are derived from the state's water/gas operations, 2) the proposed DELCORA municipal water system acquisition fails to receive necessary approvals for completion, which could impact the longer-term water rate base growth outlook barring replacement with other municipal acquisitions, and 3) longer-term growth concerns about the gas utility segment further compresses WTRG's valuation, both on an absolute basis and relative to pure-play water utilities.

WTRG	12m Price Target: **$51.00**	Price: **$44.50**	Upside: **14.6%**

Buy CL

Market cap: $11.3bn
Enterprise value: $16.9bn
3m ADTV: $53.4mn
United States
Americas Utilities
M&A Rank: 3
Americas Conviction List

GS Forecast

	12/19	12/20E	12/21E	12/22E
Revenue ($ mn)	889.7	1,571.7	1,995.4	2,113.5
EBITDA ($ mn)	521.4	777.5	1,047.8	1,122.3
EBIT ($ mn)	360.8	525.4	755.5	800.4
EPS ($)	1.47	1.55	1.66	1.80
P/E (X)	27.6	28.7	26.7	24.8
EV/EBITDA (X)	19.1	21.4	17.1	16.4
FCF yield (%)	(2.4)	(1.7)	(1.8)	(0.2)
Dividend yield (%)	2.2	2.2	2.3	2.5
Net debt/EBITDA (X)	2.3	7.2	6.0	6.1

	6/20	9/20E	12/20E	3/21E
EPS ($)	0.29	0.22	0.44	0.69

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 23 Oct 2020 close.

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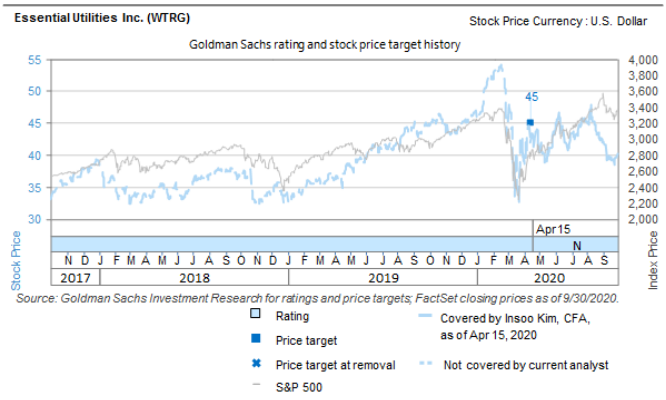

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Utilities: Tidbits and takeaways from EEI

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PM Summary

We come away from our 2020 Edison Electric Institute (EEI) meetings with management with two major themes:

1. **Clean energy transition and lowering emissions:** Companies remain focused on transitioning their generation fleet towards renewables, reducing emissions while supporting increased investments. Both state policy (Renewable Portfolio Standards) and federal tax credits (ITCs/PTCs) along with declining renewable costs are driving the transition.
2. **Shrink to grow opportunities:** Corporate simplification - either announced or in consideration - are driving many of the Diversified Utilities (CNP, DTE, EXC, PPL) as management teams seek to simplify the story and close valuation discounts.

We remain positive on utilities despite recent upticks in share prices and valuations as the sector still trades at a discount to the S&P500 versus a historical 20%-25% premium in a similar low-rate environment. Additionally, utility yields continue to screen favorably in comparison to IG bonds and the UST 10-year. Our top picks include renewable/green names such as NEP and WTRG (both Buy-rated and on the CL), while attractive generation fleet transformation plays include AEE, DUK, and PNW. For more value opportunities, we also see compelling upside in Buy-rated value names FE and PCG, along with Diversified Utilities with SOTP discounts like Buy-rated DTE, EXC and SRE (on CL).

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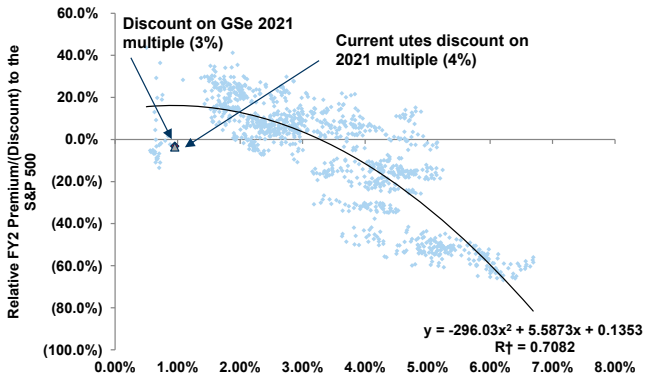
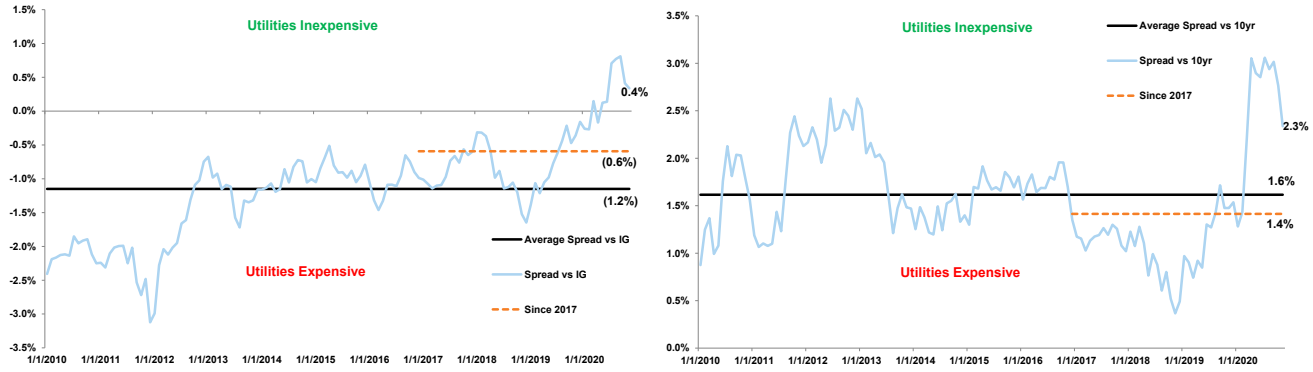
Exhibit 1: Utilities currently trade at a discount to the S&P 500, at a 20%-25% discount to what history would imply in a low rate environment
Utilities FY2 P/E premium/(discount) to the S&P vs UST 10-year yields



Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 2: Utilities continue to trade above average yield spreads in relation to IG bonds and US 10-year treasuries
Utilities yield vs IG bonds vs UST 10 year



Source: FactSet

Top 10 Takeaways from EEI

1. **WTRG expects increased municipal water system acquisition opportunities,** driven by potential increased focus on water quality at both the federal and state levels.
2. **SRE appears still super bullish LNG growth** and financing options for developing new LNG without needing sizable contributions from SRE to fund construction.
3. **Securitization and the wildfire certificate process could drive relief rallies in PCG** – as PCG does not seem significantly concerned on receiving the wildfire safety certificate in the near term and securitizing debt in the longer term.
4. **EVRG maintains high conviction in its Sustainable Transformation Plan (STP)** — recognizing though that new state legislation in KS/MO is the key driver to this, with no clarity coming before early 2021.
5. **D highlights its sizable clean energy related growth at its core regulated VA**

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electric utility - but recognizes permitting hurdles and rate making in VA (longer term) and SC (near term) present risks.

6. **EXC remains a sum of the parts story - and the company does not embed a "carbon value"** in its assessment of its ExGen subsidiary's potential value.
7. **CNP continues to see upside to its regulated growth plan,** at both the electric and gas utilities, while continuing to assess options to reduce its midstream exposure as expeditiously as possible.
8. **PNW remains confident in its robust renewable/storage investment plans,** which should achieve both de-carbonization and long-term customer rate benefit, while looking for a constructive clean energy recovery mechanism.
9. **DTE's 2021 guidance includes more contingency than normal.** Management indicated that given the ongoing pandemic and the uncertainty related to load and margin mix, they believe that they incorporated more than the typical level of conservatism in their initial guidance.
10. **More settlements in Michigan?** With both DTE/CMS announcing rate case settlements this year, the management teams indicated that the new MPSC composition coupled with significant multi-year filings approving large chunks of capex ahead of time could bode well for more settled rate cases in the future.

Company Takeaways

We hosted meetings at the fall EEI (Edison Electric Institute) conference - an industry conference for US utilities. We highlight the following company updates:

- **PPL expects to compare all options against simply reducing debt and buying back shares with potential UK sale proceeds**, but debt reduction remains key post sale to elevate FFO/debt target ~15%-16% from current ~12%-13% level - as detailed in our prior note on this topic. The company hopes, once becoming a pure play US utility, to trade more in line with peer levels post the sale. Likely a federal cash tax payer soon, diversifying into renewables may allow PPL to utilize tax credits and we note management prefers solar over wind from a competitive perspective. Upside may exist to rate base growth in Kentucky — but not till 2022 or later - as they plan to file an Integrated Resource Plan (IRP) in the state to outline gradual generation fleet changes in this coal heavy state.
- **With AZ commission elections complete, PNW remains confident in medium-term renewables/storage investment plans with conviction in ability to demonstrate cost competitiveness.** The company continues to target procurement of utility scale solar coupled with storage aggressively and believes higher clean energy in resource mix creates significant fuel savings despite initial bill impacts. In the ongoing APS rate case, PNW proposed in the recent rebuttal testimony the Advanced Energy Mechanism (AEM), which would provide rider recovery of renewable/storage investments. If not approved in the rate case, the company looks to push the proposal separately, reducing rate case filings while

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aligning clean energy investment goals. On the financing side, while the outcome of the rate case would give additional clarity on the timing/magnitude of equity issuance (current forecast at around $300-$400mn), management expects issuance timing as prior to the next rate case filing, while noting that an approval of a clean energy rider could help push back such a filing and/or mitigate the amount.

- **CMS remains well positioned to continue executing with supportive regulation and a constant eye on operational improvements.** Management reiterated the low hanging fruit of fuel (Palisades; MCV) and O&M (Karn 1&2 and defined contribution vs benefit) tailwinds benefiting the customer over the current 5 year plan. However, CMS emphasized that the real value continues to come from operational cost improvements that heighten the quality of experience for both customers and employees as ways to benefit all stakeholders in MI. The state remains focused on decarbonizing and CMS believes that their current targets and plans already remain on track or exceed those goals while offering significant growth. However, management did note that energy storage remains an area where the next IRP could see more investment sooner and the coal Campbell Units 1 &2 could potentially retire earlier. Management sees multi-year filings as providing support for potentially settling rate cases given more known and already agreed upon factors during future rate cases, but noted the ongoing electric rate case is already far along given the PFD. CMs does not view longer-term trackers as likely, preferring the flexibility with annual or near annual filings, indicating that performance based ratemaking has come up and is already evident in energy efficiency and RPS spend.
- **ETR sees, as part of its multi year guidance, modest under earning levels continuing — and sizable rate base growth as well - but regulatory risk remains.** The company anticipates earning 9%-9.5% RoE levels - below authorized - given rate increase caps or regulatory lag in a few jurisdictions like AR, MS and LA. The FERC docket for its SERI segment could present downside - they've highlighted $0.15+ of EPS at risk, largely to finance refunds, but believe they could potentially mitigate this. Recent 2020 storms likely cost roughly $2bn - they hope to securitize these, based on precedents in Louisiana and Texas - otherwise financing this could weigh on earnings slightly. Low utility rates relative to other utilities remains a tailwind for rate base growth - they seek to add $1.4bn of renewables to the system over the next few years and could add emerging technologies (a new CCGT that is hydrogen capable) as well - RFP processes, especially for its Texas utility, remain key for investors to monitor. Finally, the company - while not a large coal fired generator - still owns the sizable White Bluffs facility in Arkansas with plans to retire in the late 2020s - an earlier expected retirement, being evaluated now, could add to rate base and earnings growth.
- **AGR remains confident in its offshore wind timeline, in addition to its growth through PNM and NECEC.** On Vineyard Wind, the company is expecting final environmental impact statement (EIS) this week and final approval by end of year, but notes an approval delayed until 1Q2021 would not alter their 2024 COD target. Given this timeline, AGR would still qualify for 18% ITCs, while looking to take advantage of any extensions/changes to offshore wind ITC rules if appropriate. The

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company also reiterated its interest in onshore transmission for future offshore wind projects, which is not embedded in the current capital plan. On the New England Clean Energy Connect (NECEC) transmission project, AGR continues to monitor the Maine citizens' initiative as the group plans for a 2nd referendum in opposition, but management believes the project's clean energy and economic benefits to the state will outweigh the opposition arguments. Despite the hurdles to overcome with a project of this magnitude, management expressed interest in considering other future large-scale transmission projects to route clean energy to the NY/NE area to meet clean energy targets. Regarding the company's balance sheet forecast, while AGR looks for Moody's to relax the downgrade threshold for post the PNM acquisition, the guided 14.5%+ FFO/debt from 2022-2025 embeds a potential one-notch downgrade at Moody's.

- **The Florida utilities remain a growth engine for NEE while seeing only modest rate case risk - the renewable segment benefits from massive tailwinds and advantages.** NEE anticipates filling a joint rate case for FP&L and Gulf Power in Florida, where 4 of the current 5 PSC commissioners will oversee the 2021 rate case process. While they likely will seek a rate increase, they recognize RoE risks exist - but they also see potential for continued lower costs going forward that would create headroom for higher rate base growth. The company still sees buyer power, financing advantages, lower O&M costs, site selection skills and economies of scale as their biggest advantages in renewables given their status as the biggest US operator - and an extension of renewable tax credits would not change this, if the new administration in Washington pushes for this. Hydrogen grabs a lot of mind share today - they do not see this as a major near term (2021-25) contributor to earnings, but like energy storage 8-10 years ago, see this as worth monitoring as cost curves improve.
- **CNP sees incremental capital spend spread across its electric/gas jurisdictions,** with 2/3 of the $3bn incremental plan expected at the electric utilities (TX/IN). Electric items include transmission connections for increasing solar build in TX, investments to support customer growth (2-2.5% in TX, 1% in Indiana), while gas investments primarily consist of accelerated gas pipe replacements. Management expects the guided 1-2% annual O&M reductions through 2025 driven by unearthing sustainable O&M savings, conversion from coal to natural gas/renewables, and utilizing technology to improve efficiencies. CNP looks to shift to a majority electric utility profile - partly driving its plan to divest one or two of its regulated gas utilities - while continuing to assess options to reduce its midstream exposure as expeditiously as possible.
- **WEC benefits from a favorable service territory - especially for gas utility service - and believes the current state administration will back its recently announced fleet transformation plan**. With Governor Evers' climate task force still underway, WEC does not fully know the impact of any proposals that will emerge - but they believe retiring older coal/gas units and replacing with solar and storage, along with new gas capacity, will fit in well with broader policy objectives. Cost management could continue in the coming years — while 2020 benefited from greater than originally anticipated levels, more integration could drive even lower

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costs. As a utility in a cash tax paying status, WEC could continue buying renewable projects and keeping the tax benefits - a competitive advantage versus others who need tax equity.

- **DTE maintains outsized regulated growth and contingency in its initial 2021 guidance, noting more cost headroom over time translates to more investment from their substantial backlog of opportunities.** The current 5-year plan assumes regulated net income growth in excess of 7-8%/9% at DTE Electric/Gas, offsetting REF roll-offs and equity conversion headwinds during 2022-2023. While the current capital expenditure forecast implies slower levels during the back half of the 5-year plan, if management can find more cost savings they can pull forward more distribution and potentially renewable capex into the plan. DTE noted that given the uncertainty related to the ongoing pandemic, their initial 2021 guidance implies more than their typical 1 standard deviation below normal load in cushion. Other topics included an expectation to assess retiring the Belle River (2030) and Monroe (2040) coal plants earlier in the next IRP, which could require more capex in 2024/2025 to replace the Belle River capacity but would also require accelerated depreciation of the rate base. Management believes that providing more granularity on a standalone GSP/DTE Midstream company will create value for shareholders, highlighting the strength of their platform and opportunities for growth – especially in the Haynesville as well as the Nexus/Link platforms.
- **Potential corporate structure changes - as initially outlined by EXC in its 3Q2020 release - drove a sizable portion of our discussion with EXC,** as the company evaluates a possible separation of ExGen from the regulated businesses. Realizing higher valuation levels remains a key aspect of the decision making process - but regulatory approvals at state/federal levels remain key as well to whether they move forward or not with any changes. They do not "price in" or assume a value for carbon or a carbon tax when assessing the company's largely nuclear ExGen fleet — as they do not seem overly optimistic of a national carbon regime emerging soon - but see this as a "call option" not embedded in their base case. The company reiterated plans to meet its regulated utility EPS growth guidance given out previously - despite the impact of weak demand driven partially by COVID 19.
- **For AEP, while earned RoE's may decline, higher equity layers could offset this partially.** In our chat with management, they discussed that guidance assumes a low 9% range for earned RoE's - driven by regulatory lag in jurisdictions like Oklahoma and Louisiana - but hope to offset this with increased investment in projects with trackers and with higher equity layers in rates. The new 5-year capital spending plan incorporates not just the North Central wind project, but other smaller scale renewable spend as well as incremental transmission investment.
- **Dominion faces limited regulatory risk in the near term, but acknowledges longer term risk still exists.** The 2021 triennial earnings review in Virginia creates limited risk given the $50mn cap on revenue reductions, but the company did recognize that (1) risk in Virginia exists in the 2024 review, where no revenue reduction caps exist and (2) the ongoing South Carolina rate case may see

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intervenor testimony that seeks a far lower rate increase than sought by Dominion. Potential changes at the state utility regulatory commission remain worth monitoring in Virginia. D stays positive on gas utilities given trackers that exist in markets like Ohio, paired with opportunities to grow renewable natural gas and even do its first small scale hydrogen pilot test in Utah. D also iterated that it does not expect change in the company's views on its remaining contracted assets like Cove Point LNG or Millstone nuclear in CT.

- **SRE remains very bullish its mix of US utilities and infrastructure businesses - and expects positive LNG related news in the coming months.** With SRE having sold its Latin American utilities and its US renewable business in the last year, the company's new simplified structure should prove easier for investors to understand going forward. Rate base growth remains material in California given the transition to clean energy - and even with a potential risk to authorized RoE's for 2022 there, authorized levels remain above national averages. Texas remains a growth opportunity - they just raised rate base growth projections by $300mn and could see another $775m+ upside in the coming years - and do not expect an overly contentious rate case proceeding in 2021. On the LNG front, Sempra expects to FID the Costa Azul LNG project - and assume limited construction risk — with only $250m of Sempra's equity capital used to finance this project - and still see Port Arthur LNG as one of the few US facilities potentially moving forward in the coming years.
- **WTRG highlights increasing water quality focus as a potential catalyst to support municipal water acquisitions.** While increased federal funding for water infrastructure, if implemented, could deter certain acquisition opportunities, management expects smaller systems to continue to face funding shortages, especially when combined with potential increase in water quality standards. On its recently acquired Peoples Gas system, WTRG expects pipeline replacement to fuel robust rate base growth at Peoples, while its low pressure systems and above-ground checkpoints enhancing its operational safety.
- **ED continues to face uncertainty related to COVID-related costs and storm response,** while reiterating its equity issuance plan (up to $600mn in 2020, $1.1bn total from 2021-2022) with an update expected with 4Q2020 earnings. At CECONY, ED sees potential investment opportunities to improve grid reliability, including potential for additional undergrounding of its distribution system. ED also looks to continue growing its renewable footprint, although offshore wind remains above its risk tolerance level except for associated onshore transmission investments. Finally, management reiterated its view that its midstream equity stakes in Mountain Valley Pipeline (MVP) and Stagecoach are non-core while looking to mitigate the exposure.
- **DUK anticipates trying to put together a coalition to seek electricity related state legislation in N Carolina** – seeking (1) revised rate making – including multi-year plans, decoupling and/or trackers, (2) policy support for a timeline around coal plant retirements, (3) detailed emission reduction targets and (4) policy support for offshore wind. Cognizant of managing the rate impact, which remains key to get industrial customers on board, the company may need to agree to annual or multi-year rate caps. However, we note their IRP (Integrated Resource Plan) base

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case assumes ~1% annual rate change and the more aggressive no carbon plan assumes ~2.5% annual increases - so none that appear overly material or that would drive rate concerns for customers. Increased spend at the gas utilities will help drive overall rate base growth - they still see these businesses as attractive growth opportunities - as would higher solar related spend at the Florida electric utility. Florida remains worth monitoring given (1) a proposal to add 750 MWs of community solar, which will go before the PSC in late 2020 and (2) next year's rate case, where DUK will likely seek small rate increase levels.

- **The regulatory front and wildfire recovery will drive EIX from here**. EIX remains bullish regarding changes in California utility regulation — they see faster regulatory decisions as showing the state utility commission wants to work in a more expedited approval process. Recent approvals on securitization, insurance cost recovery, COVID 19 cost deferral and recovery, and wildfire spend recovery (2018-2020), show the state continues to see utilities as necessary "partners" in moving to a cleaner energy economy. They view the cost estimates for 2020 wildfires as likely falling within insurance recovery levels and continue to work to resolve claims related to the 2017/2018 wildfires, after reaching settlements with public entities and the subrogation claims holders. EIX still plans to issue $1bn in common equity - more likely doing so after wildfire season ends in late 2020 and as they get closer to reaching settlements with claimants from prior wildfires — and can utilize $800mn of insurance to pay out claims for now on the 2018 wildfires.
- **XEL looks to continue its robust renewable investment pipeline,** while ITC/PTC extensions - if realized - could support incremental renewable PPA buyout opportunities. Along with the renewable theme, XEL highlighted its commitment to support EV infrastructure and increased EV adoption, with $500mn of planned investments across its various jurisdictions. Finally, XEL expects to be able to grow at the upper half of 5-7% EPS growth guidance with just its base capital plan, while the proposed $1.4bn in incremental wind/solar investments could pad the growth toward the upper end of the guidance range, supported by a flattish base O&M CAGR through the mid-2020's.
- **In our discussion with PG&E Corp's (PCG) interim president and other officers, the company highlighted skills sought in incoming CEO/CFO** level personnel - with announcements likely in the months ahead on who will fill these seats. Operational experience, political and regulatory expertise remain key to the skillset needed for PCG's incoming CEO — while the CFO search focuses on individuals with strong investor relations skill sets as well as in balancing capital spend goals with the impact on customer rate levels. The company did not seem overly concerned regarding the Wildfire Safety Certificate process - they view the delay as more of a technical issue - and hope to get resolution soon. The 2019 certificate remains in place unless the state regulator outright rejects their 2020 application. PCG still anticipates $625m of costs related to the 2019 wildfire - but upside to this may exist and certainty may not emerge for another 1-2 years. They remain optimistic about cost savings opportunities as well as on securitization - they hope to finalize the regulatory docket by late spring 2021 and utilize securitization proceeds to pay down temporarily issued debt in the near term (up to $6bn), with

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plans to pay down $3bn of outstanding holding company debt over the next 2-3 years. Upside may exist to rate base forecast levels - but risks to the authorized RoE for 2022 remains given the state's cost of capital mechanism.

- **Grid infrastructure investment remains top of mind for AEE, while continuing its fleet transition initiatives.** In Illinois, while management continues to pursue passage of the proposed legislation to extend formula rate-making (expiring in 2022) while opening the doors for renewable investments, they view traditional rate-making as relatively constructive as well given a future test year and de-coupling. In Missouri, the utility noted positive feedback and reception from all stakeholders on the recently filed Integrated Resource Plan (IRP) which, combined with ongoing grid investments in the state, should provide robust long-term rate base growth. Management noted that an extension of renewable tax credits - if implemented, could warrant further acceleration of its renewable growth plan.
- **EVRG remains focused on the state legislative front in Kansas and Missouri - outcomes next year likely will significantly impact earnings growth** and realizing EPS targets. The company still believes, as outlined at 2Q2020 earnings, that retiring up to 500 MWs of coal generation earlier than planned - and securitizing these costs - and redeploying the proceeds into new renewables remains, along with raising transmission/distribution investment, the best growth strategy available. They believe strong support exists for energy transition planning in Kansas — and will seek consensus backing on this in Missouri next year - but risks exist that other low cost alternatives, besides simply company owned generation in rate base, could emerge and present a modest risk to their goals of adding more renewables to rate base. Higher transmission spend comes with limited lag — they anticipated higher levels for multiple years to help Kansas integrate wind capacity, but actually see a bit of an uptick in its smaller segment in Missouri (Missouri West). EVRG does not see asset sales as likely needed or leading to lower costs - early retirements remain the core driver.
- **AWK spoke on opportunities to address water contaminants even in the absence of a federal water quality mandate,** which could drive both organic and inorganic growth via continued acquisitions of small municipal water and wastewater systems. While private capital is present in larger systems, AWK is best positioned to do tuck-in deals with 20,000 customers or less, as they can provide investment and improved service while spreading costs across the entire AWK business. The company still expects the NY utility sale to close in early 2021, with NY commission approval the only outstanding condition. AWK continues to replace water pipes within its system, and is targeting a 100-year replacement cycle versus 120-130 years currently compared to many municipal systems at 200 years. AWK's military business continues to see good traction, with numerous opportunities and proposals currently in the works while the Homeowner Services Business has seen some headwind from COVID-19 in 2020 but margins should be stable moving forward ex-COVID.
- **NI continues to see both electric and gas utilities as integral components of the US energy mix.** Management sees an attractive growth trajectory for both types of Utilities, noting that the recent pressure on regulated natural gas valuations

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in the public markets does not appear to reflect the fundamental value they deliver for customers that is not easily replaced. The company does see opportunities to decarbonize on the natural gas side through infrastructure replacement as well as RNG, especially given Ohio and Indiana offer attractive RNG resource – noting this will represent a small amount of volume. On the electric side, management highlighted that potential renewable tax credit extensions could potentially support further acceleration of coal retirements, pulling Michigan City earlier than 2028. Separately, NI reiterated that management remains comfortable with current guidance, incorporating ~$0.05 of impact related to COVID.

- **POR continues to see state-driven clean energy goals supporting on-going renewable/storage investments in Oregon,** as well a growing focus on EV infrastructure opportunities, especially for industrial customer base. With the recent state wildfires mostly contained, POR continues to assess the overall cost from an expense/capital standpoint, although they see the levels as largely manageable and supported by the approved cost deferrals from the state commission. POR in 4Q2020 earnings looks to provide an update on both the wildfire cost estimate as well as thoughts on timing of the next base rate case; for 2021, the company looks to grow earnings (using 2019 as the base and 4-6% long-term growth forecast) driven by cost management, benefit from the completion of the Wheatridge renewable facility, and lower costs associated with the retired Boardman coal plant.
- **OGE focuses on maintaining and growing its regulated electric utility profile, primarily through continued transmission & distribution investments at its Oklahoma/Arkansas jurisdictions, supported by improving regulatory frameworks through certain investment recovery mechanisms.** While fleet de-carbonization is not a primary investment driver near-term, OGE does see select solar opportunities that could combine with gas-fired generation in replacing retiring coal plants. Finally, management views the growth of its regulated utilities as the primary use of any capital allocation opportunities.

Valuation and Key risks

PPL Corp. (PPL, Neutral): $31/sh 12 month target price is based on a sum of the parts analysis. Key risks include regulatory risk, power demand and financing.

Pinnacle West Capital Corp. (PNW, Buy): $94, 12-month price target based on 19.5x P/E multiple on 2021 EPS. Key downside risks include 1) APS rate case outcome corresponding to our bear-case scenario that could pressure valuation multiples in the near-to-medium term, 2) realized electric demand is worse than expected, impacting earnings and cash flows, 3) the November 2020 election results in a non-constructive commission, and 4) PNW is unable to secure much ownership in future renewable generation build-out, limiting rate base growth.

CMS Energy Corp. (CMS, Buy): $69, 12-month price target based on 24x 2021 P/E multiple. Key risks include regulation, legislation, cost management, and financing.

Entergy Corp. (ETR, Buy): $119, 12 month target price based on a sum of the parts analysis. Primary risks include regulatory risks, power demand and financing.

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Avangrid Inc. (AGR, Sell): $45, 12-month price target based on a sum-of-the-parts analysis. Key upside risks for AGR include 1) AGR receives approvals to defer all COVID-19 related costs, mitigating the earnings impact, 2) incremental O&M savings help offset other EPS headwinds, and 3) U.S. government extends federal renewable tax credits, which improve future renewable investment return profiles for AGR's renewable business.

NextEra Energy Inc. (NEE, Neutral): $74, 12-month price target based on a sum-of-the-parts analysis. Key risks include Florida utility regulation, renewable development, tax credit legislation, and operating cost management levels.

Centerpoint Energy Inc. (CNP, Neutral): $22, 12-month price target is based on a sum-of-the-parts valuation. Key risks include customer demand/growth, COVID-related costs, and financing.

WEC Energy Group (WEC, Sell): $88, 12-month target price based a 22x P/E multiple on our 2021 EPS. Key risks to our view include higher than expected capital spend and rate base growth for 2021+, lower than expected operating costs and improved demand.

DTE Energy Co. (DTE, Buy): $142, 12 month price target derived from a sum-of-the-parts valuation. Multiple risks exist to our current view of DTE: (1) Unlike a sale, spinoff valuation remains an unknown for shareholders, if midstream valuations change due to adjustments in legislation, taxes, or supply and demand balances in a negative way, this could impact DTE's valuation. (2) The regulated asset base – representing ~70% of earnings today and theoretically 90% post spin-off – maintains a single state regulatory environment. If MI sees significant changes in regulatory quality – especially the ability to earn timely recovery on investment as well as authorized returns — this could impact our view. (3) Similarly, demand, cost, and investment trends in the state remain critical. (4) DTE currently offers a substantial regulated growth profile, in order to finance this DTE may require equity beyond our forecasts or debt financing costs ahead of our expectations.

Exelon Corp. (EXC, Buy): $53, 12-month price target based off a SOTP analysis. Key risks include retail MWh sales, power prices, generation output, and utility regulation.

American Electric Power (AEP, Neutral): $90, 12-month target price based on SOTP. Key risks include power demand, rate case and regulatory risks, as well as financing.

Dominion Energy Inc. (D, Neutral): $84, 12-month target price based on SOTP. Key risks include regulation, project execution, power demand and financing.

Sempra Energy (SRE, Buy on CL): $150, 12-month price target derived using SOTP. Key risks include project awards, regulatory approvals, construction, and financing.

Essential Utilities (WTRG, Buy on CL): $51, 12-month price target based on SOTP. Key risks include regulation, municipal water system acquisition approvals, and longer-term growth concerns about the gas utility weighing on valuation.

ConEdison (ED, Sell): $78, 12-month price target based on 18x P/E on 2021 EPS. Risks

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include NY utility commission authorization of COVID-19 related costs and bad debt expense, NY economic conditions, renewable segment growth.

Duke Energy (DUK, Buy): $99, 12-month price target based on 19x P/E on 2021 EPS. Key risks include utility regulation, power demand and coal ash related issues.

Edison International (EIX, Buy): $74, 12-month price target based on 17x P/E on 2022 earnings discounted back to 2021. Key risks include wildfire related costs, litigation claims, utility regulation and financing.

Xcel Energy (XEL, Neutral): $71, 12-month price target based on 20x P/E on 2021 EPS. Key risks include upward revisions to rate base/EPS growth, O&M savings, renewable tax credit extension, negative rate case outcomes, less generation in rate base, materialization of PPA buyouts, COVID-19 related cash drag.

PG&E Corp. (PCG, Buy): $15, 12-month price target based on 14x P/E on 2022 EPS discounted back to 2021, and DDM. Key risks include wildfire risk, continued underearning due to legacy holding costs, financing risk and trading risk.

Ameren Corp. (AEE, Buy): $93, 12-month price target based on 24.5x P/E on 2021 EPS. Key risks include regulation, project awards, and financing.

Evergy, Inc. (EVRG, Neutral): $58, 12-month price target based on 18x P/E on 2021 EPS. Key risks include utility regulation, power demand and cost management.

American Water Works (AWK, Buy): $166, 12-month price target based on 39x P/E on 2021 EPS. Key risks include water quality issues, cost management, regulatory environment, growth at non-regulated segments, reduced ESG fund flows.

NiSource (NI, Buy): $27, 12-month price target based on 20x P/E on 2021 EPS. Key risks include Indiana regulatory approvals for renewables, earnings/cash impacts due to COVID-19, higher than expected O&M, electricity demand and customer growth, and financing.

Portland General Electric (POR, Sell): $39, 12-month price target based on 16x P/E on 2021 EPS. Key risks include COVID-19 impacts on earnings/cash, level of COVID/wildfire related cash drag, renewable ownership, and M&A target risk.

OGE Energy (OGE, Neutral): $35, 12-month price target based on 18.5x P/E on 2021 EPS. Key risks include upsized rate base growth, the company could be a target of a take-out, customer and demand growth, further distribution cuts at ENBL, COVID-19 headwinds.

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Disclosure Appendix

Reg AC

We, Michael Lapides, Insoo Kim, CFA, David Fishman, CFA, Rebecca Yuan and Adam Williams, hereby certify that all of the views expressed in this report accurately reflect our personal views about the subject company or companies and its or their securities. We also certify that no part of our compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

Unless otherwise stated, the individuals listed on the cover page of this report are analysts in Goldman Sachs' Global Investment Research division.

GS Factor Profile

The Goldman Sachs Factor Profile provides investment context for a stock by comparing key attributes to the market (i.e. our coverage universe) and its sector peers. The four key attributes depicted are: Growth, Financial Returns, Multiple (e.g. valuation) and Integrated (a composite of Growth, Financial Returns and Multiple). Growth, Financial Returns and Multiple are calculated by using normalized ranks for specific metrics for each stock. The normalized ranks for the metrics are then averaged and converted into percentiles for the relevant attribute. The precise calculation of each metric may vary depending on the fiscal year, industry and region, but the standard approach is as follows:

Growth is based on a stock's forward-looking sales growth, EBITDA growth and EPS growth (for financial stocks, only EPS and sales growth), with a higher percentile indicating a higher growth company. **Financial Returns** is based on a stock's forward-looking ROE, ROCE and CROCI (for financial stocks, only ROE), with a higher percentile indicating a company with higher financial returns. **Multiple** is based on a stock's forward-looking P/E, P/B, price/dividend (P/D), EV/EBITDA, EV/FCF and EV/Debt Adjusted Cash Flow (DACF) (for financial stocks, only P/E, P/B and P/D), with a higher percentile indicating a stock trading at a higher multiple. The **Integrated** percentile is calculated as the average of the Growth percentile, Financial Returns percentile and (100% - Multiple percentile).

Financial Returns and Multiple use the Goldman Sachs analyst forecasts at the fiscal year-end at least three quarters in the future. Growth uses inputs for the fiscal year at least seven quarters in the future compared with the year at least three quarters in the future (on a per-share basis for all metrics).

For a more detailed description of how we calculate the GS Factor Profile, please contact your GS representative.

M&A Rank

Across our global coverage, we examine stocks using an M&A framework, considering both qualitative factors and quantitative factors (which may vary across sectors and regions) to incorporate the potential that certain companies could be acquired. We then assign a M&A rank as a means of scoring companies under our rated coverage from 1 to 3, with 1 representing high (30%-50%) probability of the company becoming an acquisition target, 2 representing medium (15%-30%) probability and 3 representing low (0%-15%) probability. For companies ranked 1 or 2, in line with our standard departmental guidelines we incorporate an M&A component into our target price. M&A rank of 3 is considered immaterial and therefore does not factor into our price target, and may or may not be discussed in research.

Quantum

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Essential Utilities Inc. (WTRG): Virtual management meetings address water/gas growth opportunities; Neutral

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We hosted virtual meetings with Chris Franklin, President and CEO of water/gas utility Essential Utilities (WTRG, Neutral). Key discussion topics included 1) latest demand and financial updates around COVID-19, 2) update on the pending DELCORA municipal water system acquisition as well as the pace of other acquisition opportunities, and 3) strategic thoughts on Essential's water/gas business mix. We remain Neutral-rated WTRG, although we turn incrementally more positive given recent share underperformance versus water utilities and broader regulated utility peers.

Below are our key takeaways from the virtual NDRS:

- **WTRG continues to see COVID-19 impact as manageable,** with increased demand from its predominantly residential customer base (at both water/gas) offsetting the negative impact from lower commercial/industrial load, along with positive weather benefit in 3Q also supporting demand for the year. Regarding bad debt, deferral treatment authorized in Pennsylvania, its largest jurisdiction, should allow WTRG to execute within its guidance range for the year even when accounting for some cash drag. They look for lifting of shutoff moratoriums in the near-term, especially in PA, given the upcoming winter heating season for the gas segment.
- **Despite some opposition, WTRG expects to complete its proposed acquisition of the PA-based municipal wastewater system DELCORA.** Management noted that the dispute with the Delaware County Council stems from plans to utilize a portion of the proceeds to help manage customer bill increases through a trust. Regardless of the outcome on this matter, the company's commitment remains unchanged regarding the proposed acquisition. They now expect a final approval from the Pennsylvania commission by 1Q2021, a moderate delay from the original YE2020 forecast given an extension to the PA regulatory docket. However, given the capital spend for this business isn't slated to begin until beyond 2021, management sees the delay as immaterial to the 2021 earnings potential.
- **The company noted a rapid increase in municipal acquisition interest and activity since the start of COVID-19,** which management partly attributes to the economic pressures facing many municipalities in the current environment.

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WTRG remains active in the various bidding processes, both within its largest territory in PA but also its other jurisdictions, all which allow Fair Market Value treatment - the ability for the private utility to rate base the acquired system at FMV. However, in the next 12-18 months, **they do not anticipate a need to issue common equity** given the relative smaller size of each opportunity relative to the pending DELCORA proposal, and also given the company accounted for certain future transactions in the recent $311mn equity issuance.

- **Water quality remains a key focus, with potential investment opportunities ahead.** The company's water quality standard - 13 parts per trillion (ppt) - remains well below the EPA's 70 ppt advisory level and the CDC's 35 ppt guidance, and management sees increased federal/state focus on this issue creating potential to increase certainty on cost recovery as well capital for rate base, although not a significant portion of the overall planned investments.
- **WTRG looks to assess clean options for gas business,** although they admitted it's still very early in the process given the recent completion of the Peoples Gas system. Management believes there is a long-term need for gas, whether natural gas or other cleaner forms, while seeing old pipe replacement as a more immediate need at its newly acquired Peoples Gas to both improve reliability and reduce methane emissions.
- **WTRG plans to remain predominantly a water utility,** with organic/inorganic growth that could increase its current 70% exposure from its water segment. Management does not have any intention of expanding its gas utility footprint through other acquisitions.

We increase our 2021-2022 EPS estimates to $1.65/$1.80 from $1.63/$1.78 prior with our 2020 EPS of $1.55 unchanged, primarily to reflect 1) 2Q20 actuals and 10-Q update, 2) $311m equity issuance in 3Q20 (moderately higher than our estimate), 3) reduction in debt issuances in 2021, and 3) moderately higher earned ROE expectations at Peoples Gas to account for incremental tax repairs benefit. Our estimates reflect a 6.9% EPS CAGR from 2019-2022E, at the upper end of management's 5-7% forecast.

Our $45 (unchanged), 12-month price target is based on an SOTP approach, with 30x/22x P/E applied to the our 2021 water/gas utility EPS estimate. Upside risks to our call include: 1) Peoples Gas acquisition synergies exceed our expectations, elevating EPS growth profile, 2) tax repairs election for the PA gas utility elevates earned ROEs even above our estimate, and 3) WTRG continues to benefit from ESG fund flows, despite its water/gas utility mix profile on a pro-forma basis. Downside risks to our call include: 1) PA regulation turns less constructive, 2) the proposed DELCORA acquisition fails to receive necessary approvals, and 3) additional longer-term concerns about the gas segment further compresses multiples.

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WTRG	12m Price Target: **$45.00**	Price: **$39.60**	Upside: **13.6%**

Neutral

Market cap: $8.5bn
Enterprise value: $14.1bn
3m ADTV: $50.1mn
United States
Americas Utilities
M&A Rank: 3

GS Forecast

	12/19	12/20E	12/21E	12/22E
Revenue ($ mn) New	**889.7**	**1,571.7**	**2,032.7**	**2,165.6**
Revenue ($ mn) Old	889.7	1,593.3	2,062.8	2,180.9
EBITDA ($ mn)	521.4	784.7	1,083.1	1,179.3
EBIT ($ mn)	360.8	532.5	787.8	858.4
EPS ($) New	**1.47**	**1.55**	**1.65**	**1.80**
EPS ($) Old	1.47	1.55	1.63	1.78
P/E (X)	27.6	25.5	24.0	22.0
Dividend yield (%)	2.2	2.4	2.6	2.8
Net debt/EBITDA (X)	2.3	7.0	5.7	5.7

	6/20	9/20E	12/20E	3/21E
EPS ($)	0.29	0.22	0.43	0.61

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 16 Sep 2020 close.

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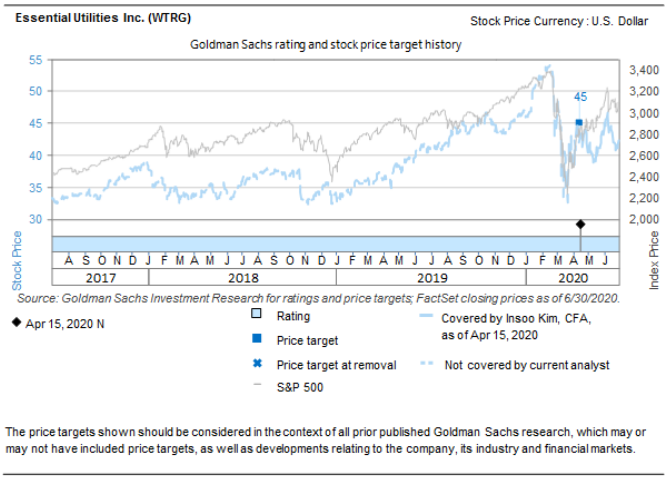

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HSBC Global Research

28 June 2019

Aqua America (WTR US)

Buy: Multi-utility creation – work-in-progress

Equities
Water Utilities

United States

- Peoples acquisition: completion now likely later in 2019 given regulatory progress; financing has been secured
- Texas: fair market value continues to drive water growth
- Maintain Buy rating; TP increased from USD41 to USD45.5

Peoples Natural Gas update (work in progress). On 11 June, 2019, Aqua America (Aqua), participated in a hearing of the Pennsylvania Public Utility Commission and filed a settlement agreement for the acquisition of Peoples Gas. Two of the parties (intervenors) to the case opposed the settlement because of a disagreement on the treatment of a small gas system. This means the acquisition is now anticipated to occur in the fall of 2019, later than Q2 as originally anticipated by Aqua. Aqua has already started to raise the cUSD2.5bn of equity to buy Peoples. It wants a sufficient equity cushion to maintain a 12-13% FFO/adjusted net debt ratio. Merger approval has already been received in W Virginia and Kentucky.

Texas adopts Fair Market Value legislation

On 12 June Aqua management commented that Texas had become the seventh state to adopt Fair Market Value legislation. This continues to be a key driver for the sales of regulated water systems (at an 'appraised value' at a premium to book value). In 2017 the American Society of Civil Engineers gave Texas a D+ rating for water and D rating for waste water. We think the combination of underinvested public health infrastructure with a mechanism for small cities to sell their systems at a premium to dedicated water companies underpins the strong attraction of US water stocks.

Maintain Buy rating with increased target price of USD45.5 from USD41: We value Aqua America via three methodologies: DCF, dividend yield and the average of a PE multiples and a SOP (rate-based) valuation. Taking the average of the three approaches gives us our target price of USD45.5 (previously USD41). In our DCF valuation, we have updated our assumption of beta from 0.60 to 0.58 which is in line with its market peers. In our multiples-based valuation, we have updated the multiples in line with the market peers. This results in an increase in PE multiple from 26.1x to 27.8x. Finally, in yield valuation, we reduce our yield from 2.25% to 2% which is in line with its peers. Overall, these changes lead to an increased TP of USD45.5 from USD41. Our TP implies 12.5% upside; we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

MAINTAIN BUY

TARGET PRICE (USD)	PREVIOUS TARGET (USD)
45.50	**41.00**
SHARE PRICE (USD)	UPSIDE/DOWNSIDE
40.45	**+12.5%**
(as of 26 Jun 2019)	

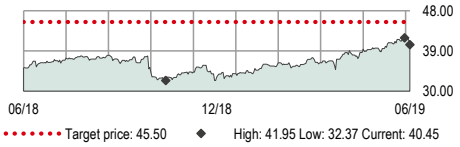
MARKET DATA

Market cap (USDm)	8,727	Free float	100%
Market cap (USDm)	8,727	BBG	WTR US
3m ADTV (USDm)	131	RIC	WTR.N

FINANCIALS AND RATIOS (USD)

Year to	12/2018a	12/2019e	12/2020e	12/2021e
HSBC EPS	1.08	1.50	1.59	1.65
HSBC EPS (prev)	-	-	1.58	1.66
Change (%)	-	-	0.6	-0.6
Consensus EPS	1.41	1.46	1.56	1.66
PE (x)	37.6	27.0	25.4	24.6
Dividend yield (%)	2.1	2.3	2.4	2.6
EV/EBITDA (x)	24.0	22.1	16.8	16.3
ROE (%)	9.7	12.9	11.6	8.5

52-WEEK PRICE (USD)



Source: Refinitiv IBES, HSBC estimates

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Financials & valuation: Aqua America

Buy

Financial statements

Year to	12/2018a	12/2019e	12/2020e	12/2021e
Profit & loss summary (USDm)				
Revenue	838	905	1,906	2,003
EBITDA	470	525	815	864
Depreciation & amortisation	-147	-160	-237	-260
Operating profit/EBIT	323	365	578	604
Net interest	-147	-84	-158	-170
PBT	178	281	420	434
HSBC PBT	176	281	420	434
Taxation	14	-14	-21	-22
Net profit	192	267	399	412
HSBC net profit	192	267	399	412
Cash flow summary (USDm)				
Cash flow from operations	369	340	675	676
Capex	-496	-500	-770	-770
Cash flow from investment	-640	-500	-5,045	-770
Dividends	-151	-162	-247	-267
Change in net debt	439	322	2,118	361
FCF equity	-176	-160	-95	-94
Balance sheet summary (USDm)				
Intangible fixed assets	53	53	928	928
Tangible fixed assets	6,718	7,058	10,991	11,501
Current assets	144	105	191	199
Cash & others	4	4	4	4
Total assets	6,961	7,262	12,156	12,674
Operating liabilities	1,546	1,420	1,545	1,558
Gross debt	2,564	2,886	5,003	5,364
Net debt	2,560	2,882	5,000	5,361
Shareholders' funds	2,009	2,114	4,765	4,910
Invested capital	5,365	5,792	10,561	11,067

Ratio, growth and per share analysis

Year to	12/2018a	12/2019e	12/2020e	12/2021e
Y-o-y % change				
Revenue	3.5	8.0	110.6	5.1
EBITDA	1.0	11.7	55.2	6.0
Operating profit	-1.8	12.9	58.4	4.5
PBT	-30.5	57.5	49.5	3.3
HSBC EPS	-20.0	39.4	6.3	3.3
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	6.8	6.2	6.7	5.3
ROE	9.7	12.9	11.6	8.5
ROA	4.5	5.1	5.8	4.7
EBITDA margin	56.1	58.0	42.8	43.1
Operating profit margin	38.6	40.3	30.3	30.1
EBITDA/net interest (x)	3.2	6.2	5.2	5.1
Net debt/equity	127.4	136.4	104.9	109.2
Net debt/EBITDA (x)	5.4	5.5	6.1	6.2
CF from operations/net debt	14.4	11.8	13.5	12.6
Per share data (USD)				
EPS Rep (diluted)	1.08	1.50	1.59	1.65
HSBC EPS (diluted)	1.08	1.50	1.59	1.65
DPS	0.85	0.91	0.99	1.07
Book value	11.29	11.88	19.04	19.62

Valuation data

Year to	12/2018a	12/2019e	12/2020e	12/2021e
EV/sales	13.5	12.8	7.2	7.0
EV/EBITDA	24.0	22.1	16.8	16.3
EV/IC	2.1	2.0	1.3	1.3
PE*	37.6	27.0	25.4	24.6
PB	3.6	3.4	2.1	2.1
FCF yield (%)	-2.0	-1.8	-1.1	-1.1
Dividend yield (%)	2.1	2.3	2.4	2.6

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2018a
GHG emission intensity*	[n/a]
Energy intensity*	[n/a]
CO_2 reduction policy	Yes
Social Indicators	**12/2018a**
Employee costs as % of revenues	[n/a]
Employee turnover (%)	[n/a]
Diversity policy	Yes

Governance Indicators	12/2018a
No. of board members	9
Average board tenure (years)	8.2
Female board members (%)	33.3
Board members independence (%)	88.9

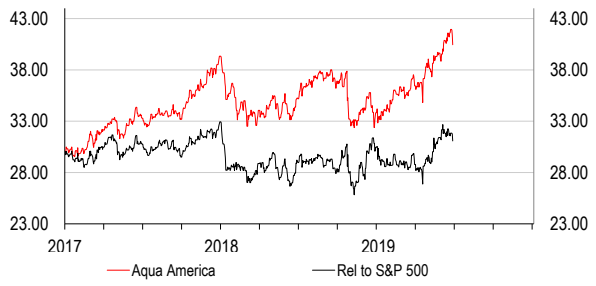
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	40.45	Free float	100%
Target price (USD)	45.50	Sector	Water Utilities
RIC (Equity)	WTR.N	Country	United States
Bloomberg (Equity)	WTR US	Analyst	Verity Mitchell
Market cap (USDm)	8,727	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 26 Jun 2019

Multi-utility creation: work-in-progress

- Peoples Natural Gas acquisition: completion now likely later in 2019 given regulatory progress; financing has been secured
- Fair market value continues to drive water growth: Texas now added to the states adopting the legislation
- Maintain Buy rating; TP increased from USD41 to USD45.5

Investment summary

Aqua America (Aqua) targets regulated asset growth of c7% through to 2021 in its water and wastewater business, supplemented by a strong pipeline of acquisitions of municipal water and wastewater systems. The majority of the states in which Aqua operates are either moving or have already moved to Fair Market Value (FMV), which allows municipalities to sell assets at an appraised value which is generally higher than book value. This 'fair' valuation offers attractive proceeds to a municipality and the ability for Aqua to earn returns on a fairly revalued rate base.

Other regulatory mechanisms, such as infrastructure surcharges allowing annual increases in rates for pipe replacement and the use of future test years in rate cases, are positive steps in removing the regulatory lag and smoothing out the time between rate cases. These changes are helping Aqua to improve the stability of revenues and allow it to accelerate investment.

The recent acquisition of Peoples Natural Gas Company, which is intended to diversify earnings into faster growing gas distribution, has increased the certainty of short-term growth. The high rate base growth (8-10%), once fully integrated, should drive short-term growth.

From a larger base and with organic growth planned in gas, accelerating water acquisitions of a larger size should maintain the 70:30 water to gas mix, which investors believe is an attractive balance of businesses.

Because of these factors we maintain our Buy rating on the stock with a target price of USD45.5.

Latest regulatory developments

On 11 June, 2019, Aqua participated in a hearing of the Pennsylvania Public Utility Commission and filed a settlement agreement for the acquisition of Peoples Gas. Two of the parties (intervenors) to the case opposed the settlement because of a disagreement on the treatment of a small gas system. This means the acquisition is now anticipated to occur in the fall of 2019, later than Q2 as originally anticipated by Aqua. Aqua has already started to raise the cUSD2.5bn of equity to buy Peoples. It wants a sufficient equity cushion to maintain a 12-13% FFO/adjusted net debt ratio. Merger approval has already been received in W Virginia and Kentucky.

PA rate case updates: Aqua's water and gas businesses have both filed for rate increases in their 'home' state of Pennsylvania (PA). It is the first time the company is using the fully projected future test year ending October 2020 for these. New rates are expected to go into effect in the fall 2019. Fair Market Value legislation continues to be a driver for the sales of regulated water systems (at an 'appraised value' at a premium to book value).

Texas adopts Fair Market Value legislation

On 12 June Aqua management commented that Texas had become the seventh state to adopt Fair Market Value legislation. This continues to be a key driver for the sales of regulated water systems (at an 'appraised value' at a premium to book value). In 2017 the American Society of Civil Engineers gave Texas a D+ rating for water and D rating for waste water. The combination of underinvested public health infrastructure with a mechanism for small cities to sell their systems at a premium to dedicated water companies underpins the strong attraction that US water stocks hold for us.

Growth

The company remains on track to grow customers at between 2% and 3% in 2019. Aqua invested USD133.8m in Q1 2019 to improve its infrastructure systems. To replace and expand its water utility infrastructure, the company expects to invest more than USD550m in 2019 and approximately USD1.4bn through 2021.

To date in 2019, the company's state subsidiaries in Ohio, Illinois and Pennsylvania have received rate awards or infrastructure surcharges totalling an estimated increase in annualized revenues of USD4.9m. Aqua currently has rate or surcharge proceedings pending in New Jersey, North Carolina and Ohio collectively totalling for USD6.3m. The timing and extent to which rate increases may be granted by the regulatory agencies will vary by state.

For Q1 2019 Aqua declared a quarterly cash dividend of USD0.2190 per share of common stock which represented 7% y-o-y growth.

Peoples transaction: break-up of the funds

Aqua has secured funding for the Peoples acquisition. Canada Pension Plan Investment Board (CPPIB) has acquired 21.3m newly issued shares of Aqua's common stock. CPPIB's investment is contingent upon the Peoples acquisition going ahead and getting final approval from the regulators. General corporate purposes include working capital and capital needs or repayment of certain revolving credit facility borrowings. During the Q1 2019 conference call Aqua management said, 'Our permanent financing plan targets a strong balance sheet and strong investment grade credit ratings for a fully regulated company.' We believe that Aqua will be able to maintain its credit ratings. Aqua America is rated Baa2 with stable outlook by Moody's. We set out our credit analysis below.

Sources and uses of funds

Sources of funds	USDm	Uses of funds	USDm
Common stock	1294	Peoples equity purchase price	2905
CPPIB Equity Investment	750	Assumption of Peoples debt	1370
Tangible equity units (mandatory convertible)	690	Private placement note refinancing	314
Debt	900	Transaction costs/ expenses	265
Assumption of Peoples debt	1370	General corporate purposes	150
Total Sources of funds	**5004**	**Total uses of funds**	**5004**

Source: Company presentation

Aqua has issued USD900m of senior notes at a weighted average yield of 3.96% with a weighted average maturity of 21 years. In addition to this, on 24 April, Aqua settled interest rate swaps (concurrent with the pricing of senior notes) that resulted in a payment by Aqua of USD83.5m compared with fair value of USD94.6m. Thus in the second quarter a beneficial charge in fair value of USD11.1m should be recorded.

Peoples transaction timeline visualised

Time line	Status
23-Oct-18	Aqua announced acquisition of peoples
13-Nov-18	Aqua files merger application with PA and WV PUCs
20-Nov-18	Aqua files merger application with KY PSC
28-Jan-19	Peoples filed a rate case for PA
8-Feb-19	Aqua filed a rate case settlement for PA
13-Mar-19	KY PSC approved merger application
27-Mar-19	Proposed merger settlement filed with WV PSC
29-Mar-19	Aqua announced USD750m equity investment from CPPIB
Apr-19	Aqua equity and debt offerings
Apr-19	WV PSC approved merger application
May-19	Aqua PA rate case expected to be in effect
4Q 2019	Targeted final resolution of PA merger proceedings
End 2019	Transaction expected to close

Source: Company presentation

Rate cases and surcharges

We can see from the table below that Aqua completed cUSD5m of rates and surcharges by Q1 2019 and has cUSD78m of rate cases and surcharges pending.

On 12 June 2019, Texas announced the adoption of Fair Market Value legislation for the purchase of the water and wastewater systems. Before these changes system values were determined by their depreciation cost, which generally did not reflect a reasonable market value for those assets and became a barrier to a sale.

Aqua's Chairman and CEO Christopher Franklin has said the new law encourages consolidation in the fragmented water and wastewater industry, enabling resources to be shared among a larger service area, which ultimately benefits customers.

Aqua 2019 rates and surcharges for water (W) and wastewater (WW)

State	Type	Annualised revenue increase (USD000)
Completed as at Q1 2019		
Illinois	Surcharge (W)	1394
Illinois	Surcharge (WW)	268
Ohio	Rate case (W)	974
Ohio	Surcharge (W)	2267
Pennsylvania	Surcharges (W/WW)	2
Total completed at Q1 2019		**4905**
Pending as at Q1 2019		
New Jersey	Rate case (W)	7202
North Carolina	Surcharge (W)	602
North Carolina	Surcharges (W/WW)	62
Ohio	Tax compliance surcharge	-3917
Ohio	Surcharge (W)	2335
Pennsylvania	Rate case (W)	58299
Pennsylvania	Rate case (WW)	13470
Total pending at Q1 2019		**78053**

Source: Company presentation

From the table below we believe that signed municipal contracts will help Aqua to reach its target of 2-3% customer growth for FY2019.

Signed municipal agreements at 1Q2019

Acquisitions	State	Type	Total customers	Rate base
New Garden	PA	WW	2106	29500
Schuykill	PA	WW	600	3600
Grant Park	IL	WW	540	2300
Cheltenham	PA	WW	10450	50250
Skyline	IL	W/WW	752	3550
East Norriton	PA	WW	4952	21000
Total			**19400**	**110200**

Source: Company presentation

2019 outlook

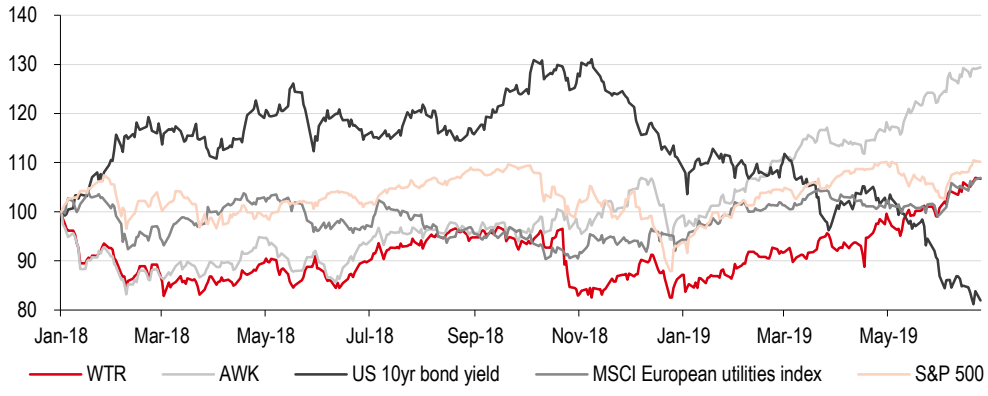
Aqua has guided for adjusted income of USD1.45 to USD1.50 per share (excluding Peoples) for 2019. Infrastructure investments of USD550m in 2019 for communities served by Aqua and investments of USD1.4bn to 2021 were confirmed at the Q1 to rehabilitate and strengthen systems. Aqua is targeting rate base growth of 7% in the water business through to 2021 and 8-10% in the gas business through to 2021. Aqua is targeting total customer growth of between 2-3% for FY2019. It will announce Q2 results on Wednesday, 7 August 2019.

Performance against peers

Aqua's share price has underperformed the S&P 500 by 3% since 1 January 2018, but it has outperformed by c5% YTD and c1.5% over 1 month. It appears that much of the scepticism about creating a multi-utility with the acquisition of Peoples has already been priced in. On our numbers, the deal is accretive in the first full year of the merged group and credit metrics remain on-track, see Credit metrics analysis below. On 2019e PE, it now trades at a discount to its water peer group and is in line with some of the US electricity utilities according to Refinitiv Datastream.

One more point to note is that the US Treasury 10 year yield is falling sharply. Aqua share price, as a defensive utility, is likely to be inversely correlated to bond yields.

Performance of Aqua America vs American Water Works vs UST 10yr vs MSCI European utilities index vs S&P 500 index



Source: Refinitiv DataStream

Change in estimates

We have updated the estimates based on the Q1 2019 results and to take account of the Pennsylvania rate case. This has impacted our estimates slightly. We had already assumed that the Peoples deal would not contribute to earnings until Q1 2020.

Change in estimates (USDm)

	2019e	2020e	2021e
EBIT			
Revised	365	578	604
Previous	365	578	604
Change	*0%*	*0%*	*0%*
Net income			
Revised	267	399	412
Previous	267	392	412
Change	*0%*	*2%*	*0%*
EPS (USD)			
Revised	1.50	1.59	1.65
Previous	1.50	1.58	1.66
Change	*0%*	*1%*	*-1%*
DPS (USD)			
Revised	0.91	0.99	1.07
Previous	0.91	0.99	1.07
Change	*0%*	*0%*	*0%*

Source: HSBC estimates

Credit metrics analysis

Aqua America is rated Baa2 with stable outlook by Moody's. To maintain this rating, Aqua will need to maintain RCF/Net debt in the range of 7-14% and FFO/Net debt in the range of 11-18%. From the calculated estimates below we can see that Aqua should be able to maintain the rating in the short term, but at the lower end of Moody's range of metrics.

Credit metrics analysis

	2019e	2020e	2021e
RCF/ Net debt	9.2%	7.8%	7.6%
FFO/ Net debt	14.8%	12.7%	12.5%

Source: HSBC estimates

Valuation and risks

We value Aqua America via three methodologies: DCF, dividend yield and the average of PE multiples and SOP (rate-based) valuation. Taking the average of the three approaches gives us our target price of USD45.5 (previously USD41).

In our DCF valuation, we have updated our assumption of beta from 0.60 to 0.58 to be in line with its market peers and have incorporated our updated estimates post Q1 2019 results. In our multiples-based valuation, we have updated the multiples in line with the market peers. This results in increase in PE multiple from 26.1x to 27.8x. Finally, in yield valuation, we have reduced our yield from 2.25% to 2% which is in line with its peers. Overall, these changes lead to an increased TP of USD45.5 from USD41. Our TP implies 12.5% upside; we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

Summary of valuation (USD)

Particulars	New	Previous
Current price as on 26-June-19	**40.5**	**NA**
DCF (updated estimates, lower beta)	46.0	39.5
Yield 2% (previously 2.25%)	49.4	43.9
SOP & Peer multiple (updated multiples)	41.0	39.6
Target price (average rounded)	**45.5**	**41.0**
Upside/ downside to target price	12.5%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity Valuation	USDm
Cost of debt		**+ DCF value**	**15,725**
Pre-tax cost of debt	3.9%	+ ST marketable assets	-
Marginal tax rate	11.0%	+ Value of associates	-
Cost of equity		+ Other assets	788
Risk-free rate	3.0%	**EV (asset side)**	**16,513**
Equity risk premium	3.0%	- Net debt (+ if Net cash)	(5,000)
Additional risk		- Quasi debt (pension)	-
Beta (previously 0.60)	**0.58**	- Value of minorities	0
Debt - 34%	3.5%	Total non-equity claims	(5,000)
Equity - 66%	4.7%	**Value of equity**	**11,513**
Cost of capital	**4.3%**	**Value per share (USD)**	**46.0**

Source: HSBC estimates

Sum-of-the-parts (SOP) and Multiples valuation

	2020e Rate base
Regulated water	
Pennsylvania	3,673
Ohio	363
Illinois	366
Texas	269
New Jersey	196
North Carolina	233
Indiana	95
Virginia	86
Regulated gas	2,733
Total	**8,014**
Price to rate base	14,424
Non-regulated 2020 PE multiple	13
Net debt 2020e, pensions & Minority	(5,000)
Estimated equity value	**9,437**
Estimated equity value per share (USD)	**37.7**
PE Multiple valuation	
2020 earnings	1.59
2020 PE sector average	27.8
Value per share	**44.3**
Average of rate base valuation and PE multiple valuation	**41.0**

Source: HSBC estimates

Downside risks

Aqua America fails to achieve the desired rate case revisions and infrastructure surcharges; it lacks organic growth from asset replacement; it cannot take advantage of the FV market legislation opportunity; its dividend grows at a lower rate than we assume.

It is not able to gain the Fair Market Value premium required in the systems it wants to acquire in Pennsylvania. Its current acquisitions of systems – New Garden and Limerick – are facing challenges to the premium proposed by Aqua.

Disclosure appendix

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Upside/Downside is the percentage difference between the target price and the share price.

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For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

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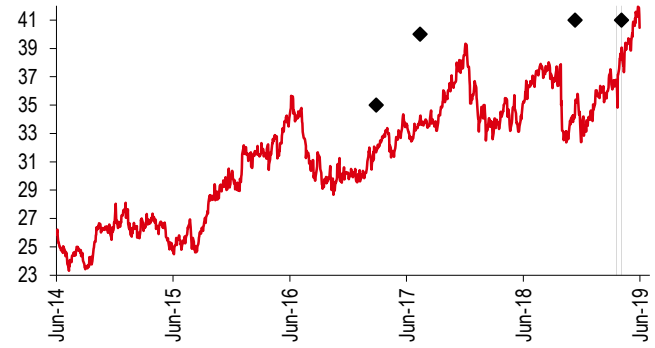
Share price and rating changes for long-term investment opportunities

Aqua America (WTR.N) share price performance USD Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	35.00	24 Mar 2017	Verity Mitchell
Price 2	40.00	08 Aug 2017	Verity Mitchell
Price 3	41.00	06 Dec 2018	Verity Mitchell
Price 4	Restricted	15 Apr 2019	
Price 5	41.00	30 Apr 2019	Verity Mitchell

Source: HSBC

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Company	Ticker	Recent price	Price date	Disclosure
AQUA AMERICA	WTR.N	40.45	26 Jun 2019	1, 2, 5, 6

Source: HSBC

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[1123548]

HSBC Global Research

27 August 2020

Essential Utilities (WTRG US)

Buy: Capital raise to underpin growth

Equities
Water Utilities

United States

- H1 results and 3% (USD311m) capital increase should underpin growth
- Fair Value legislation and infrastructure rehabilitation key drivers for growth
- Maintain Buy rating and target price of USD50

H1 2020 results and 3% capital raise: On 5 August 2020, Essential reported its H1 results. EPS was USD0.5, up 28%, and affirmed its full-year guidance of USD1.53-USD1.58. On 10 August 2020, it successfully raised an additional USD311m through issuing 6.7m new shares (c3%) of equity. The need for this to fund regulated growth was previously flagged.

Growth: Essential's equity raise will be used to underpin a stable capital structure in its growing regulated water and gas businesses. US regulators generally assume a capital structure of 50:50 debt and equity so the equilibrium on a growing rate base needs to be maintained. In addition, Essential sees opportunities for further acquisitions using the Fair Value principles. Acquisitions are mostly going to be focused on water rather than gas. Its gas expansion is at present focused on mains replacement at Peoples Gas. Essential is focusing on repair tax principles here, which it has utilised in water in Pennsylvania. The use of capital allowances to reduce taxes delays the need to file for rate cases, smoothing customer rates in times of accelerated investment.

Maintain Buy and target price of USD50: We value Essential Utilities via three methodologies: DCF, dividend yield and the average of our PE multiple and rate-based valuations. Taking the average of the three approaches gives us our target price of USD50.00 (unchanged). In our DCF, we maintain our beta at 0.6, in line with its peers. We update our estimates as explained above, which decreases our DCF valuation to USD48.1 from USD50.0. For our PE-multiple-based valuation, we update our target multiple to 31.0x from 30.0x to keep it in line with peers. We use a water peer group P/B of 2.4x (unchanged) as a proxy for a rate-based valuation, which is consistent with all US utilities under our coverage and is a proxy for EV. The average of the two increases to USD52.1 from USD51.6, reflecting our updated estimates. For our yield-based valuation, we reduce our target yield to 2.0% from 2.13%, in line with its Water and Related Utilities peers. This results in an increase in our yield valuation to USD50.1 from USD47.5. Overall, these changes lead to an unchanged target price of USD50.00, which implies 15.5% upside. We reiterate our Buy rating as we believe the combination of regulated investment growth and earnings growth is attractive.

MAINTAIN BUY

TARGET PRICE (USD)	PREVIOUS TARGET (USD)
50.00	**50.00**
SHARE PRICE (USD)	UPSIDE/DOWNSIDE
43.28	**+15.5%**
(as of 25 Aug 2020)	

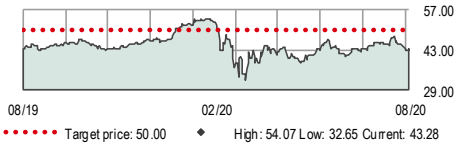
MARKET DATA

Market cap (USDm)	10,610	Free float	100%
Market cap (USDm)	10,610	BBG	WTRG US
3m ADTV (USDm)	52	RIC	WTRG.N

FINANCIALS AND RATIOS (USD)

Year to	12/2019a	12/2020e	12/2021e	12/2022e
HSBC EPS	1.04	1.53	1.66	1.79
HSBC EPS (prev)	1.04	1.55	1.67	1.79
Change (%)	0.0	-1.0	-0.8	0.0
Consensus EPS	1.48	1.48	1.66	1.80
PE (x)	41.6	28.2	26.1	24.2
Dividend yield (%)	2.2	2.3	2.5	2.7
EV/EBITDA (x)	23.8	17.5	16.7	15.9
ROE (%)	7.6	8.1	7.2	7.3

52-WEEK PRICE (USD)



Source: Refinitiv IBES, HSBC estimates

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Disclosures & Disclaimer
This report must be read with the disclosures and the analyst certifications in the Disclosure appendix, and with the Disclaimer, which forms part of it.

Issuer of report: HSBC Bank plc

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https://www.research.hsbc.com

Financials & valuation: Essential Utilities

Buy

Financial statements

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Profit & loss summary (USDm)				
Revenue	890	1,882	2,141	2,276
EBITDA	497	834	906	989
Depreciation & amortisation	-157	-249	-266	-292
Operating profit/EBIT	340	585	639	697
Net interest	-131	-150	-156	-177
PBT	212	435	484	520
HSBC PBT	209	435	484	520
Taxation	13	-35	-39	-42
Net profit	225	400	445	479
HSBC net profit	225	400	445	479
Cash flow summary (USDm)				
Cash flow from operations	339	718	729	780
Capex	-550	-950	-1,000	-1,000
Cash flow from investment	-605	-5,225	-1,277	-1,000
Dividends	-189	-262	-288	-308
Change in net debt	-1,352	2,814	535	528
FCF equity	-212	-232	-271	-220
Balance sheet summary (USDm)				
Intangible fixed assets	64	939	939	939
Tangible fixed assets	7,224	11,325	12,335	13,043
Current assets	2,011	2,152	2,188	2,207
Cash & others	1,869	1,869	1,869	1,869
Total assets	9,360	14,477	15,524	16,251
Operating liabilities	1,468	1,677	1,732	1,761
Gross debt	3,077	5,891	6,426	6,954
Net debt	1,208	4,022	4,557	5,085
Shareholders' funds	3,881	5,974	6,432	6,602
Invested capital	5,962	10,870	11,862	12,560

Ratio, growth and per share analysis

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Y-o-y % change				
Revenue	6.2	111.6	13.8	6.3
EBITDA	5.7	67.7	8.7	9.2
Operating profit	5.3	72.0	9.3	9.0
PBT	18.6	105.7	11.2	7.6
HSBC EPS	-3.4	47.4	8.3	7.6
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	6.4	6.4	5.2	5.2
ROE	7.6	8.1	7.2	7.3
ROA	4.1	4.5	3.9	4.0
EBITDA margin	55.9	44.3	42.3	43.5
Operating profit margin	38.2	31.1	29.9	30.6
EBITDA/net interest (x)	3.8	5.6	5.8	5.6
Net debt/equity	31.1	67.3	70.9	77.0
Net debt/EBITDA (x)	2.4	4.8	5.0	5.1
CF from operations/net debt	28.0	17.8	16.0	15.3
Per share data (USD)				
EPS Rep (diluted)	1.04	1.53	1.66	1.79
HSBC EPS (diluted)	1.04	1.53	1.66	1.79
DPS	0.94	1.00	1.07	1.15
Book value	17.97	22.88	24.00	24.63

Valuation data

Year to	12/2019a	12/2020e	12/2021e	12/2022e
EV/sales	13.3	7.8	7.1	6.9
EV/EBITDA	23.8	17.5	16.7	15.9
EV/IC	2.0	1.3	1.3	1.2
PE*	41.6	28.2	26.1	24.2
PB	2.4	1.9	1.8	1.8
FCF yield (%)	-2.0	-2.2	-2.5	-2.1
Dividend yield (%)	2.2	2.3	2.5	2.7

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2019a
GHG emission intensity*	n/a
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social Indicators	**12/2019a**
Employee costs as % of revenues	n/a
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	12/2019a
No. of board members	8
Average board tenure (years)	7.0
Female board members (%)	25
Board members independence (%)	87.5

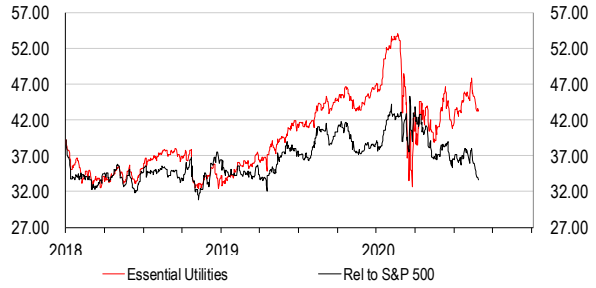
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	43.28	Free float	100%
Target price (USD)	50.00	Sector	Water Utilities
RIC (Equity)	WTRG.N	Country/Region	United States
Bloomberg (Equity)	WTRG US	Analyst	Verity Mitchell
Market cap (USDm)	10,610	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 25 Aug 2020

Capital raise underpins growth

- H1 results and USD311m (3%) capital increase to underpin growth
- Fair Value legislation and infrastructure rehabilitation key drivers for growth
- Maintain Buy rating and target price of USD50

H1 results and funding for growth

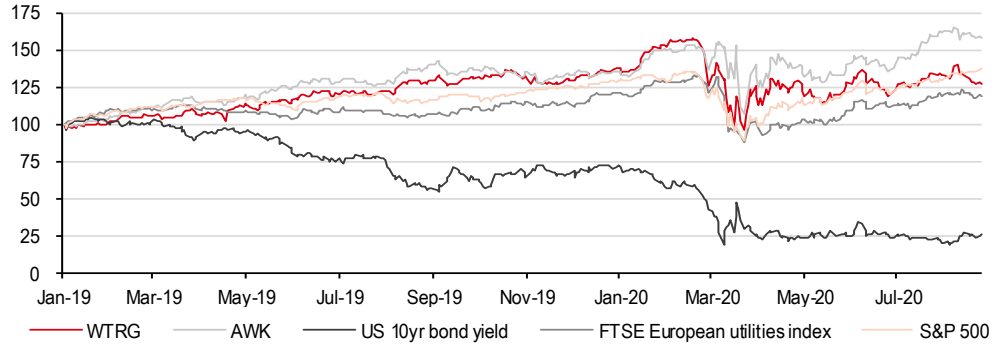
H1 results and 3%capital raise: Essential reported H1 results EPS of USD0.5 +28%. The company affirmed FY guidance of USD1.53 – USD1.58. On 10 August 2020 it successfully raised an additional USD311m 6.7m new shares (c3%) of equity (c3%) of equity. The need for this to fund regulated growth had been previously flagged.

Growth: Essential's equity raise will underpin a stable capital structure in its growing regulated water and gas businesses. US regulated assets assume a capital structure of 50:50 debt and equity so the equilibrium on a growing rate base needs to be maintained. In addition, it sees opportunities for further acquisitions using the Fair Value principles (FV). Acquisitions are mostly going to be focused on water rather than gas. Its gas expansion is at present focused on mains replacement at Peoples Gas. Essential is focusing on repair tax principles here which it has utilised in water in Pennsylvania. Use of capital allowances to reduce tax delays the need to file for rate cases smoothing customer rates in times of accelerated investment.

Performance against peers

Essential's share price has underperformed the S&P 500 by 10% since 1 January 2019. It is trading at a discount to its water peer group's 2020e PE, but in line with some of the US electricity utilities according to Refinitiv Datastream. This reflects, in our view, its multi-utility status. The US Treasury 10-year yield has fallen sharply. WTRG, as a defensive utility, should be inversely correlated to bond yields.

WTRG vs AWK vs UST 10yr vs FTSE European utilities index vs S&P500



Source: Refinitiv DataStream

Credit metrics analysis

Moody's requires RCF/net debt in the range of 7-14% and FFO/net debt in the range of 11-18% to maintain a Baa credit rating. Essential's credit metrics for 2020, shown below, meet the requirements – it currently has a Baa2 credit rating from Moody's with stable outlook. This is mainly due to the liquidity created by the company by issuing equity as mentioned above.

Credit metrics analysis

	2020e	2021e	2022e
RCF/Net Debt	9.7%	9.4%	9.2%
FFO/Net Debt	16.2%	15.7%	15.2%

Source: HSBC estimates

Estimate changes

We update our model post the H1 2020 results, which included updated guidance due to the COVID-19 pandemic and post the issuance of equity. Essential mentioned at its H1 results that growth for its municipal water segment has been more than offset by the reduction in its industrial and commercial water segments, which reflects the resilience of the municipal segment. Given that we expect increased commercial activities in H2, we increase our estimates for 2020e only slightly as shown in the table below (However, 2020e EPS is lower down due to the slight dilution from equity issuance). For 2021, we assume that Essential begins to utilise the repair tax, which lowers current taxes so increases net income, but the equity issuance dilutes EPS and DPS).

Estimate changes

	2020e	2021e	2022e
EBIT (USDm)			
Revised	585	639	697
Previous	578	646	701
Change	*1%*	*-1%*	*-1%*
Net income (USDm)			
Revised	400	445	479
Previous	394	438	469
Change	*2%*	*2%*	*2%*
EPS (USD)			
Revised	1.53	1.66	1.79
Previous	1.55	1.67	1.79
Change	*-1%*	*-1%*	*0%*
DPS (USD)			
Revised	1.00	1.07	1.15
Previous	1.01	1.09	1.18
Change	*-1%*	*-2%*	*-3%*

Source: HSBC estimates

Valuation and risks

We value Essential Utilities using the average of three approaches: 1) DCF; 2) dividend yield; and 3) the average of our PE multiple and rate-based valuations, which renders our unchanged target price of USD50.

- In our DCF, we maintain our beta at 0.6 in line with its peers. We slightly increase our estimates for 2020 but the dilution from the capital increase decreases our DCF valuation marginally from USD50.0 to USD48.1.
- For our yield-based valuation, we reduce our target yield to 2.0% from 2.13% to keep it in line with the water and related utilities peers. This increases our yield valuation to USD50.1 from USD47.5.

- For our PE multiple-based valuation in the average of a PE multiple and rate-based valuation approach, we update our target multiple to 31.0x from 30.0x to keep it in line with that of peers. We continue to use a water peer group P/B of 2.4x as a proxy for a rates-based valuation. This is consistent with all US utilities under our coverage and is a proxy for EV. The average of the two increases to USD52.1 from USD51.6, reflecting our updated estimates. We continue to use regulated water peers not gas utility peers because water utilities have higher implicit growth. Peoples was acquired because it too has an accelerated mains replacement cycle.

Overall, these changes lead to no unchanged in our target price of USD50, which implies 15.5% upside. We reiterate our Buy rating as we believe the combination of regulated investment growth and earnings growth is attractive.

Valuation summary (USD)

Particulars	New	Previous
Current price as on 25-Aug-20	**43.3**	**NA**
DCF (updated estimates)	48.1	50.0
Yield 2% (previously 2.13%)	50.1	47.5
SOTP and peer multiple (updated multiples)	52.1	51.6
Target price (average rounded)	**50.0**	**50.0**
Implied upside/downside to target price	15.5%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity Valuation	USDm
Cost of debt		**+ DCF value**	**15,681**
Pre-tax cost of debt	3.9%	+ ST marketable assets	0
Marginal tax rate	8.0%	+ Value of associates	0
Cost of equity		+ Other assets	878
Risk-free rate	2.5%	**EV (asset side)**	**16,560**
Equity risk premium	3.0%	- Net debt (+ if Net cash)	(3,993)
Additional risk		- Quasi debt (pension)	0
Beta	**0.60**	- Value of minorities	0
Debt - 34%	3.6%	Total non-equity claims	(3,993)
Equity - 66%	4.3%	Value of equity	12,566
Cost of capital	**4.1%**	**Value per share (USD)**	**48.1**

Source: HSBC estimates

Sum-of-the-parts (SOTP) using rate bases and multiple valuation

USDm	2020e Rate Base
Regulated water	
Pennsylvania	3,682
Ohio	368
Illinois	382
Texas	319
New Jersey	214
North Carolina	245
Indiana	90
Virginia	83
Regulated gas	2,451
Total	**7,834**
Price to rate base (USDm)	18,802
Non-regulated 2020 PE multiple (20x)	7
Net debt 2020e, pensions and minorities	(3,993)
Estimated equity value	14,815
Estimated equity value per share (USD)	**56.7**
PE multiple valuation	
2020 earnings per share (USD)	1.53
2020 PE sector average (x)	31.0
Value per share	**47.5**
Average of rate-based valuation and PE multiple valuation	**52.1**

Source: HSBC estimates

Downside risks: Essential Utilities failing to achieve the desired rate case revisions and infrastructure surcharges; lacking organic growth from asset replacement; inability to take advantage of the Fair Market Value legislation opportunity; dividend growth at a lower rate than we assume; inability to gain the Fair Market Value premium required in the systems it wants to acquire in Pennsylvania. Its current acquisitions of systems – New Garden and Limerick – are facing challenges to the premium proposed by Aqua.

Disclosure appendix

Analyst Certification

The following analyst(s), economist(s), or strategist(s) who is(are) primarily responsible for this report, including any analyst(s) whose name(s) appear(s) as author of an individual section or sections of the report and any analyst(s) named as the covering analyst(s) of a subsidiary company in a sum-of-the-parts valuation certifies(y) that the opinion(s) on the subject security(ies) or issuer(s), any views or forecasts expressed in the section(s) of which such individual(s) is(are) named as author(s), and any other views or forecasts expressed herein, including any views expressed on the back page of the research report, accurately reflect their personal view(s) and that no part of their compensation was, is or will be directly or indirectly related to the specific recommendation(s) or views contained in this research report: Verity Mitchell and Adam Dickens

Important disclosures

Equities: Stock ratings and basis for financial analysis

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From 23rd March 2015 HSBC has assigned ratings on the following basis:

The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

Prior to this date, HSBC's rating structure was applied on the following basis:

For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

As of 26 August 2020, the distribution of all independent ratings published by HSBC is as follows:

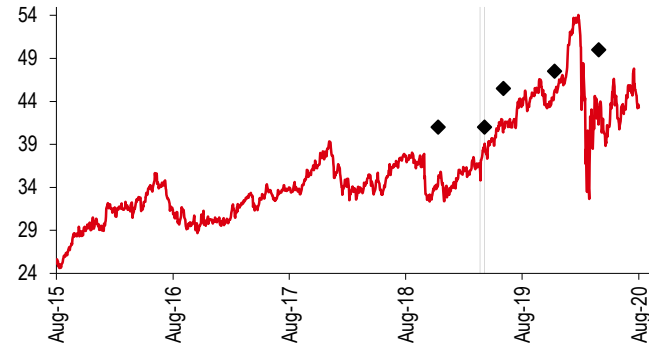
Buy	55%	(31% of these provided with Investment Banking Services)
Hold	36%	(33% of these provided with Investment Banking Services)
Sell	9%	(25% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

For the distribution of non-independent ratings published by HSBC, please see the disclosure page available at http://www.hsbcnet.com/gbm/financial-regulation/investment-recommendations-disclosures.

Share price and rating changes for long-term investment opportunities

Essential Utilities (WTRG.N) share price performance USD Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	41.00	06 Dec 2018	Verity Mitchell
Price 2	Restricted	15 Apr 2019	
Price 3	41.00	30 Apr 2019	Verity Mitchell
Price 4	45.50	28 Jun 2019	Verity Mitchell
Price 5	47.50	06 Dec 2019	Verity Mitchell
Price 6	50.00	22 Apr 2020	Verity Mitchell

Source: HSBC

To view a list of all the independent fundamental ratings disseminated by HSBC during the preceding 12-month period, please use the following links to access the disclosure page:

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HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price date	Disclosure
ESSENTIAL UTILITIES	WTRG.N	43.28	25 Aug 2020	1, 5, 6

Source: HSBC

1 HSBC has managed or co-managed a public offering of securities for this company within the past 12 months.

2 HSBC expects to receive or intends to seek compensation for investment banking services from this company in the next 3 months.

3 At the time of publication of this report, HSBC Securities (USA) Inc. is a Market Maker in securities issued by this company.

4 As of 31 July 2020, HSBC beneficially owned 1% or more of a class of common equity securities of this company.

5 As of 30 June 2020, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of investment banking services.

6 As of 30 June 2020, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of non-investment banking securities-related services.

7 As of 30 June 2020, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of non-securities services.

8 A covering analyst/s has received compensation from this company in the past 12 months.

9 A covering analyst/s or a member of his/her household has a financial interest in the securities of this company, as detailed below.

10 A covering analyst/s or a member of his/her household is an officer, director or supervisory board member of this company, as detailed below.

11 At the time of publication of this report, HSBC is a non-US Market Maker in securities issued by this company and/or in securities in respect of this company

12 As of 21 Aug 2020, HSBC beneficially held a net long position of more than 0.5% of this company's total issued share capital, calculated according to the SSR methodology1

13 As of 21 Aug 2020, HSBC beneficially held a net short position of more than 0.5% of this company's total issued share capital, calculated according to the SSR methodology.

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Additional disclosures

1 This report is dated as at 27 August 2020.

2 All market data included in this report are dated as at close 25 August 2020, unless a different date and/or a specific time of day is indicated in the report.

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Production & distribution disclosures

1. This report was produced and signed off by the author on 26 Aug 2020 17:02 GMT.

2. In order to see when this report was first disseminated please see the disclosure page available at https://www.research.hsbc.com/R/34/7TBb6VF

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[1154243]

HSBC Global Research

16 November 2020

Essential Utilities (WTRG US)

Buy: Q3 progress through regulatory complexity

Equities
Water Utilities

United States

- Q3 results – top end of annual EPS targets
- Strong acquisitions pipeline – Delcora complexity the exception to the rule; regulatory settlements for infrastructure continuing
- Maintain Buy rating, increase TP to USD55 (from USD50)

Q3 results summary. For the first nine months of 2020, customer growth for the company's water utilities totalled 1.5%. Essential invested USD554.1m in the first nine months of the year to improve its regulated water and natural gas infrastructure systems. Management expects adjusted EPS at the top end of the USD1.53-1.58 range for 2020e, with an earnings CAGR target of 5-7% for 2019 through to 2022e.

Strong pipeline of acquisitions, regulatory settlements continuing. The company has signed purchase agreements for municipal water and wastewater acquisitions that are expected to add the equivalent of more than 212,000 water and wastewater retail customers and approximately USD363m in expected rate base. Its most significant acquisition, Delcora, is mired in regulatory and legal complexity. Essential hopes that all issues will be resolved by March-April 2021. This complexity, in our view, should be regarded as the exception to what is normally a smooth process. To date in 2020, the regulated water segment has received rate awards or infrastructure surcharges in Illinois, Indiana, North Carolina, Ohio, Virginia and Pennsylvania totalling an estimated annualised revenue increase of USD21.0m.

Maintain Buy rating; increase target price from USD50 to USD55. We value Essential Utilities using the average of three approaches: (1) DCF, (2) dividend yield, and (3) the average of our PE multiple and rate-based valuations, which renders our increased target price of USD55 (previously USD50). In our DCF, we increase our estimates for 2020e slightly and roll forward our base to 2021e, which increases our valuation to USD50.80 (from USD48.10). For our yield-based approach, we maintain our target yield at 2.0%. We have rolled forward the dividend, which increases our yield valuation to USD53.70 from USD50.10. For our approach using the average of PE and rate-based valuations, we update our target multiple to 33.0x from 31.0x. We use a water peer group PB of 2.6x as a proxy for our rate-based valuation. The average of the two increases to USD61.80 (from USD52.10), reflecting our updated estimates. Peoples Natural Gas was acquired because it, too, has an accelerated mains replacement cycle. Overall, these changes lead to an increased target price of USD55 (previously USD50), which implies c23% upside from current levels. We reiterate our Buy rating as we believe the combination of regulated investment growth and earnings growth remains attractive.

MAINTAIN BUY

TARGET PRICE (USD)	PREVIOUS TARGET (USD)
55.00	**50.00**
SHARE PRICE (USD)	UPSIDE/DOWNSIDE
44.80	**+22.8%**
(as of 12 November 2020)	

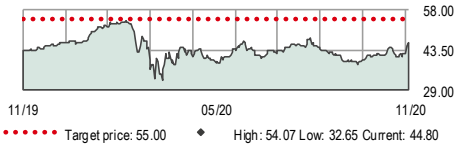
MARKET DATA

Market cap (USDm)	10,983	Free float	100%
Market cap (USDm)	10,983	BBG	WTRG US
3M ADTV (USDm)	51	RIC	WTRG.N

FINANCIALS AND RATIOS (USD)

Year to	12/2019a	12/2020e	12/2021e	12/2022e
HSBC EPS	1.04	1.61	1.67	1.81
HSBC EPS (prev)	1.04	1.53	1.66	1.79
Change (%)	0.0	5.2	0.5	1.3
Consensus EPS	1.48	1.53	1.66	1.79
PE (x)	43.1	27.8	26.9	24.8
Dividend yield (%)	2.1	2.2	2.4	2.6
EV/EBITDA (x)	24.5	18.7	17.7	16.9
ROE (%)	7.6	8.6	7.5	7.8

52-WEEK PRICE (USD)



Source: Refinitiv IBES, HSBC estimates

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Financials & valuation: Essential Utilities

Buy

Financial statements

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Profit & loss summary (USDm)				
Revenue	890	1,882	2,141	2,276
EBITDA	497	834	916	989
Depreciation & amortisation	-157	-249	-266	-292
Operating profit/EBIT	340	585	649	697
Net interest	-131	-155	-192	-201
PBT	212	430	457	495
HSBC PBT	209	430	457	495
Taxation	13	-34	-37	-40
Net profit	225	396	420	456
HSBC net profit	225	396	420	456
Cash flow summary (USDm)				
Cash flow from operations	339	713	705	757
Capex	-550	-950	-1,000	-1,000
Cash flow from investment	-605	-5,225	-1,277	-1,000
Dividends	-189	-246	-270	-289
Change in net debt	-1,352	3,443	542	532
FCF equity	-212	-237	-295	-243
Balance sheet summary (USDm)				
Intangible fixed assets	64	939	939	939
Tangible fixed assets	7,224	11,325	12,335	13,043
Current assets	2,011	2,152	2,188	2,207
Cash & others	1,869	1,869	1,869	1,869
Total assets	9,360	14,477	15,524	16,251
Operating liabilities	1,468	1,677	1,732	1,761
Gross debt	3,077	6,521	7,063	7,595
Net debt	1,208	4,652	5,194	5,726
Shareholders' funds	3,881	5,345	5,795	5,961
Invested capital	5,962	10,870	11,862	12,560

Ratio, growth and per share analysis

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Y-o-y % change				
Revenue	6.2	111.6	13.8	6.3
EBITDA	5.7	67.7	9.8	8.0
Operating profit	5.3	72.0	11.0	7.3
PBT	18.6	103.3	6.3	8.4
HSBC EPS	-3.4	55.1	3.4	8.4
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	6.4	6.4	5.3	5.2
ROE	7.6	8.6	7.5	7.8
ROA	4.1	4.5	4.0	4.0
EBITDA margin	55.9	44.3	42.8	43.5
Operating profit margin	38.2	31.1	30.3	30.6
EBITDA/net interest (x)	3.8	5.4	4.8	4.9
Net debt/equity	31.1	87.0	89.6	96.0
Net debt/EBITDA (x)	2.4	5.6	5.7	5.8
CF from operations/net debt	28.0	15.3	13.6	13.2
Per share data (USD)				
EPS Rep (diluted)	1.04	1.61	1.67	1.81
HSBC EPS (diluted)	1.04	1.61	1.67	1.81
DPS	0.94	1.00	1.07	1.15
Book value	17.97	21.79	23.00	23.66

Source: Company data, HSBC estimates

Valuation data

Year to	12/2019a	12/2020e	12/2021e	12/2022e
EV/sales	13.7	8.3	7.6	7.3
EV/EBITDA	24.5	18.7	17.7	16.9
EV/IC	2.0	1.4	1.4	1.3
PE*	43.1	27.8	26.9	24.8
PB	2.5	2.1	1.9	1.9
FCF yield (%)	-1.9	-2.2	-2.7	-2.2
Dividend yield (%)	2.1	2.2	2.4	2.6

*Based on HSBC EPS (diluted)

Source: Company data, HSBC estimates

ESG metrics

Environmental indicators	12/2019a
GHG emission intensity*	n/a
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social indicators	**12/2019a**
Employee costs as % of revenue	n/a
Employee turnover (%)	n/a
Diversity policy	Yes

Governance indicators	12/2019a
Number of board members	8
Average board tenure (years)	7.0
Female board members (%)	25
Board member independence (%)	87.5

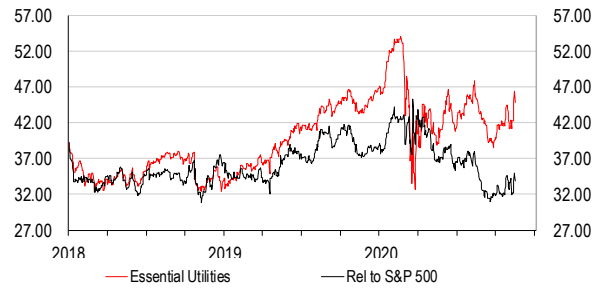
* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Source: Company data, HSBC

Issuer information

Share price (USD)	44.80	Free float	100%
Target price (USD)	55.00	Sector	Water Utilities
RIC (Equity)	WTRG.N	Country/Region	United States
Bloomberg (Equity)	WTRG US	Analyst	Verity Mitchell
Market cap (USDm)	10,983	Contact	+44 20 7991 6840

Price relative



Note: Priced at close of 12 November 2020

Source: HSBC

Q3 Progress, some regulatory complexity remains

- Q3 results – top end annual EPS targets indicated
- Strong pipeline of acquisitions – Delcora complexity the exception to the rule; regulatory settlements for infrastructure continuing
- Maintain Buy rating; increase TP to USD55 (from USD50)

Q3 2020 results summary

Essential Utilities reported Q3 results on 3 November 2020. The regulated water segment reported revenues for the quarter of USD255.7m, an increase of 5.3%. Increased volume and rates and surcharges were the largest contributors to the increase in revenues for the period, in addition to customer growth from both organic growth and acquisitions. Operations and maintenance expenses for the regulated water segment decreased by 2.2% to USD79.3m for the third quarter of 2020. The regulated natural gas segment reported revenues for the third quarter of 2020 of USD88.9m. Operations and maintenance for the same period for the regulated natural gas segment were USD59.6m and purchased gas costs were USD14.8m. The first nine months of 2020, customer growth for the company's water utilities has totalled 1.5%.

The company has signed purchase agreements for other municipal water and wastewater acquisitions that are expected to add the equivalent of over 212,000 water and wastewater retail customers and approximately USD363m in expected rate base.

Essential invested USD554.1m in the first nine months of the year to improve its regulated water and natural gas infrastructure systems and to enhance its customer service across its operations. This does not include an additional USD53.5m that was invested by Peoples, pre-closing, during the period from 1 January to 15 March 2020.

To date in 2020, the regulated water segment has received rate awards or infrastructure surcharges in Illinois, Indiana, North Carolina, Ohio, Virginia and Pennsylvania totalling an estimated increase in annualized revenues of USD21.0m.

Essential declared a quarterly cash dividend of $0.2507 +7%.

The outlook:

- Expects adjusted income per diluted common share (non-GAAP) at the top end of the USD1.53 to USD1.58 range
- Earnings growth CAGR of 5 to 7% for 2019 through to 2022
- Regulated water segment infrastructure investments of approximately USD550m in 2020
- Regulated natural gas segment infrastructure investments of approximately USD400m in 2020 on full-year basis (adjusted to include capital invested in 2020 prior to Essential's ownership)

- Infrastructure investments of approximately USD2.8bn through to 2022 in existing operations to rehabilitate and strengthen water, wastewater, and natural gas systems (including regulated natural gas segment capital invested in 2020 prior to Essential's ownership)
- Regulated water segment rate base compound annual growth rate of 6 to 7% through to 2022
- Regulated natural gas segment rate base compound annual growth rate of 8 to 10% through to 2022
- Total annual regulated water segment customer growth of between 2 and 3% on average depending upon regulatory approval

Delcora the exception that proves the rule on regulatory complexity – expect closure by March-April 2021

Management provided an update to its proposed Delcora acquisition which is currently mired in regulatory and legal complexity. There is an imminent court proceeding to decide whether there is a valid and enforceable contract in place between Essential and Delcora. In addition, there are separate issues about the Delcora trust. In addition to these legal complexities the PUC will then become involved in assessing the acquisition. Essential hopes that all issues – legal and regulatory – will be resolved by March-April 2021. This complexity, in our view, should be regarded as the exception to what is normally a smooth process.

Use of equity raise proceeds

The CEO also mentioned in the earnings call Q&A that the USD300m August equity offering wold be deployed even if there were continuing delays in the Delcora acquisition. Management is seeing a number of medium to large acquisition opportunities. Equity currently deferred would be deployed as and when needed in order to finance these acquisitions.

Acquisitions will remain focused on water and waste water. The Peoples gas rate base growth is targeted to be 8% to 10% annually without acquisitions given the need for pipe replacement.

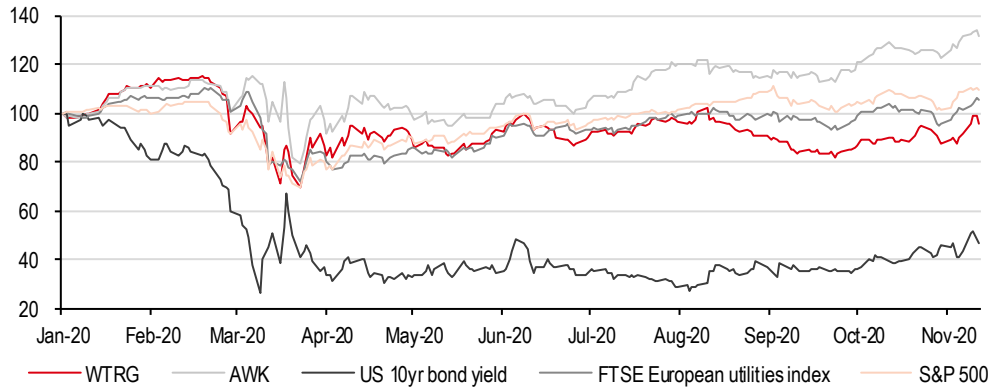
Peoples rate case use tax repair – resolution expected Q2 2021

Essential is focusing on repair tax principles which it has utilised in water in Pennsylvania. It filed a request for USD380 of repair tax in July from the Pennsylvania PUC. This is a catch-up deduction for the tax repair eligible capital invested prior to Essential's ownership of Peoples. Regulatory evidentiary hearings area expected at the end of January. The company expects a final order sometime early in the second quarter of 2021.

Performance against peers

YTD, Essential's share price has underperformed the S&P 500 by 14%. It is trading at a discount to its water peer group's 2020e PE, but in line with some of the US electricity utilities according to Refinitiv Datastream. This reflects, in our view, its multi-utility status. The US Treasury 10-year yield has fallen sharply. WTRG, as a defensive utility, should be inversely correlated to bond yields.

YTD performance of WTRG vs AWK vs UST 10yr vs FTSE European utilities index vs S&P500



Source: Refinitiv Datastream

Credit metrics analysis

Moody's requires RCF/net debt in the range of 7-14% and FFO/net debt in the range of 11-18% to maintain a 'Baa' credit rating. Essential's credit metrics for 2020, shown below, meet the requirements – it currently has a Baa2 credit rating from Moody's with stable outlook.

Credit metrics analysis

	2020e	2021e	2022e	2023e	2024e	2025e
RCF / net debt	8.6%	8.1%	8.1%	8.0%	8.1%	8.3%
FFO / net debt	13.9%	13.3%	13.1%	13.1%	13.4%	13.8%

Source: HSBC estimates

Change in estimates

We have updated our estimates post Q3 2020 results to reflect improved performance at the P&L bottom line. We continue to assume the USD300m of equity issuance, which was done on a forward basis.

Change in estimates (USDm)

	2020e	2021e	2022e
EBIT (USDm)			
Revised	585	649	697
Previous	585	639	697
Change	*0%*	*2%*	*0%*
Net income (USDm)			
Revised	396	420	456
Previous	400	445	479
Change	*-1%*	*-6%*	*-5%*
EPS (USD)			
Revised	1.61	1.67	1.81
Previous	1.53	1.66	1.79
Change	*5%*	*1%*	*1%*
DPS (USD)			
Revised	1.00	1.07	1.15
Previous	1.00	1.07	1.15
Change	*0%*	*0%*	*0%*

Source: HSBC estimates

Valuation and risks

We value Essential Utilities using the average of three approaches: (1) DCF, (2) dividend yield, and (3) the average of our PE multiple and rate-based valuations, which renders our increased target price of USD55 (previously USD50).

- In our DCF, we maintain our beta at 0.6 in line with its peers. We updated our estimates as above, moved equity issuance to for Delcora to 2021 and rolled forward our DCF valuation to 2021e which increases our valuation from USD48.10 to USD50.80.
- For our yield-based valuation, we maintain our target yield at 2.0% to keep it in line with the water and related utilities peers. We have rolled forward the dividend which increases our yield valuation to USD53.70 from USD50.10.
- For our approach using the average of PE multiple and rate-based valuations, we update our target multiple to 33.0x from 31.0x to keep it in line with that of peers. We use a water peer group PB of 2.6x as a proxy for a rate-based valuation. This is consistent with all US utilities under our coverage and is a proxy for EV. The average of the two increases to USD61.80 (from USD52.10), reflecting our updated estimates. We continue to use regulated water peers, not gas utility peers, because water utilities have higher implicit growth. Peoples was acquired because it, too, has an accelerated mains replacement cycle.

Overall, these changes lead to an increased target price of USD55 (previously USD50), which implies c23% upside from current levels. We reiterate our Buy rating as we believe the combination of regulated investment growth and earnings growth remains attractive.

Summary of valuation (USD)

Particulars	New	Previous
Current price at close of 12-Nov-2020	**44.8**	**NA**
DCF (updated estimates, rolled forward valuation)	50.8	48.1
Yield 2% (yield unchanged, dividend rolled forward)	53.7	50.1
SOP & Peer multiple (updated estimates and multiples)	61.8	52.1
Target price (average rounded)	**55.0**	**50.0**
Upside/ downside to target price	22.8%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity valuation	USDm
Cost of debt		**+ DCF value**	**16,555**
Pre-tax cost of debt	3.9%	+ ST marketable assets	0
Marginal tax rate	8.0%	+ Value of associates	0
Cost of equity		+ Other assets	878
Risk-free rate	2.5%	**EV (asset side)**	**17,433**
Equity risk premium	3.0%	- Net debt (+ if Net cash)	(4,623)
Additional risk		- Quasi debt (pension)	0
Beta (unchanged)	**0.60**	- Value of minorities	0
Debt - 32%	3.6%	Total non-equity claims	(4,623)
Equity - 68%	4.3%	Value of equity	12,811
Cost of capital	**4.0%**	**Value per share (USD)**	**50.8**

Source: HSBC estimates

Sum-of-the-parts (SOP) and multiples valuation

	2021e Rate base
Regulated water	
Pennsylvania	3,954
Ohio	393
Illinois	409
Texas	342
New Jersey	229
North Carolina	263
Indiana	96
Virginia	89
Regulated gas	2,634
Total	**8,409**
Price to rate base	21,864
Non-regulated 2020 PE multiple	9
Net debt 2020e, pensions & Minority	(4,623)
Estimated equity value	17,251
Estimated equity value per share (USD)	**68.5**
PE Multiple valuation	
2020 earnings	1.67
2020 PE sector average	33.0
Value per share	**55.1**
Average of rate base valuation and PE multiple valuation	**61.8**

Source: HSBC estimates

Downside risks: Essential Utilities failing to achieve the desired rate case revisions and infrastructure surcharges; lacking organic growth from asset replacement; inability to take advantage of the Fair Market Value legislation opportunity; dividend growth at a lower rate than we assume; inability to gain the Fair Market Value premium required in the systems it wants to acquire in Pennsylvania. Its current acquisitions of systems – New Garden and Limerick – are facing challenges to the premium proposed by Aqua.

Disclosure appendix

Analyst Certification

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The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

Prior to this date, HSBC's rating structure was applied on the following basis:

For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

As of 16 November 2020, the distribution of all independent ratings published by HSBC is as follows:

Buy	57%	(33% of these provided with Investment Banking Services)
Hold	34%	(30% of these provided with Investment Banking Services)
Sell	9%	(27% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

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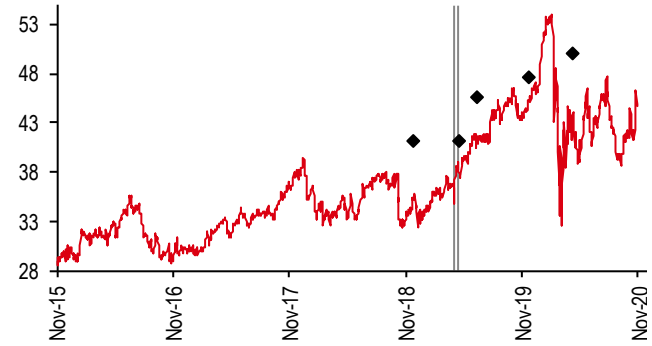
Share price and rating changes for long-term investment opportunities

Essential Utilities (WTRG.N) share price performance
USD Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	41.00	06 Dec 2018	Verity Mitchell
Price 2	Restricted	15 Apr 2019	
Price 3	41.00	30 Apr 2019	Verity Mitchell
Price 4	45.50	28 Jun 2019	Verity Mitchell
Price 5	47.50	06 Dec 2019	Verity Mitchell
Price 6	50.00	22 Apr 2020	Verity Mitchell

Source: HSBC

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HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price date	Disclosure
ESSENTIAL UTILITIES	WTRG.N	44.71	13 Nov 2020	5, 6

Source: HSBC

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10 A covering analyst/s or a member of his/her household is an officer, director or supervisory board member of this company, as detailed below.

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[1159925]

HSBC Global Research

6 December 2019

Aqua America (WTR US)

Buy: Expansion in progress

Equities
Water Utilities

United States

- 9M2019 net income up 13%; Peoples transaction to be completed in early 2020, Delcora next
- Further expansion in PA through acquisition of DELCORA
- Maintain Buy rating; increase TP from USD45.5 to USD47.5

Still growing: Aqua America (WTR) posted growth of 7.7% and 13.1% in revenue and net income respectively at its 9m results on 5 November. To date in 2019, the company's state subsidiaries in Illinois, New Jersey, North Carolina, Ohio, and Pennsylvania have received rate awards or infrastructure surcharges totalling an estimated increase to annualized revenues of USD59.8m. WTR currently has two rate case proceedings pending in Indiana totalling USD63,000. A dividend of USD0.2343 was announced and its 2019 outlook for EPS is reaffirmed of USD1.45-USD1.50.

DELCORA acquisition: a larger, deeper footprint in Pennsylvania: The September agreement with the Delaware County Regional Water Quality Control Authority (DELCORA), to acquire the municipal authority's wastewater assets for cUSD276.5m, will intensify its activities in the state. The transaction is subject to Pennsylvania Public Utility Commission (PUC) approval.

Peoples transaction to be completed in early 2020: All but two of the interveners to the case have entered into or chosen not to oppose the settlement agreement. On October 28 2019, the administrative law judge rendered a recommended decision concluding that Aqua is technically, legally and financially fit to assume control of Peoples; that the acquisition of Peoples will affirmatively promote the service, accommodation, convenience or safety of the public in some substantial way; and recommended that the Pennsylvania Public Utility Commission issue all approvals necessary for Aqua to carry out the acquisition of Peoples.

Maintain Buy rating with increased target price from USD45.5 to USD47.5: We value Aqua America via three methodologies: DCF, dividend yield and the average of PE multiples and SOP (rate-based) valuation. Taking the average of the three approaches gives us our target price of USD47.5 (previously USD45.5). We have rolled forward our estimates in all valuations detailed below. In our DCF valuation, we maintained our assumption of beta at 0.58 to be in line with its market peers and have rolled forward our valuation to FY2020e. In our multiples based valuation, we have updated the multiples in line with the market peers. This results in an increase in PE multiple from 27.8x to 29.8x. Finally, in our yield valuation, we maintain our yield at 2% which is in line with its peers. Overall, these changes lead to an increased TP of USD47.5 from USD45.5. Our TP implies 5.2% upside; we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

MAINTAIN BUY

TARGET PRICE (USD)	PREVIOUS TARGET (USD)
47.50	**45.50**
SHARE PRICE (USD)	UPSIDE/DOWNSIDE
45.14	**+5.2%**
(as of 05 Dec 2019)	

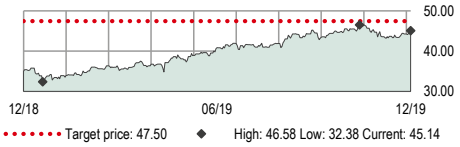
MARKET DATA

Market cap (USDm)	9,743	Free float	100%
Market cap (USDm)	9,743	BBG	WTR US
3m ADTV (USDm)	73	RIC	WTR.N

FINANCIALS AND RATIOS (USD)

Year to	12/2018a	12/2019e	12/2020e	12/2021e
HSBC EPS	1.08	1.50	1.59	1.65
HSBC EPS (prev)	1.08	1.50	1.59	1.65
Change (%)	0.0	0.0	0.0	0.0
Consensus EPS	1.41	1.48	1.58	1.66
PE (x)	41.9	30.1	28.3	27.4
Dividend yield (%)	1.9	2.0	2.2	2.4
EV/EBITDA (x)	26.2	24.0	18.1	17.5
ROE (%)	9.7	12.9	11.6	8.5

52-WEEK PRICE (USD)



Source: Refinitiv IBES, HSBC estimates

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Financials & valuation: Aqua America

Buy

Financial statements

Year to	12/2018a	12/2019e	12/2020e	12/2021e
Profit & loss summary (USDm)				
Revenue	838	905	1,906	2,003
EBITDA	470	525	815	864
Depreciation & amortisation	-147	-160	-237	-260
Operating profit/EBIT	323	365	578	604
Net interest	-147	-84	-158	-170
PBT	178	281	420	434
HSBC PBT	176	281	420	434
Taxation	14	-14	-21	-22
Net profit	192	267	399	412
HSBC net profit	192	267	399	412
Cash flow summary (USDm)				
Cash flow from operations	369	340	675	676
Capex	-496	-500	-770	-770
Cash flow from investment	-640	-500	-5,045	-770
Dividends	-151	-162	-247	-267
Change in net debt	439	322	2,118	361
FCF equity	-127	-160	-95	-94
Balance sheet summary (USDm)				
Intangible fixed assets	53	53	928	928
Tangible fixed assets	6,718	7,058	10,991	11,501
Current assets	144	105	191	199
Cash & others	4	4	4	4
Total assets	6,961	7,262	12,156	12,674
Operating liabilities	1,546	1,420	1,545	1,558
Gross debt	2,564	2,886	5,003	5,364
Net debt	2,560	2,882	5,000	5,361
Shareholders' funds	2,009	2,114	4,765	4,910
Invested capital	5,365	5,792	10,561	11,067

Ratio, growth and per share analysis

Year to	12/2018a	12/2019e	12/2020e	12/2021e
Y-o-y % change				
Revenue	3.5	8.0	110.6	5.1
EBITDA	1.0	11.7	55.2	6.0
Operating profit	-1.8	12.9	58.4	4.5
PBT	-30.5	57.5	49.5	3.3
HSBC EPS	-20.0	39.4	6.3	3.3
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	6.8	6.2	6.7	5.3
ROE	9.7	12.9	11.6	8.5
ROA	4.5	5.1	5.8	4.7
EBITDA margin	56.1	58.0	42.8	43.1
Operating profit margin	38.6	40.3	30.3	30.1
EBITDA/net interest (x)	3.2	6.2	5.2	5.1
Net debt/equity	127.4	136.4	104.9	109.2
Net debt/EBITDA (x)	5.4	5.5	6.1	6.2
CF from operations/net debt	14.4	11.8	13.5	12.6
Per share data (USD)				
EPS Rep (diluted)	1.08	1.50	1.59	1.65
HSBC EPS (diluted)	1.08	1.50	1.59	1.65
DPS	0.85	0.91	0.99	1.07
Book value	11.29	11.88	19.04	19.62

Valuation data

Year to	12/2018a	12/2019e	12/2020e	12/2021e
EV/sales	14.7	13.9	7.7	7.5
EV/EBITDA	26.2	24.0	18.1	17.5
EV/IC	2.3	2.2	1.4	1.4
PE*	41.9	30.1	28.3	27.4
PB	4.0	3.8	2.4	2.3
FCF yield (%)	-1.3	-1.6	-1.0	-1.0
Dividend yield (%)	1.9	2.0	2.2	2.4

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2018a
GHG emission intensity*	n/a
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social Indicators	**12/2018a**
Employee costs as % of revenues	n/a
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	12/2018a
No. of board members	9
Average board tenure (years)	8.2
Female board members (%)	33.3
Board members independence (%)	88.9

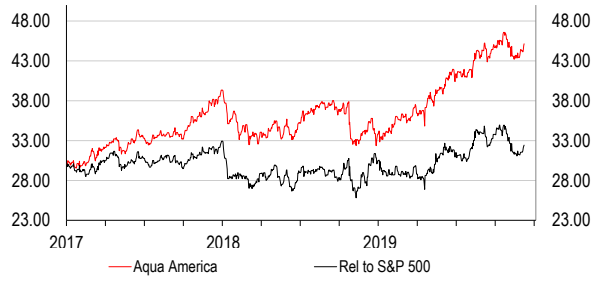
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	45.14	Free float	100%
Target price (USD)	47.50	Sector	Water Utilities
RIC (Equity)	WTR.N	Country/Region	United States
Bloomberg (Equity)	WTR US	Analyst	Verity Mitchell
Market cap (USDm)	9,743	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 05 Dec 2019

Expansion in progress

- Peoples transaction to be completed in early 2020
- Further expansion in PA through acquisition of DELCORA
- Maintain Buy rating; increase TP from USD45.5 to USD47.5

9M 2019 results summary

Aqua America (WTR) posted its 9M 2019 results on 5th November 2019. WTR posted growth of 7.7% and 13.1% in revenue and net income respectively. Employee-related costs, Peoples transaction-related expenses and growth-related costs were the main contributors to the increase in O&M expenses.

Aqua invested USD401.6m in the first nine months of the year to improve its infrastructure systems.

To date in 2019, the company's state subsidiaries in Illinois, New Jersey, North Carolina, Ohio, and Pennsylvania have received rate awards or infrastructure surcharges totalling an estimated increase to annualised revenues of USD59.8m. WTR currently has two rate case proceedings pending in Indiana totalling revenues of USD63,000. A dividend of USD0.2343 announced.

2019 outlook reaffirmed

- Adjusted income per diluted common share (non-GAAP) of USD1.45 to USD1.50
- Infrastructure investments of approximately USD550 million in 2019 for communities served by Aqua
- Infrastructure investments of approximately USD1.4 billion through to 2021 in existing operations to rehabilitate and strengthen systems
- Rate base compound annual growth rate of 7 percent through 2021
- Total customer growth of between 2 and 3 percent
- Closing of Peoples acquisition expected to occur in early 2020

DELCORA acquisition: a larger, deeper footprint in Pennsylvania

Aqua America announced in September that its Pennsylvania subsidiary, Aqua Pennsylvania Wastewater (Aqua), had signed an asset purchase agreement with the Delaware County Regional Water Quality Control Authority (DELCORA) to acquire the municipal authority's wastewater assets for cUSD276.5m. The transaction is subject to Pennsylvania Public Utility Commission (PUC) approval.

DELCORA serves a population of approximately 500,000 people in 42 municipalities in Southeast Pennsylvania. Aqua estimates that this represents the equivalent of 165,000 retail customers. The customer base consists of retail, commercial, and industrial customers and large wholesale agreements with municipal authorities. Its assets include 168 miles of combined and separate sewer mains, 14 miles of large-diameter force mains, and a 50-million gallon-per-

day wastewater treatment plant that serves the western part of its service territory. Wastewater from the eastern service territory (ESA) is treated by Philadelphia Water Department (PWD). This contract expires in 2028.

Under current arrangement with the PWD, Delcora could incur more than USD1.2bn in total costs through 2042, significantly increasing customer rates. Delcora is also building infrastructure necessary to divert ESA wastewater flows in its own plant. The majority of capex will be undertaken from 2026-28. WTR has experience with large/complex projects and already operates in many Delcora communities.

DELCORA is going to use the proceeds from WTR and put those into a trust, which will be used to offset customer rates for as long as possible given the upward pressure on rates from the investment above.

Pennsylvania PUC approval is required to complete this acquisition. Closing is expected to be in late 2020. This acquisition will be the largest municipal transaction for Aqua America and the largest water/wastewater municipal transaction in Pennsylvania's history.

Peoples transaction timeline

In March 2019, Aqua received regulatory approval for the Peoples transaction from the Kentucky Public Service Commission, and in April 2019, the company received approval from the West Virginia Public Service Commission. On June 26, 2019, the company filed a settlement agreement in the matter pending before the Pennsylvania Public Utility Commission.

On October 28, 2019, the administrative law judge rendered a recommended decision concluding that Aqua is technically, legally and financially fit to assume control of Peoples; that the acquisition of Peoples will affirmatively promote the service, accommodation, convenience or safety of the public in some substantial way; and recommended that the Pennsylvania Public Utility Commission issue all approvals necessary for Aqua to carry out the acquisition of Peoples.

The Commission will review the administrative law judge's recommendation and then issue a final order that is subject to appeal if a party so chooses. Aqua now expects the Peoples acquisition to close in early 2020.

Peoples transaction timeline

23-Oct-18	**WTR announces acquisition of Peoples**
13-Nov-18	WTR files merger application with PA and WV PUCs
20-Nov-18	WTR files merger application with KY PSC
28-Jan-19	Peoples filed a rate case for PA
8-Feb-19	WTR filed a rate case for settlement for PA
13-Mar-19	KY PSC approved merger application
27-Mar-19	Proposed merger settlement filed with WV PSC
29-Mar-19	WTR announced USD750m equity investment from CPPIB
Apr-19	WTR equity and debt offerings
Apr-19	WV PSC approved merger application
May-19	WTR PA rate case in effect
Jul-19	Peoples filed a rate case settlement for PA
28-Oct-19	PA ALJs recommended decision received
29-Oct-19	Peoples rate case in effect
Early 2020	Anticipated closing of the Peoples acquisition

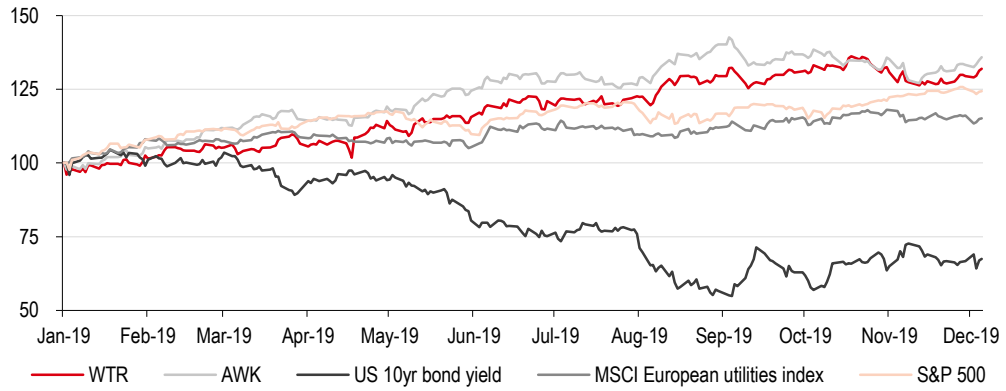
Source: Company presentation

Performance against peers

Aqua's share price has outperformed the S&P 500 by 8% since 1 January 2019. On 2020e PE, it trades at a discount to its water peer group but is in line with some of the US electricity utilities according to Refinitiv Datastream. This reflects, in our view, its future multi-utility status.

One more point to note is that the US Treasury 10-year yield has fallen sharply. WTR, as a defensive utility, should be inversely correlated to bond yields.

YTD performance of WTR vs AWK vs UST 10 yr vs MSCI European utilities index vs S&P 500



Source: Refinitiv Datastream

Valuation and risks

We value Aqua America via three methodologies: DCF, dividend yield and the average of PE multiples and SOP (rate-based) valuation. Taking the average of the three approaches gives us our target price of USD47.5 (previously USD45.5). We have rolled forward our estimates in all valuations detailed below.

In our DCF valuation, we have maintained our assumption of beta at 0.58 to be in line with its market peers and have rolled forward our valuation to FY2020e. In our multiples-based valuation, we have updated the multiples in line with the market peers. This results in an increase in PE multiple from 27.8x to 29.8x. Finally, in our yield valuation, we maintain our yield at 2% which is in line with its peers. Overall, these changes lead to an increased TP of USD47.5 from USD45.5. Our TP implies 5.2% upside; we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

Summary of valuation (USD)

Particulars	New	Previous
Current price as on 5-Dec-19	**45.1**	**NA**
DCF (rolled forward estimates)	47.5	46.0
Yield 2% (unchanged)	49.4	49.4
SOP & Peer multiple (updated peer multiples and rolled forward estimates)	45.8	41.0
Target price (average rounded)	**47.5**	**45.5**
Upside/ downside to target price	5.2%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity Valuation	USDm
Cost of debt		**+ DCF value**	**16,106**
Pre-tax cost of debt	3.9%	+ ST marketable assets	-
Marginal tax rate	11.0%	+ Value of associates	-
Cost of equity		+ Other assets	788
Risk-free rate	3.0%	**EV (asset side)**	**16,894**
Equity risk premium	3.0%	- Net debt (+ if Net cash)	(5,000)
Additional risk		- Quasi debt (pension)	-
Beta (unchanged)	**0.58**	- Value of minorities	0
Debt - 32%	3.5%	Total non-equity claims	(5,000)
Equity - 68%	4.7%	**Value of equity**	**11,894**
Cost of capital	**4.3%**	**Value per share (USD)**	**47.5**

Source: HSBC estimates

Sum-of-the-parts (SOP) and Multiples valuation

	2020e Rate base
Regulated water	
Pennsylvania	3,673
Ohio	363
Illinois	366
Texas	269
New Jersey	196
North Carolina	233
Indiana	95
Virginia	86
Regulated gas	2,733
Total	**8,014**
Price to rate base	16,027
Non-regulated 2020e PE multiple	13
Net debt 2020e, pensions & Minority	(5,000)
Estimated equity value	11,040
Estimated equity value per share (USD)	**44.1**
PE Multiple valuation	
2020e earnings	1.59
2020e PE sector average	29.8
Value per share	**47.5**
Average of rate base valuation and PE multiple valuation	**45.8**

Source: HSBC estimates

Downside risks

Aqua America fails to achieve the desired rate case revisions and infrastructure surcharges; it lacks organic growth from asset replacement; it cannot take advantage of the FV market legislation opportunity; its dividend grows at a lower rate than we assume.

It is not able to gain the Fair Market Value premium required in the systems it wants to acquire in Pennsylvania. Its current acquisitions of systems – New Garden and Limerick – are facing challenges to the premium proposed by Aqua.

Disclosure appendix

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Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

Prior to this date, HSBC's rating structure was applied on the following basis:

For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

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Hold	39%	(33% of these provided with Investment Banking Services)
Sell	9%	(25% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

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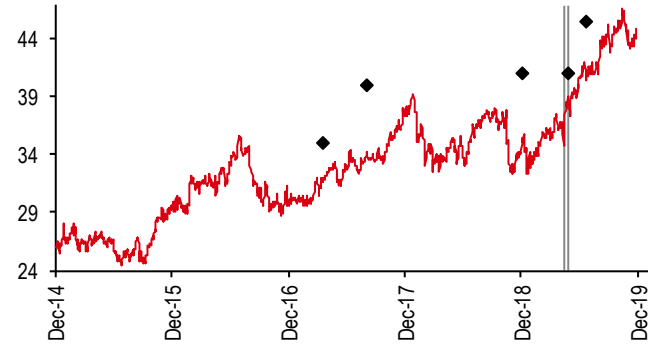
Share price and rating changes for long-term investment opportunities

Aqua America (WTR.N) share price performance USD Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	35.00	24 Mar 2017	Verity Mitchell
Price 2	40.00	08 Aug 2017	Verity Mitchell
Price 3	41.00	06 Dec 2018	Verity Mitchell
Price 4	Restricted	15 Apr 2019	
Price 5	41.00	30 Apr 2019	Verity Mitchell
Price 6	45.50	28 Jun 2019	Verity Mitchell

Source: HSBC

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Company	Ticker	Recent price	Price date	Disclosure
AQUA AMERICA	WTR.N	44.90	04 Dec 2019	1, 5, 6

Source: HSBC

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[1134671]

HSBC Global Research

22 April 2020

Essential Utilities (WTRG US)

Buy: Acquisitions in the bag for growth

Equities
Water Utilities

United States

- Water and wastewater infrastructure business relatively unaffected by COVID-19
- Peoples deal completed; DELCORA on track for 2022; regulatory mechanisms to ease rate case lag; proforma 2020
- Maintain Buy rating; TP increased from USD47.5 to USD50.0

COVID-19 update: The American Water Works Association (AWWA) published the results of an online survey on the impact of the COVID-19 emergency on its member organisations on 10 April. According to the survey, utilities are reacting swiftly to the crisis to guarantee essential services and business continuity, but two thirds expect revenue/cash flow problems within the next two months. The two factors causing financial uncertainty are changes in water demand from non-domestic customers and customer payments during the coronavirus pandemic. However capital investment in asset rehabilitation remains relatively unaffected.

Essential Utilities (EU) has already made two significant acquisitions: The focus for 2020-2022 will be on integrating these and successfully delivering rate cases. Infrastructure surcharges and test years for rate cases help to reduce the regulatory lag. 52% of EU's capex is eligible for these. This provides clarity on the cash flows and reduces uncertainties around translation of rate base growth into earnings. With the completion of the Peoples deal and the gas heating season in Q1 lowering the seasonal contribution to earnings for Q2 and Q3, the company will be reporting earnings for 2020 on a pro-forma basis to improve transparency.

Maintain Buy rating with increased target price, from USD47.5 to USD50.0: We value Essential Utilities via three methodologies: DCF, dividend yield, and the average of PE multiple and SOP (rate-based) valuations. Taking the average of the three approaches gives us our target price of USD50.0 (previously USD47.5). In our DCF valuation, we have updated our beta assumption from 0.58 to 0.60 to be in line with market peers and have updated the model for FY2019 results. Our cost of capital is updated from 4.3% to 5.9%. These changes leads to a fall in the DCF valuation from USD47.5 to USD41.1. In our PE multiple-based valuation, we have updated the multiple in line with market peers, from 29.8x to 30.0x. This leads to an increase in the PE-multiple valuation, from USD45.8 to USD46.8. Our SOP valuation rises from USD44.1 to USD57.1, driven by the updated rate base, and the average of the two rises from USD45.8 to USD52. In our yield valuation, we update our yield from 2% to 1.75%, again in line with peers. This results in an increase in the Yield valuation from USD49.4 to USD57.8. Overall, these changes lead to an increase in our TP from USD47.5 to USD50.0. Our TP implies 15.3% upside and we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

MAINTAIN BUY

TARGET PRICE (USD)	PREVIOUS TARGET (USD)
50.00	**47.50**
SHARE PRICE (USD)	UPSIDE/DOWNSIDE
43.36	**+15.3%**
(as of 17 Apr 2020)	

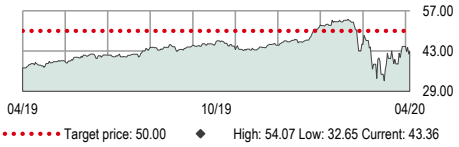
MARKET DATA

Market cap (USDm)	9,683	Free float	100%
Market cap (USDm)	9,683	BBG	WTRG US
3m ADTV (USDm)	67	RIC	WTRG.N

FINANCIALS AND RATIOS (USD)

Year to	12/2019a	12/2020e	12/2021e	12/2022e
HSBC EPS	1.04	1.56	1.68	1.81
HSBC EPS (prev)	1.50	1.59	1.65	na
Change (%)	-30.7	-2.0	1.7	na
Consensus EPS	1.48	1.56	1.64	1.77
PE (x)	41.7	27.8	25.9	23.9
Dividend yield (%)	2.2	2.3	2.5	2.7
EV/EBITDA (x)	21.9	17.0	16.2	15.4
ROE (%)	7.6	8.3	7.4	7.8

52-WEEK PRICE (USD)



Source: Refinitiv IBES, HSBC estimates

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Disclosures & Disclaimer
This report must be read with the disclosures and the analyst certifications in the Disclosure appendix, and with the Disclaimer, which forms part of it.

Issuer of report: HSBC Bank plc

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Financials & valuation: Essential Utilities

Buy

Financial statements

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Profit & loss summary (USDm)				
Revenue	890	1,895	2,097	2,230
EBITDA	497	824	897	973
Depreciation & amortisation	-157	-239	-267	-284
Operating profit/EBIT	340	585	631	689
Net interest	-131	-153	-167	-188
PBT	212	432	463	501
HSBC PBT	209	432	463	501
Taxation	13	-35	-37	-40
Net profit	225	397	426	461
HSBC net profit	225	397	426	461
Cash flow summary (USDm)				
Cash flow from operations	339	706	707	754
Capex	-550	-950	-950	-950
Cash flow from investment	-605	-5,225	-950	-950
Dividends	-189	-257	-278	-300
Change in net debt	-1,352	3,108	521	496
FCF equity	-212	-244	-243	-196
Balance sheet summary (USDm)				
Intangible fixed assets	64	939	939	939
Tangible fixed assets	7,224	11,335	12,018	12,684
Current assets	2,011	2,154	2,182	2,201
Cash & others	1,869	1,869	1,869	1,869
Total assets	9,360	14,489	15,201	15,886
Operating liabilities	1,468	1,680	1,723	1,751
Gross debt	3,077	6,186	6,707	7,203
Net debt	1,208	4,317	4,838	5,334
Shareholders' funds	3,881	5,689	5,837	5,998
Invested capital	5,962	10,879	11,548	12,204

Ratio, growth and per share analysis

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Y-o-y % change				
Revenue	6.2	113.0	10.7	6.3
EBITDA	5.7	65.8	8.9	8.4
Operating profit	5.3	72.0	7.8	9.2
PBT	18.6	104.2	7.3	8.1
HSBC EPS	-3.4	50.2	7.3	8.1
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	6.4	6.4	5.2	5.3
ROE	7.6	8.3	7.4	7.8
ROA	4.1	4.5	3.9	4.1
EBITDA margin	55.9	43.5	42.8	43.6
Operating profit margin	38.2	30.9	30.1	30.9
EBITDA/net interest (x)	3.8	5.4	5.4	5.2
Net debt/equity	31.1	75.9	82.9	88.9
Net debt/EBITDA (x)	2.4	5.2	5.4	5.5
CF from operations/net debt	28.0	16.4	14.6	14.1
Per share data (USD)				
EPS Rep (diluted)	1.04	1.56	1.68	1.81
HSBC EPS (diluted)	1.04	1.56	1.68	1.81
DPS	0.94	1.01	1.09	1.18
Book value	17.97	22.36	22.94	23.58

Valuation data

Year to	12/2019a	12/2020e	12/2021e	12/2022e
EV/sales	12.2	7.4	6.9	6.7
EV/EBITDA	21.9	17.0	16.2	15.4
EV/IC	1.8	1.3	1.3	1.2
PE*	41.7	27.8	25.9	23.9
PB	2.4	1.9	1.9	1.8
FCF yield (%)	-2.2	-2.5	-2.5	-2.0
Dividend yield (%)	2.2	2.3	2.5	2.7

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2019a
GHG emission intensity*	n/a
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social Indicators	**12/2019a**
Employee costs as % of revenues	n/a
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	12/2019a
No. of board members	8
Average board tenure (years)	7.0
Female board members (%)	25
Board members independence (%)	87.5

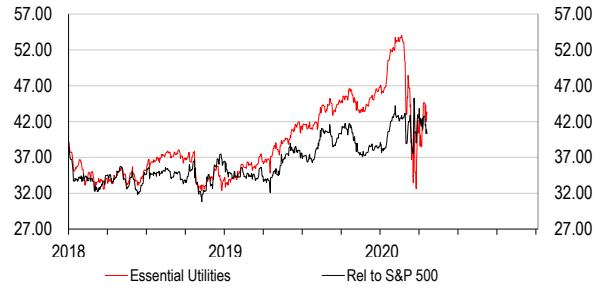
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	43.36	Free float	100%
Target price (USD)	50.00	Sector	Water Utilities
RIC (Equity)	WTRG.N	Country/Region	United States
Bloomberg (Equity)	WTRG US	Analyst	Verity Mitchell
Market cap (USDm)	9,683	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 17 Apr 2020

Acquisitions in the bag for growth

- Water and wastewater infrastructure business relatively unaffected by COVID-19
- Peoples deal completed; DELCORA on track for 2022; regulatory mechanisms to ease rate case lag; proforma 2020 results
- Maintain Buy rating; TP increased from USD47.5 to USD50.0

Uncertainties and risks due to COVID-19 pandemic

The American Water Works Association (AWWA) published the results of an online survey on the impact of the COVID-19 emergency on its member organisations on 10 April. According to the survey, utilities are reacting swiftly to the crisis to guarantee essential services and business continuity, but two thirds expect revenue/cash flow problems within the next two months. The two factors causing financial uncertainty are changes in water demand from non-domestic customers and customer payments during the coronavirus pandemic.

The two major challenges that investor-owned utilities identified were ensuring social distancing of the work force and supply chain issues for PPE. In terms of regulatory compliance, an issue that was noted was problems in accessing sampling sites. Most utilities have implemented measures to help customers: more than 90% have suspended water shut-offs, and nearly 50% have restored service to suspended accounts.

Three-pronged investment proposition

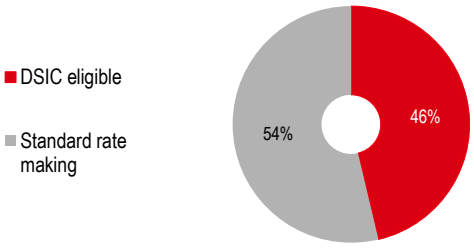
Essential Utilities has core competencies in infrastructure investment (pipes, plants, etc), regulatory affairs and operational excellence. Using these as pillars, Essential has created a 3-pronged growth strategy.

1. Municipal initiative: Driver of growing foundational water and wastewater business. This is the primary focus for the company right now.
2. Strategic M&A: Opportunistic pursuit of large, regulated utility/infrastructure targets – the company delivered on this by the Peoples gas acquisition recently completed and the DELCORA transaction which is expected to complete regulatory approvals by 2022.
3. MBAs (Market Based Activities): Complementary to regulated business. Capitalises on broader infrastructure renewals but is probably going to be less of a priority given the current challenges.

Attractive capex recovery mechanisms

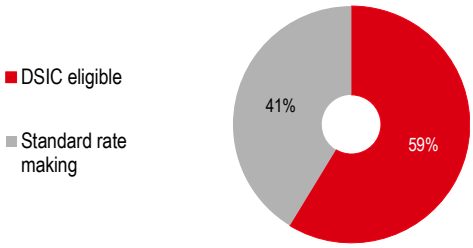
Infrastructure surcharges and test years for rate cases help to reduce regulatory lag. 52% of EU's capex is eligible for these. This provides clarity on the cash flows and reduces uncertainties around translation of the rate base growth into earnings.

Water capex: 2020-22 estimates



Source: WTRG company results presentations - FY2019

Gas capex: 2020-22 estimates



Source: WTRG company results presentations - FY2019

From the table below we can see that most of the states that Essential Utilities operates in have opted for these mechanisms, which is a positive development for the company.

State wise regulations for capex recovery

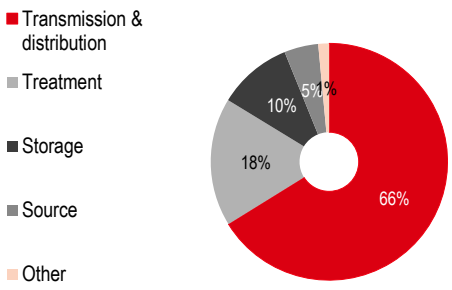
State	Allowed surcharge
Water	
Pennsylvania	7.5% W; 5%WW
Indiana	10%
Ohio	12.75% W; 9% WW
New Jersey	5%
Illinois	2.5% annual avg increase
North Carolina	5%
Gas	
Pennsylvania	5%
Kentucky	No cap

Source: WTRG company results presentations - FY2019

US water infrastructure needs offer opportunities for Aqua

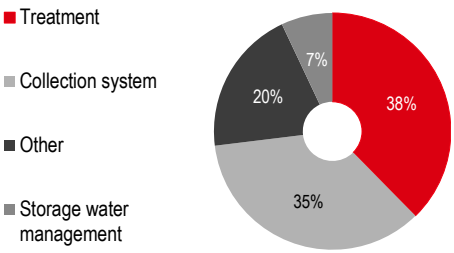
In the charts below we can see the EPA estimates of the US water infrastructure investment needs.

Water - USD473bn



Source: WTRG company results presentations - FY2019

Wastewater - USD271bn



Source: WTRG company results presentations - FY2019

Acquisitions – strong pipeline and primary focus for the company

From the table below we can see that, even with the major deal of DELCORA it has signed, Essential has a decent pipeline of acquisitions. However, due to current COVID-19 pandemic, the closure of some of these may well be delayed into 2021.

Acquisitions - closed and pending at FY2019 results

	State	Type	Total customers	Rate base (USD '000s)
Closed				
Skyline	Illinois	W / WW	752	3550
Phoenixville	Pennsylvania	W	529	2500
Grant Park	Illinois	WW	540	2300
Cheltenham	Pennsylvania	WW	9887	44558
Campbell	Ohio	W	3200	7535
Total			**14908**	**60443**
Pending				
New Garden	Pennsylvania	WW	2106	29500
East Norriton	Pennsylvania	WW	4952	21000
DELCORA	Pennsylvania	WW	198000	276500
Total			**205058**	**327000**

Source: WTRG company results presentations - FY2019

Guidance for 2020

The guidance for 2020 is as follows:

- Adjusted proforma income per diluted common share (non-GAAP) of USD1.53 to USD1.58. This illustrative guidance includes the full-year effects of the Peoples acquisition as if this transaction closed on January 1, 2020, by including an estimate of the results of Peoples for the period in 2020 prior to closing, excluding transaction-related expenses and the effects of transaction-related commitments to issue rate credits to utility customers.
- 3-year earnings CAGR 5-7% for 2019 through 2022, with the base being 2019 adjusted income per share (non-GAAP).

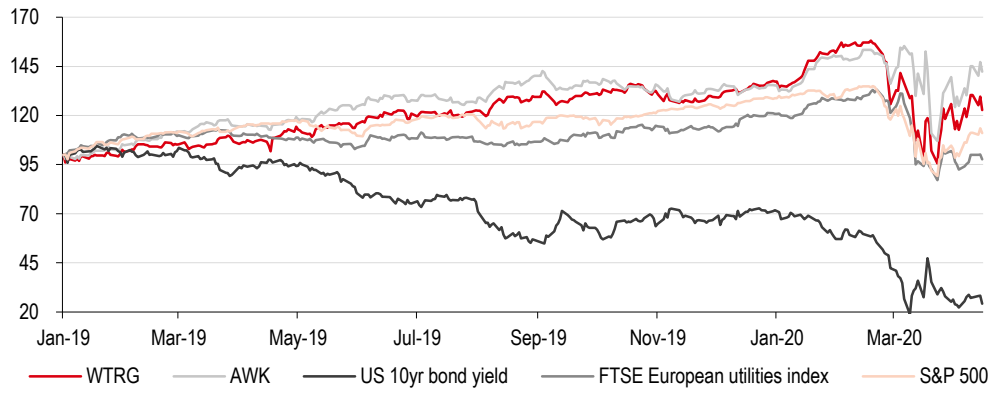
- Infrastructure investment of approximately USD550m in 2020 for communities served by the water operations.
- Infrastructure investment of approximately USD400m in 2020 for communities served by the gas operations.
- Infrastructure investment of approximately USD2.8bn through 2022 in existing water and gas operations to rehabilitate and strengthen systems.
- Rate base compound annual growth rate of 6 to 7% through 2022 in water; and 8 to 10% in gas through to 2022.
- Total annual water customer growth of between 2 and 3% on average, depending upon regulatory approval.

Performance against peers

Essential's share price has outperformed the S&P 500 by 12% since 1 January 2019. On 2020e PE, it is trading at a discount to its water peer group but in line with some of the US electricity utilities according to Refinitiv Datastream. This reflects, in our view, its future multi-utility status.

One more point to note is that the US Treasury 10-year yield has fallen sharply. WTRG, as a defensive utility, should be inversely correlated to bond yields.

Performance of WTRG vs AWK vs UST 10yr vs FTSE European utilities index vs S&P 500



Source: Refinitiv Datastream

Changes in estimates

We have updated our model for FY2019 results and the preliminary impact of COVID-19. We have also updated the model for Peoples proforma numbers for 2020 and included the DELCORA deal in our numbers from 2022. We have also updated the number of shares for 2020 to 254.4m from 215.9m in 2019 according to company guidance associated with the Peoples-related equity offering in 2019.

Change in estimates (USDm)

	2020e	2021e	2022e
EBIT			
Revised	585	631	689
Previous	578	604	
Change	*1%*	*4%*	
Net income			
Revised	397	426	461
Previous	399	412	
Change	*0%*	*3%*	
EPS (USD)			
Revised	1.56	1.68	1.81
Previous	1.59	1.65	
Change	*-2%*	*2%*	
DPS (USD)			
Revised	1.01	1.09	1.18
Previous	0.99	1.07	
Change	*2%*	*2%*	

Source: HSBC estimates

Valuation and risks

We value Essential Utilities via three methodologies: DCF, dividend yield, and the average of PE multiple and SOP (rate-based) valuations. Taking the average of the three approaches gives us our target price of USD50.0 (previously USD47.5). We have updated the model for FY2019 results.

- In our DCF valuation, we have updated our beta assumption from 0.58 to 0.60 to be in line with market peers. We have also updated the cost of debt from 3.9% to 8.5% and the marginal tax rate from 11% to 13%. These changes lead to updated cost of capital, from 4.3% to 5.9% and a fall in the DCF valuation from USD47.5 to USD41.1.
- In our PE multiple-based valuation, we have updated the multiple in line with market peers, from 29.8x to 30.0x. Our SOP valuation rises from USD44.1 to USD57.1, driven by updated rate base, and the average of the two rises from USD45.8 to USD52.
- In our Yield valuation, we update our yield from 2% to 1.75%, again in line with peers. This results in an increase in the Yield valuation from USD49.4 to USD57.8.

Overall, these changes lead to an increased TP from USD47.5 to USD50.0. Our TP implies 16.7% upside; we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

Summary of valuation (USD)

Particulars	New	Previous
Current price as on 17-Apr-20	**43.4**	**NA**
DCF (updated estimates, higher cost of capital)	41.1	47.5
Yield 1.75% (previously 2%)	57.8	49.4
SOP & Peer multiple (updated estimates and multiples)	51.9	45.8
Target price (average rounded)	**50.0**	**47.5**
Upside/ downside to target price	15.3%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity Valuation	USDm
Cost of debt		**+ DCF value**	**13,873**
Pre-tax cost of debt	8.5%	+ ST marketable assets	0
Marginal tax rate	13.0%	+ Value of associates	0
Cost of equity		+ Other assets	878
Risk-free rate	3.0%	**EV (asset side)**	**14,751**
Equity risk premium	3.0%	- Net debt (+ if Net cash)	(4,288)
Additional risk		- Quasi debt (pension)	0
Beta (previously 0.58)	**0.60**	- Value of minorities	0
Debt - 37%	7.8%	Total non-equity claims	(4,288)
Equity - 63%	4.8%	Value of equity	10,463
Cost of capital	**5.9%**	**Value per share (USD)**	**41.1**

Source: HSBC estimates

Sum-of-the-parts (SOP) and PE multiple valuations

USDm	2020e Rate Base
Regulated water	
Pennsylvania	3,682
Ohio	368
Illinois	382
Texas	319
New Jersey	214
North Carolina	245
Indiana	90
Virginia	83
Regulated gas	2,451
Total	**7,834**
Price to rate base (industry multiple)	18,802
Non-regulated (2020e peer average PE multiple)	9
Net debt 2020e, pensions & minority	(4,288)
Estimated equity value	**14,523**
Estimated equity value per share (USD)	**57.1**
PE multiple valuation	
2020e earnings per share (USD)	1.56
2020e PE sector average	30.0
Value per share	**46.8**
Average of rate base valuation and PE multiple valuation	**52.0**

Source: HSBC estimates

Downside risks

Essential Utilities fails to achieve the desired rate case revisions and infrastructure surcharges; it lacks organic growth from asset replacement; it cannot take advantage of the Fair Market Value legislation opportunity; its dividend grows at a lower rate than we assume.

It is not able to gain the Fair Market Value premium required in the systems it wants to acquire in Pennsylvania. Its current acquisitions of systems – New Garden and Limerick – are facing challenges to the premium proposed by Aqua.

Disclosure appendix

Analyst Certification

The following analyst(s), economist(s), or strategist(s) who is(are) primarily responsible for this report, including any analyst(s) whose name(s) appear(s) as author of an individual section or sections of the report and any analyst(s) named as the covering analyst(s) of a subsidiary company in a sum-of-the-parts valuation certifies(y) that the opinion(s) on the subject security(ies) or issuer(s), any views or forecasts expressed in the section(s) of which such individual(s) is(are) named as author(s), and any other views or forecasts expressed herein, including any views expressed on the back page of the research report, accurately reflect their personal view(s) and that no part of their compensation was, is or will be directly or indirectly related to the specific recommendation(s) or views contained in this research report: Verity Mitchell and Adam Dickens

Important disclosures

Equities: Stock ratings and basis for financial analysis

HSBC and its affiliates, including the issuer of this report ("HSBC") believes an investor's decision to buy or sell a stock should depend on individual circumstances such as the investor's existing holdings, risk tolerance and other considerations and that investors utilise various disciplines and investment horizons when making investment decisions. Ratings should not be used or relied on in isolation as investment advice. Different securities firms use a variety of ratings terms as well as different rating systems to describe their recommendations and therefore investors should carefully read the definitions of the ratings used in each research report. Further, investors should carefully read the entire research report and not infer its contents from the rating because research reports contain more complete information concerning the analysts' views and the basis for the rating.

From 23rd March 2015 HSBC has assigned ratings on the following basis:

The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

Prior to this date, HSBC's rating structure was applied on the following basis:

For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

As of 21 April 2020, the distribution of all independent ratings published by HSBC is as follows:

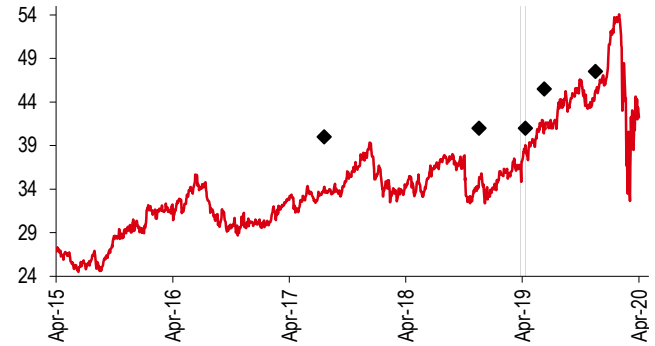
Buy	55%	(31% of these provided with Investment Banking Services)
Hold	36%	(30% of these provided with Investment Banking Services)
Sell	9%	(24% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

For the distribution of non-independent ratings published by HSBC, please see the disclosure page available at http://www.hsbcnet.com/gbm/financial-regulation/investment-recommendations-disclosures.

Share price and rating changes for long-term investment opportunities

Essential Utilities (WTRG.N) share price performance USD Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	40.00	08 Aug 2017	Verity Mitchell
Price 2	41.00	06 Dec 2018	Verity Mitchell
Price 3	Restricted	15 Apr 2019	
Price 4	41.00	30 Apr 2019	Verity Mitchell
Price 5	45.50	28 Jun 2019	Verity Mitchell
Price 6	47.50	06 Dec 2019	Verity Mitchell

Source: HSBC

To view a list of all the independent fundamental ratings disseminated by HSBC during the preceding 12-month period, please use the following links to access the disclosure page:

Clients of Global Research and Global Banking and Markets: www.research.hsbc.com/A/Disclosures

Clients of HSBC Private Banking: www.research.privatebank.hsbc.com/Disclosures

HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price date	Disclosure
ESSENTIAL UTILITIES	WTRG.N	42.24	20 Apr 2020	1, 5, 6

Source: HSBC

1 HSBC has managed or co-managed a public offering of securities for this company within the past 12 months.

2 HSBC expects to receive or intends to seek compensation for investment banking services from this company in the next 3 months.

3 At the time of publication of this report, HSBC Securities (USA) Inc. is a Market Maker in securities issued by this company.

4 As of 31 March 2020, HSBC beneficially owned 1% or more of a class of common equity securities of this company.

5 As of 29 February 2020, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of investment banking services.

6 As of 29 February 2020, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of non-investment banking securities-related services.

7 As of 29 February 2020, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of non-securities services.

8 A covering analyst/s has received compensation from this company in the past 12 months.

9 A covering analyst/s or a member of his/her household has a financial interest in the securities of this company, as detailed below.

10 A covering analyst/s or a member of his/her household is an officer, director or supervisory board member of this company, as detailed below.

11 At the time of publication of this report, HSBC is a non-US Market Maker in securities issued by this company and/or in securities in respect of this company

12 As of 15 Apr 2020, HSBC beneficially held a net long position of more than 0.5% of this company's total issued share capital, calculated according to the SSR methodology.

13 As of 15 Apr 2020, HSBC beneficially held a net short position of more than 0.5% of this company's total issued share capital, calculated according to the SSR methodology.

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Water Utilities

January 12, 2021

Essential Utilities Inc. (WTRG) - BUY

Positive Guidance Call Takeaways; Reiterate BUY Rating, $70 Fair Value

Price:	$48.18
Fair Value Estimate:	$70.00
52-Week Range:	$30.40 - $54.52
Market Cap (MM):	11,817
Shr.O/S-Diluted (mm):	245.3
Average Daily Volume:	1,053,887
Book Value:	$18.90
Dividend:	$1.00
Yield:	2.1%

FYE: Dec	2020E	2021E	2022E
EPS:	$1.58E	$1.67E	$1.78E
Prior EPS:	NC	NC	NC
P/E Ratio:	30.5x	28.9x	27.1x

Quarterly EPS:

Q1	$0.60A	$0.66E	$0.68E
Q2	$0.29A	$0.22E	$0.25E
Q3	$0.23A	$0.26E	$0.27E
Q4	$0.46E	$0.52E	$0.58E

EPS: adjusted

Quarterly Revenue (M):

Q1	$256A	$773E	$794E
Q2	$384A	$342E	$352E
Q3	$349A	$360E	$370E
Q4	$541E	$579E	$601E
Year:	$1,530E	$2,053E	$2,118E

PORTFOLIO MANAGER BRIEF

As the title of our note implies, the key takeaways from WTRG's guidance call for 2021 were all positive. Key areas focused on included earnings (2021 and long-term), capital allocation, emission reduction initiatives, and acquisitions. Given the 2021 EPS guidance range encompassed our pre-existing full year estimate, we've made no changes to our forecasts. We reiterate our BUY rating and $70 Fair Value on WTRG shares.

ANALYST NOTES

- 2021 EPS Guidance Range Encompassed Street Expectations. The expected 2021 EPS guidance range of $1.64 to $1.69 encompassed 7 of 9 published forecasts in FactSet. The company continues to see a 5-7% CAGR on a go forward basis from 2020 through 2023, and it also reiterated its 2020 adjusted EPS guidance range of $1.53 - $1.58. WTRG expects to report 4Q20 and full year 2020 results after market close on 2/24/21.
- Capital Allocation Heavily Tilted to Pennsylvania. For 2021, the capital budget is $1 billion, and of that amount, 55% ($550MM) is slated for water investment, 45% ($450MM) for gas. However, if we break out the CAPEX in terms of state allocation, it looks like approximately $875MM of the investment will occur in Pennsylvania, where WTRG gets its highest returns. One slide that caught our attention was #17, which highlights the breakout of pipe replacement through 2023. The acceleration in gas pipe replacement on a percentage basis is well above that of the water business and again is occurring in Pennsylvania.
- Emission Reductions Will Be Sizable. A fair amount of time was spent on emission reductions (Scope 1 and 2) across all operations. Using 2019 as a baseline, the Company expects a 60% reduction by 2035, and pledged to update stakeholders on the progress towards that goal every 6 months until achieved. Key elements for the gas distribution system include replacing 3,000 miles of leak prone gas distribution pipe, a gathering system repair and replacement program, accelerated leak detection and repair, fugitive gas reinjection during construction, and transitioning to CNG vehicles. For the water and wastewater operations, a commitment to source 100% renewable electricity for the States of Illinois, New Jersey, Ohio, and Pennsylvania by 2022.

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- Acquisition Pipeline Remains Strong. Building on 2020's successful acquisition program (12k new customers, $63MM rate base) in 2021 should be a fairly easy affair, given pending transactions total just shy of 225K customers and $420MM of rate base. The DELCORA transaction remains the "big prize" with its 198K customers and $276MM purchase price. The Company expects to close the DELCORA acquisition in 2Q21. WTRG is actively pursuing municipal opportunities totaling 340K total customers.
- Summary/Valuation. On-the-mark guidance, robust capital investment levels, a strong acquisition pipeline, visible earnings growth, aggressive emission reduction targets.....there was a lot more information in WTRG's "guidance call" than we expected. All the news was good and Essential Utilities continues to be our top pick in the water utility sector. Valuation remains compelling; at a P/E of 27x consensus 2022 forecasts, the shares trade 5 turns below the peer group and carry a sector-high dividend yield of 2.08%. We reiterate our BUY rating and $70 Fair Value, based on a target dividend yield of 1.5% applied to our 2021 estimated dividend of $1.06.

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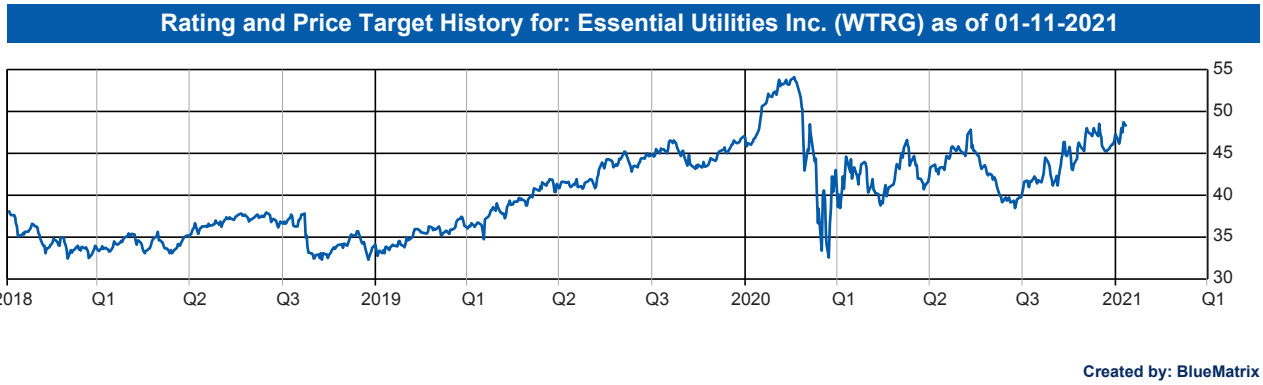

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			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	115	46.18	27	23.48
NEUTRAL [N]	134	53.82	16	11.94
SELL [S]	0	0.00	0	0.00

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Water Utilities

May 11, 2020

Essential Utilities Inc. (WTRG) - BUY

Strong 1Q20 Results in a Transformational Quarter; Reiterate BUY Rating, $70 Fair Value

Price:	$40.30
Fair Value Estimate:	$70.00
52-Week Range:	$30.40 - $54.52
Market Cap (MM):	9,874
Shr.O/S-Diluted (mm):	245.0
Average Daily Volume:	1,377,749
Book Value:	$17.58
Dividend:	$0.94
Yield:	2.3%

FYE: Dec	2019A	2020E	2021E
EPS:	$1.47A	$1.58E	$1.66E
Prior EPS:		$1.56	$1.65
P/E Ratio:	27.4x	25.5x	24.3x

Quarterly EPS:

Q1	$0.28A	$0.60A	$0.66E
Q2	$0.37A	$0.23E	$0.23E
Q3	$0.48A	$0.25E	$0.26E
Q4	$0.34A	$0.50E	$0.51E

EPS: adjusted

Quarterly Revenue (M):

Q1	$201A	$256A	$773E
Q2	$219A	$325E	$342E
Q3	$244A	$352E	$360E
Q4	$226A	$571E	$579E
Year:	$890A	$1,504E	$2,053E

PORTFOLIO MANAGER BRIEF

WTRG's 1Q20 adjusted EPS results exceeded expectations, in what was probably the most transformational quarter in the Company's history. Q1 saw the final closing of the Peoples Gas transaction, and then a filing with the IRS for tax repair at Peoples Gas. Also completed was an application with Pennsylvania Public Utility Commission (PAPUC) for the DELCORA acquisition. In addition to that the Company changed its name and stock symbol, and then activated its emergency response plans to deal with COVID-19. From our viewpoint, the investment case for ownership of WTRG shares continues to strengthen; and given the current yield of 2.3% (highest in the water sector peer group), we reiterate our BUY rating and $70 Fair Value on WTRG shares.

ANALYST NOTES

1Q20 Results Above Forecasts. On the top line, revenues increased 27% YOY, driven by the addition of Peoples Gas and new rates/surcharges in the water segment. At the bottom line, WTRG chose to elect tax repair accounting methodology for most of the Peoples Gas operations, which generated a $5.9MM tax benefit in the quarter. All-in adjusted EPS of $0.60 was above our $0.53 estimate and consensus of $0.58.

Pennsylvania is Generating Significant Acquisition Activity. While the Company's been active across its geographic footprint in terms of acquisitions, the State of Pennsylvania has been particularly meaningful when it comes to acquiring assets recently. In Q1 the Peoples Gas transaction was completed, and next up is the Delaware County Regional Water Quality Control Authority (DELCORA) which serves 42 municipalities and 500,000 people. Beyond DELCORA, the Company has two more signed agreements in Pennsylvania (New Garden and East Norriton) which will add another 7,000+ customers.

Other substantial targets that have been discussed publicly as potential asset sales in the State include the cities of Pittsburgh, Harrisburg and the Chester Water Authority. All-in the Company has signed purchase agreements expected to add the equivalent of 205,058 water & wastewater customers, with all but 512 of them in the Keystone State. Essential also noted that Virginia recently passed fair market value legislation, which is now in place in all 8 states where Essential operates. We certainly expect competition for assets where opportunities exist, but WTRG should continue to get its fair share of acquisitions within its service territories.

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COVID-19 Actions Mirror Industry-Wide Best Practices. WTRG's response to COVID-19 is mirroring utility industry best practices, including following Federal and local guidelines in the areas of health & safety. Those employees that can work remotely are doing so, and social distancing work practices are in place. The Company suspended customer shut-offs early after COVID-19 risks were identified, and is not entering customer homes for non-essential work. In terms of the balance sheet, WTRG increased liquidity via a $500MM 364 term loan in March.

Regulatory Update. YTD, the Company has completed rate case or surcharge filings for water operations in Illinois, North Carolina, Ohio and Virginia totaling $5.2MM in additional revenues. In the Natural Gas segment, surcharge filings have been completed in Kentucky and Pennsylvania totaling $977K. New base rates are expected shortly in Indiana, New Jersey, North Carolina and Ohio (total requests = $10.1MM).

Summary/Valuation. Successful completion of the Peoples Gas transaction, election of tax repair accounting methodology, additional expected benefits from catch-up tax repair deductions for past investments, the upcoming closing of the DELCORA transaction, a full pipeline of acquisition opportunities across all operating states, continued rate relief.....the list of expected positive impacts on WTRG's financials is quite extraordinary at this moment in time.

In terms of valuation, recall our view on the sector in general that as long as earnings growth continues under the regulated investment model, P/E's may fluctuate with general market conditions but over time dividend increases will continue to push share prices higher as long as 1) interest rates remain static or move lower and 2) yields on utilities compare favorably with other types of investments. We've noted some of our peers are bringing P/E multiple assumptions for utility shares lower and in some cases doing a "sum-of-the-parts" methodology, whereby each reporting segment gets its own multiple. We abandoned that methodology years ago because we found ourselves perpetually missing equity tops when yield (and dividend increases) became the primary focus for utility investors.

Returning to WTRG shares, we note the Company's primary service territory of Pennsylvania remains the most constructive in the U.S. (in our opinion) for both natural gas and water utilities. When we last revisited valuation in our industry piece back on October 7th, the U.S. 10-Year T-Note was at 1.53%. WTRG shares were trading at a P/E of 27x 2021 EPS estimates, for a yield of 2.06%. The Peoples Gas transaction had not closed (and actually dragged on a bit longer than expected), which introduced some minor element of regulatory risk. Fast forward to Friday: the U.S. 10-Year T-Note closed at 0.69%, WTRG shares are trading at a P/E of 24x 2021 EPS estimates, for a yield of 2.33%. The Peoples Gas transaction has now closed, tax repair accounting (and its bottom line benefits) are in place, and regulatory risk present in October is not a factor.

All-in, we believe P/E multiples will once again begin moving higher for all the water utilities, but especially for WTRG shares, given 1) the yield of 2.33%, versus the group average yield of 1.88%, 2) due to our expectations that interest rates will remain low, and 3) that the earnings bias is decidedly upward. The shares hit a 52-week high of $54.52 back on February 18th, and its a stronger Company with better earnings visibility today than it was just 3 months ago. Our view is that the need for yield has intensified, and will remain strong for the foreseeable future. We maintain our BUY rating and $70 Fair Value, based on a P/E of 42x our 2021 EPS estimate of $1.66.

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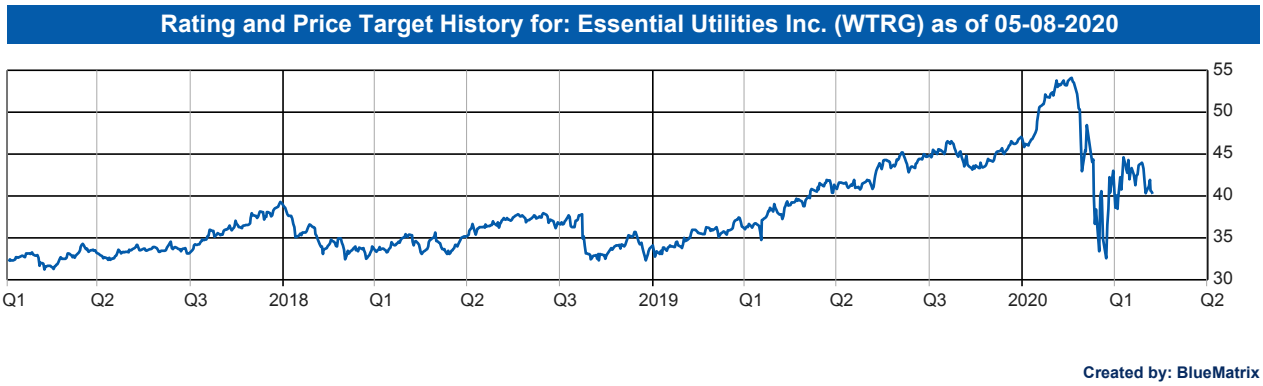

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			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	169	51.84	35	20.71
NEUTRAL [N]	156	47.85	22	14.10
SELL [S]	1	0.31	0	0.00

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Water Utilities

May 11, 2021

Essential Utilities Inc. (WTRG) - BUY

2021 Off To A Strong Start; Reiterate BUY Rating, $70 Fair Value

Price:	$46.76
Fair Value Estimate:	$70.00
52-Week Range:	$37.37 - $48.89
Market Cap (MM):	11,924
Shr.O/S-Diluted (mm):	255.0
Average Daily Volume:	1,050,480
Book Value:	$18.90
Dividend:	$1.00
Yield:	2.1%

FYE: Dec	2020A	2021E	2022E
EPS:	$1.58A	$1.69E	$1.78E
Prior EPS:		$1.67	NC
P/E Ratio:	29.6x	27.7x	26.3x

Quarterly EPS:

Q1	$0.60A	$0.72A	$0.74E
Q2	$0.29A	$0.23E	$0.27E
Q3	$0.23A	$0.29E	$0.28E
Q4	$0.46A	$0.45E	$0.50E

EPS: adjusted

Quarterly Revenue (M):

Q1	$256A	$584A	$617E
Q2	$384A	$388E	$403E
Q3	$349A	$367E	$382E
Q4	$474A	$497E	$517E
Year:	$1,463A	$1,836E	$1,920E

PORTFOLIO MANAGER BRIEF

WTRG's 1Q21 EPS results were above our and consensus forecasts, as more favorable winter weather positively impacted the gas segment's results. Despite the outperformance, 2021 EPS guidance was maintained; we've adjusted our estimates to remain "within the lines" of the expected range. All-in, 2021 and 2022 look to be very good years for the Company from an earnings perspective, and our view is WTRG shares remain one of the best values in our coverage universe. We reiterate our BUY rating and $70 Fair Value.

ANALYST NOTES

- 1Q21 Results Nicely Above Expectations. Weather was very favorable in Q1 in southwestern Pennsylvania, which drove a strong performance from WTRG's Peoples Gas operations. Consolidated adjusted EPS of $0.72 was above our $0.66 estimate, which was also consensus.
- Acquisition Updates. The Company continues to push forward on its DELCORA acquisition, which remains in litigation. Delaware County Court has upheld the validity of the sale agreement, but Delaware County has appealed to the state court. WTRG is awaiting a judge's decision for that appeal, which could take six months or more. The Company expects to settle the forward sale agreement of the 6.7MM shares (proceeds to be used primarily for the DELCORA acquisition) no later than (and close to) August 10th, 2021, the last day it can do so.
- DELCORA aside, the pipeline of opportunities continues to be robust, with 395,000 customer connections being pursued. Fair market value legislation across the geographic service territory continues to benefit acquisition activity, with West Virginia and Kentucky the most recent states to pass this type of legislation. On the 1Q21 conference call, WTRG indicated that it expected to be active in Kentucky looking for transactions going forward.
    - Guidance Maintained. For 2021, WTRG's guidance remains as follows:
    - Net income per diluted common share of $1.64 to $1.69,
    - Earnings per share growth CAGR of 5 to 7% for 2020 through 2023,
    - Regulated water segment infrastructure investments of approximately $550 million in 2021,
    - Regulated natural gas segment infrastructure investments of approximately $450 million in 2021,
    - Infrastructure investments of approximately $3 billion through 2023 to rehabilitate and strengthen water, wastewater and natural gas systems,

RESEARCH ANALYST CERTIFICATIONS AND IMPORTANT DISCLOSURES ARE ON PAGES 3 - 4 OF THIS REPORT

  - Regulated water segment rate base compound annual growth rate of 6 to 7% through 2023,
  - Regulated natural gas segment rate base compound annual growth rate of 8 to 10% through 2023,
  - Average annual regulated water segment customer (or equivalent dwelling units) growth of between 2 and 3% from acquisitions and organic customer growth.

- Summary/Valuation. WTRG share prices have been performing better recently, but still lag versus the peer group. We thought a "sum-of-the-parts" valuation might be useful given the disconnect; the gas utility operations are the most difficult to value, given "pure-play" natural gas comparables to Peoples Gas are difficult to come by. We note that Centerpoint Energy (CNP, NR) recently announced the sale of several gas utility properties for 2.5x rate base. If we use the Peoples Gas rate base of $2.5B, applying a 2.5x rate base multiple would equal a $6.25B value. If we divide that by 255MM shares, that translates to a $24.51 per share value.
- The water utility operations present less of a challenge in terms of valuation, given several comparables exist. The most direct comp is likely American Water Works (AWK, BUY) which has sizable operations in Pennsylvania and New Jersey. Those shares command a 37x P/E on 2021 consensus EPS. If we use the midpoint of 2021 EPS guidance for WTRG shares and assume approximately 70% of EPS is derived from water utility operations, that gets us to $1.16 EPS x 37 P/E = $42.92. When added to the aforementioned $24.51 gas utility valuation, that would equate to a Fair Value of $67.43.
- Sum-of-the-parts analysis aside, we favor using dividend yield for water utilities. While we acknowledge that WTRG isn't a pure-play water utility, we believe its ability to increase and pay dividends is as predictable as any water utility in our coverage universe. Currently, the group average dividend yield (including WTRG) is 1.72%, but several water utilities are trading at our target yield of approximately 1.5%. Essential Utilities is currently trading at a yield of 2.15%, highest in the peer group. Given the Company's superior operating footprint (all constructive regulatory environments), we believe the forward earnings outlook is exceptionally strong and we expect the shares to trade to a 1.5% yield based on our 2022 estimated dividend of $1.05, which generates a Fair Value of $70. All-in, regardless of what valuation metric investors choose, the potential share values we've highlighted ($67 / $70) are both higher than yesterday's closing price of $46.76. We reiterate our BUY rating on WTRG shares and $70 Fair Value.

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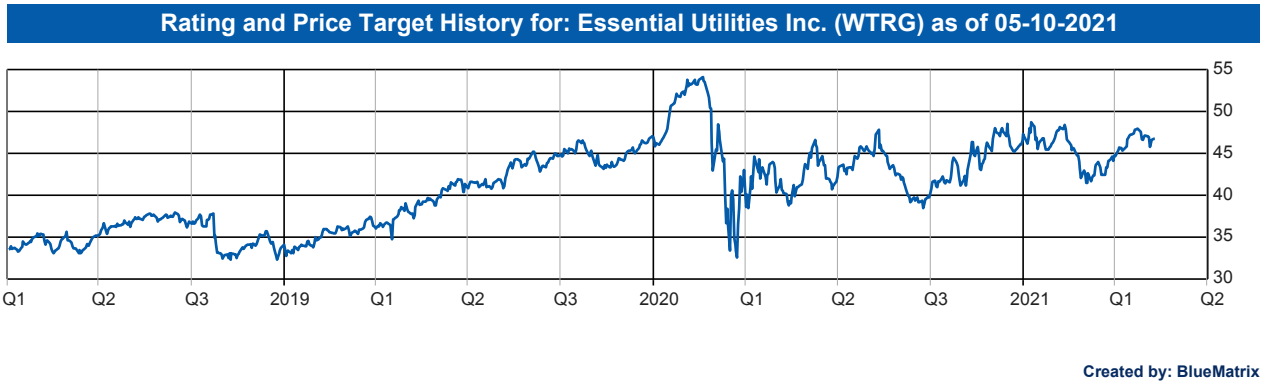
Price Charts



Janney Montgomery Scott Ratings Distribution as of 03/31/2021

			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	119	46.12	26	21.85
NEUTRAL [N]	105	40.70	7	6.67
SELL [S]	0	0.00	0	0
EXTENDED REVIEW [EXTRE]	34	13.18	10	29.41

*Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.

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Water Utilities

August 8, 2019

Aqua America, Inc. (WTR) - BUY

WTR: Solid Quarter, Strong Outlook; Maintain BUY Rating, $44 Fair Value

Price:	$42.06
Fair Value Estimate:	$44.00
52-Week Range:	$32.09 - $42.32
Market Cap (MM):	9,072
Shr.O/S-Diluted (mm):	215.7
Average Daily Volume:	1,024,918
Book Value:	$11.17
Dividend:	$0.94
Yield:	2.2%

FYE: Dec	2019E	2020E	2021E
EPS:	$1.50E	$1.56E	$1.70E
Prior EPS:	$1.39	$1.52	NC
P/E Ratio:	28.0x	27.0x	24.7x

Quarterly EPS:

Q1	$0.28A	$0.56E	$0.59E
Q2	$0.37A	$0.19E	$0.21E
Q3	$0.44E	$0.36E	$0.38E
Q4	$0.41E	$0.46E	$0.51E

Quarterly Revenue (M):

Q1	$201A	$681E	$706E
Q2	$219A	$392E	$408E
Q3	$357E	$380E	$397E
Q4	$560E	$596E	$618E
Year:	$1,345E	$2,048E	$2,129E

PORTFOLIO MANAGER BRIEF

WTR's 2Q19 results met expectations, with adjusted EPS of $0.37 meeting the consensus forecast. Quarterly results aside, new acquisition opportunities were a dominant topic during the 2Q conference call, and the pipeline of new opportunities appears to have grown substantially larger. We've made minor adjustments to our forward estimates based on the push-out of the Peoples Gas transaction (our estimates now include the combined entity beginning in 4Q19) and we maintain our BUY rating and $44 Fair Value on WTR shares.

ANALYST NOTES

- 2Q19 Results Inline with Expectations. At the top line, revenues of $219MM benefitted from growth ($4MM) and rates & surcharges ($4MM), with lower consumption providing somewhat of an offset (-$700K) and other items (-$300K). At the bottom line, adjusted EPS of $0.37 met the consensus forecast, but was below our $0.39 estimate.
- Potential Acquisition Opportunities Are Sizable (and Plentiful). Several large-scale acquisition opportunities have developed in Pennsylvania, which could add substantially to the company's size. During the quarter, WTR signed an exclusive agreement with DELCORA, a large municipal wastewater authority in southeastern PA serving 500K people in 42 municipalities. DELCORA and WTR have committed to exclusive discussions regarding DELCORA's potential acquisition. Also in play in Pennsylvania is the water, wastewater and stormwater systems for the City of Harrisburg, the state capital. Then there's the water system that comprises the Chester Water Authority, which Aqua America has pursued previously. A legal fight is taking place between the Authority and the City of Chester over who owns the assets; the city would like to entertain offers, the Authority wishes to stay independent. Overall, the acquisition environment continues to improve, aided by fair market value legislation across the company's geographic footprint.
- Summary/Valuation. With the Peoples Gas acquisition expected to close in the fall, we've already moved to combined estimates (Aqua + Peoples). We expect to continue to refine our forecasts as more information on timing and cost impacts become available, but we believe our estimates are reasonable given the data already available. The outlook for earnings growth (and dividend increases) looks particularly bright, and just on the base assets. Additional acquisitions of size (if they materialize) would likely add additional upside to our forecasts, given the company's disciplined approach when it comes to purchasing assets. In terms

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of valuation, WTR shares still have reasonable upside to our Fair Value of $44 (based on a P/E of 26x our 2021 EPS estimate of $1.70) , so we maintain our BUY rating, recommending investors add on dips, should they occur.

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Price Charts

Janney Montgomery Scott Ratings Distribution as of 06/30/2019

			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	179	55.59	40	22.35
NEUTRAL [N]	142	44.10	14	9.86
SELL [S]	1	0.31	0	0.00

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Water Utilities

September 18, 2019

Aqua America, Inc. (WTR) - BUY

DELCORA Acquisition Further Increases Pennsylvania Exposure; Reiterate BUY Rating, Fair Value to $50

Price:	$43.90
Fair Value Estimate:	$50.00
52-Week Range:	$32.09 - $45.50
Market Cap (MM):	9,474
Shr.O/S-Diluted (mm):	215.8
Average Daily Volume:	1,033,917
Book Value:	$17.73
Dividend:	$0.94
Yield:	2.1%

FYE: Dec	2019E	2020E	2021E
EPS:	$1.50E	$1.56E	$1.77E
Prior EPS:	NC	NC	$1.70
P/E Ratio:	29.3x	28.1x	24.8x

Quarterly EPS:			
Q1	$0.28A	$0.56E	$0.63E
Q2	$0.37A	$0.19E	$0.24E
Q3	$0.44E	$0.36E	$0.39E
Q4	$0.41E	$0.46E	$0.50E

Quarterly Revenue (M):			
Q1	$201A	$681E	$721E
Q2	$219A	$392E	$423E
Q3	$357E	$380E	$412E
Q4	$560E	$596E	$633E
Year:	$1,345E	$2,048E	$2,189E

PORTFOLIO MANAGER BRIEF

After the close yesterday, Aqua America announced its second large acquisition in the State of Pennsylvania within a one-year period. The company will pay $276.5MM for an estimated 165,000 retail wastewater customers from the Delaware County Regional Water Quality Control Authority (DELCORA). The announcement was widely anticipated, given previous disclosures that discussions were underway. We expect the deal to close in late 2020, and are making adjustments to our 2021 estimates to reflect anticipated benefits from the acquisition. We reiterate our BUY rating, and raise our Fair Value from $44 to $50, based on a P/E of 28x our 2021 EPS estimate of $1.77.

ANALYST NOTES

- DELCORA Acquisition As Good as it Gets. Pennsylvania has proven to be a target rich environment for Aqua America in terms of M&A, with the company once again announcing a sizable transaction. Following closely on the $4.3B Peoples Gas acquisition announcement, Aqua has come to terms with DELCORA, an expansive wastewater treatment system spanning 42 municipalities in the southeastern part of the state. The price ($276.5MM) looks very favorable, and given the number of estimated customers, likely will not generate goodwill. In the release, the company indicated the system needs $1.2B of investment through 2041, which amounts to meaningful CAPEX annually over the period. And of course, Aqua knows southeastern Pennsylvania extremely well, given its original roots dating back to its Philadelphia Suburban Corporation (previous ticker symbol PSC) days. We expect no problems with the transaction being approved by the Pennsylvania Public Utility Commission, and anticipate a closing in late 2020.
- Summary/Valuation. The last three sizable transactions - DELCORA, Peoples Gas and Limerick have all been in Aqua America's home state of Pennsylvania, which also happens to be the most constructive regulatory environment in the U.S., in our opinion. Returns are solid, the PAPUC has a great reputation of working with utilities to improve infrastructure and manage ratepayer costs, which we note cannot be said of all states across the country. We believe Aqua's demonstrated ability to significantly grow its presence (and future earnings) is worthy of a bump in its valuation, and we raise not only our 2021 EPS estimate, but our P/E multiple assumption. We reiterate our BUY rating and increase our Fair Value target from $44 to $50, based on a P/E of 28x our 2021 EPS estimate of $1.77.

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Price Charts

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Michael Gaugler 215-665-1359 mgaugler@janney.com

Water Utilities

November 5, 2019

Aqua America, Inc. (WTR) - BUY

WTR: 3Q19 Results Above Expectations; Maintain BUY Rating, $70 Fair Value

Price:	$43.56
Fair Value Estimate:	$70.00
52-Week Range:	$32.09 - $46.90
Market Cap (MM):	9,400
Shr.O/S-Diluted (mm):	215.8
Average Daily Volume:	1,151,504
Book Value:	$17.73
Dividend:	$0.94
Yield:	2.2%

FYE: Dec	2019E	2020E	2021E
EPS:	$1.47E	$1.56E	$1.70E
Prior EPS:	$1.50	NC	$1.77
P/E Ratio:	29.6x	27.9x	25.6x

Quarterly EPS:

Q1	$0.28A	$0.56E	$0.63E
Q2	$0.37A	$0.20E	$0.19E
Q3	$0.48A	$0.30E	$0.28E
Q4	$0.34E	$0.53E	$0.60E

EPS: adjusted

Quarterly Revenue (M):

Q1	$201A	$672E	$711E
Q2	$219A	$392E	$423E
Q3	$244A	$367E	$398E
Q4	$226E	$597E	$635E
Year:	$890E	$2,028E	$2,168E

PORTFOLIO MANAGER BRIEF

WTR's 3Q19 EPS results were above expectations, with adjusted EPS of $0.48 above the consensus forecast of $0.44. The company also reiterated its full year adjusted EPS guidance range of $1.45 to $1.50. With the Peoples Gas transaction now anticipated to close in 4Q19 or early 1Q20, we've removed Peoples Gas forecasts from our 4Q19 estimates (but are maintaining them for 1Q20). With both the Peoples Gas and DELCORA acquisitions moving forward, normal M&A activity and continuing rate relief, we see significant growth in the years ahead. Valuation remains attractive, as well; with the shares trading at a P/E 26x our 2021 EPS estimate of $1.70 and yielding 2.1% (highest in the peer group) we reiterate our BUY rating and $70 Fair Value.

ANALYST NOTES

- 3Q19 Adjusted EPS Results Ahead of Expectations. On the top line, revenues of $244MM were just below consensus of $250MM but higher YoY by 7.7% as rates, growth and volume all positively contributed. The company continues to experience higher O&M expenses due to the Peoples Gas transaction, which negatively impacted GAAP EPS of $0.38. Adjusted 3Q19 EPS was $0.48, 9.4% higher YoY and well above the Street estimate of $0.44.
- Major Acquisitions Still Awaiting Closing. The Peoples Gas transaction is expected to close in late 2019 or early 2020, while DELCORA is expected late 2020. For Peoples Gas, the Administrative Law Judge assigned to the case rendered a positive decision, and recommended the PA Public Utility Commission approve the acquisition. The DELCORA transaction also requires PAPUC approval.
- Regulatory Update. In the company's geographic operating footprint, its received annual rate increases totaling $59.8MM across Illinois, New Jersey, North Carolina, Ohio and Pennsylvania. Peoples Gas filed a settlement agreement in its PA rate case in July 2019, and the PAPUC authorized a $59.5MM increase on October 3, 2019. New rates become effective January 1, 2020.
- Summary/Valuation. Aqua's ability to continue executing acquisitions both large and small sets the stage for continued earnings growth in the years ahead. For both its gas and water assets, the pipeline of opportunities remains robust, and our positive investment thesis remains decidedly bullish. We maintain our BUY rating and $70 Fair Value, based on a P/E of 41x our 2021 EPS estimate of $1.70. We note the shares have the highest yield in the peer group (2.14%) and dividend growth should continue to be mid-to-high single digits for the foreseeable future.

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Price Charts

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			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	171	52.78	37	21.64
NEUTRAL [N]	151	46.60	20	13.25
SELL [S]	2	0.62	0	0.00

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Water Utilities

November 5, 2020

Essential Utilities Inc. (WTRG) - BUY

3Q20 Results Just Above Expectations; Maintain BUY Rating, $70 Fair Value

Price:	$41.19
Fair Value Estimate:	$70.00
52-Week Range:	$30.40 - $54.52
Market Cap (MM):	10,098
Shr.O/S-Diluted (mm):	245.2
Average Daily Volume:	1,230,398
Book Value:	$18.91
Dividend:	$1.00
Yield:	2.4%

FYE: Dec	2020E	2021E	2022E
EPS:	$1.58E	$1.67E	$1.78E
Prior EPS:	NC	NC	NC
P/E Ratio:	26.1x	24.7x	23.1x

Quarterly EPS:

Q1	$0.60A	$0.66E	$0.68E
Q2	$0.29A	$0.22E	$0.25E
Q3	$0.23A	$0.26E	$0.27E
Q4	$0.46E	$0.52E	$0.58E

EPS: adjusted

Quarterly Revenue (M):

Q1	$256A	$773E	$794E
Q2	$384A	$342E	$352E
Q3	$349A	$360E	$370E
Q4	$541E	$579E	$601E
Year:	$1,530E	$2,053E	$2,118E

PORTFOLIO MANAGER BRIEF

WTRG's 3Q20 adjusted EPS results were just above our expectations ($0.23 vs. $0.22) which was also consensus. The Company refined its guidance, as it now expects 2020 adjusted EPS at the upper end of its previously communicated $1.53 to $1.58 range (it also expects an earnings growth CAGR of 5-7% for 2019 thru 2022). We've made only minor adjustments to our 2020 & 2021 estimates, and introduced 2022 forecasts. We maintain our BUY rating and $70 Fair Value, based on a P/E of 39x our 2022 EPS estimate of $1.78.

ANALYST NOTES

- 3Q20 Results Just Above Expectations. On the top line, revenues of $349MM were just above our $342MM estimate (consensus was $347MM). The upside in our model surprisingly came from the Gas segment, as our estimates already factored in increased volumes in the Water segment due to the hot & dry summer. OPEX in the quarter came in roughly inline with our forecasts, and adjusted EPS of $0.23 was $0.01 above our and the consensus forecast of $0.22.
- Updated (And Refined) Guidance. For 2020, WTRG now sees adjusted EPS at the upper end of its $1.53 to $1.58 range. The Company expects an earnings growth CAGR of 5-7% for 2019 through 2022. CAPEX remains on track for $550MM for the Water segment in 2020 ($400MM for the Natural Gas segment, including investments made before WTRG ownership). Going forward, it sees $2.8B of infrastructure investment thru 2022.
- Adjusting 2020/2021 Estimates; Introducing 2022 Forecasts. We've made only minor adjustments to our 2020/2021 estimates; for 2020, we were already at the high end of the Company's $1.53 - $1.58 guidance range. We took the $0.01 of EPS from 4Q20 out of the Natural Gas segment; NOAA forecasts for the Northeast see continuing above normal temperatures through the middle of November.
- Summary/Valuation. A solid quarter, healthy M&A activity (with a robust pipeline of opportunities), strong CAPEX profile and attractive valuation are all reasons we recommend Essential Utilities shares at current price levels. We also note that shares yield 2.43%, the highest in the water utility peer group. We maintain our BUY rating and $70 Fair Value, which is based on a P/E of 39x our 2022 EPS estimate of $1.78.

RESEARCH ANALYST CERTIFICATIONS AND IMPORTANT DISCLOSURES ARE ON PAGES 2 - 3 OF THIS REPORT

IMPORTANT DISCLOSURES

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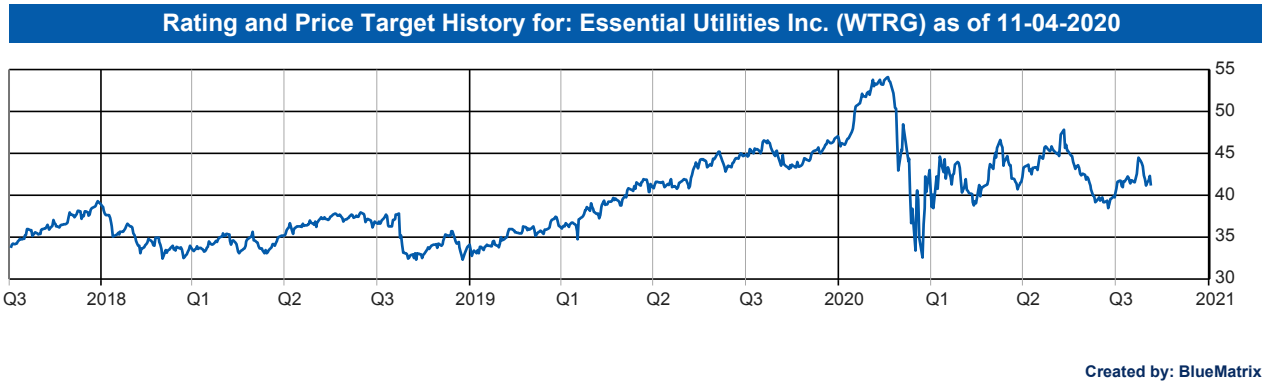

Janney Montgomery Scott Ratings Distribution as of 09/30/2020

			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	117	47.37	18	15.38
NEUTRAL [N]	130	52.63	11	8.46
SELL [S]	0	0.00	0	0.00

*Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.

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Michael Gaugler 215-665-1359 mgaugler@janney.com

Water Utilities

February 25, 2021

Essential Utilities Inc. (WTRG) - BUY

Strong Finish to 2020, Guidance For 2021 Compares Favorably; Reiterate BUY Rating, $70 Fair Value

Price:	$44.09
Fair Value Estimate:	$70.00
52-Week Range:	$30.40 - $52.00
Market Cap (MM):	10,815
Shr.O/S-Diluted (mm):	245.3
Average Daily Volume:	1,075,865
Book Value:	$18.90
Dividend:	$1.00
Yield:	2.3%

FYE: Dec	2020A	2021E	2022E
EPS:	$1.58A	$1.67E	$1.78E
Prior EPS:		NC	NC
P/E Ratio:	27.9x	26.4x	24.8x

Quarterly EPS:

Q1	$0.60A	$0.66E	$0.68E
Q2	$0.29A	$0.22E	$0.25E
Q3	$0.23A	$0.26E	$0.27E
Q4	$0.46A	$0.52E	$0.58E

EPS: adjusted

Quarterly Revenue (M):

Q1	$256A	$700E	$725E
Q2	$384A	$342E	$352E
Q3	$349A	$360E	$370E
Q4	$474A	$501E	$526E
Year:	$1,463A	$1,976E	$2,043E

PORTFOLIO MANAGER BRIEF

Essential Utilities 4Q20 adjusted EPS of $0.46 matched our estimate and was slightly ahead of consensus, and its 2021 EPS guidance range of $1.64 to $1.69 compares favorably to our our $1.67 forecast (also consensus). We've made minor adjustments to our forward estimates (see table, this page) and reiterate BUY rating and $70 Fair Value, based on a P/E of 39x our 2022 EPS estimate of $1.78. The shares yield 2.3%, highest in the water utility peer group.

ANALYST NOTES

- 4Q20 Adjusted EPS Met Expectations. On the top line, revenues of $474MM increased 109.7% YOY, benefitting from the Peoples Gas acquisition (+ $241MM) and increased volume, growth, rate and surcharge increases in the regulated water segment (+$10MM) while "other" items netted a -$3MM. On the bottom line, adjusted EPS of $0.46 matched our estimate and was a penny ahead of consensus.
- 2021 Guidance Update. For the full year, key guidance items include EPS ($1.64 to $1.69), EPS CAGR of 5% to 7% for 2020 through 2023, CAPEX of $550MM for the Water segment and $450MM for the Natural Gas segment. For the 2021 through 2023 period, CAPEX of $3B, which is expected to drive rate base compound annual growth of 6%-7% for the Water segment and 8% to 10% for the Natural Gas segment. Other items include Water segment customer growth of 2% to 3% (acquisitions and organic), reduction of Scope 1 and Scope 2 greenhouse gas emissions by 60% by 2035 and multiyear plans to achieve diverse supplier spend and employees of color.
- Regulatory Update. WTRG has received rate awards in NJ, NC, OH and PA of $8.5MM YTD. It has proceedings in VA and IN that would add an estimated $1.8MM in incremental revenues.
- Strong Acquisition Activity Continues. 2021 looks to be a very strong year for acquisitions, with the biggest announced transaction (DELCORA, 198K equivalent dwelling units) expected to receive a Pennsylvania Public Utility Commission (PAPUC) decision in March. All-in, Essential Utilities has six signed purchase agreements encompassing 227K equivalent dwelling units that will add $438MM in rate base when closed. The Company's pipeline of potential acquisitions represents 375K total water/wastewater customers. Its target for 2021 is to sign municipal deals totaling at least $100MM of rate base.

RESEARCH ANALYST CERTIFICATIONS AND IMPORTANT DISCLOSURES ARE ON PAGES 3 - 4 OF THIS REPORT

- Summary/Valuation. We remain perplexed as to why WTRG shares aren't trading at high price levels. The Company's executed in accordance with guidance, has a robust CAPEX plan for the next three years, expects 5%-7% earnings growth through 2023 and continues to close acquisitions of size, augmenting organic growth. Its regulatory risk is probably the lowest of any in the peer group with multi-state operations, and its yield at 2.3% is the highest. Within the water utility peer group, WTRG remains our top pick, and we reiterate our BUY rating and $70 Fair Value, based on a P/E of 39x our 2022 EPS estimate of $1.78. Our target yield for WTRG shares is 1.5% against an expected 2022 annualized dividend of $1.05.

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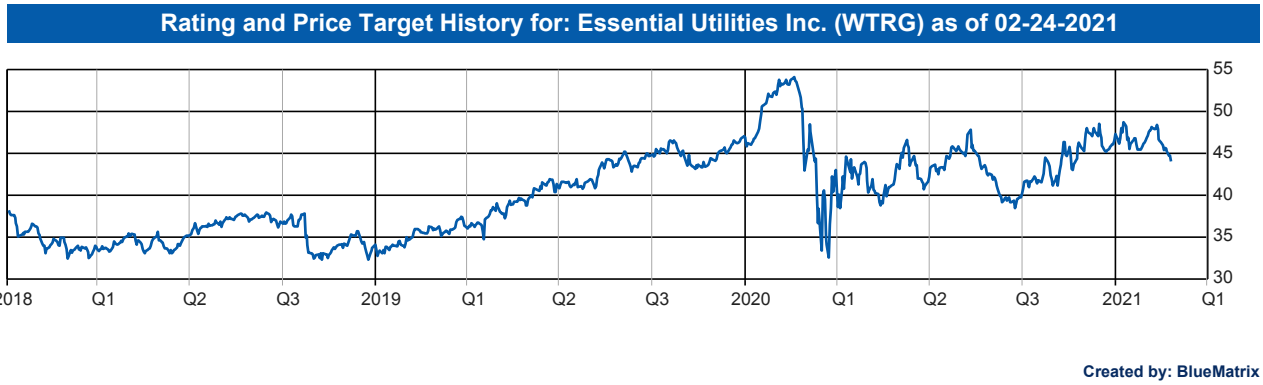
Price Charts



Janney Montgomery Scott Ratings Distribution as of 12/31/2020

			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	115	46.18	27	23.48
NEUTRAL [N]	134	53.82	16	11.94
SELL [S]	0	0.00	0	0.00

*Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.

Other Disclosures

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Water Utilities

February 28, 2020

Essential Utilities Inc. (WTRG) - BUY

4Q19 Results & 2020 Guidance On Target; Maintain BUY Rating, $70 Fair Value

Price:	$46.34
Fair Value Estimate:	$70.00
52-Week Range:	$34.79 - $54.52
Market Cap (MM):	9,999
Shr.O/S-Diluted (mm):	215.8
Average Daily Volume:	1,199,373
Book Value:	$17.90
Dividend:	$0.94
Yield:	2.0%

FYE: Dec	2019A	2020E	2021E
EPS:	$1.47A	$1.56E	$1.65E
Prior EPS:		NC	$1.70
P/E Ratio:	31.5x	29.7x	28.1x

Quarterly EPS:

Q1	$0.28A	$0.21E	$0.59E
Q2	$0.37A	$0.20E	$0.20E
Q3	$0.48A	$0.30E	$0.30E
Q4	$0.34A	$0.53E	$0.56E

EPS: adjusted

Quarterly Revenue (M):

Q1	$201A	$207E	$711E
Q2	$219A	$392E	$423E
Q3	$244A	$367E	$398E
Q4	$226A	$597E	$635E
Year:	$890A	$1,562E	$2,168E

PORTFOLIO MANAGER BRIEF

WTR's 4Q19 results met our expectations (top and bottom line), and forward proforma EPS guidance for 2020 was also on target. Looking forward, we've made minor adjustments to our forward estimates (see table, this page) and we maintain our BUY rating and $70 Fair Value on WTR shares.

ANALYST NOTES

- 4Q19 Results Met Expectations. Revenues of $226MM and adjusted EPS of $0.34 met our expectations (consensus was $222MM and $0.30, respectively). 4Q19 results for water utilities are a seasonally weak period and rarely impact water utility estimates or valuations.
- Peoples Gas Update; Just a Little Bit Longer. The Peoples Gas transaction is now expected to close on March 16, 2020, an unfortunate development given Q1 is the seasonally strongest period for Mid-Atlantic gas utilities.
- Long Awaited 2020 Guidance Arrives. Given the delays in closing the Peoples Gas transaction, Essential Utilities is offering pro-forma adjusted 2020 EPS guidance in a range of $1.53 to $1.58, which assumes ownership of Peoples Gas from January 1st (we assume management did this to provide a range of full year earnings potential and to aid analysts in modeling estimates). The company expects to see an EPS CAGR of 5%-7% over the next 3-year period.
- Adjusting Estimates. We made minor adjustments to our forward estimates (see table, this page). Those estimates are what we think the company will actually report on an adjusted basis, not pro-forma. Our proforma adjusted EPS is $1.56, with the difference between the two being the exclusion of gas results in 1Q20.
- Summary/Valuation. 4Q19 results and 2020 guidance turned out as anticipated. Rate case activity remains strong, with 3 states receiving rate awards and infrastructure surcharges totaling $4.8MM (the company has other rate activity pending in 4 states requesting $8.3MM). The acquisition pipeline remains full, and CAPEX trends are robust. 2020 is unfolding as we expected, which required minimal adjustments to estimates. In terms of valuation, we continue to forecast Essential's 2030 dividend at $1.93, which when pegged to our expected U.S. 10-year T-Note yield of 1.5%, generates a Fair Value of $70. We maintain our BUY rating on Essential Utilities.

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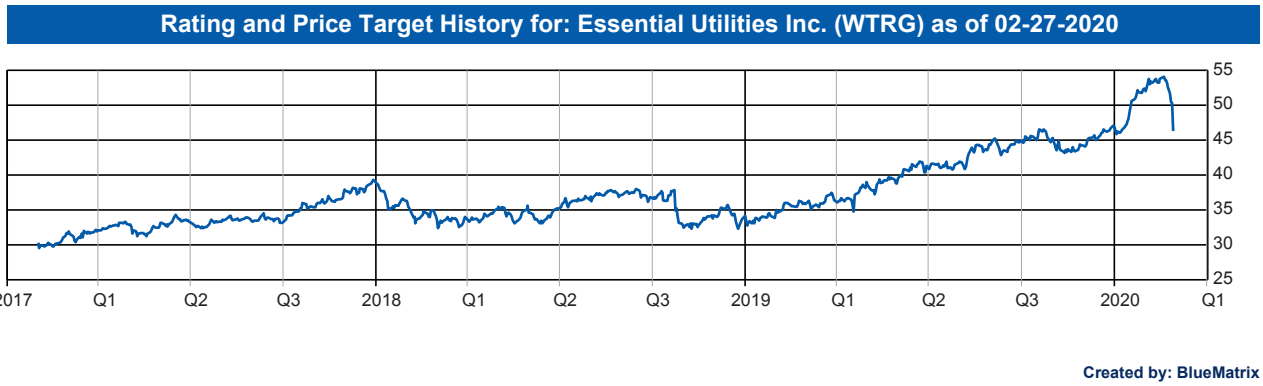

Janney Montgomery Scott Ratings Distribution as of 12/31/2019

			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	167	51.38	35	20.96
NEUTRAL [N]	157	48.31	23	14.65
SELL [S]	1	0.31	0	0.00

*Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.

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Water Utilities

March 5, 2020

Essential Utilities Inc. (WTRG) - BUY

Realigning 2020 Estimate Methodology; Maintain BUY Rating, $70 Fair Value

Price:	$48.45
Fair Value Estimate:	$70.00
52-Week Range:	$34.79 - $54.52
Market Cap (MM):	10,795
Shr.O/S-Diluted (mm):	222.8
Average Daily Volume:	1,309,471
Book Value:	$17.90
Dividend:	$0.94
Yield:	1.9%

FYE: Dec	2019A	2020E	2021E
EPS:	$1.47A	$1.56E	$1.65E
Prior EPS:		NC	NC
P/E Ratio:	33.0x	31.1x	29.4x

Quarterly EPS:

Q1	$0.28A	$0.53E	$0.59E
Q2	$0.37A	$0.20E	$0.20E
Q3	$0.48A	$0.30E	$0.30E
Q4	$0.34A	$0.53E	$0.56E

EPS: adjusted

Quarterly Revenue (M):

Q1	$201A	$207E	$711E
Q2	$219A	$392E	$423E
Q3	$244A	$367E	$398E
Q4	$226A	$597E	$635E
Year:	$890A	$1,562E	$2,168E

PORTFOLIO MANAGER BRIEF

Upon review of consensus forecasts for 2020, we are changing our 1Q20 EPS methodology from adjusted actual of $0.21 to pro-forma of $0.53 to prevent any confusion among investors. We made this distinction in our 2/28 note when we indicated our pro-forma EPS estimate for 2020 was $1.56, and there is no change in that regard. We are simply moving all of our 2020 estimates to pro-forma.

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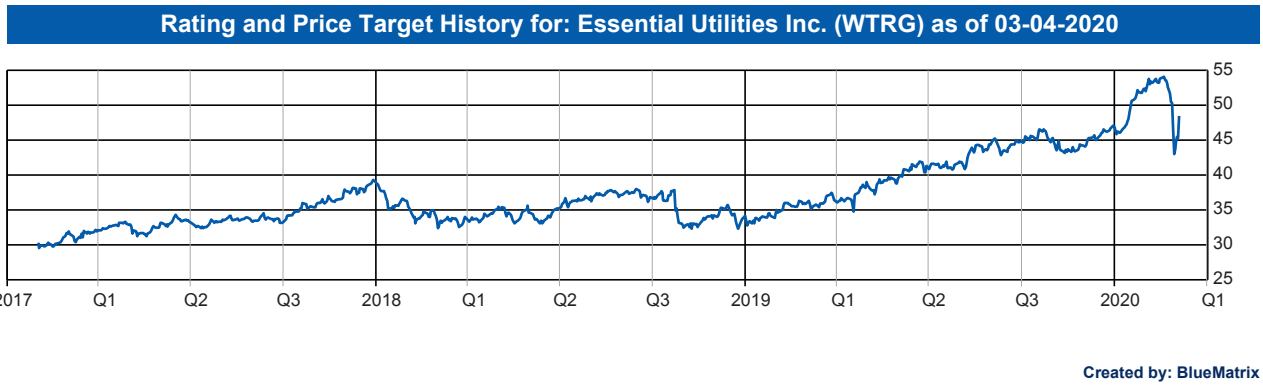

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			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	167	51.38	35	20.96
NEUTRAL [N]	157	48.31	23	14.65
SELL [S]	1	0.31	0	0.00

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Water Utilities

July 20, 2020

Essential Utilities Inc. (WTRG) - BUY

2Q20 Preview; Raising Estimates Due to Favorable Weather, Reiterate BUY Rating, $70 Fair Value

Price:	$44.71
Fair Value Estimate:	$70.00
52-Week Range:	$30.40 - $54.52
Market Cap (MM):	10,954
Shr.O/S-Diluted (mm):	245.0
Average Daily Volume:	1,139,007
Book Value:	$18.83
Dividend:	$0.94
Yield:	2.1%

FYE: Dec	2019A	2020E	2021E
EPS:	$1.47A	$1.58E	$1.67E
Prior EPS:		NC	$1.66
P/E Ratio:	30.4x	28.3x	26.8x

Quarterly EPS:

Q1	$0.28A	$0.60A	$0.66E
Q2	$0.37A	$0.28E	$0.23E
Q3	$0.48A	$0.24E	$0.26E
Q4	$0.34A	$0.46E	$0.52E

EPS: adjusted

Quarterly Revenue (M):

Q1	$201A	$256A	$773E
Q2	$219A	$352E	$342E
Q3	$244A	$342E	$360E
Q4	$226A	$541E	$579E
Year:	$890A	$1,491E	$2,053E

PORTFOLIO MANAGER BRIEF

We've increased our 2Q20 estimates materially (adjusted EPS from $0.23 to $0.28) based on favorable weather patterns for both the natural gas and water segments during the April-June time frame. Full year 2020 adjusted EPS guidance is currently $1.53 - $1.58; we see the potential for that range to tighten (to the upside) or be increased if favorable weather patterns continue. We maintain our BUY rating and $70 Fair Value on WTRG shares.

ANALYST NOTES

- Weather Should Positively Contribute to 2Q20 Results. April in the State of Pennsylvania was surprisingly cold, and we expect Essential's Peoples Gas segment results to benefit. We noted on the UGI Corp website UGI Corp weather that temperatures in April for its UGI Utilities segment (all in Pennsylvania) was 14% colder than normal in April and 23% colder in May.

  As Summer arrived, the weather changed quickly, and its been hot and dry through June and July. That should benefit Essential's water segment results, and we've raised our forecasts as a result. NOAA's 8-14 day outlook sees temperatures remaining above average across much of the United States, and a heatwave started this weekend in the Northeast.

- What Will WTRG Do With Full Year Guidance? Our previous 2Q20 adjusted EPS estimate was $0.23; now its $0.28. We were already at the high end of Company annual guidance before the change. 3Q20 weather is shaping up very nicely as well, with July hot and dry through the 19th, and the current NOAA forecast for that to continue through month-end. We've lowered our 4Q20 forecasts to remain within the Company's guidance range for the full year ($1.53 to $1.58), but we note that if we get a cold 4Q (like last year) WTRG is set-up to outperform its current guidance range.

- Summary/Valuation. Essential Utilities is off to good start in 2020. The closing of its Peoples Gas transaction, coupled with favorable weather patterns should allow it to deliver earnings at or above previous expectations. We still see plenty of upside to share prices; the 2.1% yield remains the highest in the water utility peer group, and with the U.S. 10YR T-Note yield 150bps lower, we continue to recommend accumulation at current levels. We reiterate our BUY rating and $70 Fair Value, based on a P/E of 42x our 2021 EPS estimate of $1.67 (which also equates to a 1.5% dividend yield in 2030 that assumes a 7.5% dividend CAGR).

RESEARCH ANALYST CERTIFICATIONS AND IMPORTANT DISCLOSURES ARE ON PAGES 2 - 3 OF THIS REPORT

IMPORTANT DISCLOSURES

Research Analyst Certification

I, Michael Gaugler, the Primarily Responsible Analyst for this research report, hereby certify that all of the views expressed in this research report accurately reflect my personal views about any and all of the subject securities or issuers. No part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views I expressed in this research report.

Janney Montgomery Scott LLC ("Janney") Equity Research Disclosure Legend

Essential Utilities Inc. currently is, or during the past 12 months was, a Janney Montgomery Scott LLC client. Janney Montgomery Scott LLC, provided investment banking related services.

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Janney Montgomery Scott LLC intends to seek or expects to receive compensation for investment banking services from Essential Utilities Inc. and UGI Corporation in the next three months.

The research analyst is compensated based on, in part, Janney Montgomery Scott's profitability, which includes its investment banking revenues.

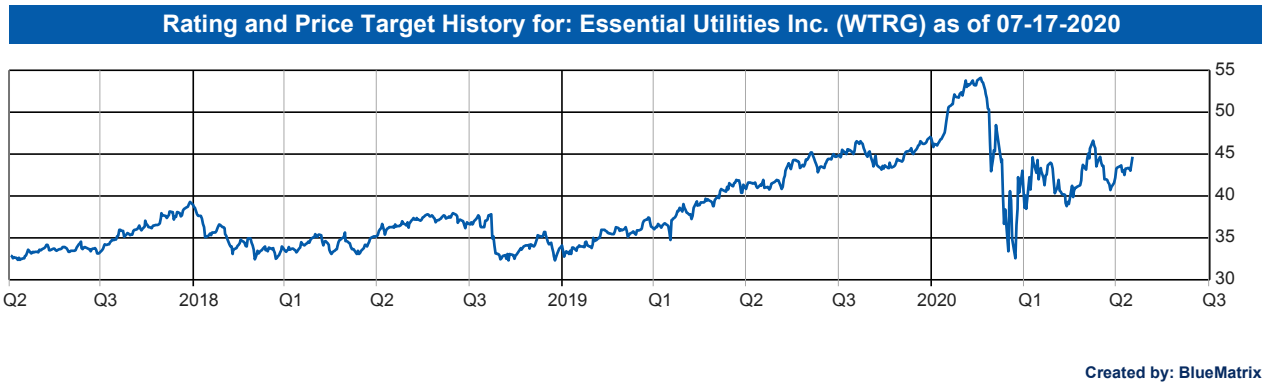
Definition of Ratings

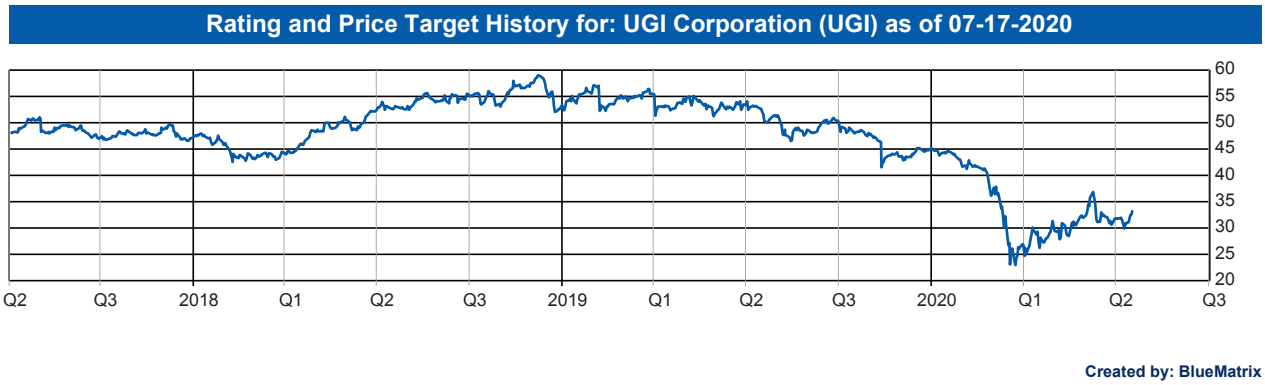
BUY: Janney expects that the subject company will appreciate in value. Additionally, we expect that the subject company will outperform comparable companies within its sector.

NEUTRAL: Janney believes that the subject company is fairly valued and will perform in line with comparable companies within its sector. Investors may add to current positions on short-term weakness and sell on strength as the valuations or fundamentals become more or less attractive.

SELL: Janney expects that the subject company will likely decline in value and will underperform comparable companies within its sector.

Price Charts





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Janney Montgomery Scott Ratings Distribution as of 06/30/2020

			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	116	46.40	26	22.41
NEUTRAL [N]	133	53.20	21	15.79
SELL [S]	1	0.40	0	0.00

*Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.

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This report is for your information only and is not an offer to sell or a solicitation of an offer to buy the securities or instruments named or described in this report. Interested parties are advised to contact the entity with which they deal or the entity that provided this report to them, should they desire further information. The information in this report has been obtained or derived from sources believed by Janney Montgomery Scott LLC, to be reliable. Janney Montgomery Scott LLC, however, does not represent that this information is accurate or complete. Any opinions or estimates contained in this report represent the judgment of Janney Montgomery Scott LLC at this time and are subject to change without notice.

Investment opinions are based on each stock's 6-12 month return potential. Our ratings are not based on formal price targets, however, our analysts will discuss fair value and/or target price ranges in research reports. Decisions to buy or sell a stock should be based on the investor's investment objectives and risk tolerance and should not rely solely on the rating. Investors should read carefully the entire research report, which provides a more complete discussion of the analyst's views. Supporting information related to the recommendation, if any, made in the research report is available upon request.

Michael Gaugler 215-665-1359 mgaugler@janney.com

Water Utilities

August 7, 2020

Essential Utilities Inc. (WTRG) - BUY

Quarterly Results Above Expectations; Reiterate BUY Rating, $70 Fair Value

Price:	$45.56
Fair Value Estimate:	$70.00
52-Week Range:	$30.40 - $54.52
Market Cap (MM):	11,164
Shr.O/S-Diluted (mm):	245.0
Average Daily Volume:	1,148,358
Book Value:	$18.83
Dividend:	$1.00
Yield:	2.2%

FYE: Dec	2019A	2020E	2021E
EPS:	$1.47A	$1.58E	$1.67E
Prior EPS:		NC	NC
P/E Ratio:	31.0x	28.8x	27.3x

Quarterly EPS:

Q1	$0.28A	$0.60A	$0.66E
Q2	$0.37A	$0.29A	$0.23E
Q3	$0.48A	$0.22E	$0.26E
Q4	$0.34A	$0.47E	$0.52E

EPS: adjusted

Quarterly Revenue (M):

Q1	$201A	$256A	$773E
Q2	$219A	$352E	$342E
Q3	$244A	$342E	$360E
Q4	$226A	$541E	$579E
Year:	$890A	$1,491E	$2,053E

PORTFOLIO MANAGER BRIEF

WTRG's 2Q20 results exceeded our and consensus expectations both on the top and bottom line. Favorable weather and higher consumption patterns among residential customers offset negative impacts from COVID-19 across C&I segments, and with 3Q weather patterns that have been hot and dry (excluding Monday's wild storm across much of the Company's service territory), the set-up is there for WTRG to meet (or exceed) the top end of its 2020 guidance range, which it reaffirmed. We reiterate our BUY rating and $70 Fair Value, based on a P/E of 42x our 2021 EPS estimate of $1.67. We continue to use estimated dividend growth over a 10-year period pegged to a 1.5% U.S. 10-year T-Note yield to derive our valuation and corresponding P/E multiple.

ANALYST NOTES

- Nothing but Good News in 2Q. On the top line, revenues of $384MM were well above our forecast of $352MM (consensus was $371MM) as favorable weather (for both the natural gas and water segments) and higher residential water consumption offset negative impacts across the commercial and industrial segments. On the bottom line, EPS of $0.29 was just a touch above our $0.28 estimate, but well above consensus of $0.23.
- Acquisitions and CAPEX Tracking to Plan. Acquisitions and organic growth in 1H20 increased the company's customer count by 1.2% (full year target is 2-3%, all in the water segment). Essential has signed purchase agreements that will add the equivalent of over 200,000 water & wastewater customers ($300MM of rate base). The bulk of that growth is tied to its planned DELCORA acquisition, which is expected to close in early 2021. In terms of investments, $293MM in 1H20 thus far, with a target of $550MM in the Water segment. For the natural gas operations, $400MM is planned for 2020 (including capital invested prior to ownership).
- Dividend Increased 7%. Essential Utilities began the week by announcing a 7% dividend increase on Monday, inline with our previous expectations. We watch dividend increases closely, given we set our Fair Value assumptions based on dividend CAGR's aligned with an anticipated US 10YR TNOTE yield of 1.5% in 2030.
- Guidance Maintained. For full year 2020, the guidance highlights are: adjusted EPS in the range of $1.53 to $1.58, earnings growth CAGR of 5-7% for the 2019-2022 time period, and CAPEX of $2.8B through 2022.

RESEARCH ANALYST CERTIFICATIONS AND IMPORTANT DISCLOSURES ARE ON PAGES 3 - 4 OF THIS REPORT

- Summary/Valuation. Essential's first full quarter owning Peoples Gas generated better-than-expected results, which will likely boost investor confidence that it can hit its financial targets and integrate big acquisitions without hiccups. That should lead to expanded valuation metrics and higher share prices. The set-up for WTRG to outperform in 3Q is in place; weather has been near-perfect since the start of the quarter July 1st (excluding Monday's torrential rains up and down the East Coast); NOAA's 8-14 day weather forecasts are calling for a continuation of the trend in the Mid-Atlantic region, where the Company has significant customer concentrations. We reiterate our BUY rating and $70 Fair Value, based on a P/E of 42x our 2021 EPS estimate of $1.67. We continue to use estimated dividend growth over a 10-year period pegged to a 1.5% U.S. 10-year T-Note yield to derive our valuation and corresponding P/E multiple. Our anticipated dividend CAGR over the period is 7.5%.

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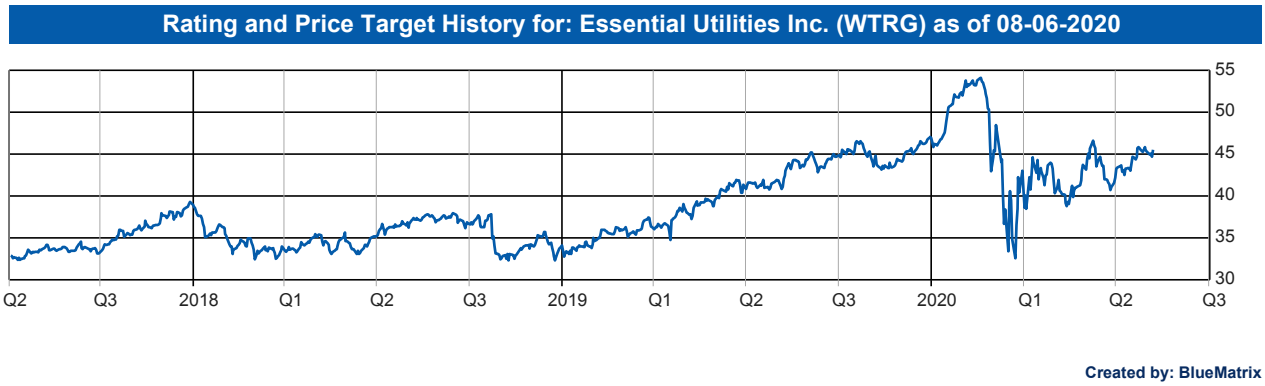

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1 July 2019

United States

EQUITIES

WTR US
Price (at 03:06, 29 Jun 2019 GMT)

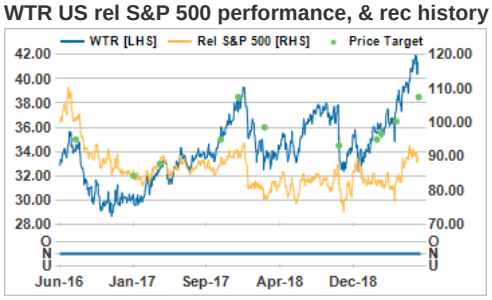
Neutral
US$41.37

Valuation - PER	US$	38.50
12-month target	US$	38.50
12-month TSR	%	-4.7
GICS sector		Utilities
Market cap	US$m	8,925
30-day avg turnover	US$m	40.8
Number shares on issue	m	215.7

Investment fundamentals

Year end 31 Dec		2018A	2019E	2020E	2021E
EPS adj	US$	1.41	1.30	1.51	1.65
EPS adj growth	%	4.5	-7.5	16.0	9.1
PER adj	x	29.4	31.8	27.4	25.1
Total DPS	US$	0.85	0.91	0.97	1.04
Total div yield	%	2.0	2.2	2.3	2.5

WTR US rel S&P 500 performance, & rec history



Note: Recommendation timeline - if not a continuous line, then there was no Macquarie coverage at the time or there was an embargo period.
Source: FactSet, Macquarie Research, July 2019
(all figures in USD unless noted)

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Aqua America (WTR US)
Not all news is good news

Key points

- Merger settlement is opposed by PAPUC's Staff.
- Peoples' gas settlement is only partial and doesn't seem to include a repair tax deduction.
- We remain on the sidelines, but boost TP to US$38.50 from US$36.50.

Event

- WTR (and AWK) have benefitted from nationalization concerns surrounding UK water utilities. Regulatory updates on WTR's pending merger with Peoples have been mixed, and so far the utilities haven't received even a tentative approval to use a repair tax deduction at Peoples. The latter seems essential for WTR to offer a positive earnings surprise for 2020 and beyond.

Impact

- **Non-unanimous merger settlement:** In early June, WTR agreed to a settlement in the Peoples merger with all but two interveners in the proceeding. The Staff of the PA PUC (I&E) disputes Peoples' treatment of a rural gas system of 1,600 connections (Goodwin/Tombaugh Gathering System), which for years has experienced gas leaks. WTR has agreed to spend US$120m in capex on the system and the spending would be recoverable through general rate cases. The I&E should present their position on the Goodwin/Tombaugh system on July 10, but for now we believe that the Staff wanted the system to be removed from Peoples' rate base and for the customers to be converted to propane, likely at Peoples' unrecoverable expense. WTR now expects an ALJ decision in late summer and the PAPUC decision by Oct/Nov.
- **Gas rate case settlement:** On Friday, Peoples reached a settlement in its pending gas rate case in PA. The settlement happened sooner than we had expected, though cancelled rate case hearings in late June suggested a settlement was imminent. We are waiting for the settlement to be made public, but for now it's our understanding that a main line replacement was excluded from the settlement and will continue to be litigated. Also, the rate case settlement doesn't seem to include any references to a future election of the repair tax deduction, which is essential to accelerate WTR's EPS growth following the Peoples deal.

Earnings and target price revision

- We updated our estimates to reflect the Peoples merger closing in late October. Our new '19/'20/'21 EPS estimates are US$1.30/1.51/1.65 vs US$1.47/1.54/1.62, respectively. We raised our TP to US$38.50 from US$36.50 to reflect a higher '21 anchor PEs for regulated water/gas utilities. Our new TP is based on 24.1x '21E water EPS plus 21.4x '21E gas EPS. Our previous TP was based on 22.8x '21E water EPS plus 21.0x '21E gas EPS.

Price catalyst

- 12-month price target: US$38.50 based on a PER methodology.
- Catalyst: Update on repair tax deduction for Peoples; 2019/2020 EPS guidance.

Action and recommendation

- We reiterate our Neutral rating.

Please refer to page 4 for important disclosures and analyst certification, or on our website www.macquarie.com/research/disclosures.

bcobrien@aquaamerica.com Ben O'Brien 07/01/19 02:00:16 PM Aqua America Inc

Fig 1 WTR: EPS proforma pending Peoples merger

	2019	2020	2021	2022
Water net income (US$m)	261.87	274.25	288.13	305.00
Gas net income (US$m)	48.14	146.16	167.76	184.54
Incremental parent interest expense after tax (US$m)	-10.5	-31.9	-31.6	-36.0
Total EPS (US$)	1.30	1.51	1.65	1.76
S/O (m)	231	257	257	257
EPS accretion vs standalone EPS (US$)	-0.17	-0.03	0.04	0.06
Water EPS	87%	71%	68%	67%
Gas EPS	13%	29%	32%	33%
Water EPS (US$)	1.13	1.07	1.12	1.19
Water PE multiple		25.3x	24.1x	22.8x
Equity value of water per share		26.95	26.96	27.11
Gas EPS (US$)	0.16	0.44	0.53	0.58
Gas PE multiple		23.1x	21.4x	19.7x
Equity value of gas per share		10.27	11.33	11.37
Total equity value per share ($)		**37.22**	**38.29**	**38.49**

Source: Macquarie Capital (USA), July 2019

Fig 2 WTR: Financial projections (US$ m except per-share data)

	2018	2019E	2020E	2021E
EBITDA	470	606	764	820
EBIT	323	454	601	648
Net interest expense	99	125	163	162
Ordinary Profit Before Tax	252	352	461	509
Income tax	1	51	73	85
Net profit	251	301	388	423
S/O (m)	**178**	**231**	**257**	**257**
Diluted EPS	**1.41**	**1.30**	**1.51**	**1.65**
DPS	**0.85**	**0.91**	**0.97**	**1.04**
Cash	5	5	5	5
Receivables	101	128	148	156
Inventory	14	18	18	18
Other short-term assets	16	16	16	16
Other-long term assets	801	801	801	801
Property, plant, and equipment	5,808	6,206	6,473	6,731
Total assets	**6,746**	**7,174**	**7,461**	**7,727**
Financial liabilities	117	117	117	117
Operating liabilities	64	81	82	84
Other liabilities	108	108	108	108
Deferred credits	2,096	2,110	2,124	2,138
Long-term debt	1,975	2,254	2,248	2,489
Shareholders' equity	2,385	2,503	2,781	2,791
Total liabilities and equity	**6,746**	**7,174**	**7,461**	**7,727**
Net income	251	301	388	423
D&A, goodwill amortisation	147	152	163	172
Other non-cash elements	25	25	25	25
Funds from operations	423	478	577	621
Non-cash working capital	8	43	22	9
Operating cash flow	430	522	599	630
Net investments in fixed assets	-555	-550	-430	-430
Net investments in financial assets	0	0	0	0
Free cash flow before dividends	-125	-28	169	200
Dividends paid	-151	-210	-250	-268
Free cash flow after dividends	-276	-238	-81	-67
Changes in capital	2	2	2	2
Changes in financial debt	273	235	78	64
Adjustment for minorities / miscellaneous	1	1	1	1
Increase in cash	1	0	0	0

Source: Company data, Macquarie Capital (USA), July 2019

Other stock mentioned: American Water Works (AWK US, US$116, Outperform, TP US$121)

bcobrien@aquaamerica.com Ben O'Brien 07/01/19 02:00:16 PM Aqua America Inc

Macquarie Quant Alpha Model Views

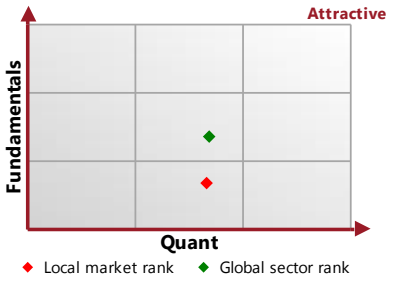
The Quant View page below has been derived from models that are developed and maintained by Sales and Trading personnel at Macquarie. The models are not a product of the Macquarie Research Department.

The quant model currently holds a marginally positive view on Aqua America. The strongest style exposure is Price Momentum, indicating this stock has had strong medium to long term returns which often persist into the future. The weakest style exposure is Valuations, indicating this stock is over-priced in the market relative to its peers.

197/448

Global rank in Utilities

% of BUY recommendations	67% (6/9)
Number of Price Target downgrades	0
Number of Price Target upgrades	2

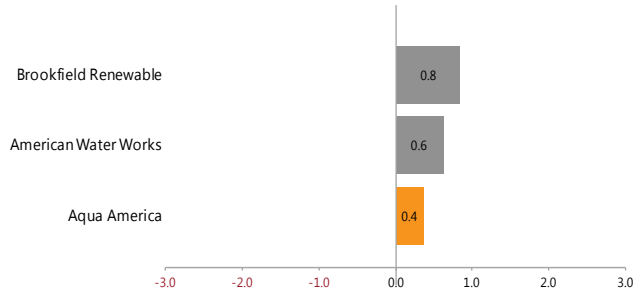


Displays where the company's ranked based on the fundamental consensus Price Target and Macquarie's Quantitative Alpha model.

Two rankings: Local market (United States) and Global sector (Utilities)

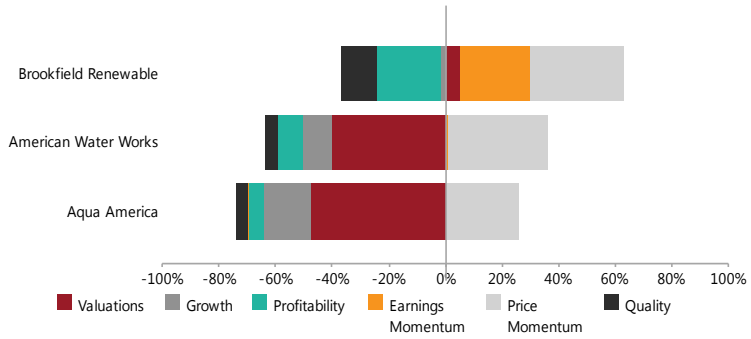
Macquarie Alpha Model ranking

A list of comparable companies and their Macquarie Alpha model score (higher is better).



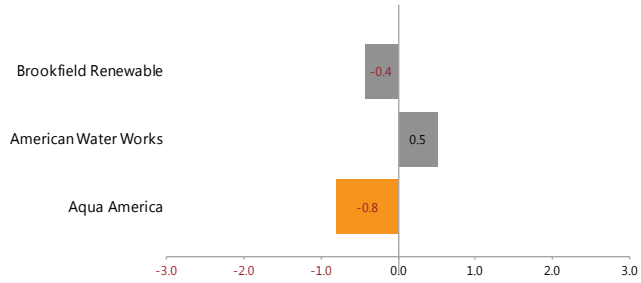
Factors driving the Alpha Model

For the comparable firms this chart shows the key underlying styles and their contribution to the current overall Alpha score.



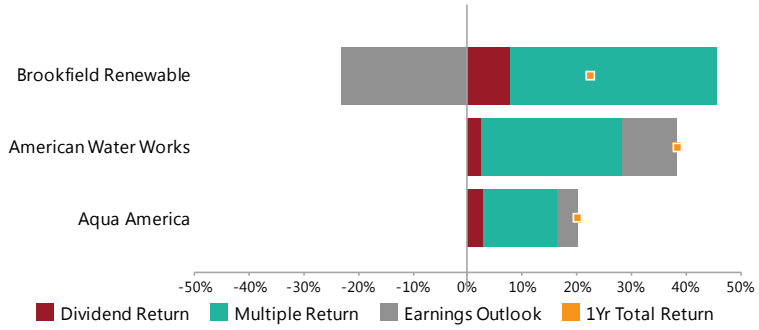
Macquarie Earnings Sentiment Indicator

The Macquarie Sentiment Indicator is an enhanced earnings revisions signal that favours analysts who have more timely and higher conviction revisions. Current score shown below.



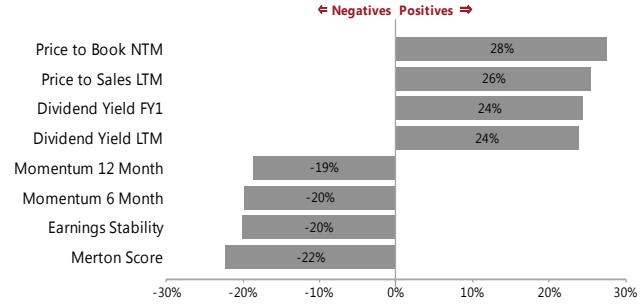
Drivers of Stock Return

Breakdown of 1 year total return (local currency) into returns from dividends, changes in forward earnings estimates and the resulting change in earnings multiple.



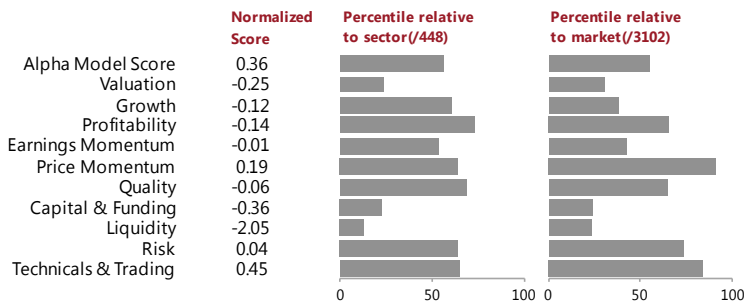
What drove this Company in the last 5 years

Which factor score has had the greatest correlation with the company's returns over the last 5 years.



How it looks on the Alpha model

A more granular view of the underlying style scores that drive the alpha (higher is better) and the percentile rank relative to the sector and market.



Source (all charts): FactSet, Thomson Reuters, and Macquarie Quant. For more details on the Macquarie Alpha model or for more customised analysis and screens, please contact the Macquarie Global Quantitative/Custom Products Group (cpg@macquarie.com)

bcobrien@aquaamerica.com Ben O'Brien 07/01/19 02:00:16 PM Aqua America Inc

Important disclosures:

Recommendation definitions

Macquarie – Asia, USA, Europe and Mazi Macquarie (SA):
Outperform – expected return >10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie - Australia/New Zealand
Outperform – expected return >10%
Neutral – expected return from 0% to 10%
Underperform – expected return <0%

Note: expected return is reflective of a Medium Volatility stock and should be assumed to adjust proportionately with volatility risk

Volatility index definition*

This is calculated from the volatility of historical price movements.

Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

Medium – stock should be expected to move up or down at least 30–40% in a year.

Low–medium – stock should be expected to move up or down at least 25–30% in a year.

Low – stock should be expected to move up or down at least 15–25% in a year.
* Applicable to select stocks in Asia/Australia/NZ

Recommendations – 12 months
Note: Quant recommendations may differ from Fundamental Analyst recommendations

Financial definitions

All "Adjusted" data items have had the following adjustments made:
Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
Excluded: non-recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

EPS = adjusted net profit / efpowa*
ROA = adjusted ebit / average total assets
ROA Banks/Insurance = adjusted net profit /average total assets
ROE = adjusted net profit / average shareholders' funds
Gross cashflow = adjusted net profit + depreciation
*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

Recommendation proportions – For quarter ending 31 March 2019

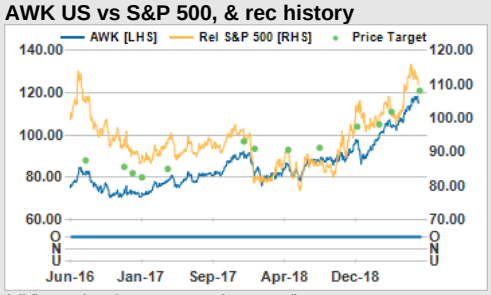
	AU/NZ	Asia	RSA	USA	CA	EUR	
Outperform	48.45%	56.50%	47.06%	51.94%	68.53%	51.76%	(for global coverage by Macquarie, 3.69% of stocks followed are investment banking clients)
Neutral	35.27%	30.15%	32.94%	42.78%	24.48%	38.19%	(for global coverage by Macquarie, 2.76% of stocks followed are investment banking clients)
Underperform	16.28%	13.35%	20.00%	5.28%	6.99%	10.05%	(for global coverage by Macquarie, 0.89% of stocks followed are investment banking clients)

Note: This table does not reflect the announced cessation of research services effective April 29, 2019, through our affiliate Macquarie Capital Markets Canada Ltd.

WTR US vs S&P 500, & rec history

(all figures in USD currency unless noted)

AWK US vs S&P 500, & rec history



(all figures in USD currency unless noted)

Note: Recommendation timeline – if not a continuous line, then there was no Macquarie coverage at the time or there was an embargo period.
Source: FactSet, Macquarie Research, July 2019

12-month target price methodology

WTR US: US$38.50 based on a PER methodology

AWK US: US$121.00 based on a Sum of Parts methodology

Company-specific disclosures:

Important disclosure information regarding the subject companies covered in this report is available at www.macquarie.com/research/disclosures.

Date	Stock Code (BBG code)	Recommendation	Target Price
01-Jul-2019	WTR US	Neutral	US$38.50
22-Apr-2019	WTR US	Neutral	US$36.50
06-Mar-2019	WTR US	Neutral	US$35.50
20-Feb-2019	WTR US	Neutral	US$35.00
24-Oct-2018	WTR US	Neutral	US$34.50
05-Mar-2018	WTR US	Neutral	US$36.00
12-Dec-2017	WTR US	Neutral	US$38.50
18-Oct-2017	WTR US	Neutral	US$35.00
11-Apr-2017	WTR US	Neutral	US$33.00
18-Jan-2017	WTR US	Neutral	US$32.00
21-Jul-2016	WTR US	Neutral	US$35.00

Target price risk disclosures:
WTR US: Our US$38.50 TP is based on 25x our proforma '21 water EPS and 21.2x proforma '21 gas EPS. Risks include: regulatory conditions for the Peoples acquisition, outcomes of pending and future rate cases, especialy in PA, cost controls, municipal M&A, and the level of market interest rates.
AWK US: Our US$111 TP is based on our 2021 SOTP. Risks to the downside include: the slower pace of future municipal acquisitions, lower cost efficiencies, and slower growth in non-regulated operations.

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Analyst certification:
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This publication was disseminated on 01 July 2019 at 07:34 UTC.

8 August 2019

United States

EQUITIES

WTR US
Price (at 22:52, 07 Aug 2019 GMT)

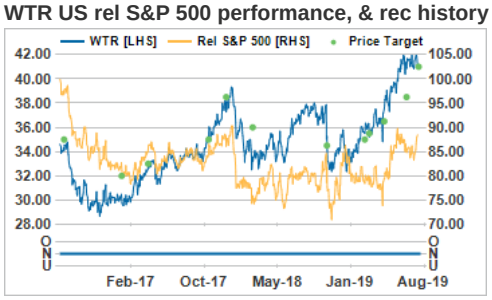
Neutral
US$42.06

Valuation - PER	US$	41.44
12-month target	US$	41.00
12-month TSR	%	-0.3
GICS sector		Utilities
Market cap	US$m	9,072
30-day avg turnover	US$m	37.3
Number shares on issue	m	215.7

Investment fundamentals

Year end 31 Dec		2018A	2019E	2020E	2021E
EPS adj	US$	1.41	1.30	1.54	1.68
EPS adj growth	%	4.5	-7.3	17.8	9.1
PER adj	x	29.9	32.3	27.4	25.1
Total DPS	US$	0.85	0.91	0.97	1.04
Total div yield	%	2.0	2.2	2.3	2.5

WTR US rel S&P 500 performance, & rec history



Note: Recommendation timeline - if not a continuous line, then there was no Macquarie coverage at the time or there was an embargo period.
Source: FactSet, Macquarie Research, August 2019
(all figures in USD unless noted)

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Aqua America (WTR US)
Pipe dream

Key points

- As a pure-play water utility, WTR would likely be trading 12% higher than currently.
- Peoples deal seemed based on repair tax deduction, but WTR is still studying it.
- Then again, repair tax deduction would just pull forward future earnings.

Event

- We've been watching WTR's pursuit of a gas utility from afar. For now, it seems like WTR's stock would likely be trading 12% higher than currently if the company had just remained a pure-play water utility. The repair tax deduction at Peoples Gas in PA could change the math, but that's likely months away.
- WTR's 2Q19 EPS of US$0.37 was in line with consensus, but excluded a US$0.02 dilution related to the higher share count associated with the Peoples deal. Inclusive of the dilution, WTR's results were in line with our US$0.35 expectation.

Impact

- **A trade-off between PE and EPS growth:** For the five years before the Peoples deal announcement, WTR traded on par with AWK on FY2 PE, though WTR grew EPS at a 4% CAGR over this period and AWK at almost 9%. If WTR had remained a pure-play water utility growing at 4-4.5% annually and the PE parity persisted, we estimate WTR would now be trading at ~US$47/share or almost 12% higher than yesterday's close. WTR currently trades at a 10% '20 PE discount to AWK on our US$1.54/sh '20 proforma EPS, though the deal is EPS neutral then.
- **Repair tax deduction at Peoples:** The diversification into the gas sector was widely expected to weigh on WTR's PE multiple, but in exchange was to align WTR's EPS growth with the 7% water rate base growth, which should happen by '21, we believe. The growth rate could be even higher depending on the repair tax deduction in PA for Peoples, but for now the US$265m (and counting) in deal fees hasn't created much shareholder value, we believe. Peoples Gas' rate case settlement in PA does not include a repair tax deduction, and WTR plans to pursue it only in '20 once it completes the assessment of how much of Peoples' capex would qualify for repair tax expensing. The repair tax was likely the core assumption underpinning the deal's EPS accretion.

Earnings and target price revision

- We raise our estimates to reflect a lower fully diluted share count assuming conversions of tangible equity units at higher stock prices. Our new '19/'20/'21 EPS estimates are US$1.30/1.54/1.68 vs US$1.30/1.51/1.65 previously. We raise our TP to US$41 from US$38.50. The TP remains based on 1.4x our '21 PE anchor for electric utilities for water and 1.2x for WTR's gas business.

Price catalyst

- 12-month price target: US$41.00 based on a PER methodology.
- Catalyst: Analyst day (Dec 5).

Action and recommendation

- We reiterate our Neutral rating.

Please refer to page 4 for important disclosures and analyst certification, or on our website www.macquarie.com/research/disclosures.

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Fig 1 WTR: EPS proforma pending Peoples merger

	2019E	2020E	2021E	2022E
Water net income (US$m)	261.87	274.25	288.13	305.00
Gas net income (US$m)	48.14	146.16	167.76	184.54
Incremental parent interest expense after tax (US$m)	-10.5	-31.9	-31.6	-36.0
Total EPS (US$)	1.30	1.54	1.68	1.79
S/O (m)	230	253	253	253
EPS accretion vs standalone EPS (US$)	-0.16	0.00	0.06	n/a
Water EPS	87%	71%	68%	67%
Gas EPS	13%	29%	32%	33%
Water EPS (US$)	1.14	1.08	1.14	1.21
Water PE multiple		27.2x	25.9x	24.6x
Equity value of water per share		29.48	29.50	29.66
Gas EPS (US$)	0.16	0.45	0.54	0.59
Gas PE multiple		23.8x	22.2x	20.6x
Equity value of gas per share		10.73	11.95	12.12
Total equity value per share		**40.21**	**41.44**	**41.78**

Source: Macquarie Capital (USA), August 2019

Fig 2 WTR: Financial projections (US$m except per share data)

	2018	2019E	2020E	2021E
EBITDA	470	605	765	821
EBIT	323	453	602	649
Net interest expense	99	125	163	162
Ordinary Profit Before Tax	252	351	462	510
Income tax	1	51	74	85
Net profit	251	300	389	424
S/O (m)	**178**	**230**	**253**	**253**
Diluted EPS	**1.41**	**1.30**	**1.54**	**1.68**
DPS	**0.85**	**0.91**	**0.97**	**1.04**
Cash	5	716	293	5
Receivables	101	128	148	156
Inventory	14	18	18	18
Other short-term assets	16	16	16	16
Other-long term assets	801	801	801	801
Property, plant, and equipment	5,808	6,206	6,473	6,731
Total assets	**6,746**	**7,884**	**7,749**	**7,727**
Financial liabilities	117	117	117	117
Operating liabilities	64	81	82	84
Other liabilities	108	108	108	108
Deferred credits	2,096	2,110	2,124	2,138
Long-term debt	1,975	2,254	2,248	1,904
Shareholders' equity	2,385	3,214	3,069	3,376
Total liabilities and equity	**6,746**	**7,884**	**7,749**	**7,727**
Net income	251	300	389	424
D&A, goodwill amortisation	147	152	163	172
Other non cash elements	25	25	25	25
Funds from operations	423	477	577	622
Non-cash working capital	8	43	22	9
Operating cash flow	430	521	600	631
Net investments in fixed assets	-555	-550	-430	-430
Net investments in financial assets	0	0	0	0
Free cash flow before dividends	-125	-29	170	201
Dividends paid	-151	-209	-246	-263
Free cash flow after dividends	-276	-238	-76	-62
Changes in capital	2	1,298	2	2
Changes in financial debt	273	-350	-350	-228
Adjustment for minorities / miscellaneous	1	1	1	1
Increase in cash	1	711	-423	-288

Source: Company data, Macquarie Capital (USA), August 2019

Stocks mentioned:

American Water Works (AWK US, US$117.42, Outperform, TP: US$121.00)

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Macquarie Quant Alpha Model Views

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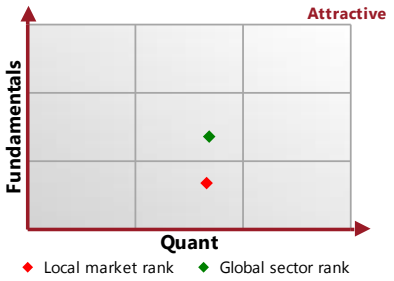
The quant model currently holds a marginally positive view on Aqua America. The strongest style exposure is Price Momentum, indicating this stock has had strong medium to long term returns which often persist into the future. The weakest style exposure is Valuations, indicating this stock is over-priced in the market relative to its peers.

197/448

Global rank in Utilities

% of BUY recommendations	67% (6/9)
Number of Price Target downgrades	0
Number of Price Target upgrades	2

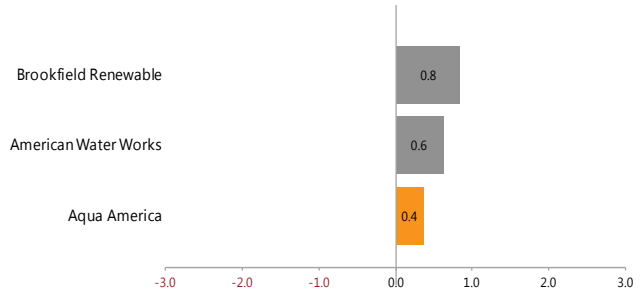


Displays where the company's ranked based on the fundamental consensus Price Target and Macquarie's Quantitative Alpha model.

Two rankings: Local market (United States) and Global sector (Utilities)

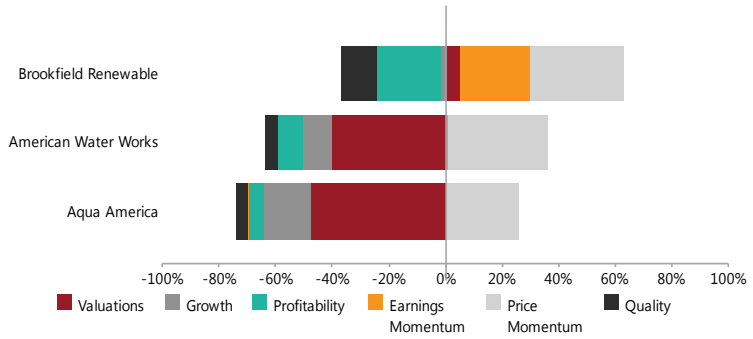
Macquarie Alpha Model ranking

A list of comparable companies and their Macquarie Alpha model score (higher is better).



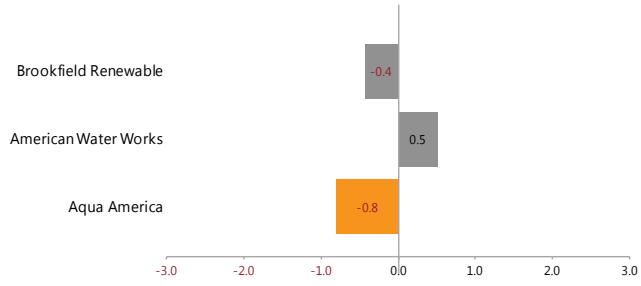
Factors driving the Alpha Model

For the comparable firms this chart shows the key underlying styles and their contribution to the current overall Alpha score.



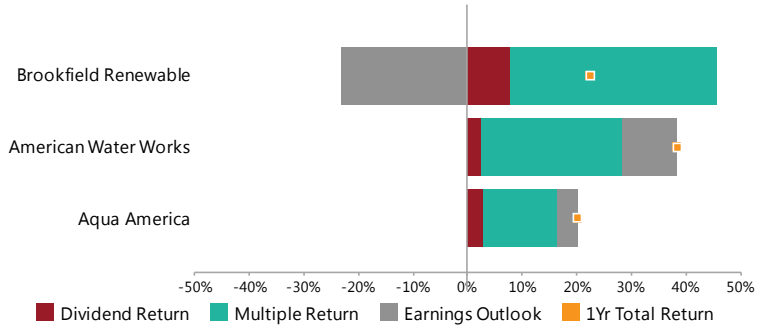
Macquarie Earnings Sentiment Indicator

The Macquarie Sentiment Indicator is an enhanced earnings revisions signal that favours analysts who have more timely and higher conviction revisions. Current score shown below.



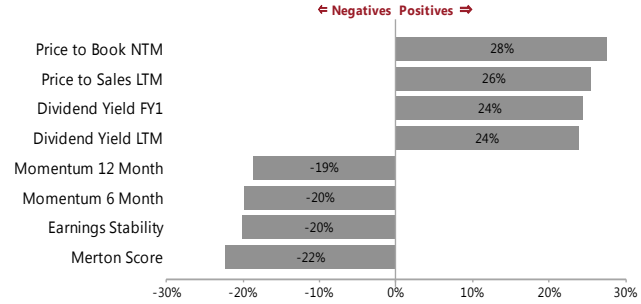
Drivers of Stock Return

Breakdown of 1 year total return (local currency) into returns from dividends, changes in forward earnings estimates and the resulting change in earnings multiple.



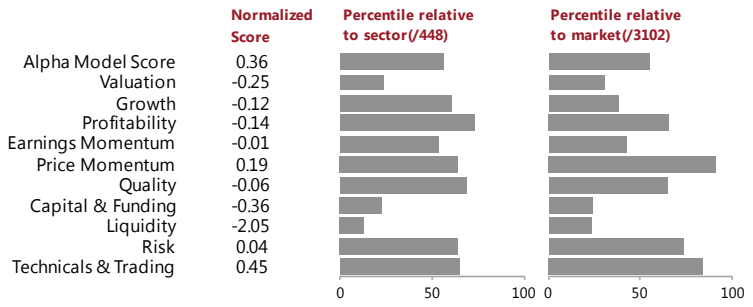
What drove this Company in the last 5 years

Which factor score has had the greatest correlation with the company's returns over the last 5 years.



How it looks on the Alpha model

A more granular view of the underlying style scores that drive the alpha (higher is better) and the percentile rank relative to the sector and market.



Source (all charts): FactSet, Thomson Reuters, and Macquarie Quant. For more details on the Macquarie Alpha model or for more customised analysis and screens, please contact the Macquarie Global Quantitative/Custom Products Group (cpg@macquarie.com)

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Recommendation definitions

Macquarie – Asia, USA, Europe and Mazi Macquarie (SA):
Outperform – expected return >10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie - Australia/New Zealand
Outperform – expected return >10%
Neutral – expected return from 0% to 10%
Underperform – expected return <0%

Note: expected return is reflective of a Medium Volatility stock and should be assumed to adjust proportionately with volatility risk

Volatility index definition*

This is calculated from the volatility of historical price movements.

Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

Medium – stock should be expected to move up or down at least 30–40% in a year.

Low–medium – stock should be expected to move up or down at least 25–30% in a year.

Low – stock should be expected to move up or down at least 15–25% in a year.
* Applicable to select stocks in Asia/Australia/NZ

Recommendations – 12 months
Note: Quant recommendations may differ from Fundamental Analyst recommendations

Financial definitions

All "Adjusted" data items have had the following adjustments made:
Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

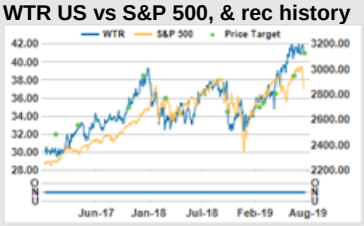
EPS = adjusted net profit / efpowa*
ROA = adjusted ebit / average total assets
ROA Banks/Insurance = adjusted net profit /average total assets
ROE = adjusted net profit / average shareholders funds
Gross cashflow = adjusted net profit + depreciation
*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

Recommendation proportions – For quarter ending 30 June 2019

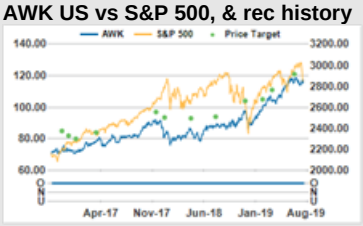
	AU/NZ	Asia	RSA	USA	EUR	
Outperform	47.41%	58.03%	49.38%	52.16%	51.95%	(for global coverage by Macquarie, 3.22% of stocks followed are investment banking clients)
Neutral	36.30%	29.24%	32.10%	42.65%	40.69%	(for global coverage by Macquarie, 3.02% of stocks followed are investment banking clients)
Underperform	16.30%	12.74%	18.52%	5.19%	7.36%	(for global coverage by Macquarie, 0.96% of stocks followed are investment banking clients)

WTR US vs S&P 500, & rec history



(all figures in USD currency unless noted)

AWK US vs S&P 500, & rec history



(all figures in USD currency unless noted)

Note: Recommendation timeline – if not a continuous line, then there was no Macquarie coverage at the time or there was an embargo period.
Source: FactSet, Macquarie Research, August 2019

12-month target price methodology

WTR US: US$41.00 based on a PER methodology

AWK US: US$121.00 based on a Sum of Parts methodology

Company-specific disclosures:
WTR US: The primary analyst has not visited this company's material operations and development assets within the past year.
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Clients receiving this report can additionally access previous recommendations (from the year prior to publication of this report) issued by this report's author at https://www.macquarieinsights.com.

Date	Stock Code (BBG code)	Recommendation	Target Price
01-Jul-2019	WTR US	Neutral	US$38.50
22-Apr-2019	WTR US	Neutral	US$36.50
06-Mar-2019	WTR US	Neutral	US$35.50
20-Feb-2019	WTR US	Neutral	US$35.00
24-Oct-2018	WTR US	Neutral	US$34.50
05-Mar-2018	WTR US	Neutral	US$36.00
12-Dec-2017	WTR US	Neutral	US$38.50
18-Oct-2017	WTR US	Neutral	US$35.00
11-Apr-2017	WTR US	Neutral	US$33.00
18-Jan-2017	WTR US	Neutral	US$32.00
21-Jul-2016	WTR US	Neutral	US$35.00

Target price risk disclosures:
WTR US: Our US$41 TP is based on 25.9x our proforma '21 water EPS and 22.2x proforma '21 gas EPS. Risks include: regulatory conditions for the Peoples acquisition, outcomes of pending and future rate cases, especialy in PA, cost controls, municipal M&A, and the level of market interest rates.
AWK US: Our US$121 TP is based on our 2021 SOTP. Risks to the downside include: the slower pace of future municipal acquisitions, lower cost efficiencies, and slower growth in non-regulated operations.

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Marquis, Renee T

From: Tucker, Shelby <SPARC@rbccm.com>
Sent: Monday, January 11, 2021 9:23 AM
To: Marquis, Renee T
Subject: [EXTERNAL] Essential Utilities (WTRG): Initiates 2021 guidance in line with RBC and consensus, reaffirms 2020 guidance, introduces voluntary emissions reductions goals (RBC SPARC)

CAUTION: This email originated from outside of the organization. Do not click links or open attachments unless you recognize the sender and know the content is safe.

RBC Capital Markets — RBC Insight — Research

Essential Utilities (WTRG): Initiates 2021 guidance in line with RBC and consensus, reaffirms 2020 guidance, introduces voluntary emissions reductions goals

Sentiment Indicator : positive

Produced by Tucker, Shelby (RBC Capital Markets, LLC) on Monday, January 11, 2021, 09:18 AM ET

Disseminated on Monday, January 11, 2021, 09:22 AM ET

Our view: WTRG introduced 2021 EPS guidance of $1.64-$1.69, in line with our estimate of $1.68 and consensus of $1.67. Management also reaffirmed its guidance to the upper end of its 2020 EPS range of $1.53-$1.58. WTRG announced its voluntary goal of reducing 60% of its Scope 1 and Scope 2 emissions by 2035 off 2019 levels, which applies to all its operations across gas, water and wastewater. On the guidance call today, we look forward to management's comments on DELCORA, updates on the proceeding for the catch-up portion of repair tax at Peoples, the timing of drawing down equity from its forward sale and the acquisition pipeline.

Essential Utilities (WTRG, Outperform, $48.72) initiated 2021 EPS guidance of $1.64-$1.69 and reaffirmed its 2020 EPS guidance to the upper end of the $1.53-$1.58 range. We are at $1.57.

DELCORA updates. Following the judge's ruling in December that upheld the validity of DELCORA's asset purchase agreement, WTRG expects a PA PUC Administrative Law Judge recommended decision in January and the DELCORA acquisition to close in the 2Q21.

Slight upward adjustments to capex and rate base. Estimated 2021 capex is $1 billion, compared to the 2020 capex spend of $950 million. The 2021-2023 capex plan stands at $3 billion, an increase from the 2020-2022 plan of $2.8 billion. This results in higher gas rate base estimates in 2021 and 2022 by $100 million and a higher 2022 water rate base estimate by $100 million. 2023 combined water and gas rate base is now estimated at $9.8 billion. Water rate base is still expected to grow at a 6-7% CAGR, excluding acquisitions, and gas is expected to grow at a 8-10% CAGR.

Conference call today at 11:00am ET. Dial in at (800)-367-2403, passcode 1177890.

Company Name	Exchange	Ticker	Rating	Risk Qualifier	Price Target	Currency	Price	Price Date
Essential Utilities Inc	NYSE	WTRG US	Outperform	Not Assigned	49.00	US Dollar	48.72	11 Jan 2021 08:29:00 ET

RBC Capital Markets, LLC
Shelby Tucker (Analyst) | (212) 428-6462 | shelby.tucker@rbccm.com

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Shelby Tucker, CFA (Analyst)
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April 24, 2020

Essential Utilities Inc

Water and Gas Do Mix After All; Initiating at Outperform

Our view: We fundamentally see Essential Utilities as trading at a discount to its 70% water/30% gas mix. While it has lost some of its ESG/water valuation veneer when it acquired Peoples Gas, we believe the "punishment does not fit the crime". Peoples is a fast-growing gas utility; the water segment should grow through active consolidation. Our sum-of-the-parts suggests $49 of value, which justifies our Outperform rating.

Key points:

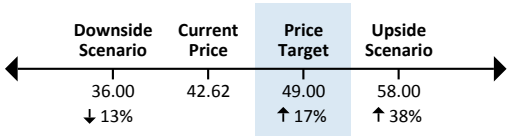
- **Essential Utilities is still primarily a water utility.** Essential Utilities (WTRG, formerly known as Aqua America) owns the second largest water utility in the country behind American Water Works. As such, it partakes in many of the broad themes that dominate the water sector: tremendous infrastructure upgrade needs, consolidation including municipal roll-ups, and, for the most part, supportive regulation. Seven out of the eight states in which WTRG's water segment, Aqua, operate have Fair Market Value legislation. Given this, we expect the company to continue to be active in water acquisitions, as exemplified by its $276.5 million pending acquisition of DELCORA, a wastewater municipal provider in Pennsylvania. Our model assumes ~$100 million of annual water acquisitions.
- **Peoples Gas is the right vehicle.** After a lot of fits and starts, WTRG finally closed mid-March its acquisition of Peoples Gas (PNG), a gas utility (LDC) with operations in Pennsylvania, West Virginia, and Kentucky. While investors can debate the wisdom for a water utility to buy a gas utility, we would be hard pressed to find a gas LDC that offers as many opportunities as Peoples does for WTRG. Both are anchored in PA, thus sharing common regulatory relationships, but PNG is in Western PA while Essential's Aqua America covers Eastern PA. This may open opportunities for WTRG to connect with water systems in the west that might have been hard to achieve otherwise. Furthermore, opportunities may exist in WV and KY for water consolidation, although Aqua is not in those states. Furthermore, Peoples Gas has multi-decade backlog of pipeline replacement that should assume strong growth for years to come.
- **Mix of business suggests $49 price target.** We believe that the best way to value the company is by assigning parent costs proportionally to Aqua and to Peoples then assign respective P/E multiples. Our base low-growth (secular) forward P/E multiples for water and gas are 24.9x and 19.3x, respectively. Given that both utilities are growing better than 4% and 3.5%, respectively, we assign a 25% premium for Aqua and 30% for People, to arrive at a blended 29.1x P/E multiple.

Outperform

NYSE: WTRG; USD 42.62

Price Target USD 49.00

Scenario Analysis*



*Implied Total Returns

Key Statistics

Shares O/S (MM):	245.0	Market Cap (MM):	10,442
Dividend:	0.92	Yield:	2.2%
		Avg. Daily Volume:	1,411,456

RBC Estimates

FY Dec	2019A	2020E	2021E	2022E
EPS, Adj Diluted	1.47	1.21	1.67	1.78
P/AEPS	29.0x	35.2x	25.5x	23.9x
DPS	0.91	0.97	1.04	1.11
Div Yield	2.1%	2.3%	2.4%	2.6%

All values in USD unless otherwise noted.

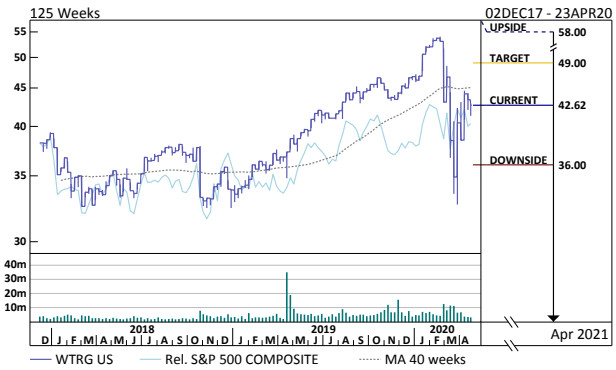
Disseminated: Apr 24, 2020 00:45ET; Produced: Apr 24, 2020 00:36ET Priced as of prior trading day's market close, EST (unless otherwise noted).

For Required Conflicts Disclosures, see Page 37.

RBC Capital Markets appreciates your consideration in the 2020 Institutional Investor All-America Research Team survey.

Target/Upside/Downside Scenarios

Exhibit 1: Essential Utilities, Inc.



Source: Bloomberg and RBC Capital Markets estimates for Upside/Downside/Target

Price target/base case

We derive our $49 price target by taking our 2021 EPS of $1.67 and using a sum of parts to account for the water and gas operating segments. We apply a 25% premium to our base multiple of 24.9x P/E for water utilities and a 30% premium to our base multiple of 19.3x P/E for gas utilities, given both utilities' greater-than-average growth rates.

Upside scenario

Our upside value of $58 assumes that WTRG executes on greater-than-expected M&A and sees even stronger-than-projected base growth at Peoples. To our 2021E EPS of $1.67 we apply 50% premium to our base multiple of 24.9x P/E for water utilities and a 50% premium to our base multiple of 19.3x P/E for gas utilities.

Downside scenario

Our downside value of $36 assumes the company does not execute on as much M&A as we forecast and that its credit metrics weaken over time, causing the company to issue equity and potentially dilute its share price. To our 2021E EPS of $1.67 we apply -10% discount to our base multiple of 24.9x P/E for water utilities and use our base multiple of 19.3x P/E for gas utilities.

Investment summary

WTRG's acquisition of Peoples and expansion into the natural gas industry creates a strong platform for future growth. We expect to see a significant amount of organic growth at Peoples as well as growth through acquisitions at the water segments. We believe WTRG's water and gas presence in ten states sets it up nicely to expand its footprint. The growing presence of Fair Market Value legislation that allows IOUs to purchase municipal systems at fair value without incurring meaningful goodwill provides a strong backdrop that should encourage transactions. We are initiating coverage with a $49 price target and an Outperform rating.

Potential catalysts:

- Increased adoption of Fair Market Value legislation opens up greater opportunities for WTRG to transact.
- Greater geographic footprint proves advantageous from an M&A standpoint, increasing the amount of acquisitions.

Risks to call:

- Lower-than-anticipated adaptation of fair market value principles across the country could dampen expectations.
- M&A transactions could require greater equity than we forecast, or could result in a weaker balance sheet than we expect.
- Less favorable regulations or disruptions within public utility commissions could weigh on growth.
- Climate variability may cause increased volatility in weather and may impact water usage and related revenue, which may not be recoverable through rates.
- Continued lockdown from coronavirus could impact revenues, through higher bad debt expenses.
- ESG investing continues to gain traction, but WTRG does not meet certain ESG criteria due to Peoples, which makes it harder to benefit from these increased flows.

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Key Questions

		Our view
1.	**Is it worth getting into the stock when it is trading at 27.0x NTM P/E?**	The answer depends on how much premium is attributed to ESG for a water-gas multi-utility. In our sum-of-the-parts analysis, we expect water/gas to contribute 70%/30% to 2021E EPS of $1.67. For water valuation, we look to the industry leader American Water Works (NYSE: AWK), which we have assumed a 35% premium above the water base P/E of 24.9x. While Aqua doesn't have the size of AWK, we believe rate base is supported by substantial capex opportunities. Nonetheless, the introduction of natural gas removes some of the ESG appeal. We apply a 25% premium to our water base P/E of 24.9x, resulting in a P/E multiple of 31.1x. Gas valuation is more straightforward. We apply a 30% premium to our gas base P/E of 19.3x, resulting in a P/E multiple of 25.1x, which we consider appropriate due to above-average rate base growth. The sum of the parts results in a blended P/E of 29.4x and total potential return of 17.0% inclusive of a 2.2% dividend yield. Our valuation suggests an attractive entry point.
2.	**What does water-gas combo mean to Essential?**	While the addition of PNG doesn't alter the regulated utility model and should be earnings accretive, it challenges the way we think about valuation as noted above. On a standalone basis, it seems clear to us that PNG now deserves a premium to valuation from its higher-than-average rate base growth (the company expects to see an 8-10% CAGR between 2019 and 2022, vs. peer utility average of 6-7%) following a period of underinvestment. On a consolidated basis, while Aqua remains a solid business, we could contemplate a discount to the lofty valuation that a pure-play water utility typically enjoys, with the involvement of natural gas and a less stellar balance sheet. In some way, the lack of an appropriate comp for a water and gas combo suggest that we are in uncharted territory.
3.	**How do balance sheet metrics fare post-PNG merger?**	Balance sheet looks less padded. We expect Essential to focus on deleveraging over the next few years. We see FFO-to-debt stabilizing in low-teens and debt-to-capital in the mid-fifties by 2023. Compared to water peers, these metrics seem may be on the lower end. However, thresholds for water utilities tend to be lower, with FFO-to-debt threshold at the 9-10% range. Currently, bonds at Essential and PNG are rated A/Baa2 and A/Baa1.
4.	**Will Fair Market Value legislation continue to expand?**	The rise of fair market value is becoming the preferred alternative to the traditional depreciated original cost method, providing mutually beneficial outcomes to both the buyer and seller of municipal systems. Sellers are able to capture the true value of their assets while buyers are allowed to add the total purchase price to rate base, without padding goodwill, dubbing the premium an "acquisition adjustment".
5.	**What are the unique characteristics of the water utility sector vs its electric and gas peers?**	The industry is 2x more capital intensive than the electric sector and 3x more than the gas sector. Despite this, water utilities generally spend the least amount of O&M dollars to maintain their assets. Over the past 20 years, water utility O&M expenses as a percent of PP&E averaged 20% compared to gas utilities of 40% and electric utilities of 60%. Further, the net PP&E to revenues ratio for investor-owned water utilities is about 5.0x, compared to electric utilities of 3.4x and natural gas utilities of 2.3x. In our view, this showcases the importance of infrastructure spending as a key characteristic of the industry's cost structure, making it difficult to reduce capital costs.

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Investment Summary

Essential Utilities Inc. (f.k.a. Aqua America, Inc.) is the second largest water and wastewater utility in the U.S., with a market capitalization of $10.6 billion. Before its entry into natural gas, Essential generated virtually all of its revenues through its regulated water utility segment (99.6% of sales) as of 2019, serving an estimated three million customers located primarily in states along the Rust Belt and Texas. On February 3, 2020, the company changed its corporate name to Essential Utilities Inc. following the acquisition of Peoples Natural Gas (PNG), and transformed into gas-water multi-utility with an expanded footprint. We expect water to remain the main contributor to earnings (70%) in 2020, though there are compelling growth opportunities across both segments. To a smaller extent, Essential also operates certain non-utility activities through Aqua Resources and Aqua Infrastructure.

Initiating coverage with $49 price target and Outperform rating. We view Essential as a solid water and gas multi-utility with substantial rate base investment opportunities in both segments. Post-merger with Peoples Natural Gas, Essential extends its operating territory to 10 states including the rust belt and Texas, with a combined rate base of $7.3 billion. The company remains deeply rooted in Pennsylvania, where 66% of combined customers are located. With the addition of PNG, Essential doubles its annual capex to ~$1 billion for 2020. From 2019 through 2022, the company expects to see to its water rate base grow at a 6-7% CAGR and its gas rate base to grow at an 8-10% CAGR. On a consolidated basis, we expect EPS to grow at a 6-7% CAGR during this time frame, an increase from a 4% CAGR between 2015 and 2019 as a pure-play water utility.

We view the regulatory environment in which Essential operates as constructive. More than half of Essential's annual capex is eligible for automatic recovery through surcharges. Further, at the water utilities, seven out of eight states have adopted the so-called Fair Market Value legislation (FMV). Under FMV, goodwill is added to rate base instead of being hung up on the balance sheet. This in turn encourages industry consolidations. Of course, not all deals are created equally. On average, we estimate $0.01 EPS accretion for every $50 million acquisition spend. Including DELCORA's $300 million acquisition (expected close early 2021), Essential has identified opportunities of various sizes that could add up to 320,000 customers, or ~10% of existing total. We also point to the eligibility of tax repair treatment which makes the PNG transaction particularly earnings accretive. Upon election with the IRS, the treatment allows previously capitalized repair costs to be expensed, resulting in higher deductions and lower tax expense without jeopardizing customer bills. An additional look-back deduction would also eligible, but requires some form of approval from the Pennsylvania PUC. We think the ability to stay away from rate cases, as in the case of Aqua Pennsylvania is especially valuable.

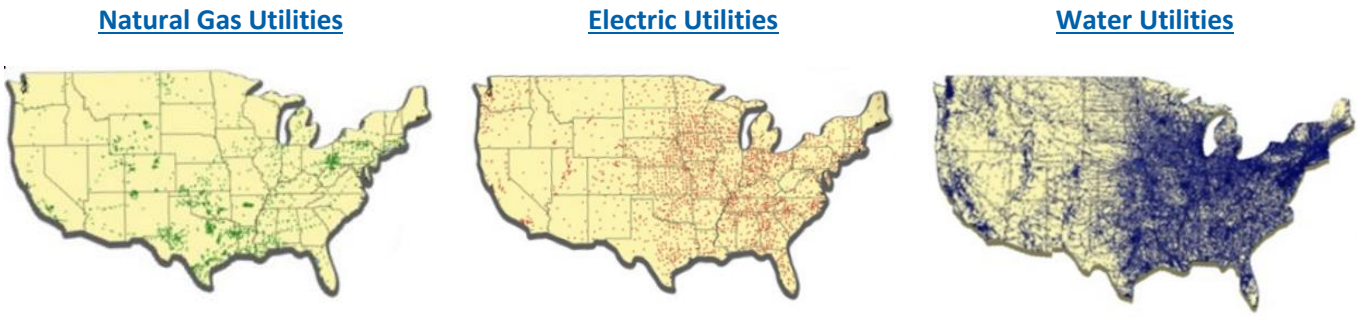
In our view, water and gas is a winning combo. Water remains Essential's core business and enjoys the benefits of an ESG play. Gas, via PNG, provides fast, complementary growth which differentiates Essential from water peers. While 2020 could be an "off-year" with a partial contribution from PNG and management focused on deleveraging, we see Essential getting back on track in 2021. The market has penalized the stock for introducing natural gas in the picture. We believe the "punishment does not fit the crime" and are bullish on the stock. We also recognize that the ESG investing movement has hit a temporary pause. As markets find some degree of normalcy – not necessarily recovery – we expect the movement to regain steam. We see Essential as one of the main beneficiaries of that trend despite its gas business.

Investment Highlights

Municipal acquisitions drive accretion

Fragmented industry ripe for municipal acquisitions. The U.S. water and wastewater industry is heavily commoditized. The fragmented nature of the water industry is highlighted by the roughly 50,000 water systems in the U.S. and about 15,000 community wastewater systems compared to 1,400 gas systems and 3,800 electric systems. Roughly 84% and 98% of the U.S. population is served by municipal water systems and wastewater systems, respectively, according the Environmental Protection Agency (EPA). This underscores the thirst for industry consolidation, in our view. Notably, investor-owned utilities only serve about 16% of the total population.

Exhibit 2: U.S. water among the most fragmented utility sectors



Source: Enviornmental Protection Agency and Energy Information Administration

Fair Market Value legislation has encouraged deal-making. Municipal acquisitions have become a popular theme over the last several years driven by a more favorable regulatory backdrop. The rise of FMV assessment of water and wastewater systems is becoming the preferred alternative to the traditional depreciated original cost method, providing mutually beneficial outcomes to both the buyer and seller of municipal systems. Sellers are able to capture the true value of their assets while buyers are allowed to add the total purchase price to rate base, without padding goodwill, dubbing the premium an “acquisition adjustment”. Currently, 12 states have implemented the measure. We estimate every $50 million (in line with historical average) that Essential deploys towards municipal acquisitions adds a run rate $0.01 to EPS. Kentucky is the only state under Essential’s operating jurisdiction that has not enacted FMV legislation.

Infrastructure surcharges permit rate adjustments outside of rate cases

Regulatory mechanisms that permit investor-owned utilities to adjust rates outside of general rate cases are referred to as infrastructure surcharges. These surcharges generally permit recovery of capital investments multiple times a year, and creates significant flexibility between rate cases. While the main benefit is to reduce regulatory lag, surcharges also allows utilities to stay away from a full rate case which subjects their rate base ROE and equity ratio to review by state commissions. In some way, utilities are able to preserve outperformance by avoiding rate cases. Surcharges come in many forms and are specific to states. For Essential, the main surcharges are the Distribution System Improvement Charge (DSIC), the Water and Sewer System Improvement Charge (WSSIC), and the Qualifying Infrastructure Plant Surcharge (QIPS). Post-PNG transaction, the Pipeline Replacement Program (PRP) also became available. The chart below illustrates the various mechanisms by state and their respective allowed surcharge.

Exhibit 3: Various surcharges employed by Essential, by state

AQUA

State	PA	IN	OH	NJ	IL	NC
Mechanism	DSIC	DSIC	SIC	DSIC	QIPS	WSSIC
Allowed Surcharge	7.5% W 5% WW	10%	12.75% W 9% WW	5%	2.5% average annual increase	5%

PEOPLES

State	PA	KY
Mechanism	DSIC	PRP
Allowed Surcharge	5%	No cap

Source: Company Presentation

Management estimates 52% of total capex between 2020 and 2022 are surcharge-eligible, while the remaining 4% must go through standard rate making. By segment, 46%/58.7% are surcharge-eligible for water/gas. We view these statistics a key component of Essential's robust capital program and long-term EPS growth.

Outsized rate base expansion; PNG as a new platform for growth

The Peoples acquisition creates a strong growth opportunity. Under its previous ownership, Peoples was severely underinvested in and now requires significant upgrades to its infrastructure. The system requires nearly 3,000 miles of gas pipeline replacement. With its accelerated pipe replacement program, the company expects rate base to grow organically at an 8-10% CAGR over the next three years. The election of repair tax at Peoples further increases earnings potential, which we discuss in more detail further down.

The acquisition of PNG represents new but complementary territory to the core water business. Peoples serves territories in Pennsylvania, Kentucky, and West Virginia. Aqua Pennsylvania's footprint is in the eastern side of PA while Peoples, headquartered in Pittsburgh, serves territories on the western side of PA. We believe the company's entrance into the gas industry will help grow its water business as well. Essential will likely be able to take advantage of its increased presence in the Pittsburgh area and entry into new states, and will find a way to aggregate more water assets.

Financial Outlook

Earnings outlook

The company forecasts rate base at its water utilities to grow at a 6-7% CAGR from 2019 through 2022 excluding rate base growth from acquisitions. Its capex is driven by investment in pipeline replacement, water treatment, and metering and IT development. Peoples Gas rate base is expected to grow at an 8-10% CAGR 2019 through 2022, as its aging distribution infrastructure requires significant pipeline replacement. Our 2020 through 2023 earnings per share estimates are $1.21, $1.67, $1.78, and $1.89. Our estimate of $1.21 reflects a partial year of earnings from Peoples as well as the effects of share dilution from 2019 financing. The $0.46 cent EPS increase in 2021 reflects a full year of earnings from Peoples, compared to three quarters in 2020. We expect earnings to increase at a +6.5% CAGR through 2023 based off 2019 adjusted EPS of $1.47. Breaking down the estimates by segment, water contributes ~64% of earnings and gas contributes ~36%. Our estimates reflect investment and continued acquisitions at its water utility and growth through investment at its gas segment. Our +6.5% EPS outlook compares to Essential's historical 4.0% EPS CAGR (2015-2019).

Dividend growth outlook

Essential has increased its common stock dividend at a 7.2% CAGR over the past four years. Our 2020 through 2023 dividend per share estimates are $0.97, $1.038, $1.110, and $1.188 and imply a DPS CAGR of 7%. The historical and forecasted payout remains in the 60%-65% range, excluding the 2020 estimate which is significantly higher due to a partial year of earnings from Peoples Gas.

Exhibit 4: Historical and projected dividend including forecasted EPS

	2018	2019	2020E	2021E	2022E	2023E
Dividend Per Share	$0.847	$0.907	$0.970	$1.038	$1.110	$1.188
Dividend Growth	*7.0%*	*7.0%*	*7.0%*	*7.0%*	*7.0%*	*7.0%*
Adjusted EPS	**$1.07**	**$1.47**	**$1.21**	**$1.67**	**$1.78**	**$1.89**
Dividend Payout Ratio	*79.1%*	*61.7%*	*80.1%*	*62.2%*	*62.5%*	*62.8%*

Source: Company data, RBC Capital Markets estimates

Sources of funds

We expect Essential to fund its capital expenditures through mostly new debt issuances and retained earnings. Regarding water M&A transactions, we expect the company to finance these transactions through a mixture of debt and equity. In 2020 we model ~$330 million equity in the second half of the year to finance its acquisitions including DELCORA, which is expected to be completed in late 2020 or early 2021. In the following years, we model a base of $50 million of equity, in some years issuing larger block amounts of equity to ensure its credit grade ratings. Historically, capex has been the largest use of cash followed by the dividend payout. Water acquisitions only accounted for ~7% of total capital deployment, but we expect this allocation to increase in future years. We do not model out any M&A transactions at Peoples, as we believe management is being careful about maintaining an earnings mix that is more heavily weighted from water operations.

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Exhibit 5: Sources and uses of funds

	2018	2019	2020E	2021E	2022E	2023E
Free Cash Flow						
Cash Flow from Operations	369	339	576	769	822	878
Common Stock Dividend	(151)	(189)	(249)	(273)	(293)	(315)
Retained Free Cash Flow	**218**	**150**	**327**	**496**	**529**	**563**
Acquisitions	(146)	(60)	(3,515)	(327)	(100)	(100)
Capital Expenditures	(496)	(550)	(810)	(960)	(969)	(979)
Net Free Cash Flow	**(424)**	**(460)**	**(3,998)**	**(790)**	**(540)**	**(516)**
Sources of Funds						
Net Long Term Debt Issuances	1,332	1,409	1,100	950	1,100	650
Net Short Term Debt Issuances	12	10	-	(10)	40	-
Common Equity Issuances	5	1,272	1,050	50	50	50
Net Debt and Equity Issuances	**1,349**	**2,692**	**2,150**	**990**	**1,190**	**700**
Ending Cash Balance	4	1,869	18	13	12	18

Source: Company data, RBC Capital Markets estimates

Credit metrics

Essential is rated A by S&P and Baa2 by Moody's. At the subsidiary level, Aqua is rated A+ and Peoples is rated A. Prior to the acquisition, the company's debt to cap ratio was maintained between 50% and 55%. In future years, we expect this ratio to trend higher and sit around the mid-fifties. Following 2020, we expect FFO-to-debt to be in the low teens, sitting around 13.4% in 2021. We see this move down to ~12% in the following years, which could point to a need to issue a larger amount of equity in 2023. This compares to its four-year historical average of around 20%.

While these metrics seem weak from a gas and electric utility perspective, water utilities may maintain their investment grade rating while having significantly higher debt to cap ratios and lower FFO-to-debt. A water utility may maintain an investment grade rating with a debt to cap as much as 60% and a FFO-to-debt as low as 9%. We expect Essential to remain comfortably far away from hitting these thresholds, and will continue to issue equity to maintain its solid credit metrics as it pursues additional acquisitions.

Exhibit 6: WTRG credit metrics

	2018	2019	2020E	2021E	2022E	2023E
Total Debt to Cap	55.7%	53.2%	51.9%	53.7%	54.5%	55.0%
EBIT Interest Coverage	3.3x	3.4x	2.6x	2.9x	2.9x	2.9x
FFO Interest Coverage	3.9x	3.4x	2.9x	3.2x	3.2x	3.2x
FFO to Net Debt	16.1%	7.1%	10.3%	13.4%	12.1%	11.9%
Discretionary Cash Flow to Debt	-10.9%	-7.7%	-7.8%	-6.7%	-6.0%	-5.3%

Source: Company data, RBC Capital Markets estimates

Repair tax is back on the table

Repair tax drove outsized EPS growth between 2013 and 2016 mostly for Aqua Pennsylvania. Essential now plans on electing repair tax for PNG in Pennsylvania. The mechanism has the benefits of keeping customer rates stable while increasing investments (and returns) without having the need to file for a lengthy rate case. For this reason, Essential has been able to stay out of a rate case on the water side since 2012, coupled with the implementation of

distribution surcharge mechanisms, which we had touched on in this report. In a nutshell, the repair tax allows certain maintenance costs previously capitalized to be expensed, effectively increasing deductions on a *tax basis* and improving cash flows. The Pennsylvania PUC then allows flow through tax accounting treatment that lets tax savings flow through to the income statement resulting in a lower effective tax rate and elevated earnings. Essential collects from customers at the statutory tax rate per the existing revenue requirement, but is expected to pay less to the tax authority. The impact is akin to a tax deferral as the benefit is the Thought in a different way, Essential collects the cost of taxes as new investments will bear the cost of higher taxes via the rate.

The amount of deduction is divided into two parts, ongoing deductions and a catch-up deduction for those costs that incurred in the past. Ongoing deductions are straightforward with Essential filing the election with the IRS. Management currently expects 8 to 12 cents of earnings accretion on a run-rate basis. The terms of the catch-up deduction would require approvals from the Pennsylvania state commission. As a reference point, the previous case with Aqua Pennsylvania allowed the deduction to be amortized over 10 years.

Balance Sheet and Expected Capital Deployment

Strong credit metrics to begin with. PNG brings metrics back to industry average. Essential's debt is rated A by S&P and Baa2 by Moody's, which is in line with the water industry. However, credit metrics look superior relative to peers excluding PNG, with debt-to-cap tracking low 50s and FFO-to-debt between high teens and low 20s in the past five years. To put these figures into perspective, AWK, a close peer to Essential before the PNG transaction, features a debt-to-capital ratio just below 60% and FFO-to-debt of mid to high teens during the same period.

Post-PNG transaction, we believe Essential's credit metrics could track closer to levels at AWK. We expect FFO-to-debt to stabilize in lower mid-teens and debt-to-capital at mid-50s, in line with company guidance of 12-14% and 50-55%, respectively. We believe towards 2023 the metrics will track farther away from the company's comfort levels, which may incentivize an equity issuance around that time. It is important to note that while credit agencies have typically considered 11-12% FFO-to-debt as the threshold for investment grade (BBB/Baa2) ratings for gas utilities, their threshold for water utilities is typically even lower in the 9-10% range. Due to the regulated nature of utilities, companies are able to flex their balance sheet to levels that would generally perceived as alarming in other industries. We also give consideration to the fact that PNG's debt (A/Baa1) is rated similarly to Essential (A/Baa2) and do not anticipate any material deterioration after the acquisition. The following summary shows credit ratings among Essential, Aqua America and PNG.

Exhibit 7: Current credit ratings for Essential, Aqua American and PNG

	S&P Global Ratings		Moody's	
	Issuer	Issuance	Issuer	Issuance
Essential	A	A-	Baa2	Baa2
AQUA (PA Subsidiary)	A	A+	--	--
PEOPLES	A	A	Baa1	Baa1

Source: Company Presentation

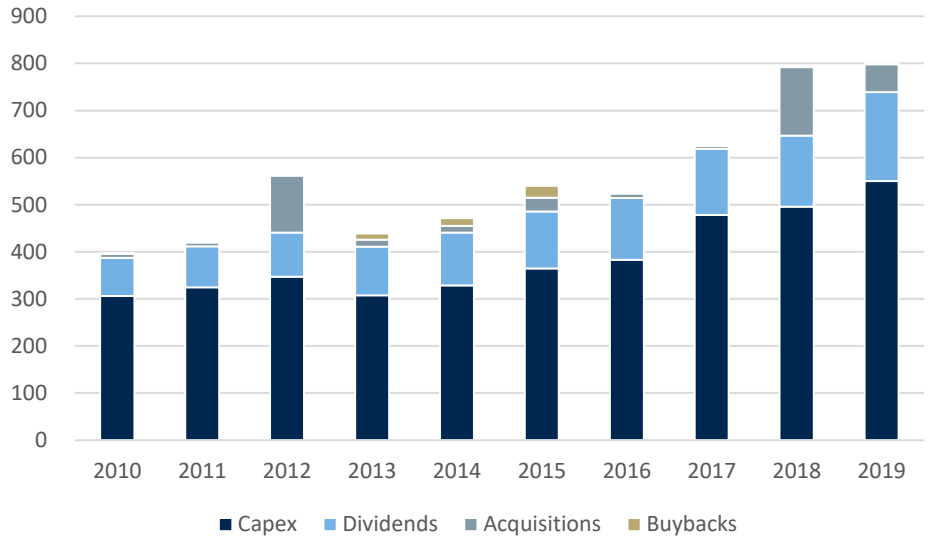
Capital deployment

Tapering expectations on dividends. Essential announced an annualized $0.94/share dividend payment in 2019. Between 2014 and 2019, dividends had achieved 7.3% CAGR along with healthy growth in earnings per share. In our outlook, we estimate dividend to grow in the 6-7% range in near term coupled with acquisitions that are in the $100 million range. Eventually, growth should taper off and fall in line with EPS growth, which we anticipate to be in the 6.0-6.5% range. We believe this enables Essential to manage a payout in the low 60s, in line with company guidance of 60-65% dividend payout. While the range is still a step up from water utility peers, which typically have payout ratios 50-60%, and is more in line with gas utility peers, we believe our estimate represents stabilizing ground after the PNG transaction.

Minimal share buybacks. Since 2010, buybacks averaged ~1% of total capital deployment. An abundance of capital projects in the water industry have stymied the need for buybacks to return capital to shareholders. Given our view of further consolidation in the industry and massive infrastructure upgrade opportunities in water pipes, we don't see buyback activity in the cards anytime soon.

Acquisitions remains a relatively small component; focus turns to organic growth following PNG transaction. Acquisitions have generally not been a large piece of capital deployment. Since 2010, acquisitions totaled 7.5% of overall capital deployment. We believe M&A could be somewhat limited now given the need to deleverage and preserve the strength of the balance sheet as Essential embarks into the gas distribution business. Management sees roughly $100 million of acquisitions per year but could inch higher if a larger deal were to close. The water industry is ripe for consolidation, in our view. We like the roll-up of municipal deals despite accretion being relatively modest. Assuming $100 million of deals, a blended 50% equity ratio and 10% ROE yields 3 cents of accretion on an increasing base, or +2% on current 2020E consensus.

Exhibit 8: Capital deployment, 2010-2019

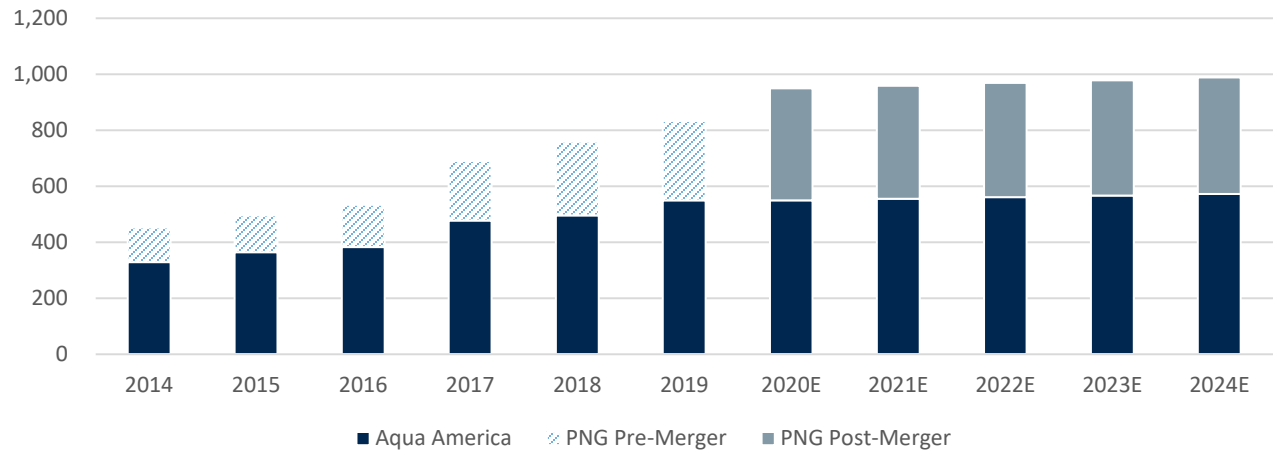


Source: Company 10K

Capital expenditures ramp up in 2020, post-PNG transaction. Core business has a healthy runway, expected to invest $1 billion infrastructure annually with a solid, organic rate base growth of 6-7% for water and 8-10% for gas. Further, more than half (52%) is recoverable through surcharges and the rest through rate cases. We view opportunities for infrastructure upgrade for both gas and water favorably. To put this into perspective, PNG plans to renew about 189 miles of pipeline per year under the long-term infrastructure investment program (LTIIP). Based on current capex expectations for 2020 of $400 million, this implies $2 million per mile of pipe. Management has indicated that there are nearly 3,000 miles of gas main suitable for replacement in Pennsylvania alone. In water and wastewater, the EPA estimates $471 billion and $271 billion worth of infrastructure investments needed as of today, respectively. We acknowledge that all pipes are not created equal and warrant different levels of investment based on deterioration. The opportunities are strongly outlined, however. We remain positive on the regulatory environment for both water and gas.

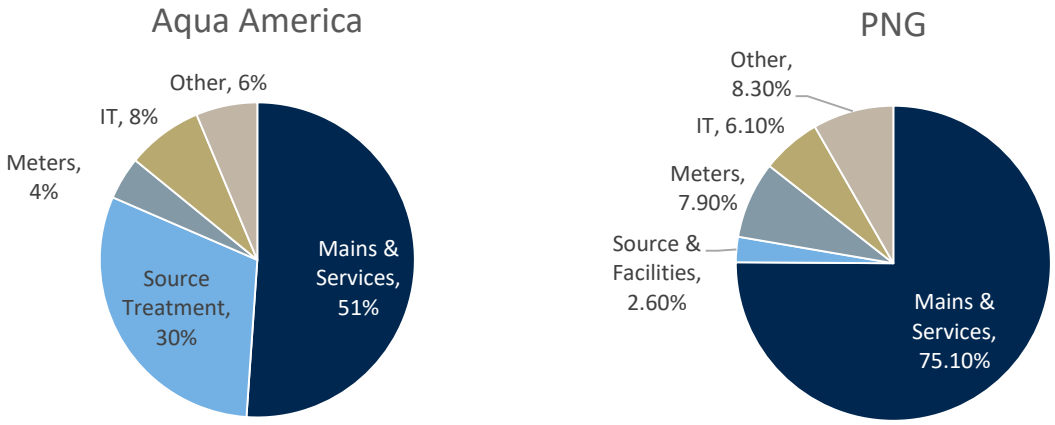
A counterweight to our capex expectations is the temptation to overgrow the gas utility. While gas investments typically generates a better return (8-10% ROE range, vs. 5-6% for water), we believe management could limit the growth in gas giving consideration to valuation of the overall utility. Earnings accretion from gas investments could erode the premium valuation that Essential enjoys from Aqua America. This is especially relevant to some investors who are concerned with ESG considerations. For 2020, we expect the gas/water capex mix to be 42%/58%. Going forward, we believe the ratio could remain static over even tilt towards water.

Exhibit 9: 2020 capex ramps up to $1 billion, slated to invest $2.8 billion, 2020E-2022E



Source: Company Presentation, RBC Capital Markets estimates

Exhibit 10: Infrastructure investments, 2020E-2022E



Source: Company Presentation

Financing

The company plans to finance its acquisitions with a mixture of debt and equity. The company has indicated that an equity issuance of ~$300 million will likely come in late 2020 as the company finances the DELCORA and other acquisitions. In 2020 and 2021 we will see the dilutive effects issuances used to fund the PNG and DELCORA transactions. Looking forward, we model $100 million in acquisitions every year, $50 million of which would be funded through equity.

Upcoming notable acquisitions

DELCORA acquisition should provide upside. In September 2019, Essential (then Aqua America) announced the acquisition of DELCORA wastewater assets for $276.5 million. The acquisition represents the largest municipal acquisition in the company's history. DELCORA is a wastewater authority that treats water for smaller municipal systems that have their own

distribution systems. DELCORA has around 15,000 customers, but the end-use customers of those municipalities total around 200,000. This generates a significant amount of follow-on opportunities to acquire the distribution wastewater systems that DELCORA serves. As with other municipal acquisitions, the company expects to see an earnings lag. Rates at municipal water and wastewater systems are significantly lower than those of investor-owned utilities. Municipalities may not be earning a return, paying taxes, or have other financial commitments, which lowers costs to the end-use customers. The company expects DELCORA to go into the Pennsylvania rate case that will most likely be filed in 2021. With new rates effective thereafter, the company expects full earnings from DELCORA in 2022.

Regulatory jurisdiction

Most of Essential's water, wastewater and now gas utility operations are subject to regulation from state commissions. As these commissions regulate billing rates and terms of services, and approval of rate cases and surcharges, they exert power over the profitability of Essential. Individual policies vary across commissions, and depend on the policies of the state. Essential has historically maintained constructive relationships with them, especially in the home ground Pennsylvania. The following is list of utility commissions within Essential's operating jurisdictions.

Exhibit 11: State utility commissions

State	Utility Commission
Pennsylvania	Pennsylvania Public Utility Commission
Ohio	Public Utilities Commission of Ohio
Texas	Public Utility Commission of Texas
Illinois	Illinois Commerce Commission
North Carolina	North Carolina Utilities Commission
New Jersey	New Jersey Board of Public Utilities
Inidiana	Indiana Utility Regulatory Commission
Virginia	Virginia State Corporation Commission
West Virginia	Public Service Commission of West Virginia
Kentucky	Kentucky Public Service Commisssion

Source: Company 10K

Risks to Rating and Price Target

Less favorable regulatory backdrop. Lower-than-anticipated adaptation of FMV principles across the country could dampen expectations and weigh on growth in the long run. Changes in or less favorable regulations or disruptions within public utility commissions could also weigh on growth.

Integration of PNG takes longer than expected. In that case, we could see higher O&M expenses in 2020 and possibly spilling into 2021. This could hinder Essential's progress to deleverage the company, on a FFO-to-debt basis. However, we view Essential to have a strong leadership with a highly experienced management team which has managed consolidations frequently in the past and believe the integration should proceed as planned.

Poor leverage metrics leads to credit downgrade. As we had noted earlier in the report, we see leverage metrics deteriorating dramatically in 2020. Despite stabilizing in 2021, these metrics cut close to rating thresholds for water utilities. Plus, we are aware of credit rating agencies' sector-wide downgrade, putting even more pressure on companies like Essential. Debt at Essential and PNG are one to two notches away above non-IG rating. Should leverage metrics deteriorate more than expected, we see a credit downgrade weighing down the stock.

Natural gas segment decreases appeal from an ESG perspective. We believe Essential's attractiveness from an ESG standpoint has lessened now that it has entered the natural gas sector. As ESG investing becomes more main stream, we expect to see greater flows into the water sector from specialized funds and awareness of ESG metrics. Water utilities, which have historically traded at a premium to electric and gas utilities, will likely see even higher premiums due to increased investor appetite. We believe that scarcity will partially mitigate the negative impact of its gas segment. There are under ten pure-play water utilities, and Essential had the second-largest water footprint when its operations were only in the water sector. We believe Essential still maintains ESG appeal, but will not benefit as much from the ESG interest as its pure-play water counterparts.

Decrease in water supply and material changes in water usage patterns. Climate variability may cause increased volatility in weather and may impact water usage and related revenue, which may not be recoverable through rates. Increased frequency of rainfall during the warmer months could also weigh on water usage and lead to lower revenues.

Decarbonisation hinders growth opportunities at the gas utility. The transition to electrification may be a risk to growth at Peoples as cities and states take stronger stances on GHG targets and continue to promote decarbonisation and electrification. Legislation and initiatives have encouraged the use of electric appliances and heating systems over traditional gas-based systems. One city in California even banned new gas connections in commercial and residential buildings. The gas distribution system is primarily decoupled, which separates volumes from earnings. This protects Peoples here from a volumes per customer standpoint, but the risk of decarbonisation comes from less connection growth. This discouragement of gas consumption could prevent the company from adding connections and potentially cause it to lose revenues if a customer were to switch entirely to an electric system. The company benefits from a customer count perspective since it charges fixed infrastructure costs, regardless of how much the ratepayer consumes. We believe states in which Peoples operates – PA, WV, and KY – are less likely to discourage the use of natural gas in the near future. However, emissions initiatives down the road could put downward pressure on the stock.

Delays in closing DELCORA. The company expects the DELCORA acquisition to close in late 2020 or early 2021. A delay in the DELCORA acquisition related to COVID-19 or for other reasons could negatively impact earnings in 2022 and onwards. If the acquisition is not

completed before the company goes into its Pennsylvania rate case in 2021, they may risk not being able to file for new rates at DELCORA. The company expects full earnings contributions from DELCORA in 2022, after new rates are implemented. If DELCORA does not make it into the rate case, the company will continue under-earn on the asset until the next rate case since rates for municipal systems are considerably lower than those of investor-owned utilities.

Extension of coronavirus lockdown could further hurt the economy and increase bad debt expenses. Utilities in general have means to recover incurred costs, though they may need to finance these costs while waiting for the commissions to determine the proper recovery mechanism, if permitted. As more customers face hardship, it would put pressure on their ability to pay their bills, including the utility bills. This, in turn, would translate into a revenue shortfall that could create a cash shortfall. We anticipate that commissions will allow these costs to be treated as a regulatory asset to be recovered over time.

Valuation

Outperform, $49 PT

Valuation framework supports high base multiple. To derive our valuation for water, we turn to the dividend discount model (DDM), which we use to calculate the sustainable value of a low-growth utility. We use the parameters that we use for gas utilities for market return (9.75%), beta (0.55), risk-free rate (3.5%), and dividend payout ratio (64%). We have changed our growth assumption to 4% for water from 3.5% for natural gas and we add a 10% ESG/water premium. This results in a base P/E for a low growing water utility at 24.9x forward P/E.

We arrive at our $49 price target using a sum-of-parts method. We apply a 25% premium to our base multiple of 24.9x P/E for water utilities and a 30% premium to our base multiple of 19.3x P/E for gas utilities. We believe both business warrant premiums due to strong growth prospects and footprints in states with constructive regulatory environments. Our price target of $49 implies a total return of ~17% and justifies our Outperform rating.

Valuation considerations

WTRG is currently trading at a 4-turn discount to water peers on 2021E EPS, despite having the second-largest water footprint. This is likely due to the loss of the benefit from the water premium that bolsters its pure-play peers as a result of Essential's plunge into natural gas. We believe the company has a solid earnings mix of 70%-30% water and a premium should still be warranted due to water segments; Essential operates the second largest water business and maintains around 25% of market cap.

We also believe that Peoples creates a strong platform for growth at both the gas and water segments. The multi-decade backlog of pipeline replacement requires significant and accelerated investment that will generate low risk organic rate base growth. Turning to the water segment, we think the water business is well-positioned to further expand its water business. We expect to see the majority of future acquisitions coming from Pennsylvania, which represents Essential's largest water and gas operating segments. We believe Essential's expansion into Western PA due to the Peoples acquisition will further secure the company's presence in the state and help drive acquisition growth for Aqua PA. The acquisition of DELCORA, whose service territories overlap with those incorporated in Aqua PA's footprint, will further increase Essential's presence in PA.

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Company Overview

Essential Utilities Inc. (f.k.a. Aqua America, Inc.) is the second largest water and wastewater utility in the U.S., measured by market capitalization. Before its entry into the natural gas industry, Essential generated virtually all of its revenues through its regulated water utility segment (99.6% of sales), serving an estimated three million customers located primarily in states along the rust belt and Texas. Essential's customer base is primarily residential (58%), followed by commercial (16%), wastewater (12%) and other (14%) customers. Essential's growth has been marked by several key transactions, including the acquisition of Peoples Natural Gas Company, LLC ("PNG") in 2020, regulated water operations in Ohio from American Water Works in 2012, regulated water operations from AquaSource in 2003 and the merger with Consumers Water Company in 1999. On February 3, 2020, the company changed its corporate name to Essential Utilities Inc. and extends services to 747,000 gas customers and expands its footprint to include Kentucky and West Virginia. As a complement to their primary regulated business, Essential also operates certain non-utility activities through Aqua Resources and Aqua Infrastructure.

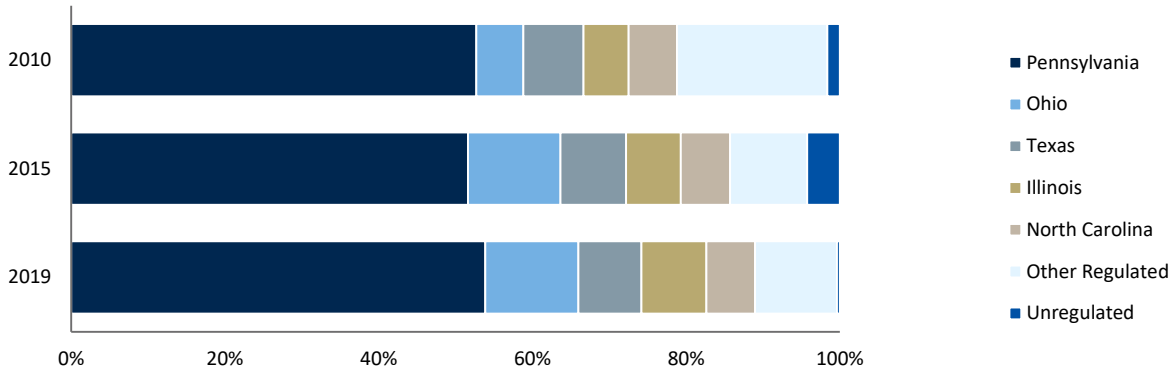
Exhibit 12: Company footprint, including Peoples Natural Gas transaction

Source: Company reports

Regulated water business

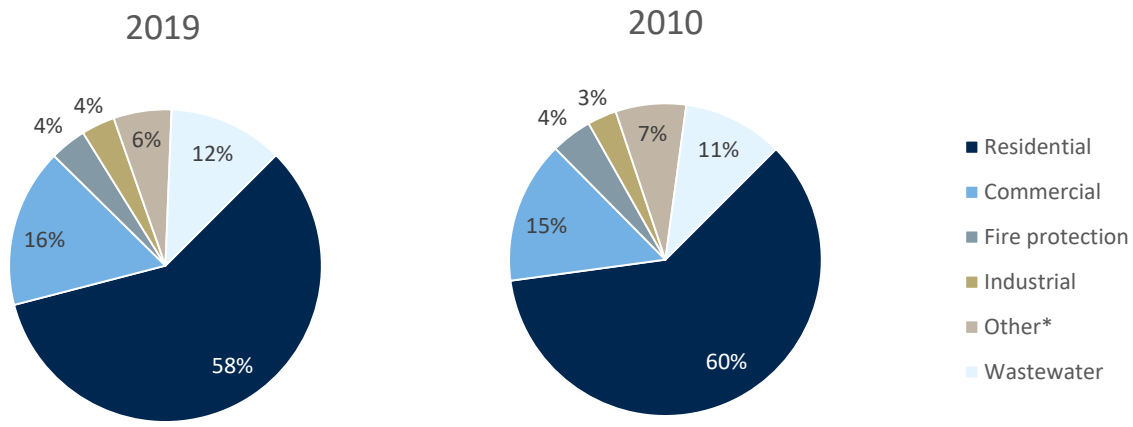
Essential generates virtually all of its revenues through its regulated water business, which serves water and wastewater customers in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana and Virginia. Historically, Pennsylvania is the main operating jurisdiction, accounting for 54% of operating revenues in 2019. Ohio, Texas, and Illinois contribute to the majority of the remaining share of revenues. Over the past decade, the percentage share across these states have remained largely in line year-over-year. Customer growth for the business has been robust, recording 1.8% CAGR in the trailing five years. The majority of customers for water services are residential (58% in 2019), followed by commercial (16%) and wastewater clients (12%).

Exhibit 13: 2019 regulated water segment revenues by state



Source: Company Presentation

Exhibit 14: Regulated water segment revenues by customer class

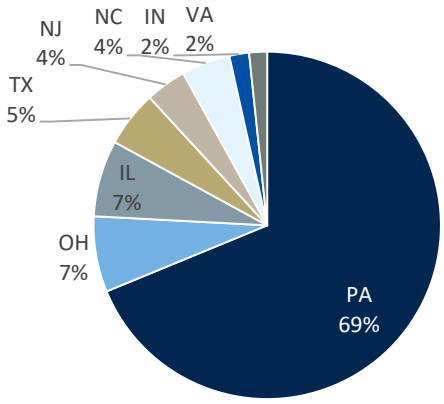


Source: Company Presentation

Water and wastewater service customers are subject to regulation by their respective state utility commissions, which determine billing rates and terms of service, among other regulatory matters. The regulated water business is dependent on water consumption which, in turn, is dependent on weather and temperature conditions much like electric and gas utilities. Generally, dry weather and high temperatures increase water consumption while above-average rainfall and low temperatures decrease water consumption. Given a regulated industry, local authorities may impose consumptions limits which could impact Essential's performance. Operating revenues for the regulated water business and operating revenues as a percentage of total were $805 million/$835 million/$886 million and 99.6%/99.6%/99.4% for 2017/2018/2019.

Utility growth is often referenced by growth in rate base. Between 2020 and 2022, rate base for water and gas are slated to ramp up at 6-7% CAGR to $6.5 billion and 8-10% CAGR to $3.0 billion, respectively. The following chart illustrates the relative sizes of water rate base as of 2018 by state.

Exhibit 15: Essential regulated water utility rate base as of 2018



Source: Company Presentation

Market-based activities

Essential conducts competitive, non-utility businesses through Aqua Resources and Aqua Infrastructure: Aqua Resources manages a water system operating and maintenance contract and offers other water solutions to customers; Aqua Infrastructure provides non-utility raw water supply services for firms in the natural gas drilling industry. Together, these businesses make up less than 0.5% of operating revenues hence immaterial to Essential's overall performance, in our view. The company's direction is consistent with a pure-play regulated utility and we believe the strategy will continue in the foreseeable future.

Peoples Natural Gas

Peoples Natural Gas ("PNG") is the largest natural gas distribution company in Pennsylvania with $2.3 billion rate base as of 2019 year-end. The company serves 747,000 customers across the Pennsylvania (93% of customers), West Virginia and Kentucky. The company's infrastructure is deeply rooted in these states, with 15,000 miles of distribution pipeline, 2,400 miles of gathering pipeline and 310 miles of intrastate transmission pipeline as of 2019. PNG is fully regulated, with 98% of earnings generated through its gas distribution business.

In October 2018, Aqua America announced the intent to acquire PNG for $4.275 billion in an all-cash transaction. The transaction closed on March 16, 2020. Much like other regulated utilities, PNG is regulated by various state commissions which determine customer tariff rates, terms of services and mergers and acquisition-related matters. On a regular basis, PNG files rate increase requests, either via riders or rate cases, to recover and earn a fair return on infrastructure spending. As with the regulated water business, the regulated gas distribution business is dependent on weather conditions and is seasonal by nature. Generally, colder weather increases gas consumption and warmer, milder weather decreases consumption. Certain states provide mechanisms that decouple gas sales from weather effects and helps smooth out earnings of gas utilities. While Pennsylvania and Kentucky offer decoupling, West Virginia does not. Given the high concentration of customers in Pennsylvania, we view the utility to be well-insulated from mild weather.

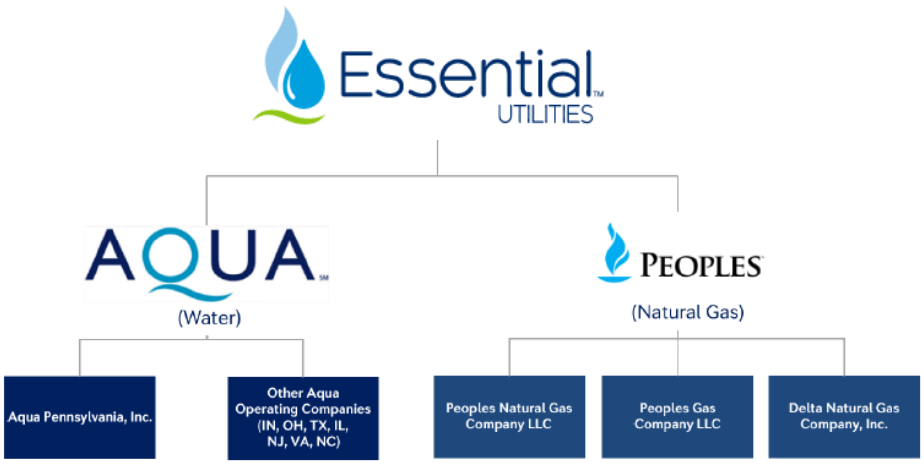
Management has indicated that it expects the business mix to stand at 70% water and 30% gas. It has also been made clear that the company wants to maintain its water-heavy earnings contribution, and will be very selective about any potential gas acquisitions moving forward.

We believe the mix of the two segments is crucial from a valuation standpoint, as this balance will play a significant role in how the stock trades compared to its utility peers.

Corporate structure – Essential Utilities

Despite consolidation in the past decades, Essential features a rather simple corporate structure. Aqua Pennsylvania, which provides regulated water and wastewater services in the state, is the largest entity within the structure and contributes to 54% of consolidated operating revenues. The figure below is a representation of the corporate structure after the PNG acquisition.

Exhibit 16: Essential Utilities corporate structure



Source: Company 10K

Management Team

Extensive industry experience. WTRG's management team has deep experience in the water utility industry, with most key executive officers serving in strategic roles at the company for extensive periods of time. We find the experience in mergers and acquisitions particularly valuable for the company, as it industry positions itself for further consolidation. The officers of Essential Utilities include:

Christopher H. Franklin – Chairman; President and Chief Executive Officer

Mr. Franklin has served as chief executive officer of Essential Utilities since July 2015 and as chairman since December 2017. Mr. Franklin was previously president and chief operating officer, regulated operations. A 20-plus-year veteran of the company, Mr. Franklin has held executive roles in public affairs, customer operations and as regional president of the company's southern and mid-western operations, where he managed eight states. While holding that post, Mr. Franklin significantly increased the performance and earnings power of these diverse state operations, while simultaneously serving as senior vice president of the company's corporate and public affairs, where he was also responsible for the company's federal, state and municipal legislative affairs, investor relations, and communications

Daniel J. Schuller – Executive Vice President and Chief Financial Officer

Mr. Schuller is executive vice president and chief financial officer for Essential. Before becoming Deputy CFO, Mr. Schuller served as Executive Vice President, Strategy and Corporate Development for Aqua America and was responsible for Aqua's strategic growth initiatives.

Mr. Schuller came to Aqua America from J.P. Morgan Asset Management – Infrastructure Investments Group where he had been an investment principal since 2007, providing strategic leadership as a director of portfolio companies including SouthWest Water Company—of which he was responsible for the 100 percent stake held by J.P. Morgan-advised investors—and Summit Utilities. Specifically for SouthWest Water, Mr. Schuller guided the company's turnaround and led its growth strategy, assessing both organic growth and acquisition opportunities. Prior to joining J.P. Morgan, Schuller was a manager at Mars & Co., an international strategy/general management consulting firm, where he led consulting engagements related to growth and profitability for Fortune 500 companies and conducted due diligence for private equity firms.

Richard S. Fox – Executive Vice President and Chief Operating Officer

Mr. Fox was named chief operating officer of Essential Utilities in July 2015. Prior to being appointed COO, he had been regional president for Aqua America since January 2012, heading all of Aqua America's utility operations in Texas, Illinois, North Carolina, Indiana and Virginia. Prior to assuming the role of regional president, he was vice president, customer operations, where he was responsible for all customer service operations for Aqua America's regulated operating subsidiaries, including the company's national customer call centers, national meter operations, and company-wide billing and collections.

Christopher P. Luning – Executive Vice President, General Counsel, and Secretary

Mr. Luning assumed the role of executive vice president, general counsel, and secretary for Essential Utilities in 2012. Mr. Luning is the company's chief legal counsel and oversees and provides strategic direction for the company's legal, human resources, internal audit, and safety departments. He provides direction on all parent company and its subsidiary matters, including corporate governance and board matters. Previously, he held the position of vice president, corporate development and was responsible for leading the Aqua America's corporate development activities, contributing to the company tripling its customer base in the previous 10-year period.

Matthew R. Rhodes – Executive Vice President, Strategy and Corporate Development

Mr. Rhodes was named executive vice president, strategy and corporate development for Essential in June 2018. Prior to this role, Mr. Rhodes served 11 years as a managing director in the investment banking division at Goldman Sachs in the global natural resources group focused on mergers and acquisitions for electric and gas utility clients. Prior to that role, Mr. Rhodes worked at Bank of America and Duke Capital Partners. Mr. Rhodes is the executive sponsor the Essential Utilities' Women Resource Group.

Robert A. Rubin – Senior Vice President, Controller and Chief Accounting Officer

Mr. Rubin was appointed senior vice president, controller and chief accounting officer (CAO) of Essential in January 2012 after having served as chief accounting officer since March 2004 and as controller for the previous five years. As CAO, Mr. Rubin is responsible for Essential's external and internal financial reporting, including that required by the Securities Exchange Commission and Sarbanes Oxley regulations. He is also responsible for taxes, coordinating external audits, corporate accounting and maintaining compliance with accounting standards and principles throughout the company.

Water Utilities in a Splash

Water is the most essential of utility services. The defensiveness of a utility sub-sector is partially defined by its ability to maintain a rate-regulated business model that creates predictable earnings and cash flows, thus allowing for a steady and foreseeable dividend. Fifty years ago, the telecommunication industry was a steady utility until competition was introduced and cellular technology disrupted it. Even twenty years ago, the generation portion of the electric industry was partially deregulated. It is conceivable that in a few decades electricity could be produced locally, thus not requiring a network of wires. Water, on the other hand, cannot be locally produced everywhere. Its pipelines form the least by-passable network among utilities. While most utility services are viewed as essential by the authorities, we believe that a premium consideration is placed on water utilities.

The U.S. water and wastewater industries are ripe for outsized investment opportunities driven by an aging infrastructure. The EPA estimates water utilities will need to invest ~$384 billion in pipes, treatment plants, and storage tanks over the next twenty years due to decades of under-investment. A competing study produced by the America Water Works Association (AWWA) estimates water infrastructure needs will total more than $1 trillion over the same timeframe, assuming pipes are replaced at the end of their service lives. As it stands today, U.S. water systems were slapped with a D+ grade from the American Society of Civil Engineers.

Municipal acquisitions drive accretion opportunities. The EPA estimates 84% of the community water market is serviced by municipalities and 98% of the wastewater systems are government-owned. Contrast that with the electric utilities sector, where investor-owned utilities (IOUs) served 72% of all electricity customers in 2017, according to Energy Information Administration (EIA), a division of the U.S. DOE. Acquisitions of municipalities have been a driver of growth for the water IOUs, having helped the nine largest companies collectively increase earnings at a 7%+ CAGR over the past ten years. Increasingly, states are creating incentives to facilitate such acquisitions, through Fair Market Value (FMV) legislation, which we will cover later. In our view, acquisitions resulting from fair market legislation will only become more prevalent and allow municipalities to focus on other community priorities.

Water lowest risk among utilities; argues for higher valuation. While water headlines can be scary (witness the Flint, Michigan disaster), most of the headlines come from poorly managed municipalities. Water investor-owned utilities (IOUs) do not suffer interruption of service like electric blackouts, the rare gas pipeline explosion, or the more numerous gas leaks. Regulatory outcomes are generally less contentious, with a greater usage of surcharges to grow revenues. The rating agencies recognize the lower risk as their thresholds for credit ratings are lower than those applied to other utilities. All else being equal, the FFO/debt for water utilities can drop to 10% or less and still retain an investment grade rating, a feat less likely to happen for electric utilities. A lower risk typically will lead to a lower discount rate and therefore a higher multiple.

ESG meaningful underlying driver for premium valuation. We believe that ESG (Environment, Social, and Governance) investing will continue to gain traction among fund managers, thus preserving a premium valuation for water utilities. On the environment side of the ledger, water utilities have the lowest carbon footprint of all utilities. Social issues revolve around the product that water utilities provide at a reasonable price. Governance issues are more akin to other industries. For example, while some companies separate the CEO and Chairman role, others do not. While more traditional ESG investors might be precluded from investing in gas/electric utilities due to nuclear assets, gas pipelines, or other aspects of the business model, we do not see a similar restriction on water utilities. Perhaps more importantly, we believe the increasing importance of ESG and the lack of publicly traded pure-play water stocks should only serve to further increase the premium valuations for companies in the industry.

Water Utilities: Industry Overview

Crippling and Aging Water Infrastructure

The average U.S. consumer has grown accustomed to the luxury of receiving clean drinking water and the management of wastewater, with little regard for the complicated and expansive systems necessary to deliver these services. For context, the United States has 1.2 million miles of drinking water supply mains and about an equal amount of sewer pipes. According to the Environmental Protection Agency (EPA) these systems are in dire need of investment, but the general public often has stark views over rising water prices, despite paying less than $0.01 per gallon. Further, water is generally the lowest percentage utility cost per household, despite being labeled as the most important service that customers receive (notably ahead of electricity and heat), according to a study conducted by Xylem Inc. (covered by Deane Dray). The discrepancy between necessary infrastructure investments and customer pushback over the rising cost of water will likely result in a dramatic shift in the way that water is priced in the future. In order for this to happen, water pricing must be restructured to cover the full costs of treatment and delivery to consumers, including expenses related to building, operating and maintaining and replacing water systems.

EPA regulates the industry at the federal level; PUCs at the state level. The EPA is tasked with setting the water quality standards while the state economic regulatory agencies, generally referred to as Public Utility Commissions (PUCs) govern the price impact of water services for investor-owned utilities. Investor-owned utilities are granted authority by each state's PUC to operate in a service area while receiving some protection from competition in exchange for quality and reliable service. The utility is entitled to a reasonable rate of return (allowed return) on prudently invested capital and can recover operating expenses. This is accomplished through rate cases.

Investments are passed onto rates via rate cases. In most states, municipal-owned water utilities generally set their own rates and do not have to go through a state PUC approval process. Political leaders are often reluctant to increase rates as that may cause unpopular opposition from voters. Thus, needed but costly infrastructure repairs may be postponed or avoided in order to keep rates low. Meanwhile, state PUC regulation of investor-owned utilities helps promote necessary infrastructure investment, rehabilitation and/or replacement, and maintenance. It does so not only by enforcing the utility's obligation to provide safe and reliable service, but also by setting rates that cover the costs of providing that service, including a fair return on invested capital.

Water is generally a good value proposition for customers

Most customers don't understand the water framework, but view water as essential. It is a fair characterization to admit that most U.S. customers overlook the value of the water that comes out of their faucets. Ratepayers of municipal systems or investor-owned utilities generally don't think about the pathway of how their water arrives in their homes or how it is treated and to what extent before being delivered. Ratepayers living in rentals may be so disassociated with water bills, they may often not be aware of the cost or dynamics of clean water, but even when paid directly ratepayers scuffle over paying on average less than a token penny per gallon of water vs a typical water bottle costing $1.50.

The average household pays roughly $540 a year for water and wastewater services compared to about $730 for soft drinks alone. In addition, water and wastewater services are typically the lowest percentage utility cost per household, representing about 12% of bills, compared to gas at 18%, telephone at 33%, and electricity at 37%. This historical underpricing of water is largely driven by lingering public perceptions that water is a fundamental human need supplied by the earth itself, i.e. free. These consumer perceptions have prevented

municipal utilities from attracting the necessary capital required to upgrade and maintain networks. Unfortunately, under-investment and inadequate water systems and/or lack of governance have caused instances like Flint, Michigan to occur, rendering national attention given the detrimental health and wellness effects of contaminated water. The water crisis in Flint displayed the disastrous consequences of lead contamination, but importantly also outlined the many other competing agendas that water utilities wrestle with including: (1) managing other drinking containments; (2) supervising wastewater treatment; and (3) handling storm water overflows. Notably, the EPA estimates 1.8 million to 3.5 million people per annum become ill from recreational contact to contaminated water. Further, the EPA estimates that about 850-900 billion gallons of untreated sewage is discharged into waterways every year due to aging pipes and inadequate resources.

Resulting from decades of underinvestment, water's aging infrastructure is in dire need of investment compounded by being the most capital intensive utility subsector. These challenges present ample investment opportunities for investor-owned utilities. The EPA estimates that $775 billion is needed to be invested in water and wastewater through 2040 due to decades of under-investment. A competing study produced by the American Water Works Association (AWWA) estimates water infrastructure needs will total more than $1 trillion over a similar timeframe, assuming pipes are replaced at the end of their service lives. As it stands today, U.S. water systems were slapped with a D+ grade and drinking water systems received a D rating from the American Society of Civil Engineers. Encouragingly, IOUs are increasing liaising with municipalities in mutual efforts to tackle the crippling and aging water infrastructure deficiencies. One of the tools is Fair Market Value legislation that we will be addressing in the next section.

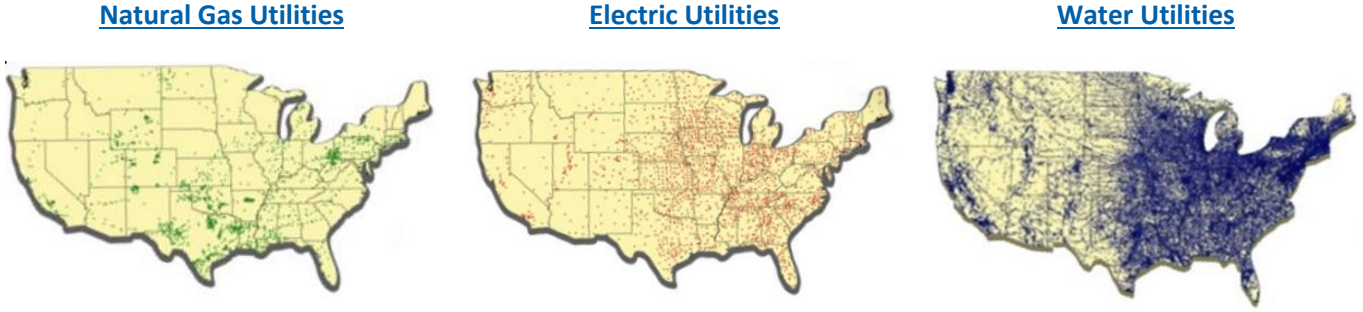
Only a fraction of the contaminants are regulated by the EPA

The EPA only regulates a fraction of the emerging water contaminants presenting a massive gap between the number of chemicals and the amount that are currently regulated. On a global scale, there are roughly 144 million chemicals registered under the Chemicals Abstracts Service. New chemicals are formed rapidly, roughly every 2.5 seconds, caused by a breakdown of existing chemicals. Further, there are about 1,400 microbial pathogens that are managed by water providers and only about 6% are regulated by the EPA. This doesn't mean that consumers aren't focused on the quality of water. For example, perfluorinated compounds (PFCs) were found in 162 water systems across the U.S. impacting 15 million people in 2017. PFCs are known to bioaccumulate and persist in the environment, and animal studies indicate that they are toxic, affecting reproduction and development, despite showing limited health effects in people. To augment to reality of not covering all bases, water utilities are increasingly implementing artificial intelligence (AI) and machine learning technologies to detect a broader range of contaminants.

Highly fragmented industry ripe for consolidation

The U.S. water and wastewater industry is heavily commoditized. The fragmented nature of the water industry is highlighted by roughly 50,000 water systems in the U.S. and about 15,000 community wastewater systems compared to 1,400 gas systems and 3,800 electric systems. Further, roughly 84% and 98% of the U.S. population is served by municipal water systems and wastewater systems, respectively. Additionally, half of the water and wastewater systems serve a population of less than 500, which generally don't provide enough scale that could warrant IOU interest.

Exhibit A: U.S. water among the most fragmented utility sectors



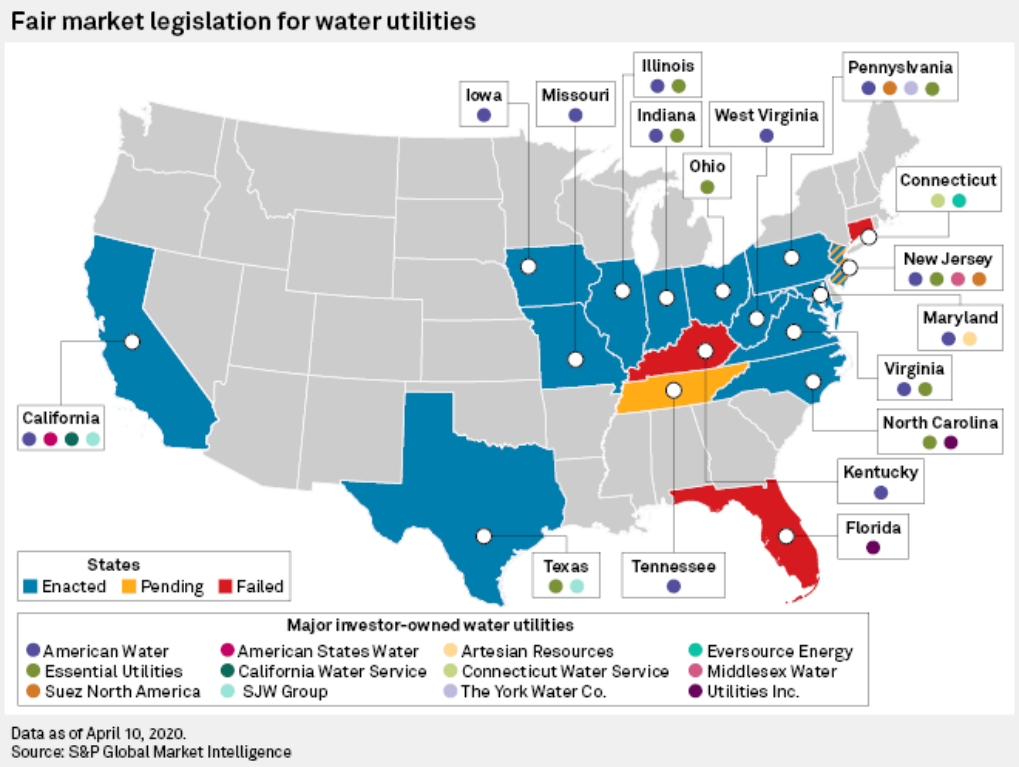
Source: Enviornmental Protection Agency and Energy Information Administration

Fair Market Value Legislation is leading to more deal-making

Fair market value assessment of water and wastewater systems is increasingly becoming a preferred alternative to the traditional depreciated original cost method, providing mutually beneficial outcomes to both the buyer and seller of municipal systems. Sellers are able to capture the true value of their assets while buyers are allowed to add the total purchase price to rate base, without padding goodwill, dubbing the premium an "acquisition adjustment". California became the first state to adopt fair market value legislation in 1997 following the passage of SB 1268. Since California's approval, eleven other states have adopted comparable approaches including Indiana, Missouri, Illinois, Iowa, Ohio, Pennsylvania, New Jersey, Maryland, and North Carolina, Texas, and Virginia. These states have subsequently turned into prime battlegrounds for IOUs fetching acquisition targets, further labeling the water industry as "ripe for consolidation". We believe that this legislation has already proven to and will continue to encourage consolidation in the water and wastewater industry. In our view, further acquisitions of municipal networks will provide operators with an option to exit the management of deteriorating water and wastewater assets, offer the ability to focus on other community priorities, and forfeit the need to comply with ever increasing environmental regulations despite having limited technical expertise. Of the 20,000 municipal water systems that are possible acquisition targets, we believe only a fraction of these are scalable enough to warrant acquisition consideration from IOUs. Companies are generally limited to their core operating states, and the acquired customer count generally needs to pass certain thresholds to be considered a viable takeout candidate.

The idea behind FMV is to create a win-win for IOUs and municipalities. In the utility world, regulators generally do not allow the acquiring company to earn on the full amount that it paid to acquire another company, if a premium is involved. Goodwill in essence becomes a stranded asset. In other industries, to the extent that you can create cost savings through synergies, paying the premium may be justified. However, utility rates are set by regulators that do not allow the company to keep the savings once a rate case is filed. These issues tend to cap the amount that companies are willing to pay for utility assets. The legislation allows IOUs to add approved goodwill to the rate base when buying a municipality or cooperative in states that feature FMV. It allows the acquiring companies to provide a better incentive for the municipality to sell its under-invested assets, while allowing the company a better opportunity to earn a fair return on the acquisition capital.

Exhibit B: Fair market value state legislation and investor-owned water utility footprints

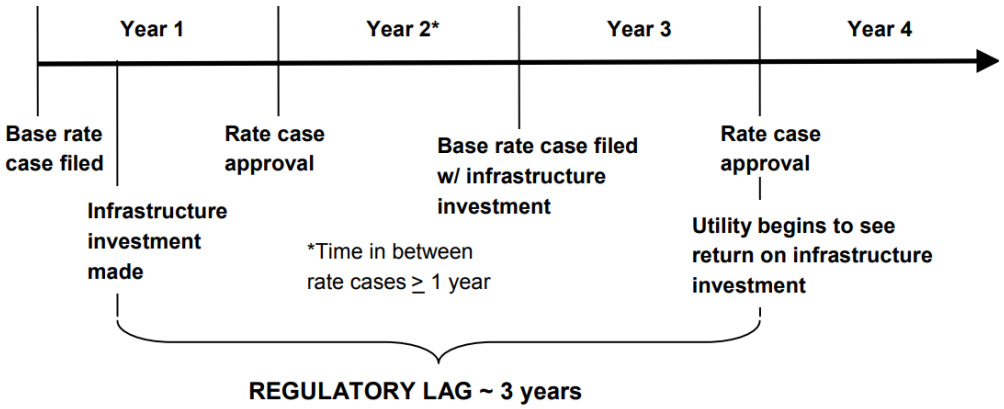


Source: Company reports, S&P Global Market Intelligence

Distribution system improvement charge

Water utilities are roughly 2x more capital intensive than their electric peers and 3x than their gas peers. As a result, repairing and replacing water and wastewater infrastructure has proven to be economically and politically challenging, primarily reflecting the impact on customer rates. To reflect this, public utility commissions (PUCs) have established infrastructure replacement surcharge programs to encourage water and wastewater infrastructure investments. Surcharge programs allow utilities to recover costs in a timelier fashion, effectively allowing them to extend the timeline between filing general rate cases, generally referred to as a stay-out. Surcharges also drive moderate base rate increases for customers, resulting in reduced customer rate shocks. Further, surcharge mechanisms help mitigate regulatory lag. Typically when a regulated water utility invests in a project, it seeks a return by filing for base rate increases through a rate case. Often, this process can be lengthy resulting in the aforementioned regulatory lag, a term coined from the time an investment is made until a utility is able to earn a return on that investment. This lag can obstruct a utilities ability to attract capital, weigh on its credit metrics, and may potentially limit necessary investments in systems.

Exhibit C: Impacting of regulatory lag



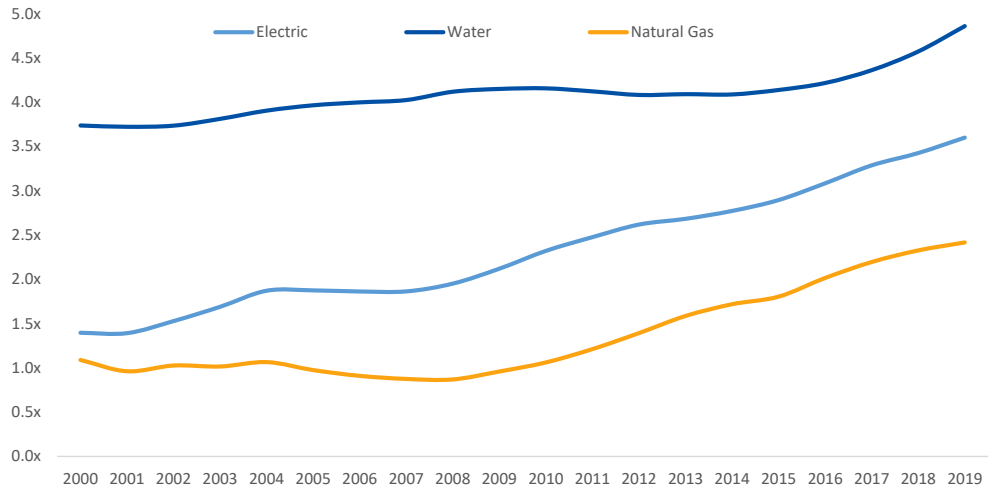
Source: American Water Works White Papers

Regulatory lag tends to have an especially adverse impact for water utilities, and consequently lead to sub-par returns during periods of heavy capital investment, due to the highly capital intensive nature of the businesses. The figure below demonstrates this dynamic. For illustrative purposes, the example showcases a historical test year (investments made during the rate case filing year would not be included in that rate case due to the investments falling outside of the test year). Assuming a general one-year timeline to conduct rate case proceedings, a utility would essentially be disallowed to earn a return on its first year's investments until year three. Surcharge rates are adjusted periodically based on infrastructure projects currently in progress or expected to be complete, but are typically reset to zero when a new base rate case begins, effectively rolling the surcharge based investments into the rate base. Further, surcharge rates are typically capped at 5.0% and 7.5% of a utility's annual revenue.

Capital intensity drives sustainable rate base growth

We believe the water utility sector has several unique and characteristics compared to the electric and gas sectors, particularly as it relates to return-generating projects and the associated revenue requirements to maintain infrastructure investments. Capital costs are mainly concentrated in pumping equipment, treatment facilities, and distribution systems. As noted previously, water utilities are roughly 2.0x more capital intensive than their electric peers and 3.0x more than their gas peers. Further, the net PP&E to revenues ratio for investor-owned water utilities is about 5.0x, compared to electric utilities of 3.4x and natural gas utilities of 2.3x. In our view, this ratio showcases the importance of infrastructure spending as a key characteristic of the industry's cost structure, and therefore making it difficult to pare back and reduce capital costs. Even as companies continue to drive their efficiency ratios lower, notably American Water Works and Aqua America, operating costs can only offset capital costs to a limited extent. In the figure below, we highlight the delta between the net utility PP&E to revenues of the three utility sub-sectors.

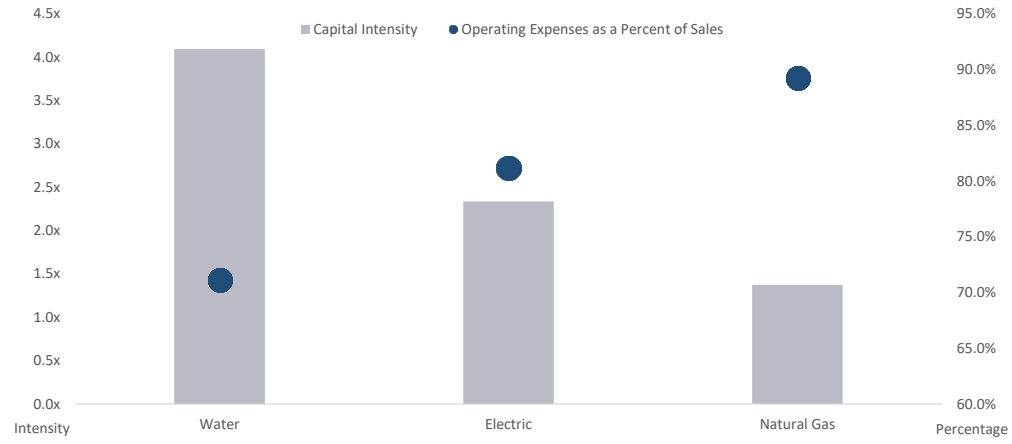
Exhibit D: Net utility PP&E to revenues



Note: Water, Natural Gas, and Electric Peers Include:
Water Peers: ARTNA, AWK, AWR, CWT, MSEX, SJW, WTRG, YORW
Natural Gas Peers: ATO, CPK, NJR, NWN, OGS, SJI, SR, SWX
Electric Peers: AEE, AEP, ED, ES, EVRG, PNM, PNW, PPL, SO, WEC, XEL
Source: Company reports

Despite the aforementioned capital intensive nature of the water utility sector, on a relative basis, companies generally spend the least amount of O&M dollars to maintain their assets vs electric and gas peers. To put this into perspective, over the past twenty years, water utility O&M expenses as a percent of PP&E averaged 20% compared to gas utilities at 40% and electric utilities at 60%. This leads us to believe that more water utility revenues are geared towards return-generating investments vs electric and gas peers which allocate a greater portion of expenses towards pass through costs that generally do not generate a return. This suggests to us that any incremental O&M savings could lead to further investment in capex dollars which eventually translate to higher rate base and earnings growth.

Exhibit E: Capital intensity and O&M expenses by utility sub-sector



Note: Water, Natural Gas, and Electric Peers Include:
Water Peers: ARTNA, AWK, AWR, CWT, MSEX, SJW, WTRG, YORW
Natural Gas Peers: ATO, CPK, NJR, NWN, OGS, SJI, SR, SWX
Electric Peers: AEE, AEP, ED, ES, EVRG, PNM, PNW, PPL, SO, WEC, XEL
Source: FactSet, Company reports, RBC Capital Markets

Environmental, Social Responsibility, and Governance

Environmental, social responsibility, and governance (ESG) principles are increasingly becoming mainstream components of investment decisions. The Global Sustainable Investment Alliance Review estimates that $17.5 trillion of sustainable-investing AUM globally proactively consider ESG components alongside financial analysis when contemplating investment decisions. To this extent, water utilities are stewards of a critical natural resource which has naturally drawn a connection to ESG principles. We believe American Water has established itself as the ESG template within the utility industry, ranking 23rd on Barron's most sustainable companies list, and the highest ranked utility.

The water utility industry generally scores higher in ESG than its electric/gas counterparts for a variety of reasons. The inherent asset profile for water utilities is considered superior to the asset profile of electric and gas utilities, principally due to the lack of coal, nuclear, natural gas, and pipelines. Additionally, water assets generally are considered higher-quality and safer.

The Sustainable Accounting Standards Board (SASB) provides a framework for analyzing ESG factors among electric, gas, and water utilities. In SASB's Materiality Map, which highlights various dimensions and general issues that would be material in evaluating a company's ESG profile, there are only two general issues that are considered material across electric, gas, and water utilities: Access & Affordability and Business Model Resilience. This highlights the inherent differences among the business profiles, in our view.

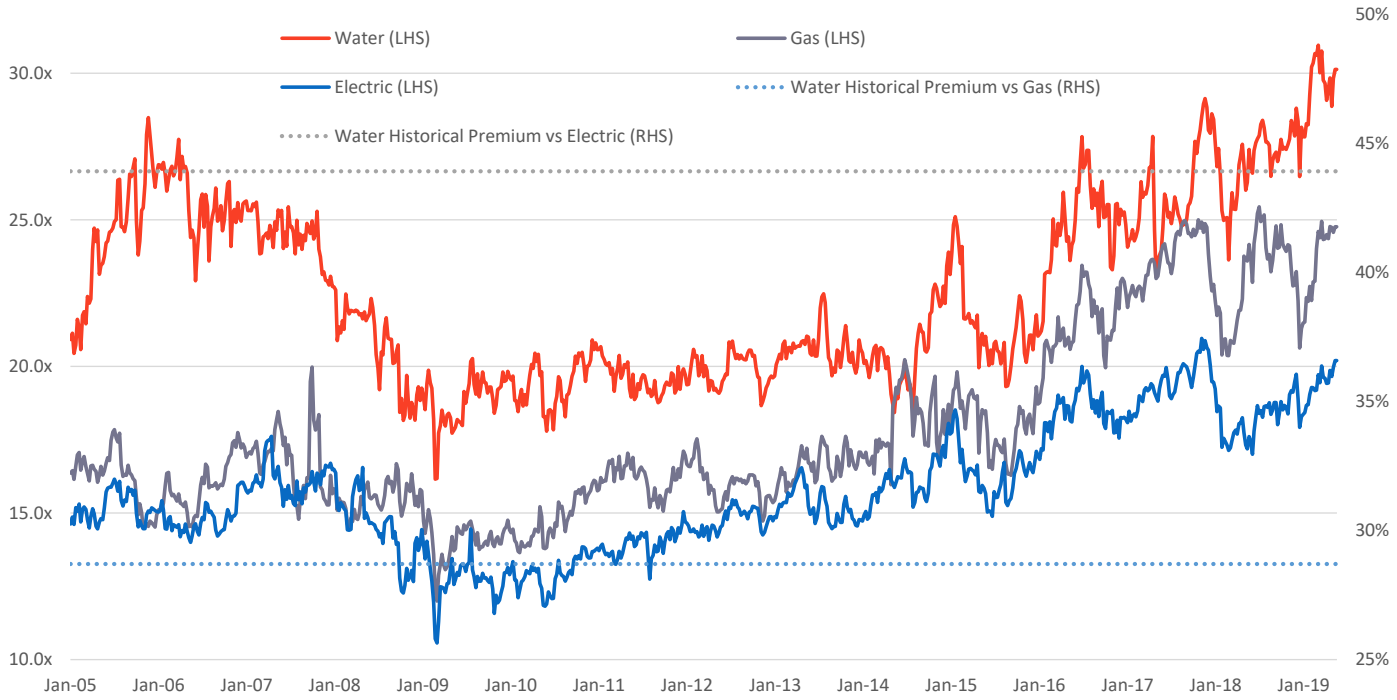
While we recognize that water utilities' environmental aspects are generally accepted as superior to electric/gas utilities, this is not the whole ESG story. When analyzing the ESG profiles of water utilities, it is important to compare water utilities among water utilities, meaning the E becomes less important on a relative basis. To us, key factors to consider include disclosure/quality of data (reporting under SASB standards, issuing sustainability reports, etc.), customer rates at or below national average, diversity of employees and Boards of Directors, and separation of CEO/Chairman.

Valuation Considerations

You Get What You Pay For

Utilities are commonly known for driving predictable earnings growth, and therefore it is common practice to use the price-to-earnings (P/E) ratio to calculate the value of utility equities. Valuations are also driven by utilities' established incumbent status, high barriers to entry, low commodity price exposure, increasing regulatory support, and steady (although generally declining) regulated returns. To this extent, regulated water, electric, and natural gas utilities have historically established what we view as 'entitled' multiples that vary quite a bit from one another. However, these utilities generally do not trade away from their respective peers (water, electric, gas) often, and instead stay within a fairly narrow band of valuation. Over the past fifteen years, water utilities averaged a ~23.0x next-twelve-month P/E ratio, reflecting a +30% premium to its natural gas peers, and a +45% premium vs its electric peers over the course.

Exhibit F: Water, natural gas, and electric utility peers forward P/E ratios



Note: Water, Natural Gas, and Electric Peers Include:
Water Peers: ARTNA, AWK, AWR, CTWS, CWT, MSEX, SJW, WTRG, YORW
Natural Gas Peers: ATO, CPK, NJR, NWN, OGS, SJI, SR, SWX
Electric Peers: AEE, AEP, ED, ES, EVRG, PNM, PNW, PPL, SO, WEC, XEL
Source: FactSet, RBC Capital Markets estimates

We believe structural differences between water utilities and their peers, which include several other factors, have contributed to the lofty historical premium. We highlight some of our observations below:

Naturally lower risk assets. Despite being the most capital intensive utility sector, water utilities are naturally lower risk assets and therefore command higher valuation multiples relative to their electric and natural gas peers. Recent PG&E investor capitulation following the devastating November 2018 Camp Fire, the natural gas explosions plaguing NiSource, or implications of fracking remind us of the elevated risks natural gas and electric utility peers absorb.

We believe prices may be moving higher. Until water is priced in a way that encourages wise use, reflects the true cost of delivering it, and allows for adequate replacement of that infrastructure, Americans will continue to take water for granted, and the infrastructure that makes it so easy for them to do so will continue to deteriorate.

Municipal acquisitions drive positive estimate revisions. Municipal acquisitions, and in particular fair market value legislation allow municipalities to be acquired for fair market prices. In turn, acquirers can add the total purchase price to the rate base, allowing water utilities to earn a return on the full rate base, without padding goodwill on the balance sheet. We estimate every $100 million deployed towards municipal acquisitions adds roughly $5 million to net income, assuming a best case scenario of regulatory lag.

Pure-play scarcity multiple applied to water peers. To a certain extent, water utility valuations are also driven by "scarcity value". This leaves funds with investment specific mandates a small selection of water utilities to invest in. There are only nine publicly traded water utilities, including Essential Utilities. Reflecting this treatment, we observed forced-selling in Essential Utilities (formerly known as Aqua America) shares in conjunction with its October 2018 Peoples Gas acquisition announcement for $4.5 billion.

Bite-sized enterprise values draw takeout considerations. The total market capitalization of publicly traded water utilities stands at roughly $44 billion vs ~$57 billion for their natural gas peers and ~$816 billion for their electric and multi-utility peers. We note that American Water Works and Essential Utilities represent about 78% of the aggregate water utility market capitalizations. In our view, this reflects the relatively bite-sized enterprise values of water utilities, despite above-average P/E ratios. To date, we've only observed Essential Utilities willing to dilute its pure-play water multiple with the announcement of its Peoples Gas acquisition, but we wouldn't rule out water acquisitions by electric and gas utilities. For now, the valuation multiple disparities present challenges to structure accretive acquisitions though we have seen more electric and gas utilities ramp up their respective ESG efforts which we believe could lead to higher valuation multiples for these entities.

Environmental, Social, and Governance (ESG) characteristics drive higher multiples. We believe utilities that have deliberately applied ESG principles fetch higher valuation multiples. The ESG model is easily implemented in the water framework given the very nature of the business models and strategic visions balance the provision of essential services with environmental stewardship, affordability, and financial integrity. To this tune, we believe ESG-focused companies generally exhibit higher quality of earnings driven by lower earnings volatility and higher return on equity. These characteristics have also drive higher P/E ratios.

Distribution Surcharge Infrastructure Changes (DSIC) arguably shift risks away from investors. Water utilities are known to stay out of rate cases and we believe this is a function of DSIC. Surcharges are reset to zero during the next rate or in the event that a company exceeds its allowed ROE.

Valuation framework

Inherent higher growth and ESG premiums lead to sustainably greater valuations. Our valuation framework for utilities is derived from the dividend discount model, where we assume a run rate risk free at 3.5% (well above the current 10-year Treasury yield of 0.65%). Exhibit G below shows the base P/E calculation that we employ for a traditional slow-growing electric utility.

Exhibit G: 3%-growing electric utility starts with a 17.8x forward P/E multiple

Cost of Equity Calculation		Absolute P/E Calculation	
Market Premium	6.3%	Dividend Payout Ratio	66.0%
Regulated Electric Beta	0.53	Dividend/Share Growth (g)	3.0%
10-Yr Treasury	3.50%	ESG premium	0.0%
Return on Equity (k)	6.8%	**RBC's Sustainable P/E**	**17.8x**

Source: Bloomberg; FactSet; RBC Capital Markets

We note that the above calculation tries to capture the long-term run rate utility, which, absent the heavy infrastructure requirements that exist in the electric business today, would likely grow only 3% a year, versus the foreseeable growth of 5%-6% a year.

There are only three variables that change for the water sector. One, we were somewhat surprised that the water utility beta is roughly in line to slightly higher than the electric beta. It may be due to the fact that the majority of water utilities are small to mid cap stocks, which can exhibit greater volatility. Two, the underpinning secular growth of the water sector is greater. We have assumed that a slow growing water company should manage to grow 4% per year. And three, we are introducing an ESG premium to our valuation with the launch of our water utility roll-out. We assume that the group starts with a 10% premium due to a combination of ESG investors and water funds that enhance the scarcity value of water stock. When we factor all that in, we arrive at a base P/E of 24.9x, as shown below. From there, we add a premium or discount based on numerous factors, including: quality of regulation, higher/lower growth rate expectation, quality of earnings/cash flow/credit, etc.

Exhibit H: 4%-growing water utility starts with a 24.9x forward P/E multiple

Cost of Equity Calculation		Absolute P/E Calculation	
Market Premium	6.3%	Dividend Payout Ratio	64.0%
Regulated Water Beta	0.55	Dividend/Share Growth (g)	4.0%
10-Yr Treasury	3.50%	ESG/water premium	10.0%
Return on Equity (k)	6.9%	**RBC's Sustainable P/E**	**24.9x**

Source: Bloomberg; FactSet; RBC Capital Markets

Essential Utilities, Inc.	Shelby G. Tucker, CFA; RBC Capital Markets
Consolidated Income Statement	**+1 (212) 428-6462; shelby.tucker@rbccm.com**

Fiscal Year Ending December 31,
($ in millions, except per share amounts)

INCOME STATEMENT	2018	2019	2020E	2021E	2022E	2023E
Revenues						
Adjusted Regulated Water Revenues	814.5	886.4	961.6	1,047.0	1,116.8	1,188.6
Regulated Natural Gas Revenues	-	-	611.8	982.8	1,030.6	1,085.6
Purchased Water	20.2	20.0	20.0	20.0	20.0	20.0
Other	3.5	3.3	5.0	5.0	5.0	5.0
Non-Recurring Revenues	-	-	-	-	-	-
Operating Revenues	**838.1**	**889.7**	**1,598.4**	**2,054.8**	**2,172.4**	**2,299.1**
Operating Expenses						
Purchased Water	(20.2)	(20.0)	(20.0)	(20.0)	(20.0)	(20.0)
Purchased Gas	-	-	(238.6)	(373.5)	(381.3)	(401.7)
Operations and Maintenance	(272.1)	(313.1)	(486.2)	(573.9)	(601.8)	(629.2)
Other Operations and Maintenance	(16.2)	(18.1)	(15.0)	(15.0)	(15.0)	(15.0)
Operations and Maintenance	(308.5)	(333.1)	(521.2)	(608.9)	(636.8)	(664.2)
Depreciation	(146.0)	(158.2)	(240.5)	(293.2)	(316.0)	(339.1)
Amortization	(0.6)	1.7	(0.5)	(0.5)	(0.5)	(0.5)
Taxes, Other than Income Taxes	(59.8)	(60.0)	(75.9)	(88.8)	(95.4)	(102.1)
Non-Recurring Operating Expenses	-	-	-	-	-	-
Operating Expenses	**(514.9)**	**(549.5)**	**(1,076.8)**	**(1,364.9)**	**(1,430.1)**	**(1,507.5)**
Operating Income	**323.2**	**340.2**	**521.6**	**689.9**	**742.4**	**791.6**
EBITDA	**469.9**	**496.6**	**762.6**	**983.6**	**1,058.9**	**1,131.2**
Adjusted EBITDA	**409.9**	**467.1**	**764.6**	**985.6**	**1,060.9**	**1,133.2**
Interest Expense	(98.9)	(100.0)	(201.7)	(237.2)	(256.8)	(271.2)
Allowance for funds during construction	13.0	16.2	16.0	16.0	16.0	16.0
Change in fair value of interest rate swap agreements	(59.779)	(23.742)				
Gain on sale of other assets	0.7	0.9	-	-	-	-
Equity (earnings) loss in joint venture	2.1	2.2	2.0	2.0	2.0	2.0
Other	(61.8)	(48.0)	-	-	-	-
EBT	**118.5**	**187.8**	**337.9**	**470.7**	**503.6**	**538.4**
Income Taxes	13.7	13.0	(27.6)	(32.7)	(34.9)	(37.2)
Effective Tax Rate	-11.5%	-6.9%	8.2%	6.9%	6.9%	6.9%
Income from Continuing Operations	**132.2**	**200.8**	**310.3**	**438.0**	**468.7**	**501.2**
Income from Discontinued Ops.	-	-	-	-	-	-
Net Income (GAAP)	**132.2**	**200.8**	**310.3**	**438.0**	**468.7**	**501.2**
Adjustments	58.8	39.0	-	-	-	-
Adjusted Net Income	**191.0**	**239.8**	**310.3**	**438.0**	**468.7**	**501.2**
Earnings Growth						
Adjusted Earnings Per Share - Diluted	**$1.07**	**$1.47**	**$1.21**	**$1.67**	**$1.78**	**$1.89**
EPS Growth	*-20.4%*	*37.3%*	*-17.6%*	*37.7%*	*6.5%*	*6.5%*
Dividend per common share	$0.8474	$0.9066	$0.9700	$1.0378	$1.1104	$1.1882
Payout Ratio	*79.1%*	*61.7%*	*80.1%*	*62.2%*	*62.5%*	*62.8%*
Dividend Growth	*7.0%*	*7.0%*	*7.0%*	*7.0%*	*7.0%*	*7.0%*
Basic Common Shares Outstanding	177.9	215.6	255.8	262.1	263.2	264.2
Diluted Common Shares Outstanding	178.4	215.9	256.3	262.6	263.7	264.7

Source: Company Reports, RBC Capital Markets Estimates

RBC Capital Markets

Essential Utilities, Inc.	Shelby G. Tucker, CFA; RBC Capital Markets
Consolidated Statements of Cash Flow and Balance Sheet	**+1 (212) 428-6462; shelby.tucker@rbccm.com**

Fiscal Year Ending December 31,

($ in millions, except per share amounts)

CASH FLOW DATA	2018	2019	2020E	2021E	2022E	2023E
Operating Activities						
Net Income (from continuing operations)	192.0	224.5	310.3	438.0	468.7	501.2
Depreciation and Amortization	146.7	156.5	241.0	293.7	316.5	339.6
Deferred Income Taxes	(15.0)	(10.4)	12.5	25.0	25.0	25.0
Provision for Doubtful Accounts	5.3	5.3	5.0	5.0	5.0	5.0
Stock Based Compensation	7.6	7.4	7.0	7.0	7.0	7.0
Gain on Sale of Utility System, Other Assets	(0.7)	(1.3)	-	-	-	-
Loss and settlement on interest rate swap agreements	59.779	(59.8)				
Equity loss in Joint Venture	-	-	-	-	-	-
Working Capital	(17.5)	0.8	-	-	-	-
Pension and other Postretirement Benefit Contributions	(14.2)	(8.6)	-	-	-	-
Other	4.5	24.2	-	-	-	-
Cash Flow from Operations	**368.5**	**338.5**	**575.8**	**768.7**	**822.2**	**877.8**
Investing Activities						
Capital Expenditures	(495.7)	(550.3)	(810.0)	(959.5)	(969.1)	(978.8)
Acquisitions, Net	(145.7)	(59.7)	(3,515.0)	(326.5)	(100.0)	(100.0)
Additions/Release of Funds Related to Construction Activity	-	-	-	-	-	-
Net Proceeds from Sale of Utility Systems	0.7	2.9	-	-	-	-
Proceeds from Note Receivable	-	-	-	-	-	-
Other - Investing	0.9	2.5	-	-	-	-
Cash Flow from Investing	**(639.8)**	**(604.6)**	**(4,325.0)**	**(1,286.0)**	**(1,069.1)**	**(1,078.8)**
Financing Activities						
Customer Advances and Contributions in Aid of Construction	7.5	9.1	10.0	10.0	10.0	10.0
Repayment of Customers' Advances	(6.2)	(6.8)	(6.0)	(6.0)	(6.0)	(6.0)
Net Proceeds of Short Term Debt	11.8	10.3		(10.0)	40.0	-
Proceeds From Long Term Debt	1,331.9	1,409.3	1,100.0	950.0	1,100.0	650.0
Repayments of Long Term Debt	(914.1)	(1,048.5)	(7.4)	(208.9)	(655.4)	(182.4)
Proceeds From Issuance of Common Stock	5.2	1,272.1	1,050.0	50.0	50.0	50.0
Proceeds From Exercised Stock Options	1.5	1.9	-	-	-	-
Proceeds from tangible equity unit issuance	-	673.6	-	-	-	-
Stock Base Compensation Windfall Tax Benefit	-	-	-	-	-	-
Repurchase of Common Stock	(2.6)	(1.9)	-	-	-	-
Dividends Paid on Common Stock	(150.7)	(188.5)	(248.6)	(272.5)	(292.8)	(314.5)
Other	(13.4)	0.8	-	-	-	-
Cash Flow from Financing	**270.7**	**2,131.4**	**1,897.9**	**512.6**	**245.8**	**207.1**
Beginning Cash Balance	4.2	3.6	1,868.9	17.7	13.0	11.9
Change in Cash	(0.6)	1,865.3	(1,851.2)	(4.7)	(1.2)	6.1
Ending Cash Balance	**3.6**	**1,868.9**	**17.7**	**13.0**	**11.9**	**17.9**

Source: Company Reports, RBC Capital Markets Estimates

RBC Capital Markets

Essential Utilities, Inc.	Shelby G. Tucker, CFA; RBC Capital Markets
Consolidated Statements of Cash Flow and Balance Sheet	**+1 (212) 428-6462; shelby.tucker@rbccm.com**

Fiscal Year Ending December 31,
($ in millions, except per share amounts)

BALANCE SHEET DATA	2018	2019	2020E	2021E	2022E	2023E
ASSETS						
Cash & Equivalents	3.6	1,868.9	17.7	13.0	11.9	17.9
Accounts Receivable	101.2	67.1	191.8	246.6	260.7	275.9
Inventory, Materials and Supplies	15.8	40.5	32.0	41.1	43.4	46.0
Gas Stored - Current Portion		18.4				
Prepayments and Other Current Assets	26.5	17.8	17.8	17.8	17.8	17.8
Total Current Assets	**147.2**	**2,012.7**	**259.3**	**318.5**	**333.8**	**357.6**
Property, Plant and Equipment						
Property, Plant & Equipment, gross	7,648.5	8,201.9	12,644.2	13,930.2	14,999.3	16,078.1
Less: Accumulated Depreciation	(1,718.1)	(1,856.1)	(3,310.8)	(3,604.5)	(3,921.0)	(4,260.6)
Property, Plant and Equipment, net	**5,930.3**	**6,345.8**	**9,333.4**	**10,325.7**	**11,078.3**	**11,817.5**
Regulatory Assets	788.1	878.1	1,181.6	1,181.6	1,181.6	1,181.6
Deferred Charges and Other Assets, Net	39.2	42.7	56.5	14.3	21.6	29.9
Investment in Joint Venture	7.0	6.0	6.0	6.0	6.0	6.0
Funds Restricted for Construction Activity	-	-	-	-	-	-
Goodwill and Intangibles	52.7	63.8	2,369.9	2,369.9	2,369.9	2,369.9
Operating lease right of use	-	12.9	68.8	68.8	68.8	68.8
Total Long Term Assets	**6,817.3**	**7,349.2**	**13,016.2**	**13,966.3**	**14,726.1**	**15,473.6**
TOTAL ASSETS	**6,964.5**	**9,362.0**	**13,275.5**	**14,284.8**	**15,060.0**	**15,831.3**
LIABILITIES						
Current Maturities of Long-Term Debt	144.5	105.1	208.9	780.4	182.4	51.5
Loan Payable	15.4	25.7	25.7	15.7	55.7	55.7
Accounts Payable	77.3	74.9	82.4	90.7	99.7	109.7
Accrued Interest	23.3	29.8	32.8	36.1	39.7	43.7
Accrued Taxes	22.2	22.8	25.1	27.6	30.3	33.3
Regulatory liabilities - current portion	-	-	-	-	-	-
Other Current Liabilities	116.1	60.6	66.6	73.3	80.6	88.7
Total Current Liabilities	**399.0**	**318.8**	**441.5**	**1,023.7**	**488.5**	**382.6**
Long Term Liabilities						
Long Term Debt, Excluding Current Portion	2,398.5	2,943.3	5,587.5	5,757.1	6,799.7	7,398.2
Deferred Income Taxes and Investment Tax Credits	845.4	936.2	948.7	973.7	998.7	1,023.7
Customers' Advances for Construction	93.3	95.6	105.6	115.6	125.6	135.6
Regulatory Liabilities	531.0	517.6	517.6	517.6	517.6	517.6
Other	97.2	102.5	102.5	102.5	102.5	102.5
Operating lease liabilities	-	11.6	11.6	11.6	11.6	11.6
Contributions in Aid for Construction	590.7	555.5	555.5	555.5	555.5	555.5
Total Deferred Credit and Other Liabilities	**4,556.2**	**5,162.3**	**7,829.0**	**8,033.6**	**9,111.2**	**9,744.7**
Total Liabilities	**4,955.1**	**5,481.1**	**8,270.5**	**9,057.3**	**9,599.6**	**10,127.2**
Shareholders' Equity						
Common Stock	90.6	111.9	118.9	125.9	132.9	139.9
Capital in Excess of Par Value	820.4	2,636.6	3,686.6	3,736.6	3,786.6	3,836.6
Retained Earnings	1,174.2	1,210.1	1,271.8	1,437.3	1,613.1	1,799.8
Treasury Stock	(75.8)	(77.7)	(77.7)	(77.7)	(77.7)	(77.7)
Accumulated Other Comprehensive Income	-	-	5.4	5.4	5.4	5.4
Noncontrolling interests	-	-	-	-	-	-
Stockholder's Equity	**2,009.4**	**3,880.9**	**5,005.0**	**5,227.5**	**5,460.4**	**5,704.1**
TOTAL LIABILITIES AND EQUITY	**6,964.5**	**9,362.0**	**13,275.5**	**14,284.8**	**15,060.0**	**15,831.3**

Source: Company Reports, RBC Capital Markets Estimates

RBC Capital Markets

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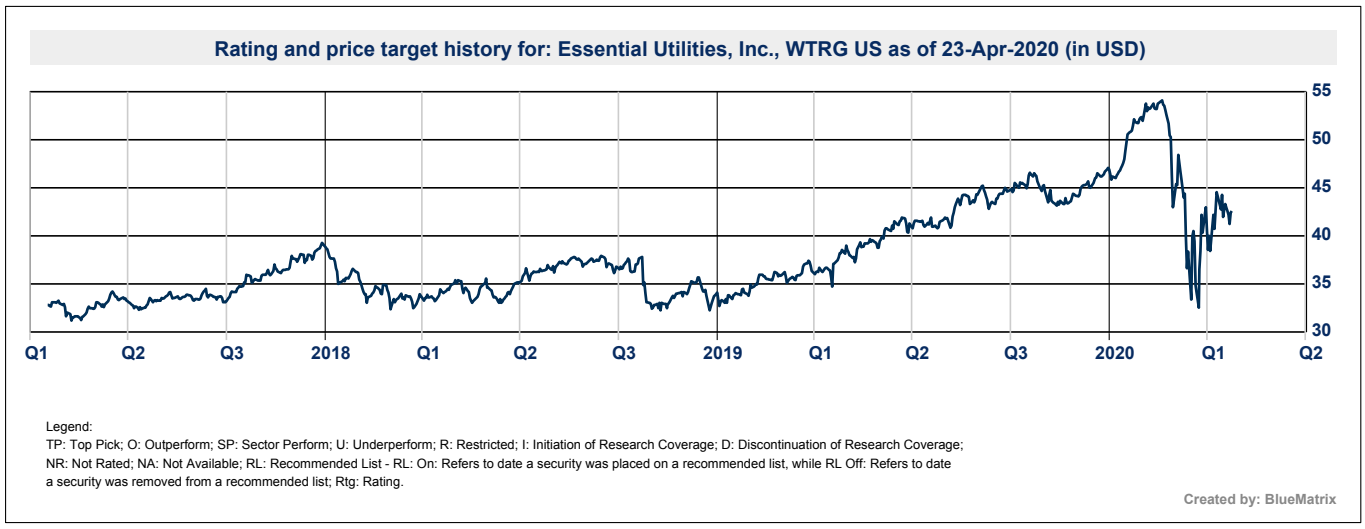
Distribution of ratings
RBC Capital Markets, Equity Research
As of 31-Mar-2020

			Investment Banking Serv./Past 12 Mos.	
Rating	Count	Percent	Count	Percent
BUY [Outperform]	755	51.64	220	29.14
HOLD [Sector Perform]	619	42.34	126	20.36
SELL [Underperform]	88	6.02	11	12.50



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Essential Utilities, Inc.

Valuation

Our $49 price target assumes WTRG trades at a 29.4x P/E multiple on our 2021 estimate of $1.67. This multiple represents a 25% premium to our base multiple of 24.9x P/E for water utilities and a 30% premium to our base multiple of 19.3x P/E for gas utilities. The implied return to our $49 price target supports our Outperform rating.

Risks to rating and price target

- Lower-than-anticipated adaptation of fair market value principles across the country could dampen expectations.
- M&A transactions could require greater equity than we forecast, or could result in a weaker balance sheet than we expect.
- Less favorable regulations or disruptions within public utility commissions could weigh on growth.
- Climate variability may cause increased volatility in weather and may impact water usage and related revenue, which may not be recoverable through rates.
- Continued lockdown from coronavirus could impact revenues, through higher bad debt expenses.
- ESG investing continues to gain traction, but WTRG does not meet certain ESG criteria due to Peoples, which makes it ineligible to benefit from these increased flows.

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January 12, 2021
Company Update
Utilities

Angie Storozynski
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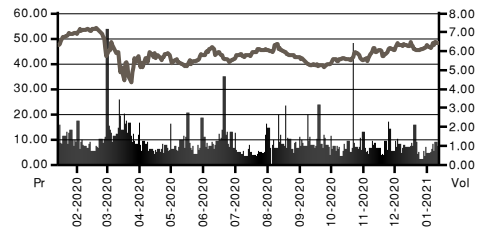
Rating:	**Neutral**
Price Target:	**N/A**

Price Target Metrics:
N/A

Current Price:	**$48.18**
Float:	244.8MM
Diluted Shares:	254.4MM
Short Interest:	9.8MM
Average Daily Volume:	920k
52 Week Range:	$30.40 - $54.52
Market Cap:	**$12,259MM**
Cash and Investments:	$5MM
Debt:	$5MM
Enterprise Value:	$12,259MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New	2023
EPS (Diluted)							
Q1 (Mar)	$0.60	$0.60A	$0.62	$0.62E	$0.63	$0.61E	$0.58E
Q2 (Jun)	$0.29	$0.29A	$0.31	$0.30E	$0.30	$0.29E	$0.28E
Q3 (Sep)	$0.23	$0.23A	$0.27	$0.27E	$0.30	$0.30E	$0.33E
Q4 (Dec)	$0.45	$0.45E	$0.46	$0.48E	$0.55	$0.58E	$0.71E
FY	$1.58	$1.58E	$1.66	$1.67E	$1.78	$1.78E	$1.90E
P/E		**30.5x**		**28.9x**		**27.1x**	**25.4x**
Dividends Per Share							
FY	$0.970	$0.970E	$1.038	$1.038E	$1.111	$1.111E	$1.188E
Dividend Yield		**2.0%**		**2.2%**		**2.3%**	**2.5%**

Essential Utilities, Inc.

(NYSE: WTRG)

Stock fully valued given market valuations of gas LDCs

Summary:
WTRG's 8.2%/10% water/gas rate base CAGR for 2020-2023 is very impressive, but fully reflected in its current share price, we believe, especially given the ongoing de-rating of gas LDCs, even those with premium rate base/earnings growth prospects. Yesterday, WTRG hosted its 2021 earnings guidance call. The midpoint of its $1.64-1.69 EPS guidance range is in line with consensus expectations.

Highlights

Strong momentum in water/wastewater municipal M&A: WTRG has $420.5MM in pending muni M&A deals on the water/wastewater side, including the $276MM DELCORA transaction which seems likely now that courts have upheld Aqua PA's purchase agreement for the asset. The deals should start boosting WTRG's water earnings in 2022/2023 assuming Aqua PA completes its next water rate case by mid-2022. That's reflected in our model which is based on an 8% water rate base CAGR for 2020-2023. Biden's likely infrastructure spending plan seems unlikely to derail the consolidation of the water/wastewater sector especially in states with the fair value legislation.

De-rating of stocks of gas LDCs: The marginal investor in stocks of US utilities continues to have a strict ESG screen hence the ongoing de-rating of stocks of gas LDCs. Among stand-alone gas LDCs, there is some P/E differentiation between strong (such as ATO or OGS) and weak EPS growers (such as SJI or NJR), but even the premium growers currently trade at a slight 3% discount to an average electric utility on 2023 EPS and at a 46% discount to an average water utility. With an 8-10% rate base CAGR for 2020-2023, WTRG's gas LDC is a fast grower, but that means it deserves to trade at just 16.5x 2023 EPS. A third of WTRG's 2023 EPS should come from gas which is the third highest in our coverage (after ATO and CMS) even after incorporating the DELCORA wastewater transaction.

Tweaking 2021 estimates, adding 2023 estimates: We raised our 2021 EPS estimate to $1.67 from $1.66 to reflect a slightly higher water rate base projection. Our 2022 EPS is unchanged as we added $300MM in equity in 2022 which fully offset the slightly higher water rate base estimate. We introduced our 2023 EPS of $1.90 which also reflects ~ $300MM in equity for that year. That should be enough to fund WTRG's current growth capex assuming the company is able to avoid paying federal cash taxes under Biden's proposed 15% minimum corporate income tax. We don't have PTs for Neutral-rated stocks, but to us, WTRG's current market valuation fully reflects its premium water/gas EPS growth prospects.

Company Description:
WTRG owns and operates water utilities (1 million accounts) and gas utilities (0.74 million accounts) in 10 states though mainly PA.

WTRG: EPS breakdown by segment ($)

WTRG	2019A	2020E	2021E	2022E	2022E	20-'23 CAGR
Regulated water utilities	1.47	1.10	1.15	1.25	1.31	
Regulated gas utilities	0.00	0.54	0.63	0.69	0.74	
Parent	0.00	-0.06	-0.12	-0.16	-0.15	
Total EPS	**1.47**	**1.58**	**1.67**	**1.78**	**1.90**	**6.4%**
DPS	**0.91**	**0.97**	**1.04**	**1.11**	**1.20**	**7.2%**
Dividend payout	62%	61%	62%	62%	63%	

Source: Company data for 2019; Seaport Global Securities

WTRG	2019A	2020E	2021E	2022E	2023E
Operational EBITDA	505	874	928	1,018	1,070
Operational EBIT	349	610	647	713	747
Net interest expense	100	202	210	233	223
Ordinary Profit Before Tax	269	437	466	512	559
Income tax	7	35	37	41	45
Net profit	262	402	429	471	515
S/O (m)	178	255	258	265	271
Diluted EPS	**1.47**	**1.58**	**1.67**	**1.78**	**1.90**
DPS	**0.91**	**0.97**	**1.04**	**1.11**	**1.20**
Cash	1,869	5	5	5	5
Receivables	108	110	113	121	126
Inventory	18	30	30	30	31
Other short-term assets	18	18	18	18	18
Other-long term assets	1,003	3,810	3,810	3,810	3,811
Property, plant, and equipment	6,346	9,081	9,659	9,929	10,181
Total assets	**9,362**	**13,054**	**13,635**	**13,913**	**14,172**
Financial liabilities	117	496	496	496	496
Operating liabilities	67	109	108	108	111
Other liabilities	108	220	220	220	220
Deferred credits	2,057	2,758	2,757	2,757	2,756
Long-term debt	2,943	4,750	5,619	5,769	5,932
Shareholders' equity	4,070	4,721	4,434	4,563	4,656
Total liabilities and equity	**9,362**	**13,054**	**13,635**	**13,913**	**14,172**
Net income	262	402	429	471	515
D&A, goodwill amortisation	156	264	281	305	323
Other non cash elements	-40	-6	-6	-6	-4
Funds from operations	379	660	704	769	833
Non-cash working capital	-40	43	-1	0	3
CFO	**339**	**703**	**703**	**769**	**836**
Net investments in fixed assets	-610	-6,675	-1,309	-925	-975
Net investments in financial assets	6	0	0	0	0
Free cash flow before dividends	**-266**	**-5,972**	**-606**	**-156**	**-139**
Dividends paid	-161	-242	-266	-293	-323
Free cash flow after dividends	-427	-6,214	-872	-449	-461
Changes in equity	1,935	302	2	298	298
Changes in financial debt	386	4,047	869	150	163
Adjustment for minorities / miscellaneous	-28	1	1	1	1
Increase in cash	1,866	-1,864	0	0	0

Essential Utilities, Inc. (WTRG) Disclosures

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Risks & Considerations for Essential Utilities, Inc. (WTRG)

Allowed ROEs for WTRG's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. WTRG's only pending rate case (in NC) is very small.

Lower sales volumes could weigh on WTRG's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, it's up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. WTRG's regulatory calendar is quiet in 2020, with a pending small rate case in NC, and a likely filing for a catch-up repair tax adjustment for Peoples in PA.

Gas utilities have a higher operating risk than water utilities: Over-pressurized gas systems seem to happen more frequently among gas utilities in the US. While we recognize that Peoples Gas is a well-managed system, WTRG's risk profile could further deteriorate with any gas-related operational issues. Additionally, investors increasingly scrutinize the carbon footprint of gas LDCs which in turn weighs on their market valuations.

Risks & Considerations for Atmos Energy Corp. Atmos Energy Corp. (ATO)

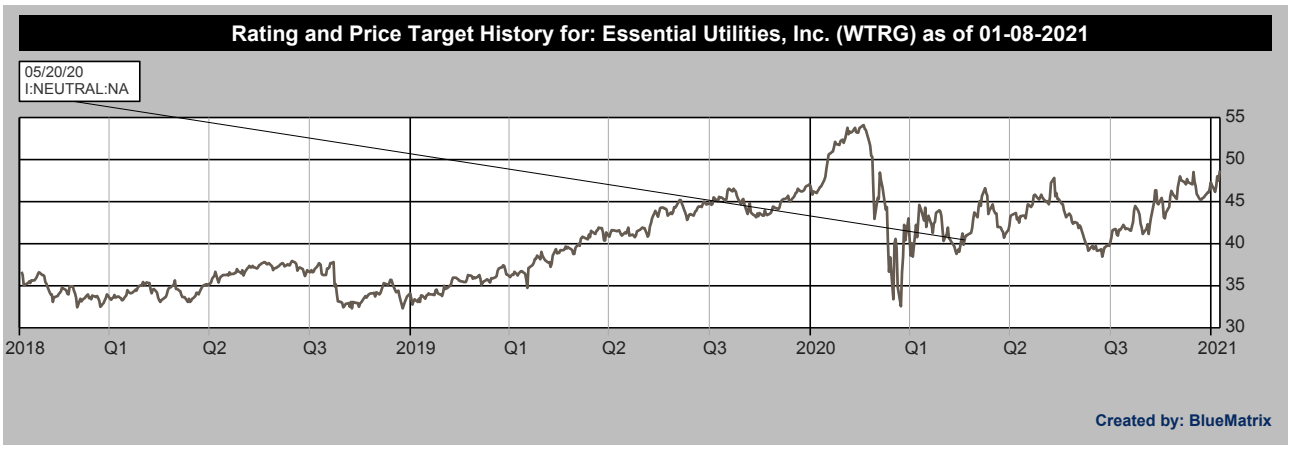
Allowed ROEs for ATO's gas LDCs and pipeline could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. ATO's gas LDCs and its pipeline have above-average allowed ROEs and equity ratios especially when compared to regulated electric utilities in TX. Future rate reviews could lead to lower allowed ROEs though cheap natural gas prices are supportive of premium returns for ATO's assets.

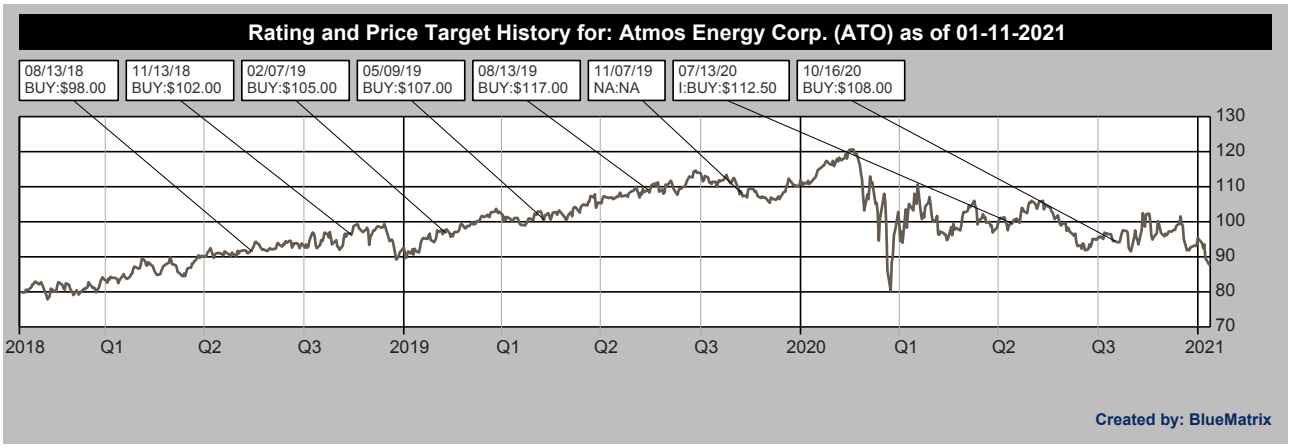
Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, it's up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings.

Gas distribution and transmission systems have a higher operating risk than electric systems: Overpressurized gas distribution pipes have led to explosions and severe regulatory repercussions especially in California and the Northeast. While ATO was not involved in any of these accidents and the company operates in very constructive regulatory regimes, we still see some elevated operating risk vs. an average regulatory utility we cover.

Other Companies Mentioned in This Report

- Atmos Energy Corp. (ATO: $87.67, Buy)
- New Jersey Resources Corp. (NJR: $35.78)
- ONE Gas Inc. (OGS: $71.92)
- South Jersey Industries Inc. (SJI: $21.86)





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NA - A rating is not assigned.

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Reduce - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.

Sell - The investment outlook and risk/reward over the following 12 months are very unfavorable on an absolute basis and relative to the peer group.

NA - A rating is not assigned.

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	Research Coverage		Investment Banking Clients*		
Rating	Count	% of Total	Count	% of Total	% of Rating Category
Buy	124	63.9%	2	100.0%	1.6%
Neutral	68	35.1%	0	0.0%	0.0%
Sell	2	1.0%	0	0.0%	0.0%
Total	194	100.0%	2	100.0%	1.0%

*Investment banking clients are companies for whom Seaport Global Securities has provided investment banking services in the previous 12 months.

Note: Ratings Distribution as of December 31, 2020

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May 20, 2020
Initiating Coverage
Utilities/Power

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Utilities/Power

Water Utilities: For growth and safety; Initiating coverage of AWK, AWR, CWT, SJW, and WTRG

Summary:
We are initiating coverage of water utilities with a bullish outlook, and **AWK** and **AWR** as our top picks, while we're Neutral on **CWT**, **SJW**, and **WTRG**.
To us, there is no better utility than a water utility:

- The water/wastewater industry remains highly fragmented with ~90% of the US population getting water/wastewater services from municipally-owned systems.
- Water/wastewater systems, especially those owned by municipalities, are heavily under-invested and often non-compliant with EPA regulations. While munis resist water/wastewater M&A, growing budget pressures coupled with fair value laws should facilitate privatizations.
- Outside of CA/HI, water/wastewater bills remain low. The current work-from-home arrangements inflate higher-margin residential water volumes, and we'd expect at least some of this volume uptick to persist beyond 2020, benefiting AWK and WTRG in particular.
- Water/wastewater capex is non-cyclical and highly fragmented.
- Water utilities have high ESG/sustainability ratings. Those translate into rich valuations and a very low cost of financing.

The debate about the right multiple for water vs. electric utilities continues. An average water utility under our coverage grows EPS/DPS at a ~9%/~8% rate or ~300 bps/~300 bps faster than an average regulated electric utility. However, the water EPS growth rates are inflated by recent M&A deals and/or non-water earnings. Based on our 2022 EPS estimates, water utilities under our coverage trade at a ~45% P/E premium to an average regulated electric utility (24.6x vs. 16.9x respectively) which is in line with the historical average. The average 2019 EV/Rate base multiple of 1.78x also seems average.

Highlights

Water utilities: Trading multiples

	Rating	Market Cap ($B)	2019 EV/Rate Base	2022 P/E	2019-2022 EPS CAGR	2019-2022 DPS CAGR
AWK	Buy	22.2	1.74x	26.2x	8.3%	10.0%
AWR	Buy	2.9	1.77x	29.2x	4.9%	7.6%
CWT	Neutral	2.2	1.76x	23.9x	11.5%	7.4%
SJW	Neutral	1.6	1.68x	21.0x	14.0%	6.9%
WTRG	Neutral	10.1	1.94x	22.7x	6.3%	7.0%
Average water			**1.78x**	**24.6x**	**9.0%**	**7.8%**

Source: FactSet, Seaport Global Securities

Water utilities: EPS/DPS CAGRs

	2019-2022 EPS CAGR	2019-2022 DPS CAGR
AWK	8.3%	10.0%
AWR	4.9%	7.6%
CWT	11.5%	7.4%
SJW	14.0%	6.9%
WTRG	6.3%	7.0%
Average	**9.0%**	**7.8%**

Source: Seaport Global Securities

AWK (Buy): AWK's scale and strong operational execution position it well to benefit from ongoing privatization of municipal water/wastewater systems. We acknowledge AWK's 60%+ debt/cap and pending/upcoming rate cases in three of its largest jurisdictions happening during the COVID-19 pandemic. Yet, the strain on municipal budgets on the back of this pandemic could further accelerate muni water deals, with AWK best positioned to consolidate the industry.

AWR (Buy): The company keeps surprising to the upside on its regulated water/electric earnings thanks to strong regulatory and operational execution in CA. Though AWR trades at the highest PE multiple among water names under our coverage, it's largely a function of its military water/wastewater contracts, we believe. When we adjust AWR's EV for those contracts, the stock trades in line with peers on 2019 EV/Rate base.

CWT (Neutral): With its rate base/customer more than a third lower than that of its public peers, CWT offers unmatched long-term EPS growth prospects. Yet, a pending decision by CA regulators in CWT's general rate case could meaningfully increase the volatility in its earnings by removing revenue decoupling and/or balancing accounts for pension/medical expenses. The latter seems likely to us.

SJW (Neutral): The recent cancelation of SJW's temporary revenue decoupling mechanism in CA and a lack of a balancing account for purchase water costs in the state have more severe earnings implications than we once expected. Through the merger with CTWS, SJW reduced its concentration on CA, but the volatility in SJW's earnings is still pretty severe. The stock trades at a large 15% P/E discount to an average water utility on our 2022 EPS though just a 5% discount based on the 2019 EV/Rate base multiples. The volatility in SJW's earnings should persist through at least 2021 because SJW's San Jose Water plans to ask for a purchased water tracker in its next general rate case in CA covering 2022-2024.

WTRG (Neutral): To us, WTRG's recent purchase of a gas utility (Peoples Gas) muddled the original water growth story in exchange for a ~150+ bps pick-up in WTRG's EPS CAGR. Management should pursue a catch-up repair tax deduction for Peoples Gas in PA, but we'd expect most of the earnings benefit to be shared with ratepayers. Given its higher operating risk profile, WTRG's gas earnings are unlikely to ever trade at a water P/E. Given the earnings mix, WTRG seems therefore fairly valued to us.

Seaport Global

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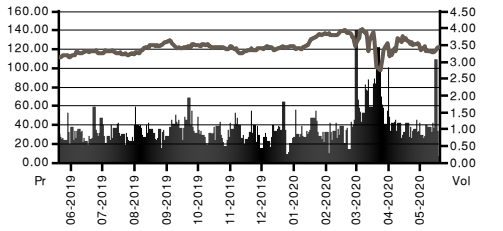
Rating:	**Buy**
Price Target:	**$130.00**

Price Target Metrics:
2022 SOTP valuation implying 28.4x 2022 EPS

Current Price:	**$120.17**
Float:	180.5MM
Diluted Shares:	181.0MM
Short Interest:	2.0MM
Average Daily Volume:	1,097k
52 Week Range:	$92.00 - $141.70
Market Cap:	**$21,751MM**
Cash and Investments:	$1MM
Debt:	$10,315MM
Enterprise Value:	$32,065MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Adjusted)				
FY	$3.61A	$3.84E	$4.23E	$4.59E
P/E	**33.3x**	**31.3x**	**28.4x**	**26.2x**
Dividends Per Share				
FY	$1.955A	$2.150E	$2.365E	$2.600E
Dividend Yield	**1.6%**	**1.8%**	**2.0%**	**2.2%**

American Water Works Company, Inc.

(NYSE: AWK)

Best-in-class water growth story

Summary:
We are initiating coverage of AWK with a Buy rating and a $130 price target based on our 2022 SOTP valuation implying 28.4x our 2022 EPS. We see the rich valuation as warranted by AWK's multi-decade investment needs, its low risk profile and growth in ESG-related investing. AWK's above-average 8.3%/10% EPS/DPS CAGR between 2019-2022 should be achievable largely regardless of future economic cycles, driven by organic capex and acquisitions of municipal water systems (~7% EPS growth), with contracted services adding an additional ~1-1.5% to the growth. Assuming no federal infrastructure bill, the current COVID-19 pandemic could, over time, boost muni water/wastewater M&A for large water operators such as AWK. We admit that it's not ideal, however, that AWK will be asking for meaningfully higher rates in three of its largest regulatory jurisdictions (NJ, PA and MO) during the COVID-19 pandemic, or that AWK's net debt/cap should exceed 60% through 2021/2022.

Highlights

Regulated utilities (~88% of 2022 EPS): AWK's 7-8% rate base CAGR between 2019 and 2024 is supported by organic water main replacement capex and acquisitions of municipal water/wastewater systems. While AWK's existing systems offer decades of growth, the customer bill affordability is the key limiting factor for the organic growth. AWK's muni M&A is focused on rural systems with 30,000-60,000 existing customer accounts in states which adopted fair value legislation or similar laws. Assuming no federal infrastructure bill, the muni M&A in the water sector could further accelerate benefiting large water utilities such as AWK in particular, we believe.

Contract-based operations (~12% of 2022 EPS): AWK provides water/wastewater services to 16 military, with pending solicitations for five more contracts, three of which to be awarded still this year. Given the 50-year duration, inflation indexation, premium returns, and the exclusive nature of these contracts we see them as even more valuable than the regulated water business. AWK won more than 50% of all new military water/wastewater service contracts offered to private contractors over the last couple of years, with AWR as the only real competitor in this field. AWK's Homeowner Services business offers warranties mainly for wastewater sewer lines not covered by homeowner's insurance. The business EPS should grow at a ~9% CAGR between 2019 and 2022. We recognize a higher risk profile of this business, reflected in a lower P/E multiple in our 2022 SOTP, but also its strong cash flow generation.

2020 earnings: Management reiterated its 2020 EPS guidance despite the COVID-19 pandemic as higher residential water consumption (~70% of total regulated sales volumes) should more than offset lower C&I volumes, and any meaningful COVID-related expenses, if material, should be deferred. Admittedly, AWK's 2020 earnings guidance always seemed conservative to us though we recognize that it's a particularly busy year on the regulatory front with AWK seeking large revenue increases (US $224MM annualized) in four states, including NJ and PA, AWK's largest jurisdictions, with a likely MO rate case coming later this year.

Company Description:
AWK is the largest publicly-traded regulated water and wastewater utility in the US with operations in 16 states, primarily in the Northeast and the Midwest, serving 3.4 million customer accounts. AWK also engages in unregulated contract-based water/wastewater services for military bases (16 bases) and provides water/wastewater line warranty services (homeowner services) to ~1.5 million residential accounts

AWK: EPS breakdown by segment ($)

AWK	2018A	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated utilities	3.32	3.60	3.80	4.16	4.50	7.7%
Unregulated ops	0.33	0.45	0.48	0.51	0.56	7.6%
Parent	-0.35	-0.44	-0.44	-0.44	-0.47	2.5%
Total EPS	**3.30**	**3.61**	**3.84**	**4.23**	**4.59**	**8.3%**
DPS	**1.78**	**1.96**	**2.15**	**2.37**	**2.60**	**10.0%**
Dividend payout	54%	54%	56%	56%	57%	

Source: Company data for 2018-2019; Seaport Global Securities

AWK - 2022 SOTP valuation

AWK - 2022 SOTP	EPS	Multiple	Value per share
Regulated utilities less parent	4.03	27.9x	112.32
Military contracts	0.19	41.9x	7.95
Homeowner services	0.37	25.0x	9.25
Total per share			**129.52**

Source: Seaport Global Securities

Risks

Allowed ROEs for AWK's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings.

Lower sales volumes could weigh on AWK's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWK has a particularly busy regulatory calendar in 2020, with rate cases in three of its largest jurisdictions – NJ, PA and MO.

Potentially higher equity needs due to weakening operating cash flows and underfunded pension funds: Lower customer collections (due to lower sales or non-payment) coupled with growing federal cash taxes and underperforming pension funds should be weighing on operating cash flows of regulated utilities especially during/following the COVID-19 pandemic. That in turn could require some deleveraging of balance sheets of regulated utilities thus more equity. AWK already announced ~$500m in new equity as soon as 2022, but the issuances could be enlarged and accelerated to protect AWK's credit ratings.

AWK	2018A	2019A	2020E	2021E	2022E
Sales	3,440	3,610	3,775	4,008	4,220
Operating expenses	1,773	1,824	1,871	1,919	1,969
EBITDA	1,667	1,786	1,904	2,089	2,251
Depreciation	545	582	626	670	714
EBIT	1,122	1,204	1,278	1,419	1,538
Net interest expense	350	382	402	442	460
Ordinary Profit Before Tax	809	872	926	1,027	1,127
Income tax	216	218	232	257	282
Net profit	593	654	695	770	845
S/O (m)	180	181	181	182	184
Diluted EPS	**3.30**	**3.61**	**3.84**	**4.23**	**4.59**
DPS	**1.78**	**1.96**	**2.15**	**2.37**	**2.60**
Cash	158	90	45	45	45
Financial and Operating Receivables	301	294	311	330	348
Inventory	41	44	44	45	46
Other short-term assets	281	857	292	292	292
Goodwill	1,575	1,501	1,501	1,501	1,501
Other-long term assets	1,458	1,664	1,664	1,664	1,664
Property, plant, and equipment	17,409	18,232	19,475	20,675	21,832
Total assets	**21,223**	**22,682**	**23,332**	**24,552**	**25,727**
Financial liabilities	1,035	814	936	936	936
Operating liabilities	175	203	194	199	204
Other liabilities	884	1,028	851	851	851
Deferred credits and other regulatory liabiliti	5,689	5,872	6,053	6,253	6,396
Long-term debt	7,576	8,639	9,472	9,896	10,408
Shareholders' equity	5,864	6,126	5,827	6,418	6,933
Total liabilities and equity	**21,223**	**22,682**	**23,332**	**24,552**	**25,727**
Net income	565	654	695	770	845
D&A, goodwill amortisation	545	582	626	670	714
Other non cash elements	308	214	181	200	220
Funds from operations	1,418	1,450	1,501	1,640	1,779
Decrease (increase) in non-cash working ca	-32	-67	-26	-15	-91
CFO	**1,386**	**1,383**	**1,475**	**1,625**	**1,688**
Net investments in fixed assets	-1,949	-1,841	-1,865	-1,865	-1,865
Net investments in financial assets	-87	-104	-104	-104	-104
Free cash flow before dividends	**-650**	**-562**	**-494**	**-344**	**-281**
Dividends paid (group + minorities)	-319	-354	-389	-431	-479
Free cash flow after dividends	-969	-916	-883	-775	-760
Increase or (repayment) of capital and subsi	892	857	883	474	562
Increase or (repayment) of financial debt	138	-36	-45	301	198
Adjustment for minorities / miscellaneous	14	27	0	0	0
Increase in cash	75	-68	-45	0	0

Seaport Global

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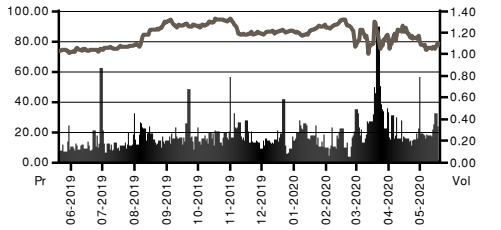
Rating:	**Buy**
Price Target:	**$84.00**

Price Target Metrics:
2022 SOTP valuation which implies 32.6x '22 EPS

Current Price:	**$75.62**
Float:	36.4MM
Diluted Shares:	37.0MM
Short Interest:	1.0MM
Average Daily Volume:	286k
52 Week Range:	$65.11 - $96.64
Market Cap:	**$2,796MM**
Cash and Investments:	$6MM
Debt:	$339MM
Enterprise Value:	$3,129MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Diluted)				
FY	$2.24A	$2.31E	$2.45E	$2.58E
P/E	**33.8x**	**32.8x**	**30.9x**	**29.3x**
Dividends Per Share				
FY	$1.160A	$1.263E	$1.351E	$1.446E
Dividend Yield	**1.5%**	**1.7%**	**1.8%**	**1.9%**

American States Water Company
(NYSE: AWR)

Pricey water utility, but with best-in-class execution

Summary:
We are initiating coverage of AWR with a Buy rating and an US$84 price target based on our 2022 SOTP valuation which implies 32.6x our 2022 EPS. Trading at 29.2x our '22 EPS, AWR is the most expensive utility under our coverage despite a peer-average EPS/DPS annual growth of ~4.9%/~7.6%. Yet, this is the only CA-based water utility which has always earned at least its allowed ROE and the Street (us included) has historically underestimated AWR's earnings power. While losses in a pension account incurred in March pose some EPS headwind for 2020, we still expect the company to beat its 2020 consensus EPS through higher regulated electric and contract-based earnings. A new general rate case and a cost of capital proceeding will determine AWR's 2022 EPS on the water side, but we still expect our/consensus estimates to turn out low.

Highlights

Regulated water/wastewater utilities (~70% of 2022 EPS): Golden States Water Company (GSWC) has been uniquely successful at earning its allowed ROE and getting regulatory approvals for higher water capex through general rate cases and separate advisory letters. The next general rate case (to be filed in July) and the cost of capital proceeding (to be filed in May 2021) should determine GSWC's earnings power for 2022-2024, and we are hoping for meaningful upside to our 2022 EPS due to higher capex though the allowed ROE (to be determined in a separate proceeding) remains uncertain.

Military contracts/ASUS (~21% of 2022 EPS): Through its unregulated American States Utility Services (ASUS) business, AWR provides water/wastewater services to 11 military bases under 50-year inflation-indexed contracts. The contracts offer periodic openers to account for incremental scope of work thus higher expenses or incremental infrastructure upgrades. Given the duration, premium returns, and the exclusive nature of these contracts we see them as even more valuable than the regulated water business. Hence, in our SOTP, we value the contracts at a 50% P/E premium to water utilities. We see at least three pending RFPs for new water/wastewater contracts for military bases, and while the contract awards may get delayed due to COVID-19, we'd expect at least one of these contracts to be awarded to AWR.

2020 earnings: Thanks to revenue decoupling on both the water and electric side, balancing accounts for both purchased water and power costs, and a catastrophic event memorandum account tracking COVID-related expenses, AWR should not see much of a COVID-19 impact on its regulated earnings if not for losses in one of its pension account, an US$0.08 YoY EPS hit in 1Q20. However, it has yet again become apparent to us that we were underestimating AWR's earnings power on the electric/water side. Management expects to fully execute its water/electric capex plan during 2020. The military contracts division saw some cost overruns during 1Q20, but that's just a timing issue.

Company Description:
AWR is the parent of Golden States Water Co. (GSWC), a regulated water (261,000 water connections in 37 systems) and electric utility (24,400 electric connections in one system) in CA, and American States Utility Services (ASUS), which engages in contract-based water and wastewater services primarily for military bases, currently 11 bases.

AWR: EPS breakdown by segment ($)

AWR	2019A	2020E	2021E	2022E	2019-2022 CAGR
Regulated water	1.62	1.64	1.73	1.82	4.1%
Regulated electric	0.15	0.18	0.20	0.21	11.9%
Military contracts/ASUS	0.47	0.49	0.52	0.55	5.4%
Total EPS	**2.24**	**2.31**	**2.45**	**2.58**	**4.9%**
DPS	**1.16**	**1.26**	**1.35**	**1.45**	**7.6%**
Dividend payout	52%	55%	55%	56%	

Source: Company data for 2019; Seaport Global Securities

AWR: 2020 Sum-Of-The-Parts valuation ($)

AWR - SOTP	Metric	Multiple	Price	Anchor PE	PE premium
2022 Regulated Water EPS	1.82	30.7x	$55.91	27.9x	10%
2022 Regulated Electric EPS	0.21	20.7x	$4.35	18.0x	15%
2022 ASUS EPS	0.55	43.2x	$23.78	27.9x	55%
Total equity value/sh			**$84.04**		

Source: Seaport Global Securities

Risks

Allowed ROEs for AWR's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. AWR's allowed ROE for its water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWR should be filing a new water rate case by July 2020 with new rates in effect in January 2021.

Returns in pension accounts impact AWR's earnings in between rate cases in CA: AWR has no balancing account tracking changes in returns in its pension accounts. Those changes can be trued up/reflected in AWR's rates during rate cases, but those take place every three years.

Military contracts are highly competitive: Through its unregulated ASUS subsidiary, AWR provides water and wastewater services to 11 military bases. The company awaits awards of up to three more of these contracts in 2020. We assume that AWR secures at least one new military contract per year in 2020-2022 though AWK, AWR's largest competitor, has been winning most of the contract awards as of late.

AWR	2018A	2019A	2020E	2021E	2022E
Total Revenues	437	474	490	504	525
Total Operating Expenses	336	347	360	369	382
Operating income	101	127	130	136	144
EBT	82	107	109	115	122
Income tax expense	18	25	24	25	27
Net income	$ 64	$ 83	$ 85	$ 90	$ 95
S/O	37	37	37	37	37
Diluted EPS	**$1.72**	**$2.24**	**$2.31**	**$2.45**	**$2.58**
DPS	**$1.06**	**$1.16**	**$1.26**	**$1.35**	**$1.45**
Net income	64	83	85	90	95
Adjustments to reconcile non-cash charges	40	42	46	48	51
Changes in assets and liabilities	33	(8)	(12)	(12)	(12)
CFO	137	117	119	126	134
Capital expenditures	(127)	(152)	(125)	(135)	(135)
Other	(1)	(1)	-	-	-
CFI	(128)	(153)	(125)	(135)	(135)
Issuance/repurchase of common stock	1	1	1	1	1
Long-term debt issued/repaid	(0)	(40)	30	45	45
Short-term debt issued/repaid	37	110	20	15	15
Dividends paid	(39)	(43)	(47)	(50)	(53)
Other	0	4	4	4	4
CFF	(2)	31	7	14	11
Net change in cash and cash equivalents	2	(6)	2	5	10
Cash and cash equivalents, end of period	7	1	3	8	18
Current assets	$ 131	$ 122	$ 125	$ 132	$ 144
PP&E	1,323	1,447	1,526	1,621	1,715
Regulatory and other assets	47	72	72	72	72
Total assets	1,501	1,641	1,723	1,825	1,931
Current liabilities	147	116	157	157	157
Long-term debt	281	281	311	356	401
Other liabilities (including construction)	516	643	643	643	643
Total liabilities	943	1,040	1,111	1,156	1,201
Total Shareholders' Equity	558	601	612	668	730
Liabilities and Shareholders' Equity	$ 1,501	$ 1,641	$ 1,723	$ 1,825	$ 1,931

Seaport Global

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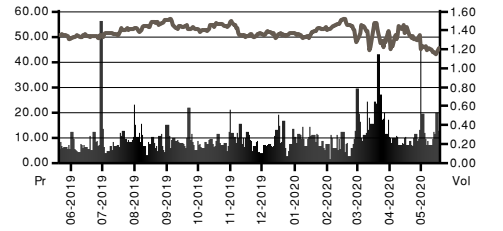
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$43.58**
Float:	48.3MM
Diluted Shares:	48.6MM
Short Interest:	1.0MM
Average Daily Volume:	335k
52 Week Range:	$39.74 - $57.48
Market Cap:	**$2,117MM**
Cash and Investments:	$141MM
Debt:	$1,143MM
Enterprise Value:	$3,120MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Diluted)				
FY	$1.31A	$1.40E	$1.70E	$1.82E
P/E	**33.2x**	**31.1x**	**25.7x**	**23.9x**
Dividends Per Share				
FY	$0.790A	$0.850E	$0.909E	$0.978E
Dividend Yield	**1.8%**	**2.0%**	**2.1%**	**2.2%**

California Water Services Group

(NYSE: CWT)

Potential earnings volatility overshadows strong rate base growth

Summary:

Thanks to its highly underinvested water systems, CWT offers the fastest earnings growth in regulated water earnings among publicly-traded companies – we project an 11.5% EPS CAGR between 2019 and 2022. However, depending on the outcome of a pending rate case in CA and given conservatism of CWT's management, we could see meaningful volatility in CWT's earnings driven by changes in sales volumes as well higher operating expenses related to pensions, medical insurance and COVID-19. Therefore, we are initiating coverage with a Neutral rating as we await the outcome of CWT's general rate case in CA by July.

Highlights

Regulated water (98% of 2022 EPS): Based on the 2019 rate base per customer connection, CWT's water systems are more than a third less invested than those of its public water peers, even despite sharp capex increases in the last two of CWT's rate cases in CA. CWT's earnings largely followed higher capex and we now project an 11% EPS CAGR between 2019 and 2022. However, CWT awaits a proposed decision in its latest general rate case in CA, and while the utility settled with the consumer advocate on key issues back in October 2019, the revenue decoupling and recovery of pension/ medical costs through balancing accounts remain disputed. We don't expect CWT to lose its revenue decoupling though balancing accounts for pension/medical costs might not get renewed, and that could add some volatility in CWT's earnings.

2020 earnings: CWT is tracking COVID-related expenses in a catastrophic memorandum account, but unlike other CA utilities, it plans to expense the costs until they are recovered in the next rate case. Also, depending on the outcome of the pending general rate case, CWT could be exposed to higher pension and medical costs given a potential removal of balancing accounts for these costs. It helps that CWT never provides earnings guidance, but we see downside to our/consensus estimates for 2020-2022 depending on the outcome of the CA rate case.

CWT: EPS/DPS projections

CWT	2018A	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.36**	**1.31**	**1.40**	**1.70**	**1.82**	**11.5%**
DPS	**0.75**	**0.79**	**0.85**	**0.91**	**0.98**	**7.4%**
Dividend payout	55%	60%	61%	54%	54%	

Source: Company data for 2018-2019; Seaport Global Securities

Company Description:

CWT operates regulated water and wastewater utilities in CA, WA, HI and NM, with 490,000 connections in CA (90%), 36,000 connections in WA (recently doubled through an acquisition), 5,000 in HI, and 8,300 connections in NM.

Risks

Allowed ROEs for CWT's regulated water utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. CWT's allowed ROE for its water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. CWT awaits a proposed decision in its 2018 general rate case in CA with rates retroactive to January 1, 2021. Though the utility reached a partial settlement with the consumer advocate late in 2019, outstanding issues involve the continuation of the revenue decoupling and balancing accounts for pension and medical expenses. Without those, CWT could see a meaningful spike in its earnings volatility.

CWT	2018A	2019A	2020E	2021E	2022E
EBIT	132	117	126	149	160
EBITDA	218	209	225	255	274
Net interest expense	38	41	44	45	47
Net income	66	63	69	87	96
EPS	**$1.36**	**$1.31**	**$1.40**	**$1.70**	**$1.82**
DPS	**$0.75**	**$0.79**	**$0.85**	**$0.91**	**$0.98**

CFO	**$ 179**	**$ 169**	**$ 189**	**$ 214**	**$ 231**
Utility plant expenditures	(272)	(274)	(275)	(285)	(285)
Other	(1)	(2)	(2)	(2)	(2)
CFI	**(273)**	**(276)**	**(277)**	**(287)**	**(287)**
Issuance of common stock	(2)	18	96	80	86
Issuance of debt	73	103	28	32	32
Dividends	(36)	(38)	(41)	(44)	(47)
Other	11	20	20	20	20
CFF	**47**	**103**	**103**	**88**	**91**
Change in cash and cash equivalents	(48)	(4)	14	15	35

Net utility plant	2,233	2,406	2,583	2,761	2,932
Cash and cash equivalents	47	43	63	78	112
Other current assets	142	142	142	142	142
Total current assets	189	184	204	219	254
Regulatory assets	354	433	433	433	433
Goodwill	3	3	3	3	3
Other assets	60	85	85	85	85
Total assets	**$ 2,838**	**$ 3,111**	**$ 3,308**	**$ 3,502**	**$ 3,707**
Total common stockholders' equity	$ 730	$ 780	$ 808	$ 851	$ 900
Long-term debt, less current maturities	710	787	814	847	879
Total capitalization	**1,440**	**1,567**	**1,622**	**1,698**	**1,778**
Total current liabilities	321	359	479	578	682
Deferred income taxes	213	223	223	223	223
Pension and postretirement benefits ot	194	259	259	259	259
Other long-term liabilities	257	270	270	270	270
Advances for construction	186	191	191	191	191
Contributions in aid of construction	225	242	262	282	302
Total capitalization and liabilities	**$ 2,838**	**$ 3,111**	**$ 3,308**	**$ 3,502**	**$ 3,707**

Seaport Global

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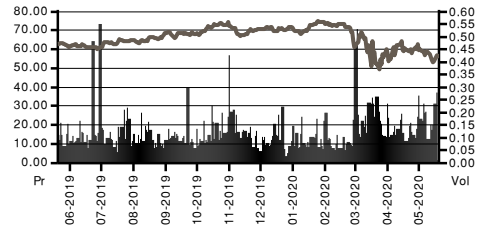
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$55.44**
Float:	26.0MM
Diluted Shares:	28.7MM
Short Interest:	0.3MM
Average Daily Volume:	160k
52 Week Range:	$45.60 - $74.99
Market Cap:	**$1,590MM**
Cash and Investments:	$28MM
Debt:	$1,471MM
Enterprise Value:	$3,032MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Diluted)				
FY	$1.78A	$1.97E	$2.42E	$2.64E
P/E	**31.1x**	**28.2x**	**22.9x**	**21.0x**
Dividends Per Share				
FY	$1.200A	$1.280E	$1.370E	$1.465E
Dividend Yield	**2.2%**	**2.3%**	**2.5%**	**2.6%**

SJW Group

(NYSE: SJW)

Earnings volatility too high to handle

Summary:

We are initiating coverage of SJW with a Neutral rating as volatility in SJW's CA earnings (~60% of our 2022 EPS) meaningfully limits the investment appeal of this pure-play regulated water utility. While last year's merger with Connecticut Water Service reduced SJW's exposure to CA and San Jose Water is likely to request a purchased water cost tracker in its next general rate case, we are at least two years away from clarity on this issue. Additionally, SJW's earnings for 2021/2022 should be highly impacted by its upcoming rate cases in CT and CA with some risks of regulatory clawbacks of any merger-related savings, especially in CA.

Highlights

Regulated water/wastewater utilities (95% of 2022 EPS): SJW operates in states with relatively constructive regulatory regimes for water utilities. CT and ME, the jurisdictions of the recently acquired Connecticut Water Service, offer revenue decoupling mechanisms and capex riders thus ensuring that the utilities fully earn their allowed ROEs. In CA, the state offers three-year visibility into capex and separates rate cases from the ROE/equity ratio proceedings, but consumer advocates have been pushing back against revenue decoupling, and San Jose Water has recently lost its temporary decoupling retroactive to 2018. Worse yet, the utility does not currently have a purchased water tracker which should cost SJW even US$0.30 in EPS this year. In TX, SJW sees meaningful growth opportunities supported by a recently adopted fair value legislation, though admittedly starting from a very low customer count. The state has recently adopted a capex recovery rider (DSIC).

2020 earnings: Management issued its first ever earnings guidance in February, but had to lower it by 13% just two months later due to sharply higher purchased water costs due to the lower surface water availability of just ~1.1B vs. 3.5B gallons typically. Additionally, while SJW can track (and eventually recover) COVID-related expenses (including bad debts) in CA through a catastrophic event memorandum account, the utility could see lower capex deployed in the state during 2020, with a catch up in 2021. While SJW no longer has even a temporary revenue decoupling in CA, the COVID pandemic should result in a net increase in water sales volumes as SJW's customer base is predominantly residential (60% of revenues) and apartment buildings dominate among commercial accounts. Those higher volumes could offer some earnings benefit in 2020.

SJW: EPS/DPS growth prospects

SJW	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.78**	**1.97**	**2.42**	**2.64**	**14.0%**
DPS	**1.20**	**1.28**	**1.37**	**1.47**	**6.9%**
Dividend payout	67%	65%	57%	55%	

Source: Company data for 2019; Seaport Global Securities

Company Description:

SJW Group is a regulated water and wastewater utility serving ~390,000 accounts across CA, CT, TX and ME. SJW merged with Connecticut Water Service in October 2019.

Risks

Allowed ROEs for SJW's regulated water utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. SJW's allowed ROE for its CA water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. SJW should file a rate case for its new CT business in 2021. Also, the CA utility of SJW should go through a general rate case in the state in 2021 and state regulators could attempt to claw-back some synergies related to the recent merger with CTWS.

SJW's CA earnings are highly volatile: Now that SJW no longer has even a temporary decoupling mechanism in CA, it's CA earnings change along with changes in volumes and changes in purchased water costs. SJW plans to ask for a purchased water cost balancing account in the next rate case in CA, but that means that 2021 could be another weak earnings year before the regulatory fix arrives for 2022, if at all.

SJW	2019A	2020E	2021E	2022E
EBITDA	157	210	231	242
Net income	51	56	69	76
EPS diluted	**$1.78**	**$1.97**	**$2.42**	**$2.64**
DPS	**$1.20**	**$1.28**	**$1.37**	**$1.47**
CFO	**$ 130**	**$ 139**	**$ 158**	**$ 167**
CFI	**(1,018)**	**(216)**	**(277)**	**(257)**
Issuance of common stock	0.0	0.0	0.0	0.0
Issuance of debt	502	113	113	113
Dividends	-34	-36	-39	-40
CFF	**485**	**101**	**99**	**99**
Change in cash and cash equivalents	-403	24	-21	9
Net utility plant	2,206	2,323	2,495	2,644
Cash and cash equivalents	18	42	21	30
Other current assets	109	112	115	117
Total current assets	127	154	136	148
Regulatory assets	114	114	114	114
Goodwill	628	628	628	628
Other assets	57	57	57	57
Total assets	**3,132**	**3,276**	**3,430**	**3,591**
Total common stockholders' equity	$ 890	$ 974	$ 990	$ 1,009
Long-term debt, less current	1,261	1,187	1,195	1,203
Total capitalization	**2,151**	**2,161**	**2,185**	**2,212**
Total current liabilities	235	349	460	574
Deferred income taxes	196	193	190	188
Pension and postretirement benefits oth	108	108	108	107
Other long-term liabilities	45	45	45	45
Advances for construction	112	135	157	180
Contributions in aid of construction	286	286	286	286
Total capitalization and liabilities	**3,132**	**3,276**	**3,430**	**3,591**

Seaport Global

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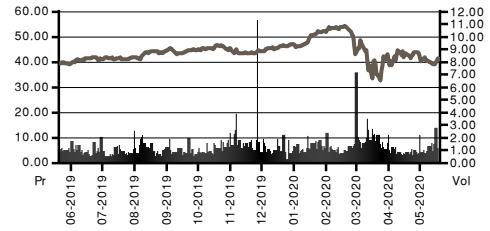
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$39.90**
Float:	244.3MM
Diluted Shares:	255.1MM
Short Interest:	5.3MM
Average Daily Volume:	1,130k
52 Week Range:	$30.40 - $54.52
Market Cap:	**$10,177MM**
Cash and Investments:	$5MM
Debt:	$4,754MM
Enterprise Value:	$14,925MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Diluted)				
FY	$1.47A	$1.55E	$1.66E	$1.76E
P/E	**27.1x**	**25.7x**	**24.1x**	**22.7x**
Dividends Per Share				
FY	$0.907A	$0.970E	$1.038E	$1.111E
Dividend Yield	**2.3%**	**2.4%**	**2.6%**	**2.8%**

Essential Utilities, Inc.

(NYSE: WTRG)

Gas deal muddled the water

Summary:

We are initiating coverage of WTRG with a Neutral rating as we see the stock as close to fairly valued given its water/gas utility mix. WTRG's ~6.3%/7% EPS/DPS CAGR between 2019-2022 should be driven by a 6-7% water and 8-10% rate base growth as well as merger-related synergies related to Peoples Gas. To us, the recent addition of the gas utility to WTRG's core water utility business has diminished the scarcity value of the pure-play water utility in exchange for just a ~150 bps pick-up up in WTRG's consolidated EPS growth. WTRG should try to get some incremental gas utility earnings in PA through a catch-up repair tax deduction, though we'd expect the earnings benefit to be largely clawed back by the state. Assuming no federal infrastructure bill, WTRG could see some incremental municipal water/wastewater M&A on the back of the COVID-19 pandemic, but we prefer to play this benefit through AWK.

Highlights

Regulated water (~67% of 2022 EPS): WTRG's 6-7% water rate base CAGR through 2022 does not incorporate growth through muni acquisitions of water/wastewater systems though WTRG has been very successful at those, especially in PA, its key jurisdiction (68% of 2019 water rate base). All in, we expect WTRG to deliver a ~7% rate base CAGR through 2022, off of 2019 of $5B. Without a federal infrastructure bill supporting upgrades of municipal water/wastewater system, they are likely to be sold to private operators, such as WTRG, at an accelerated pace, following the COVID-19 outbreak, we believe. The growth in WTRG's water rate base should outpace the growth in its water net income through 2022, however, as the Aqua PA pulled forward its earnings through a repair tax election in 2012.

Regulated gas (~33% of 2022 EPS): The 8-10% rate base CAGR on the gas side, together with a recently completed gas rate case in PA and some cost efficiencies related to the merger with WTRG should deliver a 17% net income CAGR for Peoples between 2019 and 2022. That in turn should drive a 6.3% consolidated EPS CAGR for WTRG. That's 100-150 bps higher than our net income growth expectations for WTRG's standalone water business, and admittedly, there could be some further upside to the gas capex and PA could allow WTRG to retain a portion of a catch-up repair tax adjustment. We remain skeptical, however, about the strategic rationale of the gas acquisition as to us it has diminished the scarcity value of WTRG's water utility.

2020 earnings: With higher residential water volumes offsetting lower C&I consumption (~20% of total volumes) and regulators likely allowing for deferrals of COVID costs, WTRG doesn't see risks related to its pro forma 2020 EPS guidance of $1.53-1.58, especially with additional cost levers on the back of the Peoples merger. This should be a quiet year on the regulatory front except for a pending small rate case in NC and a likely filing for a catch-up repair tax deduction in PA, though the timing of the latter is uncertain given the pandemic.

WTRG: EPS breakdown by segment ($)

WTRG	2018A	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated water utilities	1.41	1.47	1.09	1.16	1.22	
Regulated gas utilities	0.00	0.00	0.57	0.67	0.70	
Parent	0.00	0.00	-0.10	-0.17	-0.16	
Total EPS	**1.41**	**1.47**	**1.55**	**1.66**	**1.76**	**6.3%**
DPS	**0.85**	**0.91**	**0.97**	**1.04**	**1.11**	**7.0%**
Dividend payout	60%	62%	62%	63%	63%	

Source: Company data for 2018-2019; Seaport Global Securities

Company Description:

WTRG owns and operates water utilities (1 million accounts) and gas utilities (0.74 million accounts) in 10 states though mainly PA.

Risks

Allowed ROEs for WTRG's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. WTRG's only pending rate case (in NC) is very small.

Lower sales volumes could weigh on WTRG's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. WTRG's regulatory calendar is quiet in 2020, with a pending small rate case in NC, and a likely filing for a catch-up repair tax adjustment for Peoples in PA.

Gas utilities have a higher operating risk than water utilities: Overpressurized gas systems seem to happen more frequently among gas utilities in the US. While we recognize that Peoples Gas is a well-managed system, WTRG's risk profile could further deteriorate with any gas-related operational issues.

WTRG	2018A	2019A	2020E	2021E	2022E
Operational EBITDA	470	505	868	920	984
Operational EBIT	323	349	604	641	690
Net interest expense	99	100	201	209	227
Ordinary Profit Before Tax	252	269	431	459	490
Income tax	1	7	34	37	39
Net profit	251	262	396	422	451
S/O (m)	178	178	255	255	256
Diluted EPS	**1.41**	**1.47**	**1.55**	**1.66**	**1.76**
DPS	**0.85**	**0.91**	**0.97**	**1.04**	**1.11**
Cash	4	1,869	5	5	5
Receivables	101	108	109	113	118
Inventory	16	18	30	30	30
Other short-term assets	26	18	18	18	18
Other-long term assets	887	1,003	3,810	3,810	3,810
Property, plant, and equipment	5,930	6,346	8,962	9,113	9,249
Total assets	**6,965**	**9,362**	**12,934**	**13,089**	**13,230**
Financial liabilities	117	117	496	496	496
Operating liabilities	63	67	109	109	109
Other liabilities	108	108	220	220	220
Deferred credits	2,068	2,057	2,758	2,757	2,757
Long-term debt	2,398	2,943	4,750	5,063	5,384
Shareholders' equity	2,210	4,070	4,601	4,444	4,264
Total liabilities and equity	**6,965**	**9,362**	**12,934**	**13,089**	**13,230**
Net income	251	262	396	422	451
D&A, goodwill amortisation	147	156	264	279	294
Other non cash elements	-54	-40	-6	-6	-6
Funds from operations	344	379	654	695	738
Non-cash working capital	25	-40	43	0	-1
CFO	**369**	**339**	**697**	**694**	**738**
Net investments in fixed assets	-641	-610	-6,555	-765	-780
Net investments in financial assets	2	6	0	0	0
Free cash flow before dividends	**-271**	**-266**	**-5,858**	**-71**	**-42**
Dividends paid	-151	-161	-229	-245	-284
Free cash flow after dividends	-422	-427	-6,087	-316	-327
Changes in capital	2	1,935	2	2	3
Changes in financial debt	421	386	4,220	313	323
Adjustment for minorities / miscellaneous	-2	-28	1	1	1
Increase in cash	-1	1,866	-1,864	0	0

Utilities/Power Disclosures

I, Angie Storozynski, hereby certify: (1) that all of the views expressed in this report accurately reflect my personal views about any and all of the subject securities or issuers; and (2) that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

As with all employees of Seaport Global Securities LLC, a portion of our analysts' compensation is paid from the total collection of revenues from all areas of the firm including but not limited to Investment Banking and Sales and Trading departments. In no instance are research analysts' compensation directly derived from Investment Banking revenues.

Risks & Considerations for American Water Works Company, Inc. American Water Works Company, Inc. (AWK)

Allowed ROEs for AWK's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings.

Lower sales volumes could weigh on AWK's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWK has a particularly busy regulatory calendar in 2020, with rate cases in three of its largest jurisdictions – NJ, PA and MO.

Potentially higher equity needs due to weakening operating cash flows and underfunded pension funds: Lower customer collections (due to lower sales or non-payment) coupled with growing federal cash taxes and underperforming pension funds should be weighing on operating cash flows of regulated utilities especially during/following the COVID-19 pandemic. That in turn could require some deleveraging of balance sheets of regulated utilities thus more equity. AWK already announced ~$500m in new equity as soon as 2022, but the issuances could be enlarged and accelerated to protect AWK's credit ratings.

Other Companies Mentioned in This Report

- American Water Works Company, Inc. (AWK: $120.17, Buy)
- California Water Services Group (CWT: $43.58)
- Essential Utilities, Inc. (WTRG: $39.90)
- American States Water Company (AWR: $75.62)
- SJW Group (SJW: $55.44)

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Buy - The investment outlook and risk/reward over the following 12 months are favorable on an absolute basis and relative to the peer group.

Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.

Sell - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.

NA - A rating is not assigned.

Prior to Feb 1., 2017, Seaport Global Securities analyst ratings included:

Buy - The investment outlook and risk/reward over the following 12 months are very favorable on an absolute basis and relative to the peer group.

Speculative Buy - The investment outlook over the following 12 months is very favorable on an absolute basis and relative to the peer group, however, there is higher than average risk associated with the investment that could result in material loss.

Accumulate - The investment outlook and risk/reward over the following 12 months are favorable on an absolute basis and relative to the peer group.

Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.

Reduce - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.

Sell - The investment outlook and risk/reward over the following 12 months are very unfavorable on an absolute basis and relative to the peer group.

NA - A rating is not assigned.

Ratings Distribution

	Research Coverage		Investment Banking Clients*		
Rating	Count	% of Total	Count	% of Total	% of Rating Category
Buy	49	55.1%	3	75.0%	6.1%
Neutral	36	40.4%	0	0.0%	0.0%
Sell	4	4.5%	1	25.0%	25.0%
Total	89	100.0%	4	100.0%	4.5%

*Investment banking clients are companies for whom Seaport Global Securities has provided investment banking services in the previous 12 months.

Note: Ratings Distribution as of March 31, 2020

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May 28, 2020
Flash Note
Utilities/Power
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Utilities/Power

Investor feedback on utilities/power stocks - Part 2

Summary:
Since our initiation of coverage of the Utilities sector last week, we've collected various feedback from clients. As a follow-up to part 1 (click here), we offer additional perspectives on our coverage universe.

- **DTE**'s midstream business continues to weigh on the stock's valuation though investors recognize DTE's exceptional financial track record plus some potential upside to the midstream earnings.
- Investors recognize that **EXC** and **PEG** do not currently reflect any value for their merchant power businesses, with little differentiation between both stocks, but see little incentive to support the names ahead of FRR decisions in IL/NJ and an update on a federal investigation of EXC's lobbying practices in IL.
- The recent short squeeze and upcoming regulatory updates are likely behind a strong outperformance of **AGR** and **PPL** vs. the XLU since our launch (+7.8% for AGR and +9.3% for PPL vs. +5% for XLU). The stories continue to face challenges, but AGR's NY rate case settlement should be filed any day now and the BOEM should update its review of the Vineyard Wind project in mid-June. Ofgem, the UK electric/gas utility regulator, should update its thoughts on allowed returns for electric transmission and gas distribution networks in late June, and that could be neutral to marginally positive for PPL, we believe.
- The recent rally among smid-cap stocks seems to have supported smaller water utilities, with **AWK**, our top pick for water names, trailing smaller names, **SJW** in particular, despite no fundamental updates. Among water names, AWK continues to attract most investor support, especially from those with an ESG mandate. Hedge funds remain attracted to **WTRG** given potential upside to gas earnings in PA and some expecting WTRG's gas earnings to gradually gain a water P/E multiple vs. the current 30% discount, we estimate. Investors recognize AWR's strong operational and financial track record despite a pension-related earnings hit in 1Q20.

Highlights

Regulated/diversified electric/gas utilities:

AGR (Neutral): The updated rate case settlement for AGR's NY utilities (NYSEG & RG&E) should be out any day and that, together with management's outreach has triggered a debate on AGR's bear investment thesis. In ME, AGR has filed a court challenge to the inclusion of the NECEC electric transmission project on the November ballot – a court decision would need to come out before September 11 when the ballots should be printed. Last week's FERC decision on the MISO electric transmission ROE and the methodology to set it has been widely seen as constructive by investors though more for AEP/FE rather than New England transmission operators (AGR/ES). The new methodology when updated for a 100 bps RTO adder would imply a wider range of reasonableness, with the high end 10.6-10.7%, we estimate. Challenges to FERC transmission ROEs for New England operators are still pending, they cover a different/earlier period (thus a higher interest rate environment) and FERC has not yet opined on additional non-RTO ROE adders and thus a cap on the all-in transmission ROEs for new projects. AGR currently earns ~11.3% in all-in transmission ROEs in CT and ME (vs. ~11.5% for ES), so we/investors don't see much (if any) downside to AGR's transmission earnings assuming higher incentive caps. Management still expects the BOEM to comment on the Vineyard Wind (VW) offshore wind project (a supplement to VW's Environmental Impact Statement) on June 12 and the Bureau to issue the final permit for the project in December 2020. Assuming no additional delays, we hope for some positive implications for AGR and ES.

DTE (Buy): Among all of our Buy-rated names, we had expected most constructive investor feedback on DTE given that the stock seemed to be trading even below the fair value of its regulated utilities (assuming a CMS-like P/E). The feedback has been mixed with the stock just marginally outperforming the XLU since our launch though gaining some strength this week. In general, investors recognize DTE's strong execution track record and its premium regulated utilities in MI. They admit that DTE's midstream business is less commodity-price sensitive than average, that it could benefit from higher gathering demand in the Northeast in 2021 and that NEXUS could see some longer-term contracts if/when ACP/MVP pipelines get delayed. Yet, an average investor would rather create a "synthetic DTE" by buying shares of CMS and a midstream business, though the latter would have to come at a negative equity value to truly reflect DTE's current valuation. We hope that with strong operational execution, no negative updates from Antero/Southwestern, and further construction delays for MVP/ACP the DTE stock should continue to re-rate through the end of 2020.

EXC (Buy)/PEG (Neutral): Investors don't see much difference between the two stocks or the reason to support either one any time soon. Neither implies any value for their respective merchant power businesses even though both should see some upside to their nuclear power earnings from IL and NJ eventually pursuing the FRR option outside of the PJM capacity market. For EXC, investors seem reluctant to support the stock ahead of an update on a pending federal investigation of Exelon's/ComEd's lobbying practices in IL or the November legislative session in the state where the FRR future could be decided. For PEG, though the company thinks no

legislation is needed for NJ to pursue an FRR option, the NJ BPU (state's utility regulator) is unlikely to opine on the FRR until early/mid-2021, we believe. In the meantime, PEG's electric transmission ROE should drop and the company is likely to pursue an equity stake in Orsted's Ocean Wind offshore wind project off the coast in NJ, likely intensifying the debate about the future of margins of PEG's gas plants in NJ/MD/CT.

PPL (Neutral): Investors seem unanimously surprised by our Neutral stance on the name despite ongoing FX pressures and the lack of growth prospects for PPL's US utilities until 2025 or beyond. Our Neutral rating was based a combination of somewhat fair valuation and our expectations that Ofgem's pending review of allowed equity returns for electric transmission and gas distribution won't result in an incremental reduction in the equity return (RORE) on the back of lower interest rates. The returns are still coming down however – starting April 2023, we'd expect the realized RORE for WPD to not exceed 9% vs. ~13-13.5% currently. Since our launch, PPL has outperformed the XLU by 420 bps and now the stock seems to imply a 37% premium to the 2022 EV/RAB for WPD assuming just a 5% discount to PPL's slow growing US utilities. The valuation yet again looks rich to us though PPL's 6% 2020 dividend yield does provide some support, and we believe the company could maintain the current level of dividends given lower regulated utility capex.

Water utilities:

AWK (Buy): Investors continue to like the story and, for once, few questioned AWK's current valuation premium vs. an average electric utility (~52% on our 2022 estimates). Investors appreciate how resilient the stock has been YTD (+0.7% vs. -8.7% for XLU and -5.4% for S&P 500). The heavy regulatory calendar for 2020 doesn't seem to worry investors.

AWR (Buy): Dedicated water utility investors recognize AWR's strong earnings/operational track record despite a large pension-related earnings hit in 1Q20. The high valuation premium we assign to AWR's (and AWK's) military contracts has received some debate, but overall we've heard little to no pushback to our bullish stance on AWR especially given growing volatility in earnings of AWR's peers in CA, CWT and SJW.

WTRG (Neutral): Hedge funds and some long-onlys remain attracted to WTRG given potential upside to gas earnings in PA and some expecting WTRG's gas earnings to gradually gain a water P/E multiple vs. the current 30% discount, we estimate. We recognize incremental cost levers on the back of the Peoples merger and that the look back repair tax application to be filed for the business in PA could deliver incremental earnings though it's tough for us to say how meaningful the EPS benefit would be after sharing with ratepayers. We do admit, however, that the stock does not currently discount any incremental earnings upside in PA.

Utilities/Power Disclosures

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Other Companies Mentioned in This Report

- Avangrid, Inc. (AGR: $43.50, Neutral)
- American States Water Company (AWR: $81.73, Buy)
- PPL Corporation (PPL: $27.60, Neutral)
- Essential Utilities, Inc. (WTRG: $42.87, Neutral)
- Exelon Corporation (EXC: $38.38, Buy)
- SJW Group (SJW: $61.38, Neutral)
- American Electric Power Company, Inc. (AEP: $84.69, Buy)
- American Water Works Company, Inc. (AWK: $123.72, Buy)
- DTE Energy Company (DTE: $108.27, Buy)
- Public Service Enterprise Group Inc. (PEG: $50.56, Neutral)
- Eversource Energy (ES: $80.51, Buy)
- Utilities Select Sector SPDR Fund ETF (XLU: $58.97)
- FirstEnergy Corp. (FE: $42.26, Buy)
- CMS Energy Corporation (CMS: $57.51, Buy)

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Explanation of Ratings

Seaport Global Securities analyst ratings include (effective Feb. 1, 2017):

Buy - The investment outlook and risk/reward over the following 12 months are favorable on an absolute basis and relative to the peer group.
Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.
Sell - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.
NA - A rating is not assigned.

Prior to Feb 1., 2017, Seaport Global Securities analyst ratings included:

Buy - The investment outlook and risk/reward over the following 12 months are very favorable on an absolute basis and relative to the peer group.
Speculative Buy - The investment outlook over the following 12 months is very favorable on an absolute basis and relative to the peer group, however, there is higher than average risk associated with the investment that could result in material loss.
Accumulate - The investment outlook and risk/reward over the following 12 months are favorable on an absolute basis and relative to the peer group.
Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.
Reduce - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.
Sell - The investment outlook and risk/reward over the following 12 months are very unfavorable on an absolute basis and relative to the peer group.
NA - A rating is not assigned.

Ratings Distribution

	Research Coverage		Investment Banking Clients*		
Rating	Count	% of Total	Count	% of Total	% of Rating Category
Buy	49	55.1%	3	75.0%	6.1%
Neutral	36	40.4%	0	0.0%	0.0%
Sell	4	4.5%	1	25.0%	25.0%
Total	89	100.0%	4	100.0%	4.5%

*Investment banking clients are companies for whom Seaport Global Securities has provided investment banking services in the previous 12 months.

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Utilities

2Q20 Earnings Preview (Correction*)

Summary:
We expect strong 2Q20 earnings prints for electric utilities thanks to strong residential electric sales, sooner-than expected recovery in C&I loads, and aggressive cost-cutting. Consensus estimates look stale to us, but we expect the strongest positive surprises from MI utilities, **CMS** and **DTE**, though no increase in the 2020 EPS guidance for **DTE** at this point, **SRE**, thanks to tax benefits and cost efficiencies at SDG&E/SoCalGas, and **AEP**, thanks to aggressive cost-cutting which started before COVID. We struggle to call **ETR** results.

There should be plenty of volatility in earnings of water stocks, **CWT** and **AWR** in particular, and that's even before CA makes changes to the revenue decoupling mechanism (WRAM). There should be few surprises from **AWK** and **WTRG**. We chase **AWK** and raise our price target to $145.50 from $130.

Power/retail stocks in TX, **NRG** and **VST**, should report very strong results even though we have yet to see scarcity in spot power prices in ERCOT. Thanks to solid 1H20 results both **NRG** and **VST** should be tracking ahead of the midpoint of their 2020 EBITDA guidance ranges, but we don't expect them to narrow/raise the guidance just yet. We raised our 2021/2022 EBITDA estimates for **VST** to reflect additional hedges.

We updated 2Q20 earnings estimates for: **AEP, AES, AGR, ATO, AWK, AWR, CMS, CWT, D, DTE, DUK, EIX, ES, ETR, EXC, FE, NRG, PCG, PEG, PPL, SJW, SO, SRE, VST and WTRG**. We also increased our price target for **AWK**.
*(*Correction made to the original version of this note: Our 2Q20 estimate for PEG displayed on page 3 has been corrected.)*

Highlights

Electric/gas utilities

An earlier than expected recovery in C&I loads coupled with cost-cutting and some YoY weather benefit should deliver strong earnings beats for MI utilities, **CMS** and **DTE**, in our view. **AEP's** aggressive cost-cutting started pre-COVID should support 2Q20 results while the load weakness should be largely in-line with management's forecasts from the 1Q20 call. The company plans to provide an updated capex and cash flow schedule through 2023 which should incorporate lower capex in 2020 and the $2B North Central Wind project (and its financing). **D** and **SO** should have some weather-related headwinds in 2Q20, but updates on the Vogtle cost schedule (Unit 3 % completion in May and June) and cost contingency being utilized should dominate **SO**'s earnings call. **SO** kept its May 2021 in-service date for Vogtle unit 3 to help with managing the scheduling of the construction work on the site, but the decision has not been well-received by investors. **DUK** plans to provide an update on its capex replacement for the cancelled ACP pipeline only on the 4Q20 earnings call, but we'd expect the replacement for the $2B capex reduction to start only in 2022.

Water utilities

AWK and **WTRG** should have relatively easy YoY comps in the Northeast/Mid-Atlantic as 2Q19 was very rainy, and **WTRG** now has additional cost levers thanks to the Peoples Gas merger. We don't expect any meaningful COVID impacts on their 2Q20 or annual 2020 earnings. Intervener testimonies in **AWK's** NJ rate case should be made public any day now – this rate case together with similar proceedings in PA and MO should dominate **AWK's** earnings call. We are chasing **AWK's** stock by raising our price target to $145.50 from $130 previously.

WTRG's pending acquisition of the Delcora wastewater system in PA has run into legal issues, making investors concerned about the future of municipal water/wastewater M&A.

In CA, Commissioner Guzman Aceves has yet again proposed to do away with the current full revenue decoupling mechanism (WRAM) for investor-owned water utilities, calling it ineffective at promoting water conservation. The CPUC should consider/vote on the proposed decision as soon as August 6. **AWR's** GSWC will have filed its new General Rate Case (GRC) by then while **CWT's** and **AWK's** GRCs in CA are already pending. We therefore assume that any changes to the WRAM, if any, would apply to these companies only in the next GRC, starting in 2024.

CWT keeps waiting for an approval of its GRC to record a revenue increase. In the meantime, **CWT's** quarterly results should continue to come well below expectations. We expect **AWR** to fully recoup the $0.08 EPS hit recorded in 1Q20 related to the underperformance of its pension funds.

Power/retail

The TX load has recovered to pre-COVID levels and while we have seen no real scarcity in power prices so far this summer, strong retail results supported by lower than expected bad debt and optimization of generation hedges should support 2020 EBITDA for **VST** and **NRG** at least at the midpoint of their annual guidance. We don't expect them to narrow the guidance yet, however, as August tends to be a crucial earnings month for both companies.

NRG should provide an update on its 2020 capital allocation strategy which might include another retail acquisition. **VST** hasn't given up on some uplift to forward power curves in TX happening in late August/early September, like we saw last year. Yet, even without the recovery and thanks to additional power hedges, the downside to 2021 EBITDA seems now lower than the $200-250MM below the midpoint of the 2020 guidance range that VST used to quote as a COVID-related downside scenario. Therefore, we raised our 2021/2022 EBITDA expectations for VST to $3,135MM/3,044MM up from $3,034MM/3,009MM, respectively.

We expect **AES** to keep its new/lowered EPS guidance range for 2020 though 2Q20 should be weak on a combination of the DPL/ Argentina/IPL hits, with the earnings uplift from cost-cutting and Southland's PPA should kick in only in 3Q20. The OH and IN load seem to be performing ahead of management's expectations from the 1Q20 earnings call. We await an update on another divestiture of coal-fired plant, potentially Maritza in Bulgaria, we believe.

2Q20 EPS/EBITDA Estimates for Utilities and Power Stocks

Regulated electric/gas utilities	Seaport 2Q20 EPS ($)	Consensus 2Q20 EPS ($)	Seaport/Consensus
AEP	**1.09**	0.99	10%
AGR	0.36	0.33	9%
ATO	0.80	0.76	5%
CMS	**0.46**	0.36	28%
D	0.81	**N/A**	N/A
DTE	**1.35**	1.14	18%
DUK	1.05	1.02	3%
EIX	1.20	1.16	3%
ES	0.76	0.79	-4%
ETR	**1.10**	1.25	-12%
EXC	**0.42**	0.45	-7%
FE	0.56	0.55	2%
PCG	1.00	0.94	6%
PEG	**0.57**	0.62	-8%
PPL	0.55	0.56	-2%
SO	0.66	0.69	-4%
SRE	**1.82**	1.19	53%

Regulated water utilities	Seaport 2Q20 EPS ($)	Consensus 2Q20 EPS ($)	Seaport/Consensus
AWK	0.98	0.95	3%
AWR	**0.70**	0.63	11%
CWT	**0.25**	0.64	-61%
SJW	0.70	0.66	6%
WTRG	0.23	0.24	-4%

Power/retail	Seaport 2Q20 EPS/EBITDA $/$MM	Consensus 2Q20 EPS/EBITDA $/$MM	Seaport/Consensus
AES	**0.22**	0.28	-21%
NRG	550	521	6%
VST	**840**	729	15%

Source: FactSet for consensus, Seaport Global Securities

Comp Sheet: Utilities & Power

Regulated electric utilities	Share price ($) 7/15/2020	Rating	Price target ($)	2022 PE	Premium/Discount to Avg 2022 P/E ex
AEP	84.68	Buy	91.00	**16.8x**	-5%
AGR	45.20	Neutral	N/A	**17.3x**	-2%
CMS	59.74	Buy	65.00	**19.6x**	11%
D	75.45	Buy	91.00	**18.2x**	3%
DTE	109.20	Buy	133.50	**14.7x**	-17%
DUK	80.43	Neutral	N/A	**15.8x**	-11%
EIX	55.28	Buy	70.00	**10.2x**	-42%
ES	85.00	Buy	93.00	**20.6x**	17%
ETR	96.24	Buy	114.00	**15.2x**	-14%
EXC	38.05	Buy	44.00	**14.0x**	-21%
FE	40.82	Buy	50.00	**14.8x**	-16%
PCG	9.20	Neutral	50.00	**8.5x**	-52%
PEG	52.40	Neutral	N/A	**15.4x**	-13%
PPL	25.69	Sell	25.00	**14.3x**	-19%
SO	53.02	Buy	63.00	**14.9x**	-16%
SRE	123.15	Buy	142.00	**15.0x**	-15%
Average P/E for regulated electrics with exclusions				**17.7x**	

Regulated water utilities	Share price ($) 7/15/2020	Rating	Price target ($)	2022 PE	Premium/Discount to Avg 2022 P/E ex
AWK	134.06	Buy	145.50	**29.2x**	9%
AWR	77.21	Buy	84.00	**29.9x**	12%
CWT	48.00	Neutral	N/A	**26.4x**	-1%
SJW	62.63	Neutral	N/A	**23.7x**	-11%
WTRG	43.04	Neutral	N/A	**24.4x**	-9%
Average P/E for regulated water utilities				**26.7x**	**51%**

Power/retail	Share price ($) 7/15/2020	Rating	Price target ($)	2022 PE/FCF yield	Premium/Discount to Avg 2022 P/E ex
AES	15.07	Buy	17.00	**9.1x**	N/A
NRG	34.02	Buy	42.50	**16.7%**	N/A
VST	19.30	Buy	24.00	**20.0%**	N/A

Source: FactSet, Seaport Global Securities

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- Sempra Energy (SRE: $123.15, Buy)
- NRG Energy, Inc. (NRG: $34.02, Buy)
- Entergy Corporation (ETR: $96.24, Buy)
- Vistra Energy Corp. (VST: $19.30, Buy)
- American States Water Company (AWR: $77.21, Buy)
- Essential Utilities, Inc. (WTRG: $43.04, Neutral)
- Duke Energy Corp. (DUK: $80.43, Neutral)
- Atmos Energy Corp. (ATO: $100.64, Buy)
- Eversource Energy (ES: $85.00, Buy)
- FirstEnergy Corp. (FE: $40.82, Buy)
- Public Service Enterprise Group Inc. (PEG: $52.40, Neutral)
- SJW Group (SJW: $62.63, Neutral)
- DTE Energy Company (DTE: $109.20, Buy)
- Southern Co. (SO: $53.02, Buy)
- American Electric Power Company, Inc. (AEP: $84.68, Buy)
- California Water Services Group (CWT: $48.00, Neutral)
- American Water Works Company, Inc. (AWK: $134.06, Buy)
- AES Corporation (AES: $15.07, Buy)
- Dominion Energy, Inc. (D: $75.45, Buy)
- Avangrid, Inc. (AGR: $45.20, Neutral)
- Edison International (EIX: $55.28, Buy)
- Exelon Corporation (EXC: $38.05, Buy)
- PG&E Corporation (PCG: $9.20, Neutral)
- PPL Corporation (PPL: $25.69, Sell)

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Neutral	42	34.1%	0	0.0%	0.0%
Sell	5	4.1%	1	33.3%	20.0%
Total	123	100.0%	3	100.0%	2.4%

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August 11, 2020
Industry Update
Utilities

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Utilities

Water utilities – Updated thoughts following 2Q20 earnings season

Summary:
There is no better utility than a water utility, but even they have regulatory issues like potential changes to the revenue decoupling in CA or regulatory/legal delays to asset acquisitions/sales like with **AWK** in NY or **WTRG** in PA. **AWK** and **AWR** remain our favorite water utilities, and we are impressed with **WTRG**'s strong growth prospects on the gas side, especially if the catch-up repair tax deduction in PA is approved. We updated our thoughts on **AWK, CWT, SJW,** and **WTRG**. We are raising our PT for **AWK**. Also note that we published an update on **AWR** last week (link).
Managements of **AWK** and **AWR** will be attending Seaport's Virtual Summer Conference on August 26. Please use the link to register for the event (registration link).

Highlights

AWK – Teflon stock: The COVID-related drop in C&I sales volumes more than offset higher residential sales, leading to a $0.04 EPS hit to AWK's regulated earnings in 2Q20. Management chose not to offset it with cost-cutting though the hot and dry summer in the Mid-Atlantic and the Midwest should do the trick. We have very limited visibility into AWK's large pending rate cases (requesting $294MM in annualized revenue increases) and the sale of the NY system is getting delayed. Yet, those are still not enough to diminish AWK's investment appeal to us. Therefore, we reiterate our Buy rating and raise our PT to $152 from $145.50.

AWR – Appealing EPS/DPS growth despite decoupling uncertainty: Potential changes to AWR's water revenue decoupling caught us by surprise, but we'd still expect the company to earn its allowed ROEs on the water and electric side, and the military contract business to deliver incremental growth. We raise our 2020/2022 EPS and 2020-2022 DPS estimates. We recently trimmed our PT to $83 from $84 to reflect the risk to the water decoupling and reiterated our Buy rating.

CWT – Waiting continues: Last week, the CPUC delayed its decision on changes to the full decoupling mechanism for water utilities (WRAM). Yet, depending on the outcome of a pending rate case in CA (GRC) and given conservatism of CWT's management, we could see meaningful volatility in CWT's earnings driven by changes in sales volumes as well higher operating expenses related to pensions, medical insurance and COVID-19. The stock trades at a 7% 2022 P/E discount to an average water utility which seems fair to us.

SJW – Delivering against lowered guidance: SJW maintained its lowered 2020 EPS guidance range as the $0.30/share EPS hit for higher purchased water costs remained unchanged, water sales were not materially impacted by COVID, and the accounts collections, though slowing, remained strong. The stock trades at an 8% 2022 P/E discount to an average water utility which seems a bit rich to us given the higher-than-average volatility in SJW's sales volumes and thus realized ROEs. We maintain our Neutral rating.

WTRG – Catch-up repair tax deduction in PA: WTRG sees no negative earnings impact from COVID as stronger residential sales offset lower C&I volumes, and the recent merger with Peoples Gas adds cost levers. The catch-up repair tax deduction in PA would extend the strong mid-teen annual EPS growth rate for gas through even 2026. The future of the DELCORA wastewater acquisition remains uncertain, but WTRG already issued equity to finance it. We maintain our Neutral rating.

Comp sheet - water utilities

Regulated water utilities	Share price ($) 8/10/2020	Rating	Price target ($)	Market cap ($B)	2020 Div Yield	2022 EPS ($)	2022 PE
AWK	149.11	Buy	152.00	27.0	1.4%	4.59	**32.5x**
AWR	79.85	Buy	83.00	3.0	1.6%	2.61	**30.6x**
CWT	48.98	Neutral	N/A	2.4	1.7%	1.82	**26.9x**
SJW	71.06	Neutral	N/A	2.0	1.8%	2.64	**26.9x**
WTRG	47.81	Neutral	N/A	11.7	2.0%	1.77	**27.0x**
Average P/E for regulated water utilities					**1.7%**		**28.8x**

Source: FactSet, Seaport Global Securities

Seaport Global

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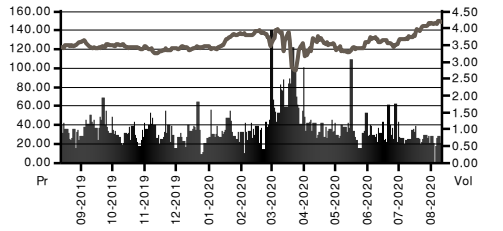
Rating:	**Buy**
Price Target:	**$152.00**

Price Target Metrics:
2022 SOTP valuation implying 33.2x 2022 EPS

Current Price:	**$149.11**
Float:	180.7MM
Diluted Shares:	181.0MM
Short Interest:	2.5MM
Average Daily Volume:	763k
52 Week Range:	$92.00 - $150.47
Market Cap:	**$26,989MM**
Cash and Investments:	$569MM
Debt:	$9,593MM
Enterprise Value:	$36,013MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Adjusted)							
FY	$3.61A	$3.84	$3.85E	$4.23	$4.23E	$4.59	$4.59E
P/E	**41.3x**		**38.8x**		**35.2x**		**32.5x**
Dividends Per Share							
FY	$1.955A	$2.150	$2.150E	$2.365	$2.365E	$2.600	$2.600E
Dividend Yield	**1.3%**		**1.4%**		**1.6%**		**1.7%**

American Water Works Company, Inc.

(NYSE: AWK)

Teflon stock; raising PT

Summary:
The COVID-related drop in C&I sales volumes more than offset higher residential sales, leading to a $0.04 EPS hit to AWK's regulated earnings in 2Q20. Management chose not to offset it with cost-cutting though the hot and dry summer in the Mid-Atlantic and the Midwest should do the trick. We have very limited visibility into AWK's large pending rate cases (requesting $294MM in revenue increases) and the sale of the NY system is getting delayed. Yet, those are still not enough to diminish AWK's investment appeal to us. Therefore, we reiterate our Buy rating and raise our PT to $152 from $145.50.

Highlights

COVID hit to earnings: In 1H20, the COVID-related pick up in residential sales volumes was not enough to offset lower C&I sales, leading to a $0.04 EPS hit to regulated earnings. Management doesn't want to make arbitrary cost reductions to offset this (hopefully) one-time earnings hit. Given the hot and dry summer in the Mid-Atlantic and the Midwest, the weather-driven spike in usage should offset the COVID expenses, especially as AWK's water demand should have become more sensitive to CDDs and changes in precipitation levels, we believe.

Rate cases: 2020 is a very busy regulatory year for AWK, and we have little clarity on its pending rate cases, in particular in NJ and CA. The interveners in the NJ case filed their testimonies, but those haven't been made public by the regulator/BPU. In CA, the regulator/CPUC proposed to remove full revenue decoupling for water utilities (WRAM) given that it has not resulted in water conservation. The vote of the Commission on this issue has been delayed, and for now, we assume that AWK's pending general rate case in the state should not be affected thus providing visibility into realized ROEs in CA through 2023.

NY asset sale: In November 2019, AWK announced the sale of its NY operations to Liberty Utilities for $608MM and hoped to finalize the transaction in 2H20. The regulatory review of the deal got originally delayed due to COVID, and the NY PSC recently extended from August 3 to October 15 the deadline for munis to submit municipalization proposals for their systems within AWK's NY service territory. Long Island, NY is a challenging jurisdiction for AWK, so we remain hopeful the sale transaction should eventually close, and the ~$400MM in net proceeds should offset AWK's future equity needs.

Estimates and valuation: Our 2021/2022 EPS estimates remain unchanged as we await outcomes of AWK's numerous rate cases. We raised our 2020 EPS estimate to $3.85 from $3.84 based on YTD results and as we expect the summer weather to offset the COVID impact. We raised our PT to $152 from $145.50 as we continue to chase the stock. Our new PT is based on our 2022 SOTP valuation and implies a 33.2x 2022 EPS up from 32x previously.

Company Description:
AWK is the largest publicly-traded regulated water and wastewater utility in the US with operations in 16 states, primarily in the Northeast and the Midwest, serving 3.4 million customer accounts. AWK also engages in unregulated contract-based water/wastewater services for military bases (16 bases) and provides water/wastewater line warranty services (homeowner services) to ~1.5 million residential accounts

AWK: EPS breakdown by segment ($)

AWK	2018A	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated utilities	3.32	3.60	3.92	4.32	4.67	9.1%
Unregulated ops	0.33	0.45	0.49	0.52	0.56	7.6%
Parent	-0.35	-0.44	-0.56	-0.61	-0.64	13.3%
Total EPS	**3.30**	**3.61**	**3.85**	**4.23**	**4.59**	**8.3%**
DPS	**1.78**	**1.96**	**2.15**	**2.37**	**2.60**	**10.0%**
Dividend payout	54%	54%	56%	56%	57%	

Source: Company data for 2018-2019; Seaport Global Securities

AWK: 2020 SOTP valuation ($)

AWK - 2022 SOTP	EPS	Multiple	Value per share
Regulated utilities less parent	4.03	32.3x	130.17
Military contracts	0.19	50.0x	9.50
Homeowner services	0.37	32.3x	11.95
Total per share			**151.62**

AWK	2018A	2019A	2020E	2021E	2022E
Sales	3,440	3,610	3,777	4,010	4,221
Operating expenses	1,773	1,824	1,871	1,919	1,969
EBITDA	1,667	1,786	1,906	2,091	2,253
Depreciation	545	582	626	670	714
EBIT	1,122	1,204	1,280	1,421	1,539
Net interest expense	350	382	402	442	460
Ordinary Profit Before Tax	809	872	928	1,029	1,129
Income tax	216	218	232	257	282
Net profit	593	654	696	771	847
S/O (m)	180	181	181	182	184
Diluted EPS	**3.30**	**3.61**	**3.85**	**4.23**	**4.59**
DPS	**1.78**	**1.96**	**2.15**	**2.37**	**2.60**
Cash	158	90	45	45	45
Financial and Operating Receivables	301	294	311	330	348
Inventory	41	44	44	45	46
Other short-term assets	281	857	292	292	292
Goodwill	1,575	1,501	1,501	1,501	1,501
Other-long term assets	1,458	1,664	1,664	1,664	1,664
Property, plant, and equipment	17,409	18,232	19,475	20,675	21,832
Total assets	**21,223**	**22,682**	**23,332**	**24,552**	**25,727**
Financial liabilities	1,035	814	936	936	936
Operating liabilities	175	203	194	199	204
Other liabilities	884	1,028	851	851	851
Deferred credits and other regulatory liabiliti	5,689	5,872	6,053	6,254	6,397
Long-term debt	7,576	8,639	9,470	9,893	10,403
Shareholders' equity	5,864	6,126	5,828	6,420	6,937
Total liabilities and equity	**21,223**	**22,682**	**23,332**	**24,552**	**25,727**
Net income	565	654	696	771	847
D&A, goodwill amortisation	545	582	626	670	714
Other non cash elements	308	214	181	201	220
Funds from operations	1,418	1,450	1,503	1,642	1,780
Decrease (increase) in non-cash working ca	-32	-67	-26	-15	-91
CFO	**1,386**	**1,383**	**1,477**	**1,626**	**1,690**
Net investments in fixed assets	-1,949	-1,841	-1,865	-1,865	-1,865
Net investments in financial assets	-87	-104	-104	-104	-104
Free cash flow before dividends	**-650**	**-562**	**-492**	**-343**	**-279**
Dividends paid (group + minorities)	-319	-354	-389	-431	-479
Free cash flow after dividends	-969	-916	-881	-774	-758
Increase or (repayment) of capital and subsi	892	857	881	473	560
Increase or (repayment) of financial debt	138	-36	-45	301	198
Adjustment for minorities / miscellaneous	14	27	0	0	0
Increase in cash	75	-68	-45	0	0

Seaport Global

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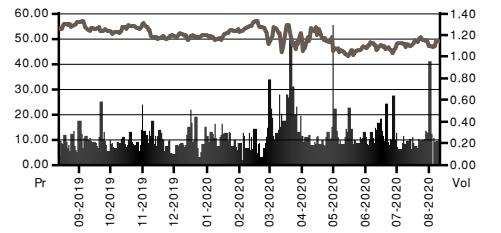
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$48.98**
Float:	48.9MM
Diluted Shares:	48.9MM
Short Interest:	0.8MM
Average Daily Volume:	263k
52 Week Range:	$39.74 - $57.48
Market Cap:	**$2,397MM**
Cash and Investments:	$114MM
Debt:	$1,182MM
Enterprise Value:	$3,465MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
FY	$1.31A	$1.40	$1.39E	$1.70	$1.70E	$1.82	$1.82E
P/E	**37.3x**		**35.2x**		**28.8x**		**26.9x**
Dividends Per Share							
FY	$0.790A	$0.850	$0.850E	$0.909	$0.909E	$0.978	$0.978E
Dividend Yield	**1.6%**		**1.7%**		**1.9%**		**2.0%**

California Water Services Group

(NYSE: CWT)

Waiting continues

Summary:

Last week, the CPUC delayed its decision on changes to the full decoupling mechanism for water utilities (WRAM). Yet, depending on the outcome of a pending rate case in CA (GRC) and given conservatism of CWT's management, we could see meaningful volatility in CWT's earnings driven by changes in sales volumes as well higher operating expenses related to pensions, medical insurance and COVID-19. The stock trades at a 7% 2022 P/E discount to an average water utility which seems fair to us.

Highlights

Potential changes to revenue decoupling: One of CPUC Commissioner has renewed her previous proposal to do away with WRAM for CA water utilities as, according to her, it has failed to result in water conservation. The proposed decision related to this issue has been held by the Commission at least until the August 27 meeting of the CPUC. The Commissioner proposed to adopt WRAM changes only in the next rate following the CPUC approval which, if adopted as currently proposed, would mean CWT should retain the full decoupling until the end of 2022, our current assumption.

Awaiting proposed decision in 2020 GRC: The CPUC should issue a proposed decision in this case by late August. While most of the issues in the rate case were settled, the revenue decoupling mechanism and balancing accounts for pension and healthcare expenses were not a part of the settlement.

Estimates and valuation: We lowered our 2020 EPS estimate by $0.01 to $1.38 to reflect COVID-related expenses which are being expensed despite a catastrophic memorandum account which other CA utilities use to defer these costs. CWT trades at a 7% 2022 P/E discount to an average water utility in the US despite premium EPS growth prospects. Yet, the discount seems fair to us given the ongoing uncertainty regarding CWT's general rate case and the potential volatility in CWT's future earnings power.

Company Description:

CWT operates regulated water and wastewater utilities in CA, WA, HI and NM, with 490,000 connections in CA (90%), 36,000 connections in WA (recently doubled through an acquisition), 5,000 in HI, and 8,300 connections in NM.

CWT: EPS breakdown by segment ($)

CWT	2018A	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.36**	**1.31**	**1.39**	**1.70**	**1.82**	**11.5%**
DPS	**0.75**	**0.79**	**0.85**	**0.91**	**0.98**	**7.4%**
Dividend payout	55%	60%	61%	54%	54%	

Source: Company data for 2018-2019; Seaport Global Securities

CWT	2018A	2019A	2020E	2021E	2022E
EBIT	132	117	125	149	160
EBITDA	218	209	224	255	274
Net interest expense	38	41	44	45	47
Net income	66	63	68	87	96
EPS	**$1.36**	**$1.31**	**$1.39**	**$1.70**	**$1.82**
DPS	**$0.75**	**$0.79**	**$0.85**	**$0.91**	**$0.98**

CFO	**$ 179**	**$ 169**	**$ 188**	**$ 214**	**$ 231**
Utility plant expenditures	(272)	(274)	(275)	(285)	(285)
Other	(1)	(2)	(2)	(2)	(2)
CFI	**(273)**	**(276)**	**(277)**	**(287)**	**(287)**
Issuance of common stock	(2)	18	96	80	86
Issuance of debt	73	103	28	32	32
Dividends	(36)	(38)	(41)	(44)	(47)
Other	11	20	20	20	20
CFF	**47**	**103**	**103**	**88**	**91**
Change in cash and cash equivalents	(48)	(4)	13	15	35

Net utility plant	2,233	2,406	2,583	2,761	2,932
Cash and cash equivalents	47	43	62	77	112
Other current assets	142	142	142	142	142
Total current assets	189	184	204	219	253
Regulatory assets	354	433	433	433	433
Goodwill	3	3	3	3	3
Other assets	60	85	85	85	85
Total assets	**$ 2,838**	**$ 3,111**	**$ 3,307**	**$ 3,501**	**$ 3,707**
Total common stockholders' equity	$ 730	$ 780	$ 807	$ 850	$ 899
Long-term debt, less current maturities	710	787	814	847	879
Total capitalization	**1,440**	**1,567**	**1,622**	**1,697**	**1,778**
Total current liabilities	321	359	479	578	682
Deferred income taxes	213	223	223	223	223
Pension and postretirement benefits ot	194	259	259	259	259
Other long-term liabilities	257	270	270	270	270
Advances for construction	186	191	191	191	191
Contributions in aid of construction	225	242	262	282	302
Total capitalization and liabilities	**$ 2,838**	**$ 3,111**	**$ 3,307**	**$ 3,501**	**$ 3,707**

Seaport Global

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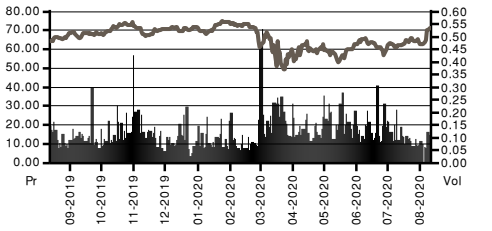
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$71.06**
Float:	26.0MM
Diluted Shares:	28.7MM
Short Interest:	0.5MM
Average Daily Volume:	94k
52 Week Range:	$45.60 - $74.99
Market Cap:	**$2,038MM**
Cash and Investments:	$23MM
Debt:	$1,508MM
Enterprise Value:	$3,523MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
FY	$1.78A	$1.97	$2.00E	$2.42	$2.43E	$2.64	$2.64E
P/E	**39.8x**		**35.5x**		**29.3x**		**26.9x**
Dividends Per Share							
FY	$1.200A	$1.280	$1.280E	$1.370	$1.370E	$1.465	$1.465E
Dividend Yield	**1.7%**		**1.8%**		**1.9%**		**2.1%**

SJW Group

(NYSE: SJW)

Delivering against lowered guidance

Summary:

SJW maintained its lowered 2020 EPS guidance range as the $0.30/share EPS hit for higher purchased water costs remained unchanged, water sales were not materially impacted by COVID, and the accounts collections, though slowing, remained strong. The stock trades at an 8% 2022 P/E discount to an average water utility which seems a bit rich to us given the higher-than-average volatility in SJW's sales volumes and thus realized ROEs. We maintain our Neutral rating.

Highlights

CA: The water usage volumes tracked authorized sales levels with higher residential sales offsetting lower C&I volumes. San Jose Water had adequate water supplies and continues to expect a ~$0.30 EPS hit in 2020 from the lower availability of surface water. The utility's three-year capex in CA of $320MM remains achievable.

CT: The recent Isaiah storm caused widespread power outages in the state, forcing ~100 facilities of CT Water to run on back-up generators, but the water service continued uninterrupted. We assume that Connecticut Water should be able to defer and subsequently recover incremental costs related to the storm.

Estimates and valuation: SJW reaffirmed its previously lowered 2020 EPS guidance range of $1.95-2.05. In 1H20, SJW recorded $0.12/share in merger-related cost benefits in $0.12/share in other benefits, ahead of our prior expectations. We raised our 2020/2021 EPS estimates to $2.00/2.43 from $1.97/2.42 to reflect stronger-than-expected sales volumes in CA during 2020 and some incremental cost efficiencies in both 2020 and 2021. SJW trades at an 8% 2022 P/E discount to an average water utility while offering a stronger-than-average EPS growth (though with an above-average volatility) and an average DPS growth. To us, SJW deserves a 10%+ discount to an average utility and that's why we stick to our Neutral rating.

Company Description:

SJW Group is a regulated water and wastewater utility serving ~390,000 accounts across CA, CT, TX and ME. SJW merged with Connecticut Water Service in October 2019.

SJW: EPS breakdown by segment ($)

SJW	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.78**	**2.00**	**2.43**	**2.64**	**14.1%**
DPS	**1.20**	**1.28**	**1.37**	**1.47**	**6.9%**
Dividend payout	67%	64%	56%	55%	

Source: Company data for 2019; Seaport Global Securities

SJW	2019A	2020E	2021E	2022E
EBITDA	157	213	242	253
Net income	51	57	70	76
EPS diluted	**$1.78**	**$2.00**	**$2.43**	**$2.64**
DPS	**$1.20**	**$1.28**	**$1.37**	**$1.47**
CFO	**$ 130**	**$ 151**	**$ 169**	**$ 178**
CFI	**(1,018)**	**(216)**	**(277)**	**(257)**
Issuance of common stock	0.0	0.0	0.0	0.0
Issuance of debt	502	113	113	113
Dividends	-34	-36	-39	-40
CFF	**485**	**101**	**99**	**99**
Change in cash and cash equivalents	-403	36	-9	20
Net utility plant	2,206	2,312	2,473	2,611
Cash and cash equivalents	18	54	45	65
Other current assets	109	112	115	117
Total current assets	127	166	159	182
Regulatory assets	114	114	114	114
Goodwill	628	628	628	628
Other assets	57	57	57	57
Total assets	**3,132**	**3,277**	**3,431**	**3,593**
Total common stockholders' equity	$ 890	$ 967	$ 984	$ 1,003
Long-term debt, less current	1,261	1,187	1,195	1,203
Total capitalization	**2,151**	**2,154**	**2,179**	**2,206**
Total current liabilities	235	357	467	581
Deferred income taxes	196	193	190	188
Pension and postretirement benefits oth	108	108	108	107
Other long-term liabilities	45	45	45	45
Advances for construction	112	135	157	180
Contributions in aid of construction	286	286	286	286
Total capitalization and liabilities	**3,132**	**3,277**	**3,431**	**3,593**

Seaport Global

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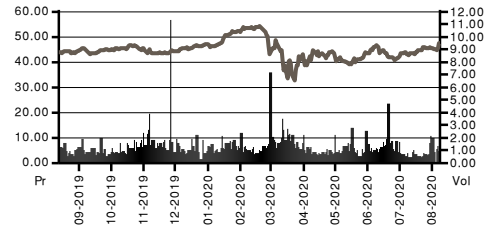
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$47.81**
Float:	244.6MM
Diluted Shares:	254.4MM
Short Interest:	6.4MM
Average Daily Volume:	865k
52 Week Range:	$30.40 - $54.52
Market Cap:	**$12,164MM**
Cash and Investments:	$5MM
Debt:	$5MM
Enterprise Value:	$12,165MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
FY	$1.47A	$1.55	$1.56E	$1.66	$1.66E	$1.76	$1.77E
P/E	**32.5x**		**30.7x**		**28.9x**		**27.0x**
Dividends Per Share							
FY	$0.907A	$0.970	$0.970E	$1.038	$1.038E	$1.111	$1.111E
Dividend Yield	**1.9%**		**2.0%**		**2.2%**		**2.3%**

Essential Utilities, Inc.

(NYSE: WTRG)

Catch-up repair tax deduction in PA

Summary:
WTRG sees no negative earnings impact from COVID as stronger residential sales offset lower C&I volumes, and the recent merger with Peoples Gas adds cost levers. The catch-up repair tax deduction in PA would extend the strong mid-teen annual EPS growth rate at Peoples through even 2026. The future of the DELCORA wastewater acquisition remains uncertain, but WTRG already issued equity to finance it. We maintain our Neutral rating.

Highlights

No COVID impact on earnings: With stronger residential sales volumes offsetting lower C&I sales and regulatory deferrals of bad debts and other COVID-related expenses, WTRG saw no earnings impact from the pandemic in 1H20. We could see some positive earnings impact if the current heat continues in PA – dry lawns should be eyesores to residential customers working from home during COVID.

Catch-up repair tax deduction for Peoples Gas in PA: Last week, following consultations with the regulator (PA PUC), Peoples Gas field its long-awaited application in this case. The additional tax deduction of $380.7MM (~$141MM tax benefit) is related to federal and state taxes for tax years 2012-2019 and through March 2020. The company proposed a $14MM annual customer credit for four years (2021-2024) which would represent less than a 2% reduction in a residential monthly bill. It seems very low to us, but is constrained by Peoples' limited tax capacity as the utility uses forward-looking repair tax deductions especially in 2021 and 2022. The remaining $85MM in tax deductions would be used by Peoples in 2023-2026 to boost realized ROEs by reducing the tax expense. It's an interesting proposal as it extends the current strong earnings growth at Peoples through 2026, but doesn't change the growth trajectory through 2022 thus avoiding a likely fierce regulatory battle in PA.

DELCORA wastewater acquisition: Aqua PA believes it has a legally-binding purchase agreement for the wastewater system from last November and the regulatory approval process of the transaction at the PA PUC should conclude in early 2021, assuming no delays. The Delaware County sued to stop the sale and by mid-September a judge in the case should rule if the County has a right to stop the sale transaction. The issue seems to be who gets the net proceeds from the sale transaction (~$200MM) – the County or a trust which would offset future ratepayer bill increases as Aqua plans to invest $700MM in the system over the next couple of years. Last night, WTRG priced a 6.7MM share equity forward which should finance the DELCORA deal, we believe, even though the future of the transaction seems uncertain to us.

Estimates and valuation: We raised our 2020 EPS estimate by $0.01 to $1.56 to reflect favorable weather and no COVID-related EPS drag. We raised our 2022 EPS by $0.01 to $1.77 to reflect marginally higher merger-related cost efficiencies. WTRG trades in line with CWT and slightly higher than SJW based on our 2022 EPS estimates which seems fair to us given that ~30% of WTRG's EPS should come from a gas LDC rather than a water utility.

Company Description:
WTRG owns and operates water utilities (1 million accounts) and gas utilities (0.74 million accounts) in 10 states though mainly PA.

WTRG: EPS breakdown by segment ($)

WTRG	2018A	2019A	2020E	2021E	2022E	19-'22 CAGR
Regulated water utilities	1.41	1.47	1.09	1.16	1.23	
Regulated gas utilities	0.00	0.00	0.53	0.62	0.70	
Parent	0.00	0.00	-0.06	-0.12	-0.16	
Total EPS	**1.41**	**1.47**	**1.56**	**1.66**	**1.77**	**6.4%**
DPS	**0.85**	**0.91**	**0.97**	**1.04**	**1.11**	**7.0%**
Dividend payout	60%	62%	62%	63%	63%	

Source: Company data for 2018-2019, Seaport Global Securities

WTRG	2018A	2019A	2020E	2021E	2022E
Operational EBITDA	470	505	868	920	986
Operational EBIT	323	349	604	641	692
Net interest expense	99	100	201	209	227
Ordinary Profit Before Tax	252	269	431	459	492
Income tax	1	7	34	37	39
Net profit	251	262	396	422	453
S/O (m)	178	178	254	255	256
Diluted EPS	**1.41**	**1.47**	**1.56**	**1.66**	**1.77**
DPS	**0.85**	**0.91**	**0.97**	**1.04**	**1.11**
Cash	4	1,869	5	5	5
Receivables	101	108	109	113	118
Inventory	16	18	30	30	30
Other short-term assets	26	18	18	18	18
Other-long term assets	887	1,003	3,810	3,810	3,810
Property, plant, and equipment	5,930	6,346	8,962	9,113	9,249
Total assets	**6,965**	**9,362**	**12,934**	**13,089**	**13,230**
Financial liabilities	117	117	496	496	496
Operating liabilities	63	67	109	109	109
Other liabilities	108	108	220	220	220
Deferred credits	2,068	2,057	2,758	2,757	2,757
Long-term debt	2,398	2,943	4,750	5,081	5,401
Shareholders' equity	2,210	4,070	4,601	4,425	4,247
Total liabilities and equity	**6,965**	**9,362**	**12,934**	**13,089**	**13,230**
Net income	251	262	396	422	453
D&A, goodwill amortisation	147	156	264	279	294
Other non cash elements	-54	-40	-6	-6	-6
Funds from operations	344	379	654	695	740
Non-cash working capital	25	-40	43	0	-1
CFO	**369**	**339**	**697**	**694**	**740**
Net investments in fixed assets	-641	-610	-6,555	-765	-780
Net investments in financial assets	2	6	0	0	0
Free cash flow before dividends	**-271**	**-266**	**-5,858**	**-71**	**-40**
Dividends paid	-151	-161	-247	-264	-284
Free cash flow after dividends	-422	-427	-6,105	-334	-325
Changes in capital	2	1,935	2	2	3
Changes in financial debt	421	386	4,238	331	321
Adjustment for minorities / miscellaneous	-2	-28	1	1	1
Increase in cash	-1	1,866	-1,864	0	0

Utilities Disclosures

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Risks & Considerations for American Water Works Company, Inc. American Water Works Company, Inc. (AWK)

Allowed ROEs for AWK's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings.

Lower sales volumes could weigh on AWK's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWK has a particularly busy regulatory calendar in 2020, with rate cases in three of its largest jurisdictions – NJ, PA and MO.

Potentially higher equity needs due to weakening operating cash flows and underfunded pension funds: Lower customer collections (due to lower sales or non-payment) coupled with growing federal cash taxes and underperforming pension funds should be weighing on operating cash flows of regulated utilities especially during/following the COVID-19 pandemic. That in turn could require some deleveraging of balance sheets of regulated utilities thus more equity. AWK already announced ~$500m in new equity as soon as 2022, but the issuances could be enlarged and accelerated to protect AWK's credit ratings.

Risks & Considerations for American States Water Company American States Water Company (AWR)

AWR's water utility (GSWC) could see volatility in earnings due to usage: The CPUC considers changes to the current water revenue decoupling mechanism (WRAM). While it should not impact GSWC until the next rate case, covering 2024-2026, CA utility consumer advocates push for an immediate change to the decoupling mechanism. GSWC has always excelled at earning at least its allowed ROE in CA, but it could prove challenging with WRAM.

Allowed ROEs for AWR's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. AWR's allowed ROE for its water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWR should be filing a new water rate case by July 2020 with new rates in effect in January 2021.

Returns in pension accounts impact AWR's earnings in between rate cases in CA: AWR has no balancing account tracking changes in returns in its pension accounts. Those changes can be trued up/reflected in AWR's rates during rate cases, but those take place every three years.

Military contracts are highly competitive: Through its unregulated ASUS subsidiary, AWR provides water and wastewater services to 11 military bases. The company awaits awards of up to three more of these contracts in 2020. We assume that AWR secures at least one new military contract per year in 2020-2022 though AWK, AWR's largest competitor, has been winning most of the contract awards as of late.

Risks & Considerations for California Water Services Group California Water Services Group (CWT)

Allowed ROEs for CWT's regulated water utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. CWT's allowed ROE for its water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. CWT awaits a proposed decision in its 2018 general rate case in CA with rates retroactive to January 1, 2021. Though the utility reached a partial settlement with the consumer advocate late in 2019, outstanding issues involve the continuation of the revenue decoupling and balancing accounts for pension and medical expenses. Without those, CWT could see a meaningful spike in its earnings volatility.

Risks & Considerations for SJW Group SJW Group (SJW)

Allowed ROEs for SJW's regulated water utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. SJW's allowed ROE for its CA water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. SJW should file a rate case for its new CT business in 2021. Also, the CA utility of SJW should go through a general rate case in the state in 2021 and state regulators could attempt to claw-back some synergies related to the recent merger with CTWS.

SJW's CA earnings are highly volatile: Now that SJW no longer has even a temporary decoupling mechanism in CA, it's CA earnings change along with changes in volumes and changes in purchased water costs. SJW plans to ask for a purchased water cost balancing account in the next rate case in CA, but that means that 2021 could be another weak earnings year before the regulatory fix arrives for 2022, if at all.

Risks & Considerations for Essential Utilities, Inc. Essential Utilities, Inc. (WTRG)

Allowed ROEs for WTRG's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average

10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. WTRG's only pending rate case (in NC) is very small.

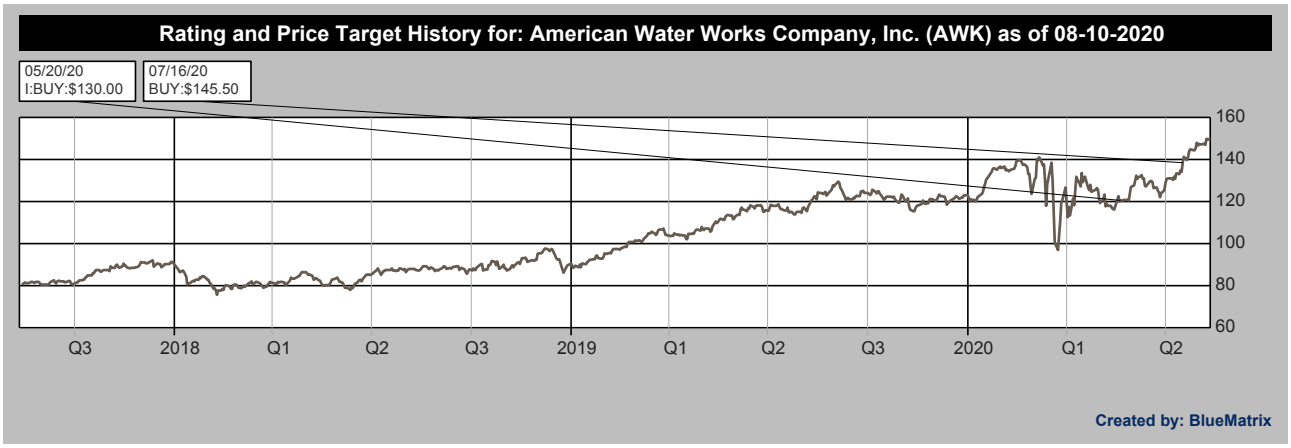
Lower sales volumes could weigh on WTRG's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

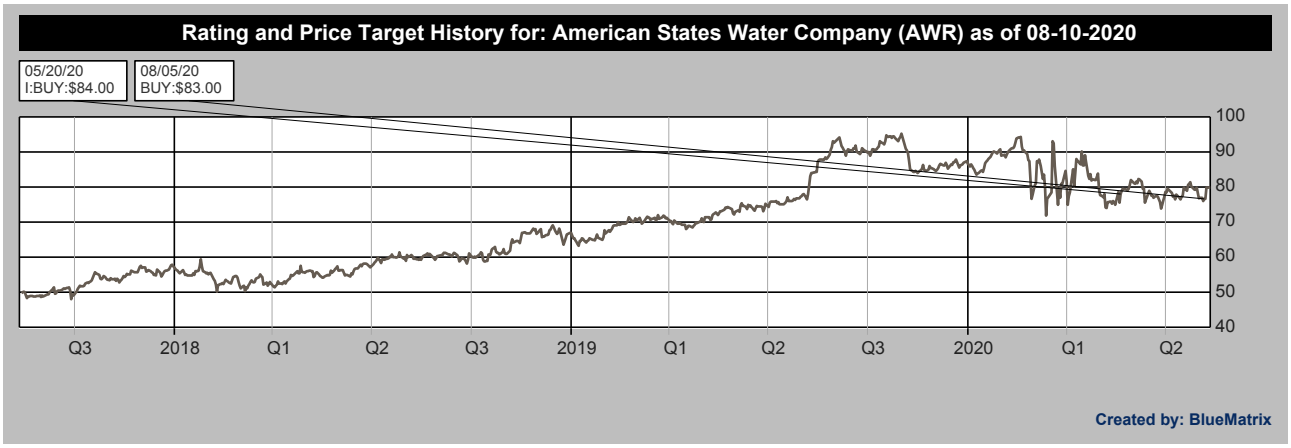
Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. WTRG's regulatory calendar is quiet in 2020, with a pending small rate case in NC, and a likely filing for a catch-up repair tax adjustment for Peoples in PA.

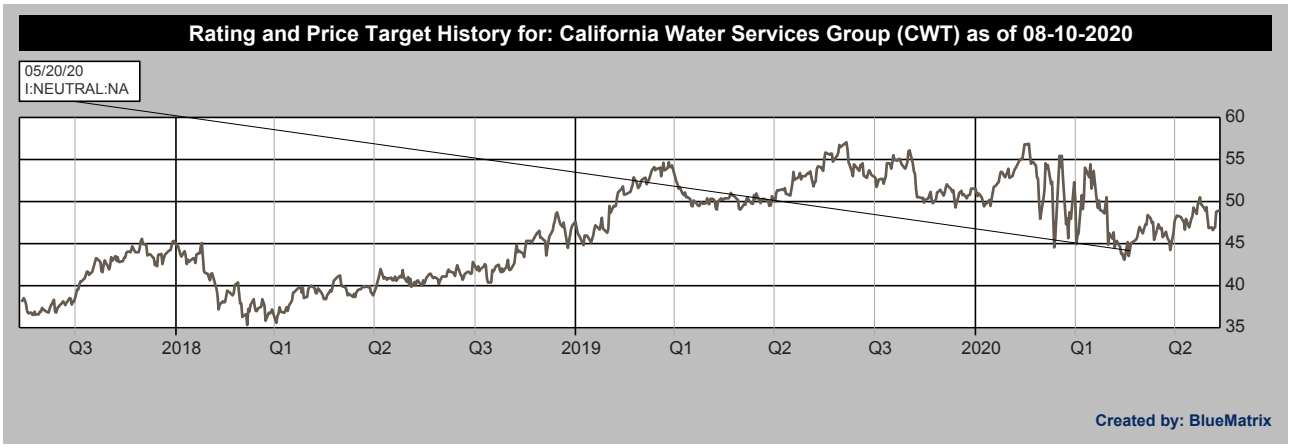
Gas utilities have a higher operating risk than water utilities: Overpressurized gas systems seem to happen more frequently among gas utilities in the US. While we recognize that Peoples Gas is a well-managed system, WTRG's risk profile could further deteriorate with any gas-related operational issues.

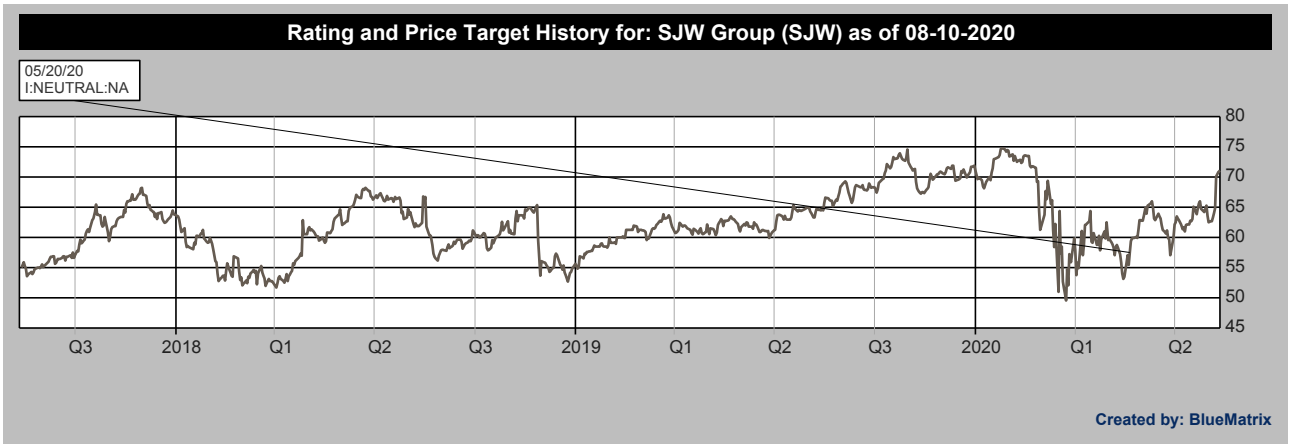
Other Companies Mentioned in This Report

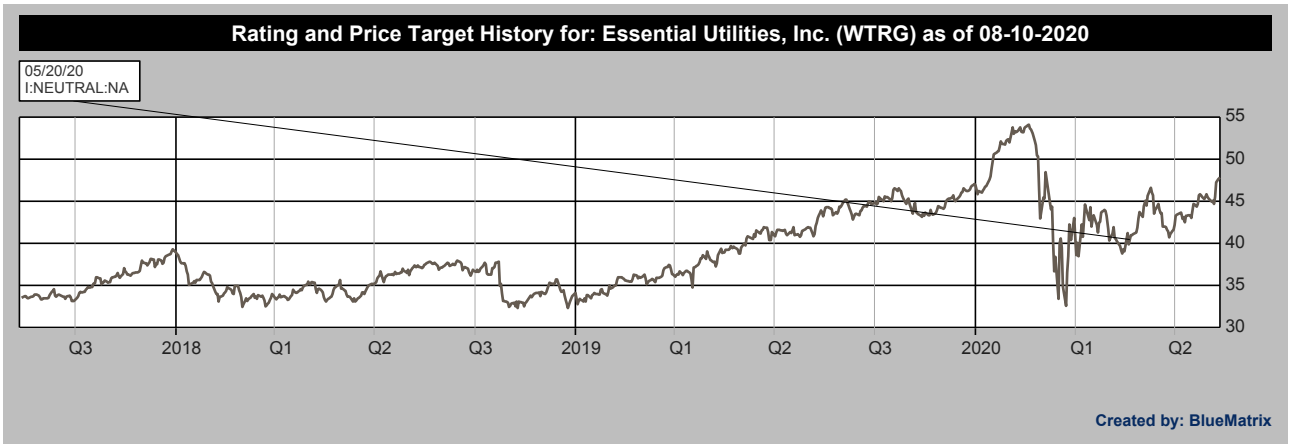
- American Water Works Company, Inc. (AWK: $149.11, Buy)
- California Water Services Group (CWT: $48.98, Neutral)
- Essential Utilities, Inc. (WTRG: $47.81, Neutral)
- American States Water Company (AWR: $79.85, Buy)
- SJW Group (SJW: $71.06, Neutral)











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Sell - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.
NA - A rating is not assigned.

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Accumulate - The investment outlook and risk/reward over the following 12 months are favorable on an absolute basis and relative to the peer group.
Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.
Reduce - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.
Sell - The investment outlook and risk/reward over the following 12 months are very unfavorable on an absolute basis and relative to the peer group.
NA - A rating is not assigned.

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	Research Coverage		Investment Banking Clients*		
Rating	Count	% of Total	Count	% of Total	% of Rating Category
Buy	76	61.8%	2	66.7%	2.6%
Neutral	42	34.1%	0	0.0%	0.0%
Sell	5	4.1%	1	33.3%	20.0%
Total	123	100.0%	3	100.0%	2.4%

*Investment banking clients are companies for whom Seaport Global Securities has provided investment banking services in the previous 12 months.

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October 01, 2020
Industry Update
Utilities

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Utilities

Water Utilities: Updated thoughts ahead of 3Q20 earnings season

Summary:
The bifurcation in market valuations of US utility stocks stretches to water utilities though it's less pronounced than that among electric utilities. AWK, the top YTD performer among all utilities in the US, beating even NEE, trades at an 19% 2022 P/E premium to all water utilities in the US. The premium grew from just ~1% when we launched coverage in mid-May as investors increasingly flock to (almost) pure-play water utilities with strong ESG growth stories. While gas utilities should contribute only a third of WTRG's earnings and PA is highly supportive of natural gas, WTRG continues to derate on the back of its recent gas LDC acquisition. The stock once trading in line with AWK on FY3, currently trades at a 29% discount to AWK on our 2022 EPS estimates, even though WTRG's muni wastewater M&A pipeline has never been this impressive. Yet, the muni project pipeline is highly dependent on a November court ruling on the DELCORA wastewater system acquisition in PA ($276.5MM) and that uncertainty holds us back. The change to full water revenue decoupling (WRAM) and ongoing delays to CWT's general rate case decision in CA continue to weigh on CWT and AWR, with yet another ugly earnings print likely for CWT. We are increasingly comfortable with the strong earnings trajectory for the two CA water utilities, but remain on the sidelines on CWT as we brace another knee-jerk reaction on a likely big earnings miss in 3Q20.

Highlights

AWK – Strongest utility stock performer and counting: AWK is up ~21% YTD vs. XLU down ~8% and the second best performing water utility, MSEX, down ~2%. Since we launched coverage of AWK in mid-March, AWK's valuation premium to an average water utility grew from less than 1% to 19% currently on 2022 P/Es along with the bifurcation of electric/gas/water utility multiples driven by ESG investors. Though AWK trades at 32.4x our 2022 EPS, we cannot find a better regulated utility growth story in the US even during a year filled with important rate cases. Therefore, we reiterate our Buy rating.

AWR – We can live with WRAM changes, if any, but we'd like to see more military contract awards: We are increasingly comfortable with AWR's ability to earn at least its allowed ROE on the water and electric side, and grow its dividends at a ~9% CAGR through 2022, regardless of future changes to the full water decoupling mechanism (WRAM) which should kick in in 2025, if at all. We'd like to see at least one more military contract award, with at least one more pending solicitation to be resolved in October/ November, we believe. We reiterate our Buy rating.

CWT – Another ugly quarterly print ahead of us, but rate case outcome should be fine, eventually: This should be yet another ugly earnings season for CWT as CA regulators yet again delayed a decision in CWT's never-ending general rate case (GRC), this time until early November. Based on our expectations for the GRC outcome, CWT trades at a 16% 2022 P/E discount to AWR and just a 5% premium to SJW despite heavily under-invested assets of CWT likely driving a premium 11% EPS CAGR through 2022, with little volatility given that the full WRAM modification seems unlikely to impact CWT until 2023. We are concerned of another a knee-jerk pullback in CWT's stock on the back of the upcoming 3Q20 print and that's why we remain on the sidelines.

WTRG – Gas-related discount seemed likely, but it came sooner and larger than expected: We were always skeptical about WTRG's pursuit of a gas LDC, even a fast-growing one, as we worried it would diminish the scarcity value of WTRG's water utility business. Yet, we didn't anticipate the sharp de-rating of gas LDC stocks we saw YTD on concerns over their carbon footprint and electrification of house heating. We don't expect WTRG's ~9% annual gas rate base growth in PA to moderate any time soon, and WTRG's water muni deal pipeline is the strongest in the company's history. We remain on the sidelines as we await a court ruling of the DELCORA acquisition in early November, but find WTRG's value proposition compelling.

Water Utilities: Comp Sheet

Regulated water utilities	Share price ($) 10/01/2020	Rating	Price target ($)	Market cap ($B)	2020 Div Yield	2022 EPS ($)	2022 PE
AWK	148.57	Buy	152.00	26.9	1.4%	4.59	**32.4x**
AWR	76.12	Buy	83.00	2.8	2.8%	2.61	**29.2x**
CWT	44.61	Neutral	N/A	2.2	1.9%	1.82	**24.5x**
SJW	61.57	Neutral	N/A	1.8	2.1%	2.64	**23.3x**
WTRG	40.78	Neutral	N/A	10.0	2.4%	1.78	**22.9x**
Average P/E for regulated water utilities					**2.1%**		**26.5x**

Source: FactSet, Seaport Global Securities

Seaport Global

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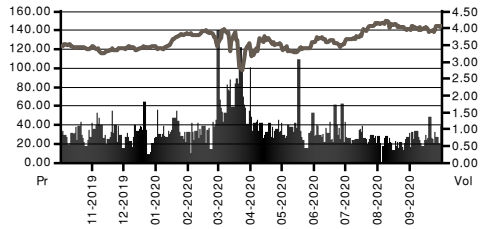
Rating:	**Buy**
Price Target:	**$152.00**

Price Target Metrics:
2022 SOTP valuation implying 33.2x 2022 EPS

Current Price:	**$148.57**
Float:	180.7MM
Diluted Shares:	181.0MM
Short Interest:	2.2MM
Average Daily Volume:	753k
52 Week Range:	$92.00 - $150.47
Market Cap:	**$26,891MM**
Cash and Investments:	$569MM
Debt:	$9,593MM
Enterprise Value:	$35,915MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Adjusted)				
FY	$3.61A	$3.85E	$4.23E	$4.59E
P/E	**41.1x**	**38.6x**	**35.1x**	**32.3x**
Dividends Per Share				
FY	$1.955A	$2.150E	$2.365E	$2.600E
Dividend Yield	**1.3%**	**1.4%**	**1.6%**	**1.8%**

American Water Works Company, Inc.

(NYSE: AWK)

Strongest utility stock performer YTD and counting

Summary:

AWK is up ~21% YTD vs. XLU down ~8% and the second best performing water utility, MSEX, down ~2%. Since we launched coverage of AWK in mid-March, AWK's valuation premium to an average water utility grew from less than 1% to 19% currently on 2022 P/Es along with the bifurcation of electric/gas/water utility multiples driven by ESG investors. Though AWK trades at 32.4x our 2022 EPS, we cannot find a better regulated utility growth story in the US even during a year filled with important rate cases. Therefore, we reiterate our Buy rating.

Highlights

COVID and hot/dry summer: According to NOAA, cooling degree days in NJ/PA/IL were up 24%/27%/39% vs. normal and while the precipitation levels were just slightly below normal, we'd expect AWK's residential sales to be sharply up, especially given COVID-related work from home arrangements. C&I sales in the Mid-Atlantic could serve as a drag, but then again some of AWK's service territories fully resumed C&I operations during 3Q20.

Rate cases: We await hearings in AWK's NJ rate case during October. In CA, the regulator/CPUC recently removed the full revenue decoupling for water utilities (WRAM), but AWK's current general rate case should not be impacted. We hope changes among CPUC commissioners could eventually lead to a new/modified WRAM by the time AWK's new rates will be due in 2024.

NY asset sale: In November 2019, AWK announced the sale of its NY operations to Liberty Utilities for $608MM. Long Island munis have until October 15 to submit municipalization proposals for their water systems within AWK's NY service territory. The Massapequa Water District already submitted their proposal to the NY PSC while Sea Cliff and Hempstead continue to consider a municipalization route. AWK remains optimistic about the closing of the NY sale transaction even if small parts of the system were to be excluded due to municipalization.

Military contracts: AWK was recently awarded its 17th water and wastewater service contract for military bases. This time it is a 50-year $771MM contract for the Joint Base Lewis-McChord in WA. This contract is more than 50% larger than AWK's past military contracts, and the company expects another contract award this year, potentially this month. Given the duration, annual indexation and likely expansion of scope of these contracts, we continue to value them at a sharp premium to even regulated water operations.

Homeowner services: AWK entered into a partnership with Iberdrola TX to offer residential customers in the state an optional cooling repair and maintenance plan as well as a surge protection plan. We assume that is the deal which was previously delayed due to COVID. The services covered by this partnership seem unrelated to water which is nothing new for AWK's Homeowner Services business, but it's not ideal for water purists. Then again if we can live with NEE's gas E&P, we can live with AWK's air conditioner service contract.

Company Description:

AWK is the largest publicly-traded regulated water and wastewater utility in the US with operations in 16 states, primarily in the Northeast and the Midwest, serving 3.4 million customer accounts. AWK also engages in unregulated contract-based water/wastewater services for military bases (17 bases) and provides water/wastewater line warranty services (homeowner services) to ~1.5 million residential accounts.

AWK: EPS breakdown by segment ($)

AWK	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated utilities	3.60	3.92	4.32	4.67	9.1%
Unregulated ops	0.45	0.49	0.52	0.56	7.6%
Parent	-0.44	-0.56	-0.61	-0.64	13.3%
Total EPS	**3.61**	**3.85**	**4.23**	**4.59**	**8.3%**
DPS	**1.96**	**2.15**	**2.37**	**2.60**	**10.0%**
Dividend payout	54%	56%	56%	57%	

Source: Company data for 2019; Seaport Global Securities

Seaport Global

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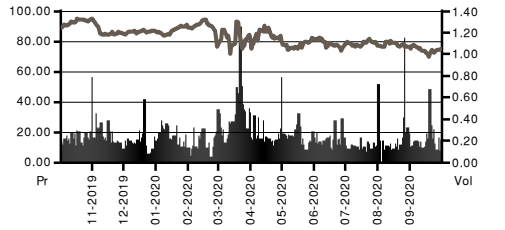
Rating:	**Buy**
Price Target:	**$83.00**

Price Target Metrics:
2022 SOTP valuation which implies 31.8x '22 EPS

Current Price:	**$76.10**
Float:	36.4MM
Diluted Shares:	37.0MM
Short Interest:	0.9MM
Average Daily Volume:	227k
52 Week Range:	$65.11 - $96.64
Market Cap:	**$2,816MM**
Cash and Investments:	$6MM
Debt:	$330MM
Enterprise Value:	$3,139MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Diluted)				
Q1 (Mar)	$0.35A	$0.38A	$0.50E	$0.54E
Q2 (Jun)	$0.64A	$0.69A	$0.64E	$0.68E
Q3 (Sep)	$0.69A	$0.77E	$0.79E	$0.84E
Q4 (Dec)	$0.55A	$0.48E	$0.51E	$0.54E
FY	$2.24A	$2.33E	$2.45E	$2.61E
P/E	**34.0x**	**32.7x**	**31.1x**	**29.2x**
Dividends Per Share				
FY	$1.160A	$1.280E	$1.390E	$1.495E
Dividend Yield	**1.5%**	**1.7%**	**1.8%**	**2.0%**

American States Water Company
(NYSE: AWR)

We can live with WRAM changes, but we'd like to see more military contract wins

Summary:
We are increasingly comfortable with AWR's ability to earn at least its allowed ROE on the water and electric side, and grow its dividends at a ~9% CAGR through 2022, regardless of future changes to the full water decoupling mechanism (WRAM) which should kick in in 2025, if at all. We'd like to see at least one more military contract award, with at least one more pending solicitation to be resolved in October/November, we believe. We reiterate our Buy rating.

Highlights

Modifications to full water decoupling and GSWC's pending rate case: In late August, the CPUC removed the full water revenue decoupling (WRAM) for all four investor-owned water utilities in CA which currently use the mechanism, including AWR's GSWC. The Commission ruled that the WRAM removal should impact "any future general rate case applications filed after the effective date of this decision" so we assume that GSWC's current rate case/GRC (filed on July 15) should not be impacted. Comm. Ranldoph who dissented the WRAM change is assigned to GSWC's rate case which, to us, bodes well for the company given that the Commissioner should not be open to the suggestions from the consumer advocate (ORA) to include the WRAM change in the pending proceeding. Assuming a statutory 18-month review period of the rate case, GSWC's new rates should be decided by the end of 2021 and remain in effect through the end of 2024. Therefore, we'd expect the WRAM changes to affect GSWC's earnings only in 2025, if at all. Management insists the company should do just fine even under the new Monterey-style WRAM, and GSWC has a history of earning at least its allowed ROE on the water side. We are still hopeful the Commission could change its mind on the full WRAM, especially given that the current term of Comm. Guzman-Aceves, the author of the WRAM change, should expire by the end of 2022, i.e. before the filing of GSWC's next general rate case.

ASUS: AWK rather than AWR was recently awarded a particularly large $771MM military water/wasterwater service contract in WA, but we expect at least one (if not two) more military contract awards in October/early November. We still hope AWR's ASUS can get at least one more contract though for now, our 2021-2022 estimates assume ASUS growth driven by existing contracts and changes in the scope of work under them.

Company Description:
AWR is the parent of Golden States Water Co. (GSWC), a regulated water (261,000 water connections in 37 systems), Beaver Valley Electric Service (BVESI), an electric utility (24,400 electric connections in one system) in CA, and American States Utility Services (ASUS), which engages in contract-based water and wastewater services primarily for military bases, currently 11 bases.

AWR: EPS breakdown by segment ($)

AWR	2019A	2020E	2021E	2022E	2019-2022 CAGR
Regulated water	1.62	1.66	1.73	1.85	4.6%
Regulated electric	0.15	0.18	0.20	0.21	11.9%
Military contracts/ASUS	0.47	0.49	0.52	0.55	5.4%
Total EPS	**2.24**	**2.33**	**2.45**	**2.61**	**5.3%**
DPS	**1.16**	**1.28**	**1.39**	**1.49**	**8.8%**
Dividend payout	52%	55%	57%	57%	

Source: Company data for 2019; Seaport Global Securities

Seaport Global

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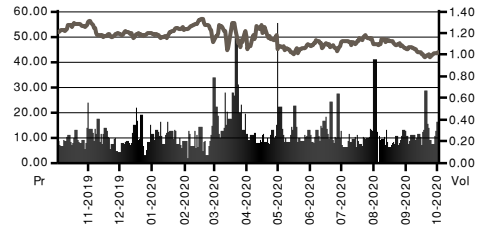
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$44.64**
Float:	49.0MM
Diluted Shares:	49.4MM
Short Interest:	0.9MM
Average Daily Volume:	271k
52 Week Range:	$39.74 - $57.36
Market Cap:	**$2,205MM**
Cash and Investments:	$114MM
Debt:	$1,182MM
Enterprise Value:	$3,273MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
FY	$1.31A	$1.39	$1.39E	$1.70	$1.70E	$1.82	$1.82E
P/E	**34.0x**		**32.0x**		**26.3x**		**24.5x**
Dividends Per Share							
FY	$0.790A	$0.850	$0.850E	$0.909	$0.909E	$0.978	$0.978E
Dividend Yield	**1.8%**		**1.9%**		**2.0%**		**2.2%**

California Water Services Group

(NYSE: CWT)

Another ugly quarterly print ahead of us, but rate case outcome should be fine

Summary:
This should be yet another ugly earnings season for CWT as CA regulators yet again delayed a decision in CWT's never-ending general rate case (GRC), this time until early November. Based on our expectations for the GRC outcome, CWT trades at a 16% 2022 P/E discount to AWR and just a 5% premium to SJW despite heavily under-invested assets of CWT likely driving a premium 11% EPS CAGR through 2022, with little volatility given that the full WRAM modification seems unlikely to impact CWT until 2023. We are concerned of another a knee-jerk pullback in CWT's stock on the back of the upcoming 3Q20 print and that's why we remain on the sidelines.

Highlights

Change to full revenue decoupling and CWT's pending general rate case in CA: In late August, the CPUC removed the full water revenue decoupling (WRAM) for all four investor-owned water utilities in CA which currently use the mechanism, including CWT. The Commission ruled that the WRAM removal should impact "any future general rate case applications filed after the effective date of this decision". CWT's management believes that it means its current never-ending rate case, covering 2020-2022, won't be impacted, though WRAM remains one of several contested items in the proceeding which was partially settled in October 2019. We assume the WRAM change, if any, won't impact CWT's earnings until 2023.

Another ugly quarterly print ahead of us: The CPUC yet again extended the statutory decline to resolve CWT's general rate case (GRC), this time until early November. We remain optimistic that new/higher rates should kick in still this calendar year, and will be retroactive to 1/1/20, making 4Q20 a big earnings quarter. Yet, in the meantime, we'd expect a ~45% EPS miss vs. adjusted consensus for 3Q20. Yes, it will be just due to timing, but that explanation didn't help the stock following the 1Q20 and 2Q20 earnings misses.

Estimates and valuation: Our 2020-2022 annual estimates remain unchanged as we await the final GRC decision. We changed the quarterly distribution of earnings in 2020 to sharply lower 3Q20 results. Based on our expectations for the GRC outcome, CWT trades at a 16% 2022 P/E discount to AWR and just a 5% premium to SJW despite heavily underinvested assets of CWT likely driving a premium 11% EPS CAGR through 2022 with little volatility given that the full WRAM modification seems unlikely to impact CWT until 2023. We are concerned of another knee-jerk pullback in CWT's stock on the back of the upcoming 3Q20 print and that's why we remain on the sidelines.

Company Description:
CWT operates regulated water and wastewater utilities in CA, WA, HI and NM, with 490,000 connections in CA (90%), 36,000 connections in WA (recently doubled through an acquisition), 5,000 in HI, and 8,300 connections in NM.

CWT: EPS breakdown by segment ($)

CWT	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.31**	**1.39**	**1.70**	**1.82**	**11.5%**
DPS	**0.79**	**0.85**	**0.91**	**0.98**	**7.4%**
Dividend payout	60%	61%	54%	54%	

Source: Company data for 2019; Seaport Global Securities

CWT	2018A	2019A	2020E	2021E	2022E
EBIT	132	117	125	149	160
EBITDA	218	209	224	255	274
Net interest expense	38	41	44	45	47
Net income	66	63	68	87	96
EPS	**$1.36**	**$1.31**	**$1.39**	**$1.70**	**$1.82**
DPS	**$0.75**	**$0.79**	**$0.85**	**$0.91**	**$0.98**

CFO	**$ 179**	**$ 169**	**$ 188**	**$ 214**	**$ 231**
Utility plant expenditures	(272)	(274)	(275)	(285)	(285)
Other	(1)	(2)	(2)	(2)	(2)
CFI	**(273)**	**(276)**	**(277)**	**(287)**	**(287)**
Issuance of common stock	(2)	18	96	80	86
Issuance of debt	73	103	28	32	32
Dividends	(36)	(38)	(41)	(44)	(47)
Other	11	20	20	20	20
CFF	**47**	**103**	**103**	**88**	**91**
Change in cash and cash equivalents	(48)	(4)	13	15	35

Net utility plant	2,233	2,406	2,583	2,761	2,932
Cash and cash equivalents	47	43	62	77	112
Other current assets	142	142	142	142	142
Total current assets	189	184	204	219	253
Regulatory assets	354	433	433	433	433
Goodwill	3	3	3	3	3
Other assets	60	85	85	85	85
Total assets	**$ 2,838**	**$ 3,111**	**$ 3,307**	**$ 3,501**	**$ 3,707**
Total common stockholders' equity	$ 730	$ 780	$ 807	$ 850	$ 899
Long-term debt, less current maturities	710	787	814	847	879
Total capitalization	**1,440**	**1,567**	**1,622**	**1,697**	**1,778**
Total current liabilities	321	359	479	578	682
Deferred income taxes	213	223	223	223	223
Pension and postretirement benefits ot	194	259	259	259	259
Other long-term liabilities	257	270	270	270	270
Advances for construction	186	191	191	191	191
Contributions in aid of construction	225	242	262	282	302
Total capitalization and liabilities	**$ 2,838**	**$ 3,111**	**$ 3,307**	**$ 3,501**	**$ 3,707**

Seaport Global

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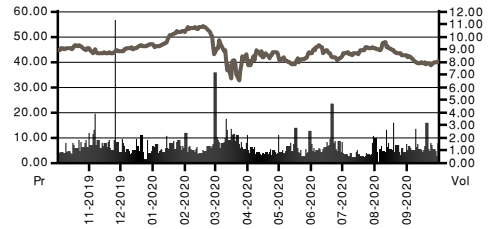
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$40.83**
Float:	244.6MM
Diluted Shares:	254.4MM
Short Interest:	13.1MM
Average Daily Volume:	1,290k
52 Week Range:	$30.40 - $54.52
Market Cap:	**$10,389MM**
Cash and Investments:	$5MM
Debt:	$5MM
Enterprise Value:	$10,389MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
FY	$1.47A	$1.56	$1.58E	$1.66	$1.66E	$1.77	$1.78E
P/E	**27.7x**		**25.9x**		**24.6x**		**22.9x**
Dividends Per Share							
FY	$0.907A	$0.970	$0.970E	$1.038	$1.038E	$1.111	$1.111E
Dividend Yield	**2.2%**		**2.4%**		**2.5%**		**2.7%**

Essential Utilities, Inc.

(NYSE: WTRG)

Gas-related discount seemed likely, but it came sooner and larger than expected

Summary:

We were always skeptical about WTRG's pursuit of a gas LDC, even a fast-growing one, as we worried it would diminish the scarcity value of WTRG's water utility business. Yet, we didn't anticipate the sharp de-rating of gas LDC stocks we saw YTD on concerns over their carbon footprint and electrification of house heating. We don't expect WTRG's ~9% annual gas rate base growth in PA to moderate any time soon, and WTRG's water muni deal pipeline is the strongest in the company's history. We remain on the sidelines as we await a court ruling of the DELCORA acquisition in early November, but find WTRG's value proposition compelling.

Highlights

COVID and hot/dry summer: According to NOAA, cooling degree days in Philly were up 27% vs. normal and while the precipitation levels were just slightly below normal, those drying lawns were likely an eyesore for Aqua PA's residential customers working from home. Therefore, we'd expect residential sales volumes to be up sharply vs. management's assumptions. Granted that lower C&I volumes should moderate the earnings impact, but we'd expect very strong prints from WTRG (and AWK) in 3Q20, even with changes in the quarterly distribution in gas earnings, especially with incremental regulatory deferrals of COVID-related expenses.

De-rating of gas LDCs: To us, the March 2020 addition of Peoples Gas LDC to WTRG's core water utility business diminished the scarcity value of the pure-play water utility which used to trade on par with AWK on FY3 EPS. Following the acquisition, WTRG's annual EPS growth picked up by 150-200 bps vs. our prior water-only expectations, but the stock now trades at a 29% 2022 P/E discount to AWK. In 3Q20, WTRG's stock closely tracked that of ATO, a fast-growing gas LDC from the South, with both stocks sharply underperforming XLU by 900 bps and 850 bps, respectively. We continue to project a ~9% annual rate base growth for WTRG's Peoples in PA and ATO in TX, but investors increasingly question the longevity of this infrastructure replacement cycle given the growing push to decarbonize house heating in Europe. Ongoing gas pipe replacement should continue to reduce methane leaks and blending of RNG should lower the carbon footprint of gas LDCs without any detriment to their earnings growth over the next decade if not longer, we believe, as electric heat pumps gain on popularity. Even if hydrogen becomes a commercially viable option in 2030+, gas distribution systems will likely be retrofitted to accommodate this highly flammable, low density gas. In other words, we don't expect the rate base growth of gas LDCs to slow down any time soon.

Municipal wastewater M&A and equity funding: With the recent wastewater system acquisition in Makefield, PA, WTRG has $359MM in pending muni deals in the state, the largest backlog we can recall in Aqua's/WTRG's history. The backlog includes the DELCORA wastewater acquisition ($276.5MM) which continues to face legal challenges, but WTRG's management feels comfortable with its ability to close the transaction in late March/April 2021, following a delayed PA PUC review, and even issued ~$300MM in equity forwards, half of which should finance the DELCORA transaction. WTRG/Aqua PA insists that they have a legally binding asset purchase agreement (APA) for the wastewater system, but courts should rule on the APA validity only November 4-5. The DELCORA transaction should be additive to WTRG's water earnings only in 2022 following Aqua PA's rate case to be filed next year.

Estimates and valuation: We raised our 2020 EPS estimate by $0.02 to $1.58 to reflect very favorable weather in PA during 3Q20 and no COVID-related EPS drag. We raised our 2022 EPS by another $0.01 to $1.78 to reflect a partial earnings impact related to the DELCORA acquisition diluted by a higher share count. WTRG is now the cheapest water utility under our coverage though not if we account for ongoing de-rating of gas LDCs, even those with premium rate base growth such as ATO. We are admittedly attracted to WTRG at this level, but stay on the sidelines as we await court's decision on the DELCORA APA in early November.

Company Description:
WTRG owns and operates water utilities (1 million accounts) and gas utilities (0.74 million accounts) in 10 states though mainly PA.

WTRG: EPS breakdown by segment ($)

WTRG	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated water utilities	1.47	1.10	1.17	1.26	
Regulated gas utilities	0.00	0.54	0.61	0.69	
Parent	0.00	-0.06	-0.13	-0.16	
Total EPS	**1.47**	**1.58**	**1.66**	**1.78**	**6.7%**
DPS	**0.91**	**0.97**	**1.04**	**1.11**	**7.0%**
Dividend payout	62%	62%	63%	62%	

Source: Company data for 2019; Seaport Global Securities

WTRG	2018A	2019A	2020E	2021E	2022E
Operational EBITDA	470	505	874	923	1,000
Operational EBIT	323	349	610	645	706
Net interest expense	99	100	201	209	227
Ordinary Profit Before Tax	252	269	436	463	506
Income tax	1	7	35	37	40
Net profit	251	262	402	426	466
S/O (m)	178	178	255	257	261
Diluted EPS	**1.41**	**1.47**	**1.58**	**1.66**	**1.78**
DPS	**0.85**	**0.91**	**0.97**	**1.04**	**1.11**
Cash	4	1,869	5	5	5
Receivables	101	108	110	113	120
Inventory	16	18	30	30	30
Other short-term assets	26	18	18	18	18
Other-long term assets	887	1,003	3,810	3,810	3,810
Property, plant, and equipment	5,930	6,346	8,962	9,113	9,249
Total assets	**6,965**	**9,362**	**12,935**	**13,090**	**13,232**
Financial liabilities	117	117	496	496	496
Operating liabilities	63	67	109	109	109
Other liabilities	108	108	220	220	220
Deferred credits	2,068	2,057	2,758	2,757	2,757
Long-term debt	2,398	2,943	4,750	5,347	5,659
Shareholders' equity	2,210	4,070	4,602	4,160	3,991
Total liabilities and equity	**6,965**	**9,362**	**12,935**	**13,090**	**13,232**
Net income	251	262	402	426	466
D&A, goodwill amortisation	147	156	264	279	294
Other non cash elements	-54	-40	-6	-6	-6
Funds from operations	344	379	659	698	753
Non-cash working capital	25	-40	43	0	-1
CFO	**369**	**339**	**702**	**698**	**752**
Net investments in fixed assets	-641	-610	-6,555	-1,032	-780
Net investments in financial assets	2	6	0	0	0
Free cash flow before dividends	**-271**	**-266**	**-5,853**	**-334**	**-28**
Dividends paid	-151	-161	-242	-266	-290
Free cash flow after dividends	-422	-427	-6,095	-600	-317
Changes in equity	2	1,935	302	2	3
Changes in financial debt	421	386	3,928	597	313
Adjustment for minorities / miscellaneous	-2	-28	1	1	1
Increase in cash	-1	1,866	-1,864	0	0

Utilities Disclosures

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Other Companies Mentioned in This Report

- American Water Works Company, Inc. (AWK: $148.57, Buy)
- California Water Services Group (CWT: $44.64, Neutral)
- NextEra Energy, Inc. (NEE: $282.76, Buy)
- SJW Group (SJW: $61.60, Neutral)
- American States Water Company (AWR: $76.10, Buy)
- Essential Utilities, Inc. (WTRG: $40.83, Neutral)
- Middlesex Water Co. (MSEX: $63.42)
- Atmos Energy Corp. (ATO: $95.47, Buy)

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Sell - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.
NA - A rating is not assigned.

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Accumulate - The investment outlook and risk/reward over the following 12 months are favorable on an absolute basis and relative to the peer group.
Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.
Reduce - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.
Sell - The investment outlook and risk/reward over the following 12 months are very unfavorable on an absolute basis and relative to the peer group.
NA - A rating is not assigned.

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	Research Coverage		Investment Banking Clients*		
Rating	Count	% of Total	Count	% of Total	% of Rating Category
Buy	76	61.8%	2	66.7%	2.6%
Neutral	42	34.1%	0	0.0%	0.0%
Sell	5	4.1%	1	33.3%	20.0%
Total	123	100.0%	3	100.0%	2.4%

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October 21, 2020
Industry Update
Utilities
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Utilities

Utilities/Power: Investor sentiment

Summary:
We summarized key investor arguments for electric/gas utility and power stocks with the most positive (AES, ES, ETR, EXC, FE, NEE, NRG), most negative (AGR, ATO, SRE, WTRG) and the tug-of-war sentiment (DTE, DUK, EIX, PPL, SO and VST) ahead of the 3Q20 earnings season and the annual EEI financial conference.

Highlights

Names with most positive investors' sentiment (in alphabetical order):

AES (AES, Buy, PT $21):
- Green wave - more renewable power/storage PPAs + incremental coal plant retirements/divestitures;
- Growth in regulated utility capex/earnings in IN/OH;
- IG rating from S&P as soon as early November.

Entergy (ETR, Buy, PT $113):
- Visible/above-average rate base growth;
- Improving capex execution and regulatory relationships;
- Truly discounted valuation and low customer bills even after securitization of growing storm costs.

Eversource (ES, Buy, PT $99):
- 3Q20 miss + likely delay of the South Fork offshore wind project + likely regulatory fine in CT following storm Isaias.
- Yet, annual EPS growth should rise to 7% for 2021-2023 thanks to Columbia Gas.
- ~10% annual EPS growth in 2024/2025 thanks to offshore wind.

Exelon (EXC, Buy, PT $45):
- Spin-off of ExGen/Constellation seems unlikely any time soon.
- Yet, Biden's wind/Blue sweap could lead to carbon pricing which would be highly beneficial for merchant nuclear plants;
- Current valuation doesn't reflect much value for ExGen.

FirstEnergy (FE, Buy, PT $42):
- Update on the DOJ investigation of lobbying practices surrounding the HB 6 in OH - a potential settlement without admission of any wrongdoing? The first update from CEO since 2Q20 call.
- Continued strong operational performance;
- Current valuation reflects unraveling of regulatory setup in OH (ESP settlement and changes to overearning/SEED test) which are seen as increasingly unlikely;
- A likely M&A target once the DOJ risk is addressed.

NextEra Energy (NEE, Buy, PT $324):
- Accelerating renewable power spending seems largely independent of November election results;
- Marginal investor in US utilities has an ESG mandate so NEE should continue to outperform XLU;
- Biden's win/Blue sweep would be additive to growth of NEER;
- NEE needs to watch its earnings mix for credit reasons - a large regulated utility acquisition could grow in importance after the Democratic sweep.

NRG Energy (NRG, Buy, PT $48):
- Proposed sale of PJM plants and incremental cost efficiencies at NRG could eliminate $750MM in converts to finance Direct Energy;
- PJM coal plant divestitures should boost NRG's ESG profile;
- 20%+ 2022 FCF yield with fewer questions about the longevity of cash flows.

Names with most negative investors' sentiment (in alphabetical order):

Atmos Energy (ATO, Buy, PT $108):
- Marginal equity investor for US utilities is an ESG investor, and he's not interested in gas LDCs, even those in gas supportive states (like TX or PA);
- ATO's P/E premium is measured vs. P/Es of other gas LDCs and not all electric/gas utilities; as other gas LDCs derate so does ATO.

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- ATO's upcoming addition to the DJUA could boost the stock.

Avangrid (AGR, Neutral, PT N/A):
- Stock sharply re-rated thanks to renewable power halo effect even though AGR's Renewables business struggles;
- Analyst day (Nov 5) should (yet again) re-set earnings expectations:
  - Whisper buy-side expectations for 2022 EPS of $2.45 are already meaningfully below sell-side consensus expectations, however, though the $1.95 midpoint of the new 2020 EPS guidance was lower than the $2.10 whisper number.
- Potential combination with PPL/WPD could still be possible, and could be decided by Iberdrola, AGR's majority owner, in December/ January.

Essential Utilities (WTRG, Neutral, PT N/A):
- Peoples Gas should increasingly suppress WTRG's P/E multiple as ESG investors stay away from gas LDCs;
- WTRG may need to spin off the gas LDC to rebuild its water P/E, or be taken over by an electric/gas utility.

Sempra Energy (SRE, Buy, PT $144):
- Expansion of Cameron or construction of ECA/Port Arthur LNG facilities now very unlikely;
- Monetization of a portion of Cameron LNG terminal should be difficult following lengthy storm-related outages (no backup power);
- Lack of extension of franchise agreement with San Diego would be a major negative leaving SRE with a gas LDC in CA, with limited long-term growth prospects;
- Share buyback is not being executed, and it's announcement on the 2Q20 earnings call is seen by many as an attempt to boost the stock price ahead of a potential regulated utility acquisition in TX. Yet, the company could still reiterate their willingness to support the stock with buybacks.

Tug of war names (in alphabetical order):

DTE Energy (DTE, Buy, PT $133.50):
- Management seems focused on correcting its stock's valuation discount.
- Yet, a spin-off of midstream assets might not create much (if any) shareholder value: a smid-cap midstream stock (~$3-3.5B in market cap) with a major technical overhang (as utility investors will want out) should not trade well.
- Instead, DTE could try to dilutive its midstream exposure through an acquisition of a regulated utility, preferably an electric utility with a contiguous service territory. CMS seems like an unlikely seller so it would have to be outside of MI.

Duke Energy (DUK, Neutral, PT N/A):
- NEE-DUK combination could create very meaningful shareholder value for both companies, and many LO investors continue to expect the combination to eventually happen; A lot depends on the outcome of the November elections.
- A blue sweep in D.C. could make the combination even more likely as NEE should need to address its earnings mix with a likely re-acceleration of its renewable power growth.
- A blue sweep in NC could boost DUK's standalone value and its appeal to NEE.
- The regulatory approval of the combination should be challenging. Investors believe the transaction is being blocked by DUK's Board/management only partly due to regulatory concerns.

Edison International (EIX, Buy, PT $62) and PG&E (PCG, Neutral, PT N/A):
- Recent rebound in stocks of EIX/PCG is seen as driven by a value trade rather than any fundamental reasons,
- Yet, we are getting close to the beginning of a seasonal trade in CA electric utilities.
- The Victims Trust doesn't seem to be shedding PCG's stock. And EIX could be announcing additional settlements of 20172018 wildfires.
- Yet, both stocks need to issue equity as soon as December/January.

PPL (PPL, Neutral, PT N/A):
- The sale of WPD is still months away and 2020 results from the business should disappoint due to COVID.
- Recent CMA rulings on ROEs/capex of UK water utilities are seen as positive for WPD's future earnings power and thus its sale price.
- Yet, WPD's sale would create meaningful shareholder value only if it's sold at north of 1.45x 2021 EV/RAB and PPL manages to eliminate practically all tax leakage.
- It's still possible, especially if Iberdrola were to agree to a swap between WPD and a majority stake in AGR. Yet, it remains unclear if Iberdrola is open to it, and the outcome of the US elections could determine the value of AGR.

Southern Company (SO, Buy, PT $66):
- Cold hydro testing is done and hot functional testing could start as soon as mid/late-November.
- Yet, the duration of the HFT is unknown and no one knows what SO's Georgia Power should uncover once the reactor (Vogtle Unit 3) is pressurized and the stream generator is turned on.

Vistra Energy (VST, Buy, PT $24):

- The stock looks cheap on practically every metric and buybacks should start in early 2021.
- Yet, VST's merchant renewable power/storage investments in TX conflict with VST's bullish views on fwd power prices in the state.
- Investors would prefer more buybacks or an investment in a renewable power developer (like AES's acquisition of sPower). Otherwise, terminal value questions should continue to weigh on the stock.

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Other Companies Mentioned in This Report

- AES Corporation (AES: $20.00, Buy)
- Atmos Energy Corp. (ATO: $94.28, Buy)
- Duke Energy Corp. (DUK: $92.06, Neutral)
- Eversource Energy (ES: $92.24, Buy)
- FirstEnergy Corp. (FE: $31.83, Buy)
- NRG Energy, Inc. (NRG: $33.18, Buy)
- PPL Corporation (PPL: $28.07, Neutral)
- Sempra Energy (SRE: $129.68, Buy)
- Essential Utilities, Inc. (WTRG: $42.10, Neutral)
- Avangrid, Inc. (AGR: $54.06, Neutral)
- DTE Energy Company (DTE: $121.34, Buy)
- Edison International (EIX: $59.75, Buy)
- Exelon Corporation (EXC: $42.40, Buy)
- NextEra Energy, Inc. (NEE: $300.99, Buy)
- PG&E Corporation (PCG: $10.92, Neutral)
- Southern Co. (SO: $58.60, Buy)
- Vistra Energy Corp. (VST: $18.95, Buy)
- Entergy Corporation (ETR: $106.22, Buy)

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Ratings Distribution

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Buy	102	61.1%	1	100.0%	1.0%
Neutral	62	37.1%	0	0.0%	0.0%
Sell	3	1.8%	0	0.0%	0.0%
Total	167	100.0%	1	100.0%	0.6%

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October 23, 2020
Industry Update
Utilities
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Utilities

Utilities/Power/Yieldcos/Water - What we've learned this week

Summary:
AEP's results and comments on the OH political risk bode well for FE. We'd expect solid EEI updates from both, and we're raising our PT for AEP ahead of them. AES's settlement in OH is more impressive than the grid modernization capex would indicate. AGR's proposed acquisition of PNM caught us by surprise, and why the EPS accretion math should work, the addition of NM to AGR's already challenging regulatory jurisdictions surprised us. The deal coupled with commentary from IBE's holders do not bode well for PPL's pending sale of WPD (RAB multiples and a tax shield) though the stock seems to already reflect that. NEE's renewable power growth keeps accelerating and with that the company's need to add regulated utilities. The NEE-DUK deal could look even better after the elections so it's too early to give up on it. SO's updated schedule for its new Vogtle nuke is a bit longer than we had hoped for, but way better than the bear case. And lastly, smid-cap water utilities are getting a technical boost (i.e., AWR, CWT, SJW, WTRG). They do seem undervalued based on fundamentals, but the recent/ongoing move is more about quant screens. Also note that we've updated our models for AEP, NEE, and NEP with this update.

Highlights

AEP (Buy, PT $99 up from $96) and FE (Buy, PT $42) – More regulated renewables at EEI + shedding of OH overhang which bodes well for FE

- There were few surprises from AEP's 3Q20 print, but management plans to comment on AEP's rate based renewable power investments (incremental to the $2B North Central Wind) during the upcoming EEI conference. It sounds like the company plans to pursue renewable power capex in VA and IN, and besides ESG benefits, it should get AEP's EPS CAGR closer to 7% from the current 6.5%, we estimate.
- AEP seems to have shed most of the overhang related to the HB 6 in OH, and investors seem increasingly hopeful that FE will act the same way. FE delayed its 3Q20 print until Nov 2, the day before the elections with the latter being increasingly seen as a particularly sensitive event in OH.
- We updated our model and our annual estimates for AEP remain unchanged, but we raised our PT to $99 from $96 on lower risks in OH. No changes to our estimates/PT for FE as we await management's EEI update.

AES (Buy, PT $21) – Capex boost in OH is small, but lots of positives from PUCO settlement; regulated capex updates from IPL on 3Q20 call

- DP&L, AES's OH regulated utility, just settled with state utility regulators (PUCO) on grid modernization capex, among others. The utility can now invest $249MM over the next four years which is small, but that's just a part of DP&L capex program which includes FERC transmission investments. Also, through the settlement DP&L confirmed its ability to continue to collect $80MM annually under the rate stabilization charge (RSC) and resolved three overearning (SEET) tests. The utility also plans to file another rate case. We expect an update on AES's regulated generation capex in IN (for IPL) on the 3Q20 call.
- No changes to estimates or PT for AES.

AGR (Neutral, PT N/A) and PPL (Neutral, PT N/A) – PNM merger and WPD's valuation

- The PNM acquisition came as a surprise to investors even though everybody seemed aware of IBE's (and thus AGR's) plans to grow its regulated utility presence in the US. A change to the NM utility commission is on the ballot on November 3 – if approved, PNM/AGR could be regulated by three new Commissioners appointed by the Legislature instead of the current five elected Commissioners. That could be an improvement starting Jan 1, 2023, yet the question remains how this potential change should impact the conduct of the current Commissioners over the next 26 months. They will be reviewing the AGR-PNM merger while trying to secure a job on the new downsized Commission. That could mean a longer-than-expected approval process for the deal, investors believe.
- We had openly hoped for a combination of AGR and PPL given IBE's past interest in WPD, PPL's UK distribution networks. Yet, we are hearing from IBE shareholders that the Spanish renewable power major thought the WPD deal would have been too big for them and would have detracted from IBE's renewable power focus. That's bad news for WPD's likely valuation, we believe, as consortiums of financial investors (infra funds) now seem like the most likely buyers of PPL's UK business, and the 1.5x+ EV/RAB seems increasingly unlikely. Then there is the potential Biden win in November and a likely change in the federal tax law which would follow. That in turn could impact the tax leakage associated with the WPD sale. Investors believe that WPD needs to sell above 1.35x 2021 EV/RAB and eliminate practically any tax leakage to create any meaningful shareholder value for PPL at the stock's current share price. And that still seems realistic to us.
- No changes to our recently-updated estimates for AGR. No changes to PPL.

NEE (Buy, PT $324) – 15GW renewable backlog, but regulated utility M&A dominates investor minds

- NEER keeps adding new storage/wind/solar contracts, and the accelerating growth in those unregulated contract-based operations continue to fuel questions on regulated utility M&A. Stand-alone ITCs for storage projects on the back of Biden's wind could lead to retrofits of NEER's existing wind farms thus further boosting the NEER growth. Management emphasizes no pre-set earnings mix or credit concerns, but depending on the outcome of November elections (both federal and state), the NEE-DUK merger rationale could get another boost. As we mentioned in our recent note, investors are increasingly optimistic on this eventual combination.
- We updated our model for NEE and our annual estimates and PT for NEE (and DUK) remain unchanged as we await the eventual outcome of November elections.

NEP (Buy, PT $70) – 15% YoY growth in 4Q20 distributions/share

- The 3Q20 wind (96% of normal) and solar power generation dropped YoY which was in line with our below-consensus expectations for NEP and other yieldcos. Yet, NEP delivered on a 15% YoY growth in unit distributions per share and its ~70% payout ratio leaves plenty of room to continue the ~15% annual growth in distributions through 2022 without any additional outside project acquisitions. It also helps that NEP pursues organic growth through the repowering a of a 125MW wind project in CO or an addition of backup compression capacity at the Agua Dulce gas compressor station, both just completed ahead of schedule and on budget. The repowering of the 100MW Baldwin wind farm in ND should be complete by the year-end.
- We marginally increased our 2020/2021 EBITDA estimates for NEP following the 3Q20 print to $1,263M/$1,291MM up from $1,260MM/$1,289MM, respectively. Our PT remains unchanged.

SO (Buy, PT $66) – Pressurization of Vogtle Unit 3 and operations of its steam generator will start only in January 2021, a month later than hoped

- SO provided a construction update on Vogtle Unit 3. The cold hydro testing (CHT) is done, but hot functional testing (HFT) which involves the pressurization of the nuclear reactor and first-time operations of the steam generator won't start until January 2021. That's later than we had hoped for – we had expected a 1-2 month gap between the end of CHT and the beginning of HFT thus implying a start of HFT by mid-December at the latest. The duration of HFT testing remains unclear though, for now, SO/Georgia Power expect the nuclear fuel load in April 2021. The end of HFT is widely seen as the main de-risking event for the Vogtle nuclear project so the wait continues.
- No changes to our estimates or PT for SO.

Water utilities (AWR/CWT/SJW/WTRG) - Technical trade boosting the group, especially smid caps

- We keep hearing from generalist investors that their equity strategists/internal quant screens predict a rally in stocks of US water utilities. We rarely pay attention to those comments unless they come from a couple unrelated sources and we see the recent consistent outperformance of these names which doesn't seem driven by fundamentals. We like the group based on fundamentals, even with the recent change to water revenue decoupling in CA.
- No changes in estimates or PTs for the water utilities under our coverage.

Utilities Disclosures

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Other Companies Mentioned in This Report

- American Electric Power Company, Inc. (AEP: $91.95, Buy)
- NextEra Energy, Inc. (NEE: $303.35, Buy)
- PPL Corporation (PPL: $28.51, Neutral)
- Duke Energy Corp. (DUK: $93.07, Neutral)
- PNM Resources, Inc. (PNM: $49.97)
- American States Water Company (AWR: $79.27, Buy)
- SJW Group (SJW: $64.50, Neutral)
- Avangrid, Inc. (AGR: $49.84, Neutral)
- NextEra Energy Partners LP (NEP: $64.86, Buy)
- Southern Co. (SO: $61.08, Buy)
- FirstEnergy Corp. (FE: $33.08, Buy)
- AES Corporation (AES: $20.49, Buy)
- California Water Services Group (CWT: $47.96, Neutral)
- Essential Utilities, Inc. (WTRG: $44.29, Neutral)

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Neutral	62	37.1%	0	0.0%	0.0%
Sell	3	1.8%	0	0.0%	0.0%
Total	167	100.0%	1	100.0%	0.6%

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Note: Ratings Distribution as of September 30, 2020

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November 16, 2020
Industry Update
Utilities
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Utilities

Water Utilities: Updated thoughts following 3Q20 prints/EEI meetings

Summary:
We continue to like water utilities in the US, especially given the recently gained earnings visibility for Buy-rated AWK in NJ and CWT in CA. AWK's large balance sheet makes it best-positioned to benefit from acquisitions of municipally- and privately-owned water and wastewater systems while the company keeps collecting additional water/wastewater service contracts for military bases. Buy-rated AWR has been less lucky in those military contract solicitations though two more of the contracts should be awarded still this year. Worse yet, the work under AWR's existing military contracts has been delayed due to COVID. The re-rating of CWT's stock on the back of its general rate case decision in CA came earlier than we hoped and the stock now looks (almost) fairly valued to us. SJW's 2021 guidance, if any, could disappoint due to the potential impact of La Nina on SJW's surface water production volumes in CA and some uncertainty related to the upcoming rate case in CT. WTRG pushes back against the discounted valuation of its gas LDC given its strong growth prospects, which we don't dispute, though we look toward the proposed DELCORA wastewater system acquisition in PA to change WTRG's earnings mix more toward water.
We continue to chase AWK hence we increased our PT to $175 from $152. We tweaked earnings estimates for AWK/AWR/CWT/SJW.

Highlights

AWK (Buy, PT $175 up from $152): A large balance sheet and a strong ESG profile increasingly matter among regulated water utilities in the US especially as acquisitions of municipally- and privately-owned water and wastewater systems continue to gain momentum. We reiterate our Buy rating on AWK, marginally raise estimates, and (again) increase our PT to $175 from $152 as we continue to chase the stock.

AWR (Buy, PT $83 unchanged): We were surprised by ongoing COVID-related delays of work under AWR's military water/wastewater contracts. Worse yet, AWK rather than AWR has been awarded the latest (and the largest) military contract though we await updates on two more contract awards over the next 45 days. We can live with eventual changes to AWR's full water revenue decoupling in CA as long as the company secures additional military contracts. We stick to our Buy rating and $83 PT.

CWT (Neutral, PT N/A): We delayed any rating changes on CWT until after its 3Q20 earnings print, in anticipation of yet another big earnings miss vs. consensus given the lack of a final decision in CWT's general rate case in CA. Yet, management decided to book an earnings catch up related to the rate case already in 3Q20 based on a Proposed Decision and comments on it from the CPUC consumer advocate. The stock jumped ~14% during a week following its earnings print vs. ~4% for XLU and ~5% for smid cap water names. Now, CWT trades at just a 4% 2022 P/E discount to an average regulated water utility in the US which seems almost fair to us. Therefore, we stick to our Neutral rating.

SJW (Neutral, PT N/A): San Jose Water's Monterey-style WRAM benefited SJW's earnings thanks to favorable weather and a COVID-related uptick in residential sales, though the earnings uplift was a bit lower than we had hoped. We remain concerned about the potential impact of the ongoing La Nina and the uncertainty surrounding the upcoming rate case in CT on SJW's 2021 guidance, if the company even decides to issue one in early 2021. Therefore, we remain on the sidelines on SJW even though the stock trades at a 15% 2022 P/E to an average regulated water utility.

WTRG (Neutral, PT N/A): While we share WTRG's rate base/earnings growth expectations for its gas LDC, we look to the pending acquisition of the DELCORA wastewater system in PA as a way to boost WTRG's earnings mix more towards water. We remain on the sidelines until we get more legal/regulatory clarity on this large wastewater system acquisition.

Seaport Global

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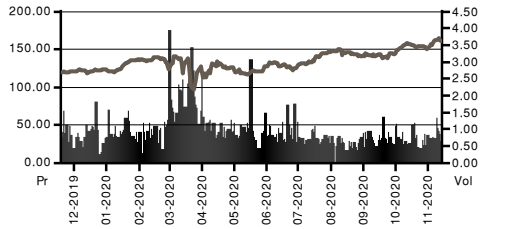
Rating:	**Buy**
Price Target:	**$175.00**

Price Target Metrics:
2022 SOTP valuation implying 38x 2022 EPS

Current Price:	**$161.31**
Float:	180.7MM
Diluted Shares:	181.0MM
Short Interest:	1.5MM
Average Daily Volume:	768k
52 Week Range:	$92.00 - $172.56
Market Cap:	**$29,197MM**
Cash and Investments:	$569MM
Debt:	$9,593MM
Enterprise Value:	$38,221MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Adjusted)							
FY	$3.61A	$3.85	$3.87E	$4.23	$4.25E	$4.59	$4.60E
P/E	**44.6x**		**41.7x**		**37.9x**		**35.1x**
Dividends Per Share							
FY	$1.955A	$2.150	$2.150E	$2.365	$2.365E	$2.600	$2.600E
Dividend Yield	**1.2%**		**1.3%**		**1.5%**		**1.6%**

American Water Works Company, Inc.

(NYSE: AWK)

Size & pure-play profile increasingly matter in US water sector; raising PT

Summary:
A large balance sheet and a strong ESG profile increasingly matter among regulated water utilities in the US especially as acquisitions of municipally- and privately-owned water and wastewater systems continue to gain momentum. We reiterate our Buy rating on AWK, marginally raise estimates, and (again) increase our PT to $175 from $152 as we continue to chase the stock.
We met with AWK's management during the annual EEI conference.

Highlights

NJ rate case: The NJ BPU approved AWK's general rate case settlement in the state and in general, the order seemed constructive. AWK received a $39MM increase in annual revenues (vs. $87.7MM requested) starting Nov 1, 2020, based on a rate base of $3.57B (down $69MM from the requested level), an allowed ROE of 9.6% (vs. 10.5% requested, but flat vs. the previous ROE) and an equity ratio of 54.6% (marginally up from 54% previously). The settlement and thus the final order didn't include acquisition adjustments related to the goodwill paid in Shorelands/Haddonfield/ Roxbury transactions or a revenue stabilization mechanism (aka revenue decoupling). We expect NJ AWK to ask for decoupling in the next rate case, while the acquisition adjustments for avoided capex related to privately-owned water/wastewater systems should be decided by the BPU within the next 2-3 months. The Board previously found that an acquisition adjustment is appropriate only when a utility can demonstrate specific benefits to its incumbent customers (rather than just for the system being acquired) stemming from the proposed acquisition or when the system being acquired is distressed. AWK believes the acquisition premium should be recoverable because the three transactions should result in avoided capital spending over the next 5-10 which should be in excess of that the premium over the book value that AWK paid. For now, the $31MM is not included in AWK's rate base and while it's very small vs. AWK's $14.6B total rate base, the BPU ruling in these acquisition adjustment cases could have very meaningful implications for any future larger acquisitions of investor-owned water utilities in NJ, we believe.

NY asset sale: Management still hopes to close its pending sale of NY operations to Liberty Utilities in early 2021 despite delays from the NY PSC to allow for municipalization plans being filed in Long Island and now proposed legislative initiatives. Gov. Cuomo recently proposed a new bill which, among others, would "expedite and clarify the process of utility franchise revocation for recurring failures" and require the NY PSC to study "whether private water suppliers like American Water on Long Island should come under municipal control". The new legislation would require the NY PSC to issue a report on the potential municipalization of the Long Island water utilities by April 2021, but AWK hopeful the regulatory review of the Liberty Utilities deal could be concurrent with PSC's work on this report.

Military contracts: AWK awaits two more military water/wastewater contracts awards this year – the last three contracts were awarded exclusively to AWK though for now we assume the next two contracts should be split between AWK and AWR. Management reminded us that back in 2000, AWK faced 10 competitors in military water/wastewater contract solicitations, but AWR is now the only credible competitor. AWK won't provide any disclosures on the profitability of this segment of its market-based businesses, partly because that would allow us to back into profit margins for the highly competitive

homeowners' services business, but we see these 50-year inflation-adjusted contracts as even more lucrative than any of AWK's regulated utility franchises.

Changes to estimates and PT: AWK raised its 2020 GAAP EPS guidance to $3.87-3.93 up from $3.79-3.89. The guidance includes a $0.05 EPS net hit related to COVID and a summer weather benefit ($0.10) as well as a $0.06 lower depreciation expense related to the NY system held for sale. The $0.06 benefit was not included in the original adjusted EPS guidance range and is excluded from our estimates. Still, given the strong 3Q20 print, we raised our 2020 adjusted EPS estimate to $3.87 up from $3.85. We marginally increased our 2021/2022 EPS estimates to reflect the recently awarded military contract which was much larger than expected. Our new 2021/2022 EPS estimates are $4.25/4.60 up from $4.23/4.59. We continue to chase the stock even though the P/E multiple is increasingly hard for us to defend. Our new PT of $175 (up from $152) implies a 38x 2022 P/E multiple.

Company Description:
AWK is the largest publicly-traded regulated water and wastewater utility in the US with operations in 16 states, primarily in the Northeast and the Midwest, serving 3.4 million customer accounts. AWK also engages in unregulated contract-based water/wastewater services for military bases (17 bases) and provides water/wastewater line warranty services (homeowner services) to ~1.5 million residential accounts.

AWK: EPS estimates by segment ($)

AWK	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated utilities	3.60	3.94	4.34	4.68	9.1%
Unregulated ops	0.45	0.49	0.52	0.56	7.6%
Parent	-0.44	-0.56	-0.61	-0.64	13.3%
Total EPS	**3.61**	**3.87**	**4.25**	**4.60**	**8.4%**
DPS	**1.96**	**2.15**	**2.37**	**2.60**	**10.0%**
Dividend payout	54%	56%	56%	57%	

Source: Company data for 2019; Seaport Global Securities

AWK: 2022 SOTP valuation ($)

AWK - 2022 SOTP	EPS	Multiple	Value per share
Regulated utilities less parent	4.04	39.0x	157.56
Military contracts	0.19	50.0x	9.50
Homeowner services	0.37	23.0x	8.51
Total per share			**175.57**

Source: Seaport Global Securities

AWK	2019A	2020E	2021E	2022E
Sales	3,610	3,780	4,025	4,233
Operating expenses	1,824	1,881	1,927	1,977
EBITDA	1,786	1,899	2,098	2,257
Depreciation	582	615	670	714
EBIT	1,204	1,284	1,428	1,543
Net interest expense	382	399	442	460
Ordinary Profit Before Tax	872	935	1,036	1,133
Income tax	218	234	259	283
Net profit	654	701	777	850
S/O (m)	181	181	183	185
Diluted EPS	**3.61**	**3.87**	**4.25**	**4.60**
DPS	**1.96**	**2.15**	**2.37**	**2.60**
Cash	90	45	45	45
Financial and Operating Receivables	294	311	332	349
Inventory	44	44	45	46
Other short-term assets	857	292	292	292
Goodwill	1,501	1,501	1,501	1,501
Other-long term assets	1,664	1,664	1,664	1,664
Property, plant, and equipment	18,232	19,486	20,686	21,843
Total assets	**22,682**	**23,343**	**24,564**	**25,739**
Financial liabilities	814	936	936	936
Operating liabilities	203	194	198	203
Other liabilities	1,028	851	851	851
Deferred credits and other regulatory liabiliti	5,872	6,054	6,256	6,400
Long-term debt	8,639	9,475	9,893	10,400
Shareholders' equity	6,126	5,833	6,430	6,949
Total liabilities and equity	**22,682**	**23,343**	**24,564**	**25,739**
Net income	654	701	777	850
D&A, goodwill amortisation	582	615	670	714
Other non cash elements	214	182	202	221
Funds from operations	1,450	1,499	1,648	1,784
Decrease (increase) in non-cash working ca	-67	-26	-17	-90
CFO	**1,383**	**1,472**	**1,632**	**1,694**
Net investments in fixed assets	-1,841	-1,865	-1,865	-1,865
Net investments in financial assets	-104	-104	-104	-104
Free cash flow before dividends	**-562**	**-497**	**-337**	**-275**
Dividends paid (group + minorities)	-354	-389	-432	-480
Free cash flow after dividends	-916	-886	-769	-755
Increase or (repayment) of capital and subsi	857	886	468	557
Increase or (repayment) of financial debt	-36	-45	301	198
Adjustment for minorities / miscellaneous	27	0	0	0
Increase in cash	-68	-45	0	0

Seaport Global

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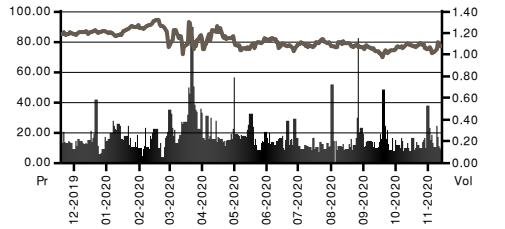
Rating:	**Buy**
Price Target:	**$83.00**

Price Target Metrics:
2022 SOTP valuation which implies 33x '22 EPS

Current Price:	**$77.20**
Float:	36.4MM
Diluted Shares:	37.0MM
Short Interest:	0.9MM
Average Daily Volume:	201k
52 Week Range:	$65.11 - $96.64
Market Cap:	**$2,857MM**
Cash and Investments:	$8MM
Debt:	$440MM
Enterprise Value:	$3,289MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
Q1 (Mar)	$0.35A	$0.38	$0.38A	$0.50	$0.49E	$0.54	$0.53E
Q2 (Jun)	$0.64A	$0.69	$0.68A	$0.64	$0.63E	$0.68	$0.67E
Q3 (Sep)	$0.69A	$0.77	$0.72A	$0.79	$0.77E	$0.84	$0.83E
Q4 (Dec)	$0.55A	$0.48	$0.52E	$0.51	$0.50E	$0.54	$0.53E
FY	$2.24A	$2.33	$2.30E	$2.45	$2.39E	$2.61	$2.56E
P/E	**34.5x**		**33.6x**		**32.3x**		**30.2x**
Dividends Per Share							
FY	$1.160A	$1.280	$1.280E	$1.390	$1.390E	$1.495	$1.495E
Dividend Yield	**1.5%**		**1.7%**		**1.8%**		**1.9%**

American States Water Company
(NYSE: AWR)

COVID continues to impact execution of military contracts; still awaiting new contract awards

Summary:
We were surprised by ongoing COVID-related delays of work under AWR's military water/wastewater contracts. Worse yet, AWK rather than AWR has been awarded the latest (and the largest) military contract though we await updates on two more contract awards over the next 45 days. We can live with eventual changes to AWR's full water revenue decoupling in CA as long as the company secures additional military contracts. We stick to our Buy rating and $83 PT.

Highlights

Military contracts: AWR awaits awards of two military water/wastewater contracts awards over the next 45 days – the last three contracts were awarded exclusively to AWK though for now we assume the next two contracts should be split between AWR and AWK. COVID continues to delay some current work and expansions of scope of some of AWR's current military contracts. As a result, management now expects to earn only $0.46 in 2020 EPS for this segment (ASUS) and for the earnings to stay largely flat YoY in 2021 assuming the COVID pandemic continues.

Modifications to full water decoupling (WRAM) and GSWC's pending rate case: We continue to expect the recent full WRAM changes to affect AWR's/GSWC's earnings only in 2025, if at all. Management insists the company should do just fine even under the new Monterey-style WRAM, and GSWC has a history of earning at least its allowed ROE on the water side. We are still hopeful the Commission could change its mind on the full WRAM, especially that all investor-owned water utilities in CA with the full WRAM have asked for the rehearing of the CPUC decision and, if unsuccessful, seem willing to challenge the decision in courts. The current term of Comm. Guzman-Aceves, the author of the WRAM change, should expire by the end of 2022, i.e. before the filing of GSWC's next general rate case.

Changes to estimates: We lowered our estimates to reflect the weaker earnings for existing military contracts (ASUS) and some uncertainty around new contract awards given that AWK (rather than AWR) has been winning all of the recent awards. Our new 2020/2021/2022 EPS estimates are $2.29/2.39/2.56 down from $2.33/2.45/2.61, respectively.

Company Description:
AWR is the parent of Golden States Water Co. (GSWC), a regulated water (261,000 water connections in 37 systems), Beaver Valley Electric Service (BVESI), an electric utility (24,400 electric connections in one system) in CA, and American States Utility Services (ASUS), which engages in contract-based water and wastewater services primarily for military bases, currently 11 bases.

AWR: EPS breakdown by segment ($)

AWR	2019A	2020E	2021E	2022E	2019-2022 CAGR
Regulated water	1.62	1.65	1.72	1.83	4.2%
Regulated electric	0.15	0.18	0.20	0.21	11.9%
Military contracts/ASUS	0.47	0.46	0.47	0.52	3.4%
Total EPS	**2.24**	**2.29**	**2.39**	**2.56**	**4.6%**
DPS	**1.16**	**1.28**	**1.39**	**1.49**	**8.8%**
Dividend payout	52%	56%	58%	58%	

Source: Company data for 2019; Seaport Global Securities

AWR	2018A	2019A	2020E	2021E	2022E
Total Revenues	437	474	481	497	518
Total Operating Expenses	336	347	351	362	374
EBIT	101	127	130	135	144
Net income	$ 64	$ 83	$ 85	$ 88	$ 95
S/O	37	37	37	37	37
Diluted EPS	**$1.72**	**$2.24**	**$2.29**	**$2.39**	**$2.56**
DPS	**$1.06**	**$1.16**	**$1.28**	**$1.39**	**$1.49**
Net income	64	83	85	88	95
Adjustments to reconcile non-cash charges	40	42	46	48	51
Changes in assets and liabilities	33	(8)	(12)	(12)	(12)
CFO	137	117	119	125	134
Capital expenditures	(127)	(152)	(115)	(145)	(155)
Other	(1)	(1)	-	-	-
CFI	(128)	(153)	(115)	(145)	(155)
Issuance/repurchase of common stock	1	1	1	1	1
Long-term debt issued/repaid	(0)	(40)	30	45	45
Short-term debt issued/repaid	37	110	20	15	20
Dividends paid	(39)	(43)	(47)	(51)	(55)
Other	0	4	4	4	4
CFF	(2)	31	7	13	14
Net change in cash and cash equivalents	2	(6)	11	(8)	(7)
Cash and cash equivalents, end of period	7	1	12	4	(3)
Current assets	$ 131	$ 122	$ 135	$ 129	$ 124
PP&E	1,323	1,447	1,519	1,621	1,729
Regulatory and other assets	47	72	72	72	72
Total assets	1,501	1,641	1,726	1,821	1,925
Current liabilities	147	116	157	157	157
Long-term debt	281	281	311	356	401
Other liabilities (including construction)	516	643	643	643	643
Total liabilities	943	1,040	1,111	1,156	1,201
Total Shareholders' Equity	558	601	614	665	723
Liabilities and Shareholders' Equity	$ 1,501	$ 1,641	$ 1,726	$ 1,821	$ 1,925

Seaport Global

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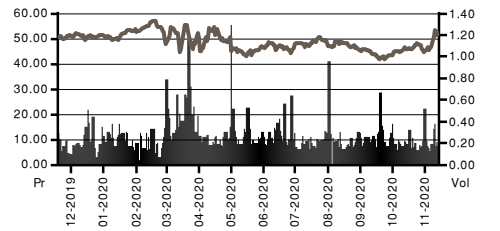
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$52.38**
Float:	49.4MM
Diluted Shares:	49.4MM
Short Interest:	0.8MM
Average Daily Volume:	221k
52 Week Range:	$39.74 - $57.36
Market Cap:	**$2,588MM**
Cash and Investments:	$114MM
Debt:	$1,182MM
Enterprise Value:	$3,655MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
Q1 (Mar)	$(0.16)A	$(0.42)	$(0.42)A	$(0.12)	$(0.12)E	$(0.08)	$(0.08)E
Q2 (Jun)	$0.35A	$0.11	$0.11A	$0.43	$0.42E	$0.53	$0.53E
Q3 (Sep)	$0.88A	$0.78	$1.94A	$0.85	$0.85E	$0.95	$0.95E
Q4 (Dec)	$0.24A	$1.03	$0.24E	$0.54	$0.54E	$0.43	$0.43E
FY	$1.31A	$1.49	$1.87E	$1.70	$1.70E	$1.83	$1.83E
P/E	**39.8x**		**27.9x**		**30.9x**		**28.6x**
Dividends Per Share							
FY	$0.790A	$0.850	$0.850E	$0.909	$0.909E	$0.978	$0.978E
Dividend Yield	**1.5%**		**1.6%**		**1.7%**		**1.9%**

California Water Services Group

(NYSE: CWT)

Re-rating came faster than we expected

Summary:

We delayed any rating changes on CWT until after its 3Q20 earnings print, in anticipation of yet another big earnings miss vs. consensus given the lack of a final decision in CWT's general rate case in CA. Yet, management decided to book an earnings catch up related to the rate case already in 3Q20 based on a Proposed Decision and comments on its from the CPUC consumer advocate. The stock jumped ~14% during a week following its earnings print vs. ~4% for XLU and ~5% for smid cap water names. Now, CWT trades at just a 4% 2022 P/E discount to an average regulated water utility in the US which seems almost fair to us. Therefore, we stick to our Neutral rating.

Highlights

2020 earnings catch up came earlier and was bigger than we expected: CWT booked YTD adjustments to its CA earnings in 3Q20 based on a Proposed Decision (PD) in its pending general rate case (GRC) and comments from the consumer advocate on the PD. We were clearly surprised by this move as CWT's management tends to be very conservative on any regulatory adjustments. The earnings adjustments were meaningfully higher than we had anticipated, even adjusting for the accelerated true up in YTD earnings, and seemed driven by one-time adjustments for the 2017 TCJA-related tax customer refund. This is why our 2021/2022 estimates, which drive our rating, remained unchanged while our 2020 estimates went up sharply.

Change to CWT's full revenue decoupling (WRAM) only in 2023, if at all: In late August, the CPUC removed the full water revenue decoupling (WRAM) for all four investor-owned water utilities in CA which currently use the mechanism, including CWT. The Commission ruled that the WRAM removal should impact "any future general rate case applications filed after the effective date of this decision". The PD agreed with CWT's stance and as a result, CWT's earnings in CA should be impacted only starting 2023 if at all. CWT along with the remaining three investor-owned water utilities in CA have asked for rehearing of the CPUC decision, and if unsuccessful, the utilities seem ready to challenge the decision in courts.

Estimates and valuation: We raised our 2020 estimates (to $1.87 from $1.49) to reflect YTD results and cost deferrals which meaningfully exceeded our expectations. Our 2021-2022 estimates remain unchanged. Following a recent rally, CWT not trades at just a 4% discount to an average regulated water utility which seems almost fair to us. The company has highly underinvested utility assets in CA, but management's conservatism results in volatility in earnings which in effect reduce the rate base growth appeal of CWT. Therefore, we remain on the sidelines.

Company Description:

CWT operates regulated water and wastewater utilities in CA, WA, HI and NM, with 490,000 connections in CA (90%), 36,000 connections in WA (recently doubled through an acquisition), 5,000 in HI, and 8,300 connections in NM.

CWT: EPS breakdown by segment ($)

CWT	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.31**	**1.87**	**1.70**	**1.83**	**11.7%**
DPS	**0.79**	**0.85**	**0.91**	**0.98**	**7.4%**
Dividend payout	60%	45%	54%	53%	

Source: Company data for 2019; Seaport Global Securities

CWT	2019A	2020E	2021E	2022E
EBIT	117	149	148	163
EBITDA	209	248	255	277
Net interest expense	41	44	45	47
Net income	63	92	87	96
EPS	**$1.31**	**$1.87**	**$1.70**	**$1.83**
DPS	**$0.79**	**$0.85**	**$0.91**	**$0.98**

CFO	**$ 169**	**$ 211**	**$ 214**	**$ 231**
Utility plant expenditures	(274)	(275)	(285)	(285)
Other	(2)	(2)	(2)	(2)
CFI	**(276)**	**(277)**	**(287)**	**(287)**
Issuance of common stock	18	96	80	86
Issuance of debt	103	28	32	32
Dividends	(38)	(41)	(44)	(47)
Other	20	20	20	20
CFF	**103**	**103**	**88**	**91**
Change in cash and cash equivalents	(4)	37	15	35

Net utility plant	2,406	2,583	2,761	2,932
Cash and cash equivalents	43	86	100	136
Other current assets	142	142	142	142
Total current assets	184	227	242	277
Regulatory assets	433	433	433	433
Goodwill	3	3	3	3
Other assets	85	85	85	85
Total assets	**$ 3,111**	**$ 3,331**	**$ 3,524**	**$ 3,731**
Total common stockholders' equity	$ 780	$ 831	$ 874	$ 923
Long-term debt, less current maturities	787	814	847	879
Total capitalization	**1,567**	**1,645**	**1,720**	**1,802**
Total current liabilities	359	479	578	682
Deferred income taxes	223	223	223	223
Pension and postretirement benefits ot	259	259	259	259
Other long-term liabilities	270	270	270	270
Advances for construction	191	191	191	191
Contributions in aid of construction	242	262	282	302
Total capitalization and liabilities	**$ 3,111**	**$ 3,331**	**$ 3,524**	**$ 3,731**

Seaport Global

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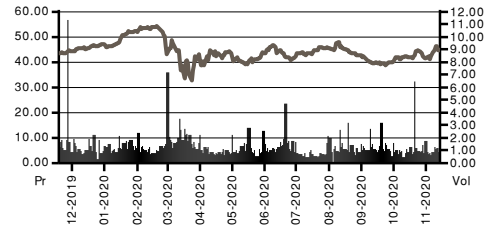
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$44.71**
Float:	244.8MM
Diluted Shares:	254.4MM
Short Interest:	11.0MM
Average Daily Volume:	1,188k
52 Week Range:	$30.40 - $54.52
Market Cap:	**$11,376MM**
Cash and Investments:	$5MM
Debt:	$5MM
Enterprise Value:	$11,376MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
FY	$1.47A	$1.58	$1.58E	$1.66	$1.66E	$1.78	$1.78E
P/E	**30.4x**		**28.3x**		**27.0x**		**25.2x**
Dividends Per Share							
FY	$0.907A	$0.970	$0.970E	$1.038	$1.038E	$1.111	$1.111E
Dividend Yield	**2.0%**		**2.2%**		**2.3%**		**2.5%**

Essential Utilities, Inc.

(NYSE: WTRG)

DELCORA deal is increasingly important as it should dilute gas LDC exposure

Summary:
While we share WTRG's rate base/earnings growth expectations for its gas LDC, we look to the pending acquisition of the DELCORA wastewater system in PA as a way to boost WTRG's earnings mix more towards water. We remain on the sidelines until we get more legal/regulatory clarity on this large wastewater system acquisition.

Highlights

Gas LDCs and ESG investing: We continue to project a ~9% annual rate base growth for WTRG's Peoples in PA, but investors increasingly question the longevity of this infrastructure replacement cycle given the growing push to decarbonize house heating in Europe. Ongoing gas pipe replacement should continue to reduce methane leaks and blending of RNG should lower the carbon footprint of gas LDCs without any detriment to their earnings growth over the next decade if not longer, we believe, as electric heat pumps gain on popularity. In other words, we don't expect the rate base growth of gas LDCs especially those in gas-supportive states like PA to slow down any time soon. However, the marginal US water utility investor seems to have a strict ESG mandate and WTRG's 30% of earnings coming from gas LDCs seems to diminish the investment appeal of WTRG's stock. The DELCORA acquisition, if successful, should reduce the gas LDC earnings contributions hence the transaction is increasingly important for the stock.

DELCORA acquisition: WTRG has $363MM in pending muni water/wastewater deals in PA (and TX), the largest backlog we can recall in Aqua's/WTRG's history. The backlog includes the DELCORA wastewater acquisition ($276.5MM) which continues to face legal challenges, but WTRG's management feels comfortable with its ability to close the transaction in late March/April 2021, following a delayed PA PUC review. WTRG/ Aqua PA insists that they have a legally binding asset purchase agreement (APA) for the wastewater system, but courts should rule on the APA validity only within the next 60 days. The DELCORA transaction should be additive to WTRG's water earnings only in 2022 following Aqua PA's rate case to be filed next year.

Estimates and valuation: WTRG's 3Q20 earnings and management's guidance toward the high-end of its 2020 EPS target range came in line with our expectations. Our 2020-2022 EPS estimates remain unchanged. We recognize that WTRG's gas utility is in good regulatory jurisdictions and has strong rate base/earnings growth prospects, similar to those of ATO. WTRG's water utility is an average grower unless the company should be successful with the DELCORA acquisition, we believe. Excluding the DELCORA deal, WTRG's stock now adequately reflects its current earnings mix and growth prospects, we believe. Therefore, we remain on the sidelines until we grow more comfortable with the DELCORA deal actually closing.

Company Description:
WTRG owns and operates water utilities (1 million accounts) and gas utilities (0.74 million accounts) in 10 states though mainly PA.

WTRG: EPS estimates per segment ($)

WTRG	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated water utilities	1.47	1.10	1.17	1.25	
Regulated gas utilities	0.00	0.54	0.61	0.69	
Parent	0.00	-0.06	-0.13	-0.16	
Total EPS	**1.47**	**1.58**	**1.66**	**1.78**	**6.7%**
DPS	**0.91**	**0.97**	**1.04**	**1.11**	**7.0%**
Dividend payout	62%	61%	63%	62%	

Source: Company data for 2019, Seaport Global Securities

WTRG	2019A	2020E	2021E	2022E
Operational EBITDA	505	874	923	1,000
Operational EBIT	349	610	645	706
Net interest expense	100	202	210	228
Ordinary Profit Before Tax	269	437	464	507
Income tax	7	35	37	41
Net profit	262	402	427	466
S/O (m)	178	255	258	262
Diluted EPS	**1.47**	**1.58**	**1.66**	**1.78**
DPS	**0.91**	**0.97**	**1.04**	**1.11**
Cash	1,869	5	5	5
Receivables	108	110	113	120
Inventory	18	30	30	30
Other short-term assets	18	18	18	18
Other-long term assets	1,003	3,810	3,810	3,810
Property, plant, and equipment	6,346	8,962	9,113	9,249
Total assets	**9,362**	**12,935**	**13,090**	**13,232**
Financial liabilities	117	496	496	496
Operating liabilities	67	109	109	109
Other liabilities	108	220	220	220
Deferred credits	2,057	2,758	2,757	2,757
Long-term debt	2,943	4,750	5,346	5,658
Shareholders' equity	4,070	4,602	4,161	3,992
Total liabilities and equity	**9,362**	**12,935**	**13,090**	**13,232**
Net income	262	402	427	466
D&A, goodwill amortisation	156	264	279	294
Other non cash elements	-40	-6	-6	-6
Funds from operations	379	660	699	754
Non-cash working capital	-40	43	0	-1
CFO	**339**	**703**	**699**	**753**
Net investments in fixed assets	-610	-6,555	-1,032	-780
Net investments in financial assets	6	0	0	0
Free cash flow before dividends	**-266**	**-5,852**	**-333**	**-27**
Dividends paid	-161	-242	-266	-290
Free cash flow after dividends	-427	-6,095	-599	-316
Changes in equity	1,935	302	2	3
Changes in financial debt	386	3,927	596	313
Adjustment for minorities / miscellaneous	-28	1	1	1
Increase in cash	1,866	-1,864	0	0

Seaport Global

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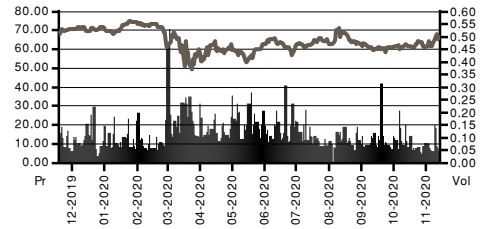
Rating:	**Neutral**
Price Target:	**N/A**

Price Target Metrics:
N/A

Current Price:	**$66.17**
Float:	26.0MM
Diluted Shares:	28.7MM
Short Interest:	0.3MM
Average Daily Volume:	73k
52 Week Range:	$45.60 - $74.99
Market Cap:	**$1,899MM**
Cash and Investments:	$20MM
Debt:	$1,505MM
Enterprise Value:	$3,384MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
Q1 (Mar)	$0.21A	$0.08	$0.08A	$0.23	$0.23E	$0.26	$0.26E
Q2 (Jun)	$0.48A	$0.69	$0.69A	$0.70	$0.70E	$0.79	$0.79E
Q3 (Sep)	$0.68A	$0.95	$0.91A	$0.82	$0.82E	$0.92	$0.92E
Q4 (Dec)	$0.42A	$0.33	$0.36E	$0.59	$0.59E	$0.65	$0.65E
FY	$1.78A	$2.05	$2.04E	$2.35	$2.35E	$2.62	$2.62E
P/E	**37.1x**		**32.5x**		**28.2x**		**25.3x**
Dividends Per Share							
FY	$1.200A	$1.280	$1.280E	$1.370	$1.370E	$1.465	$1.465E
Dividend Yield	**1.8%**		**1.9%**		**2.1%**		**2.2%**

SJW Group
(NYSE: SJW)

2021 guidance, if any, could disappoint

Summary:
San Jose Water's Monterey-style WRAM benefited SJW's earnings thanks to favorable weather and a COVID-related uptick in residential sales, though the earnings uplift was a bit lower than we had hoped. We remain concerned about the potential impact of the ongoing La Nina and the uncertainty surrounding the upcoming rate case in CT on SJW's 2021 guidance, if the company even decides to issue one in early 2021. Therefore, we remain on the sidelines on SJW even though the stock trades at a 15% 2022 P/E to an average regulated water utility.

Highlights

Tweaking estimates: We trimmed our recently increased 2020 EPS estimate to $2.04 from 2.05 based on SJW's 3Q20 earnings print. Our 2021/2022 EPS estimates remain unchanged. We continue to be concerned about SJW's 2021 EPS guidance range given the likely La Nina impact on its surface water production levels as well as an uncertain outcome of its CT rate case. We wouldn't be surprised if management decided not to provide 2021 EPS guidance in early 2021 which would not be well-received, we believe. Please see our most recent note on SJW for our latest thoughts on the name.

Company Description:
SJW Group is a regulated water and wastewater utility serving ~390,000 accounts across CA, CT, TX and ME. SJW merged with Connecticut Water Service in October 2019.

SJW: EPS breakdown by segment ($)

SJW	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.78**	**2.04**	**2.35**	**2.62**	**13.7%**
DPS	**1.20**	**1.28**	**1.37**	**1.47**	**6.9%**
Dividend payout	67%	63%	58%	56%	

Source: Company data for 2019; Seaport Global Securities

SJW	2019A	2020E	2021E	2022E
EBITDA	157	211	236	248
Net income	51	58	67	75
EPS diluted	**$1.78**	**$2.04**	**$2.35**	**$2.62**
DPS	**$1.20**	**$1.28**	**$1.37**	**$1.47**
CFO	**$ 130**	**$ 151**	**$ 167**	**$ 177**
CFI	**(1,018)**	**(216)**	**(277)**	**(257)**
Issuance of common stock	0.0	0.0	0.0	0.0
Issuance of debt	502	113	113	113
Dividends	-34	-36	-39	-40
CFF	**485**	**101**	**99**	**99**
Change in cash and cash equivalents	-403	36	-12	19
Net utility plant	2,206	2,313	2,474	2,612
Cash and cash equivalents	18	54	42	62
Other current assets	109	112	115	117
Total current assets	127	166	157	179
Regulatory assets	114	114	114	114
Goodwill	628	628	628	628
Other assets	57	57	57	57
Total assets	**3,132**	**3,278**	**3,430**	**3,591**
Total common stockholders' equity	$ 890	$ 966	$ 980	$ 999
Long-term debt, less current	1,261	1,187	1,195	1,203
Total capitalization	**2,151**	**2,153**	**2,175**	**2,202**
Total current liabilities	235	359	470	583
Deferred income taxes	196	193	190	188
Pension and postretirement benefits oth	108	108	108	107
Other long-term liabilities	45	45	45	45
Advances for construction	112	135	157	180
Contributions in aid of construction	286	286	286	286
Total capitalization and liabilities	**3,132**	**3,278**	**3,430**	**3,591**

Utilities Disclosures

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Risks & Considerations for American Water Works Company, Inc. American Water Works Company, Inc. (AWK)

Allowed ROEs for AWK's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings.

Lower sales volumes could weigh on AWK's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWK has a particularly busy regulatory calendar in 2020, with rate cases in three of its largest jurisdictions – NJ, PA and MO.

Potentially higher equity needs due to weakening operating cash flows and underfunded pension funds: Lower customer collections (due to lower sales or non-payment) coupled with growing federal cash taxes and underperforming pension funds should be weighing on operating cash flows of regulated utilities especially during/following the COVID-19 pandemic. That in turn could require some deleveraging of balance sheets of regulated utilities thus more equity. AWK already announced ~$500m in new equity as soon as 2022, but the issuances could be enlarged and accelerated to protect AWK's credit ratings.

Risks & Considerations for American States Water Company American States Water Company (AWR)

AWR's water utility (GSWC) could see volatility in earnings due to usage: The CPUC recently modified the full water decoupling mechanism (WRAM). While it should not impact GSWC until the next rate case, covering 2025-2027, CA utility consumer advocates push for an immediate change to the decoupling mechanism. GSWC has always excelled at earning at least its allowed ROE in CA, but it could prove challenging with WRAM.

Allowed ROEs for AWR's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. AWR's allowed ROE for its water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWR should be filing a new water rate case by July 2020 with new rates in effect in January 2021.

Returns in pension accounts impact AWR's earnings in between rate cases in CA: AWR has no balancing account tracking changes in returns in its pension accounts. Those changes can be trued up/reflected in AWR's rates during rate cases, but those take place every three years.

Military contracts are highly competitive: Through its unregulated ASUS subsidiary, AWR provides water and wastewater services to 11 military bases. The company awaits awards of up to three more of these contracts in 2020. We assume that AWR secures at least one new military contract per year in 2020-2022 though AWK, AWR's largest competitor, has been winning most of the contract awards as of late.

Risks & Considerations for California Water Services Group California Water Services Group (CWT)

Allowed ROEs for CWT's regulated water utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. CWT's allowed ROE for its water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. CWT awaits a proposed decision in its 2018 general rate case in CA with rates retroactive to January 1, 2021. Though the utility reached a partial settlement with the consumer advocate late in 2019, outstanding issues involve the continuation of the revenue decoupling and balancing accounts for pension and medical expenses. Without those, CWT could see a meaningful spike in its earnings volatility.

Risks & Considerations for SJW Group SJW Group (SJW)

Allowed ROEs for SJW's regulated water utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. SJW's allowed ROE for its CA water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. SJW should file a rate case for its new CT business in 2021. Also, the CA utility of SJW should go through a general rate case in the state in 2021 and state regulators could attempt to claw-back some synergies related to the recent merger with CTWS.

SJW's CA earnings are highly volatile: Now that SJW no longer has even a temporary decoupling mechanism in CA, it's CA earnings change along with changes in volumes and changes in purchased water costs. SJW plans to ask for a purchased water cost balancing account in the next rate case in CA, but that means that 2021 could be another weak earnings year before the regulatory fix arrives for 2022, if at all.

Risks & Considerations for Essential Utilities, Inc. Essential Utilities, Inc. (WTRG)

Allowed ROEs for WTRG's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average

10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. WTRG's only pending rate case (in NC) is very small.

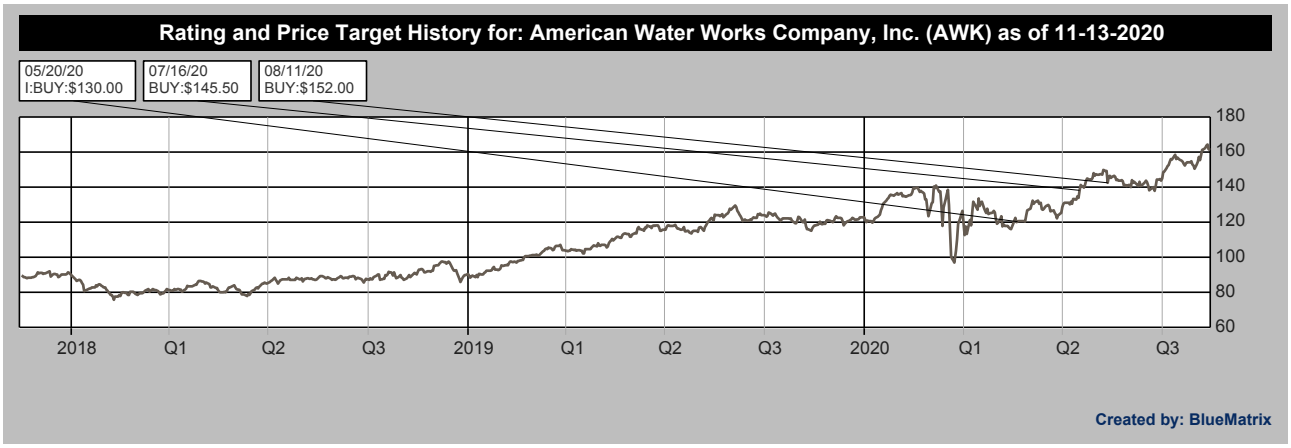
Lower sales volumes could weigh on WTRG's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

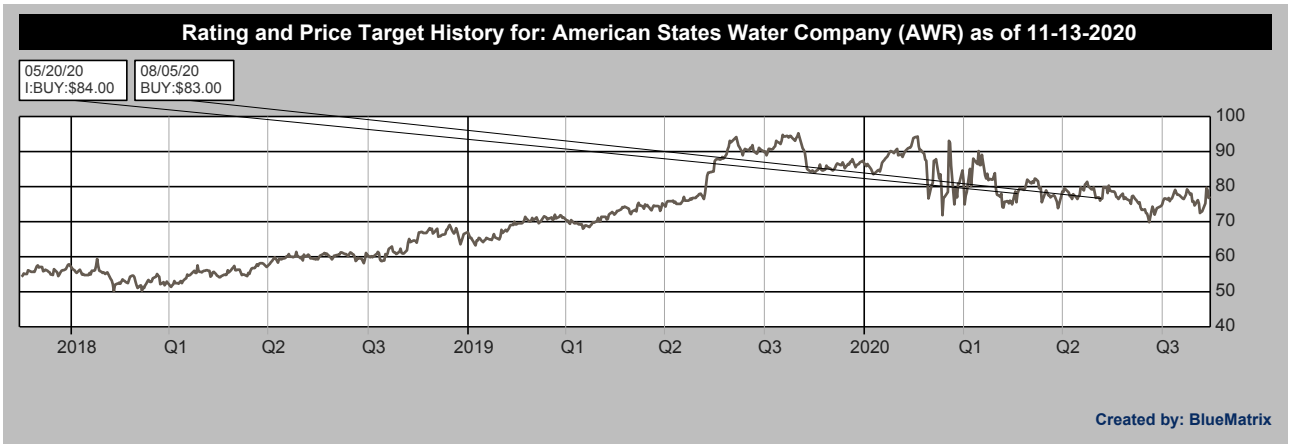
Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, it's up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. WTRG's regulatory calendar is quiet in 2020, with a pending small rate case in NC, and a likely filing for a catch-up repair tax adjustment for Peoples in PA.

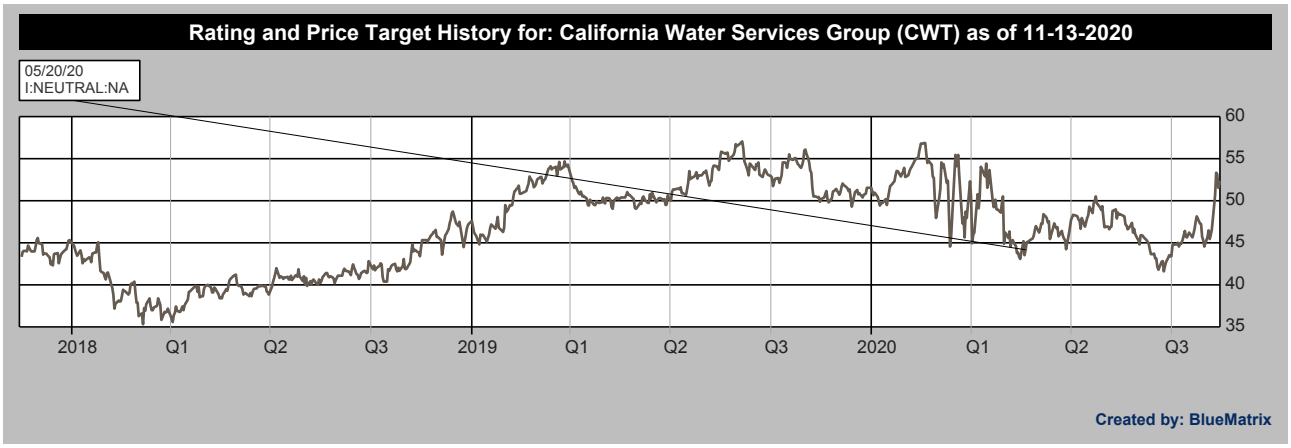
Gas utilities have a higher operating risk than water utilities: Over-pressurized gas systems seem to happen more frequently among gas utilities in the US. While we recognize that Peoples Gas is a well-managed system, WTRG's risk profile could further deteriorate with any gas-related operational issues. Additionally, investors increasingly scrutinize the carbon footprint of gas LDCs which in turn weighs on their market valuations.

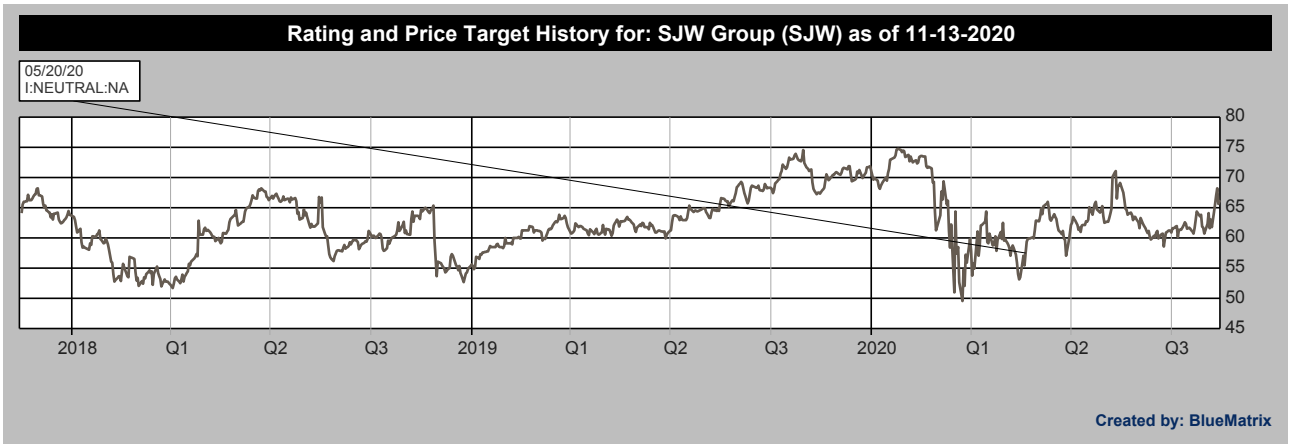
Other Companies Mentioned in This Report

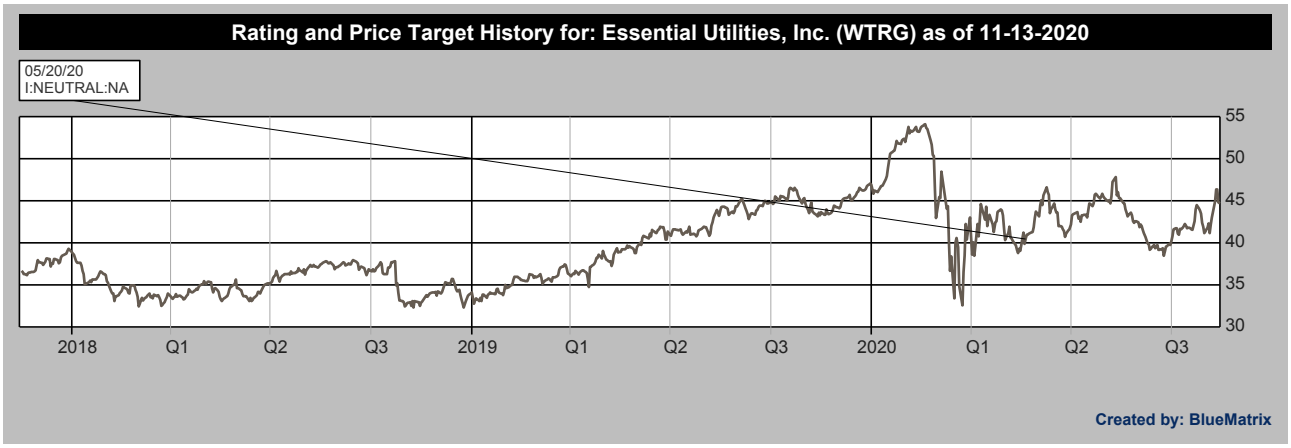
- American Water Works Company, Inc. (AWK: $161.31, Buy)
- California Water Services Group (CWT: $52.38, Neutral)
- Essential Utilities, Inc. (WTRG: $44.71, Neutral)
- American States Water Company (AWR: $77.20, Buy)
- SJW Group (SJW: $66.17, Neutral)











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NA - A rating is not assigned.

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Accumulate - The investment outlook and risk/reward over the following 12 months are favorable on an absolute basis and relative to the peer group.

Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.

Reduce - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.

Sell - The investment outlook and risk/reward over the following 12 months are very unfavorable on an absolute basis and relative to the peer group.

NA - A rating is not assigned.

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Rating	Research Coverage Count	Research Coverage % of Total	Investment Banking Clients* Count	Investment Banking Clients* % of Total	Investment Banking Clients* % of Rating Category
Buy	102	61.1%	1	100.0%	1.0%
Neutral	62	37.1%	0	0.0%	0.0%
Sell	3	1.8%	0	0.0%	0.0%
Total	167	100.0%	1	100.0%	0.6%

*Investment banking clients are companies for whom Seaport Global Securities has provided investment banking services in the previous 12 months.

Note: Ratings Distribution as of September 30, 2020

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This report is intended exclusively for:
bcobrien@ aquaamerica.com

First Read

Aqua America Inc

Line of Sight to Merger Close Not as Clear as Expected

Equities

Americas
Water Utilities

12-month rating	**Buy**
12m price target	**US$42.00**
Price	**US$41.12**

RIC: WTR.N **BBG:** WTR US

Trading data and key metrics

52-wk range	US$41.12-32.37
Market cap.	US$7.34bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	461
Avg. daily value (m)	US$17.4
Common s/h equity (12/19E)	US$2.15bn
P/BV (12/19E)	3.4x
Net debt / EBITDA (12/19E)	5.1x

EPS (UBS, diluted) (US$)

	12/19E	
	UBS	Cons.
Q1E	0.30	0.28
Q2E	0.39	0.40
Q3E	0.47	0.41
Q4E	0.32	0.36
12/19E	1.48	1.46
12/20E	1.58	1.56
12/21E	1.68	1.66

Two Intervenor Holdouts Take the Merger down a Litigated Path

During the hearing yesterday at the PA Public Utilities Commission for the merger between WTR and Peoples, it was disclosed that WTR reached a settlement with most intervenors in the case, with the exception of two parties to the docket: the Bureau of Investigation and Enforcement (BIE) and the Office of Small Business Advocate (OSBA). WTR filed an 8K today with little detail regarding the sticking points for the two intervenors; however, as we understand it, BIE (which is effectively the PUC Staff) disagrees with an aspect of the settlement reached with the other parties related to a small gas system (Goodwin Tombaugh ~1,600 customers) within Peoples. As a result of failing to reach an all-party settlement, the merger case will have to proceed through a litigated process to address the outstanding issues. Although at this stage we don't believe the issues put the transaction in jeopardy, this development is disappointing. We had anticipated that WTR would be successful in reaching settlement with all parties based on the confidence that management portrayed earlier in the process, as well as indications that transaction financing would only be issued when there was "line of sight" to merger close. In April, WTR issued $900MM debt, $650MM convertible equity units, and ~$1.3B in common equity, in addition to another $750MM that will be placed privately upon merger close.

Peoples Rate Case

The Peoples rate case is proceeding on a parallel path at the PA commission. Settlement discussions are expected to begin ~early-July and WTR expects to be more active in Peoples' rate case once settlement discussions begin. Rate case proceedings in PA have a history of settlement. It remains unclear if/how the intervenor issues in the merger docket would weave into the rate case.

Next Steps

Briefs in the merger docket are due July 10 and reply briefs are due July 25. WTR now expects the merger to close fall 2019, as opposed to its original projection for a close in mid-2019.

Valuation: $42 Price Target

We value WTR at a 25.2x P/E on 2021e EPS of $1.68.

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Highlights (US$m)	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
Revenues	820	810	838	881	921	956	995	1,033
EBIT (UBS)	326	329	337	370	399	425	454	482
Net earnings (UBS)	234	240	251	265	281	299	319	342
EPS (UBS, diluted) (US$)	1.32	1.35	1.41	1.48	1.58	1.68	1.79	1.92
DPS (US$)	0.74	0.79	0.88	0.94	1.00	1.07	1.15	1.23
Net (debt) / cash	(1,891)	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)

Profitability/valuation	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
EBIT margin %	39.7	40.6	40.3	42.0	43.3	44.5	45.6	46.7
ROIC (EBIT) %	9.0	8.4	7.9	8.0	8.0	8.1	8.3	8.4
EV/EBITDA (core) x	16.2	17.0	17.6	18.9	18.1	17.4	16.7	15.8
P/E (UBS, diluted) x	23.9	24.8	25.0	27.7	26.1	24.5	23.0	21.5
Equity FCF (UBS) yield %	0.2	(1.6)	(1.6)	(1.8)	0.2	0.5	0.9	1.2
Net dividend yield %	2.3	2.4	2.5	2.3	2.4	2.6	2.8	3.0

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$41.12 on 12 Jun 2019 18:43 EDT

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Forecast returns

Forecast price appreciation	+2.1%
Forecast dividend yield	2.3%
Forecast stock return	+4.4%
Market return assumption	6.9%
Forecast excess return	-2.5%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 1% discount to the 2021 average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 7% discount to reflect impact of lower P/E associated with gas earnings.

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	47%	25%
Neutral	FSR is between -6% and 6% of the MRA.	39%	22%
Sell	FSR is > 6% below the MRA.	14%	19%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 31 March 2019.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

KEY DEFINITIONS:Forecast Stock Return (FSR) is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months. In some cases, this yield may be based on accrued dividends. **Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium). **Under Review (UR)** Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation. **Short-Term Ratings** reflect the expected near-term (up to three months) performance of the stock and do not reflect any change in the fundamental view or investment case. **Equity Price Targets** have an investment horizon of 12 months.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Aqua America Inc[16]	WTR.N	Buy	N/A	US$41.12	12 Jun 2019

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date
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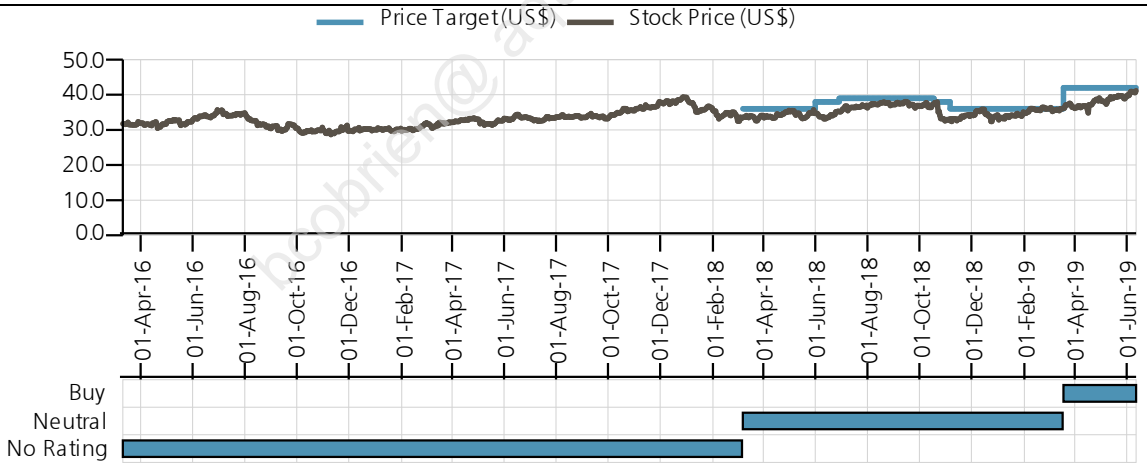
Aqua America Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2016-03-11	31.72	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy

Source: UBS; as of 12 Jun 2019

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Q2 2020 Earnings Preview

North America Power & Utilities, Alternative Energy, and Environmental Services

Equities

North America
Utilities

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Regulated Utilities: Strong Weather Comparison

We expect favorable weather conditions helped offset the impact of the pandemic on demand. 2Q'20 degree days rose 12% above last year and 9% above normal with the biggest impacts in the Midwest and Northeast. Our forecasts average 5% above consensus and 2% above 2Q'19. Consensus may still be developing but we see few if any shortfalls versus consensus. Names that will likely create the most interest for investors are Buy-rated DTE, DUK, PCG, PEG and SRE and Neutral-rated EVRG, PNW and SO. Our water utility forecasts are in line with consensus with positive quarters for Neutral-rated AWK and AWR. We expect to hold a conference call on Monday, July 20 at 10 AM with a dial in number of 800-950-3502 and a code 21966464.

Power: 2Q Beats on Weather and Retail Acquisitions; Updating UBSe EBITDA

Our 2Q'20 Adjusted EBITDA estimates are above consensus for both NRG and VST at $543mln and $819mln respectively. We expect bad debts and volume dislocations from COVID-19 were not as bad as anticipated in 2Q and weather provided a positive volume offset. VST results will be driven by OPI cost savings offsetting lower capacity payments, the retail acquisitions of Crius and Ambit and better pricing in ERCOT due to the commercial impact noted on the 1Q '20 call. NRG results will be driven by the Stream retail acquisition, better weather, and margin enhancement at retail. VST and NRG were both significantly hedged for the balance of 2020 at the time of the 1Q'20 earnings calls. We are updating our UBSe Adj. EBITDA. NRG to $1,986 /$1,840/$1,737mln and VST to $3,444/$3,087/$3,076mln for '20/21/22 respectively.

Alternative Energy

We expect 2Q20 calls to focus on 2H20 demand given the on-going recovery from COVID-19 troughs in April; the potential for further policy support after the 2020 election; and impacts of corporate actions (RUN/VSLR merger, Maxeon spin from SPWR); as well as GNRC's storage product update (initiation).

Environmental Services

The MSW names operationally weathered the COVID-19 economic downturn (top pick WCN). We continue to see value in the more depressed share prices of CVA and ECOL. As the election approaches we expect increased focus on potential for higher tax rates.

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Figure 1: Electric Utilities Universe

Rating	Ticker	Company	7/16/2020 Price	Price Target	Total Return inc. Div. Yld	UBS 2019A EPS	UBS 2020A EPS	UBS 2021E EPS	UBS 2022E EPS	2021 P/E Ratio	2021 Prem/ Disc	2022 P/E Ratio	2022 Prem/ Disc	Current Dividend Yield	5 Yr EPS Growth	5 Yr DPS Growth	Regulatory Quartile
Buy (CBE)	PCG	PG&E Corp	$9.02	$15	66%	$3.93	$1.41	$0.98	$1.11	9.2x	(49%)	8.1x	(53%)	0.0%	N/A	N/A	3rd
Buy	SRE	Sempra Energy	$122.63	$172	43%	$6.78	$7.45	$7.84	$8.33	15.6x	(14%)	14.7x	(14%)	3.2%	6.2%	8.1%	3rd
Buy	EIX	Edison International	$56.09	$75	38%	$4.70	$4.45	$4.67	$4.80	12.0x	(34%)	11.7x	(32%)	4.5%	1.2%	4.0%	3rd
Buy	DUK	Duke Energy	$81.07	$102	30%	$5.05	$5.07	$5.27	$5.50	15.4x	(15%)	14.7x	(14%)	4.7%	3.7%	2.0%	1st
Buy	EXC	Exelon	$38.06	$48	30%	$3.22	$2.98	$2.99	$3.10	12.7x	(30%)	12.3x	(28%)	4.0%	0.1%	5.3%	3rd
Buy	ETR	Entergy Corp	$98.33	$121	27%	$5.33	$5.62	$5.90	$6.30	16.7x	(8%)	15.6x	(9%)	3.8%	6.0%	2.3%	2nd
Buy	FE	FirstEnergy Corp	$41.29	$50	25%	$2.58	$2.50	$2.62	$2.74	15.7x	(13%)	15.1x	(12%)	3.8%	3.8%	4.5%	2nd
Buy	PNM	PNM Resources	$39.13	$47	23%	$2.16	$2.16	$2.38	$2.50	16.4x	4%	15.6x	6%	3.1%	5.9%	5.5%	4th
Buy	PPL	PPL Corporation	$25.85	$30	22%	$2.92	$2.40	$2.40	$2.45	10.8x	(41%)	10.6x	(38%)	6.4%	-3.7%	0.0%	1st
Buy	DTE	DTE Energy	$109.70	$130	22%	$6.30	$6.61	$7.21	$7.58	15.2x	(16%)	14.5x	(15%)	3.7%	6.8%	6.0%	1st
Buy	PEG	Public Service Ent Group	$52.91	$62	21%	$3.28	$3.31	$3.41	$3.58	15.5x	(15%)	14.8x	(13%)	3.7%	5.0%	4.8%	2nd
Buy	EMA	Emera Inc (C$)	$55.94	$65	20%	$2.60	$2.76	$3.07	$3.28	18.2x	15%	17.1x	15%	4.3%	5.3%	4.5%	1st
Buy	AES	AES Corp.	$14.88	$17	18%	$1.36	$1.38	$1.55	$1.67	9.6x	(47%)	8.9x	(48%)	3.8%	6.9%	4.8%	1st
Buy	FTS	Fortis Inc (C$)	$54.10	$62	18%	$2.55	$2.66	$2.93	$3.12	18.5x	2%	17.3x	2%	3.4%	7.3%	6.0%	3rd
Buy	NEE	NextEra Energy	$268.38	$305	16%	$8.37	$9.08	$9.84	$10.55	27.3x	50%	25.4x	49%	1.9%	7.9%	10.0%	1st
Buy	ACO	ATCO Ltd. (C$)	$42.31	$47	15%	$3.18	$2.91	$3.25	$3.41	13.0x	(17%)	12.4x	(16%)	4.1%	3.6%	7.1%	4th
Buy	OGE	OGE Energy Corp	$31.90	$35	15%	$2.16	$2.17	$2.21	$2.31	14.5x	(20%)	13.8x	(19%)	4.9%	3.5%	5.0%	3rd
Buy	AEP	American Electric Power	$85.09	$94	14%	$4.24	$4.30	$4.65	$4.93	18.3x	1%	17.3x	1%	3.3%	5.5%	5.7%	2nd
Buy	D	Dominion Energy	$76.95	$81	10%	$4.13	$3.50	$3.87	$4.12	19.9x	9%	18.7x	9%	4.9%	2.5%	-4.1%	2nd
Neutral	ED	Consolidated Edison	$71.84	$76	10%	$4.38	$4.25	$4.58	$4.76	15.7x	(14%)	15.1x	(12%)	4.3%	3.2%	3.5%	4th
Neutral	CU	Canadian Utilities Ltd (C$)	$34.41	$36	9%	$2.23	$2.04	$2.25	$2.37	15.3x	(3%)	14.5x	(2%)	4.8%	3.2%	4.8%	4th
Neutral	CMS	CMS Energy	$60.33	$64	9%	$2.49	$2.68	$2.87	$3.05	21.0x	16%	19.8x	16%	2.7%	7.0%	7.0%	1st
Neutral	LNT	Alliant Energy	$49.73	$52	8%	$2.33	$2.45	$2.60	$2.72	19.1x	5%	18.3x	7%	3.1%	5.5%	6.2%	1st
Neutral	POR	Portland General	$42.32	$44	8%	$2.39	$2.44	$2.60	$2.64	16.3x	(10%)	16.0x	(6%)	3.6%	3.8%	6.0%	3rd
Neutral	SO	Southern Company	$53.74	$55	7%	$3.11	$3.20	$3.31	$3.56	16.2x	(11%)	15.1x	(12%)	4.6%	6.0%	3.9%	1st
Buy	AEE	Ameren Corp	$76.79	$80	7%	$3.35	$3.47	$3.76	$4.04	20.4x	12%	19.0x	11%	2.6%	6.6%	6.0%	2nd
Neutral	EVRG	Evergy	$61.41	$62	4%	$2.89	$3.06	$3.24	$3.46	19.0x	4%	17.8x	4%	3.3%	5.1%	5.3%	3rd
Neutral	WEC	WEC Energy Group	$87.76	$88	3%	$3.58	$3.75	$3.98	$4.23	22.0x	21%	20.8x	22%	2.9%	6.2%	6.7%	1st
Neutral	PNW	Pinnacle West Capital Corp	$80.56	$79	2%	$4.77	$4.85	$4.90	$5.14	16.4x	(10%)	15.7x	(8%)	3.9%	3.5%	6.0%	4th
Neutral	ES	Eversource Energy	$85.81	$85	2%	$3.46	$3.67	$3.87	$4.08	22.2x	22%	21.0x	23%	2.6%	6.0%	5.9%	2nd
Sell	CUP	Caribbean Utilities Corp Ltd	$15.49	$15	1%	$0.84	$0.69	$0.79	$0.89	19.7x	25%	17.5x	18%	4.5%	6.6%	7.1%	4th
Neutral	XEL	Xcel Energy	$64.99	$64	1%	$2.64	$2.77	$3.02	$3.20	21.5x	18%	20.3x	19%	2.5%	5.7%	6.0%	2nd
Sell	H	Hydro One Ltd (C$)	$27.26	$24	(8%)	$1.41	$1.37	$1.42	$1.49	19.1x	5%	18.3x	7%	3.6%	3.8%	4.7%	4th
Sell	HE	Hawaiian Electric Industries	$37.00	$32	(10%)	$1.88	$1.99	$1.82	$2.20	20.3x	12%	16.8x	(2%)	3.6%	3.1%	3.2%	4th
Overall Average (unnormalized, inc. Gas Midstream)										**16.7x**		**15.7x**					
Electric Utility Normalized (including Gas Midstream)										**18.2x**		**17.1x**					

Source: FactSet, UBS Equity Research

Figure 2: Water Utilities Universe

Rating	Ticker	Company	7/16/2020 Price	UBS Price Target	Total Return inc. Div. Yld	UBS 2018A EPS	UBS 2019A EPS	UBS 2020E EPS	UBS 2021E EPS	2021E P/E Ratio	2021E Prem/ Disc	Current Dividend Yield	5 Yr EPS Growth	5 Yr DPS Growth
Neutral	WTRG	Essential Utilities	$43.88	$45	5%	$1.41	$1.48	$1.58	$1.68	26.2x	(15%)	2.0%	6.6%	7.0%
Neutral	AWK	American Water	$138.32	$139	2%	$3.30	$3.63	$3.85	$4.17	33.1x	8%	1.3%	6.9%	10.0%
Neutral	SJW	SJW Group	$63.02	$62	0%	$2.51	$2.03	$2.34	$2.49	25.3x	(18%)	1.9%	8.3%	7.0%
Sell	AWR	American States Water	$77.59	$70	(8%)	$1.73	$2.03	$2.25	$2.36	32.9x	7%	1.4%	7.3%	6.0%
Sell	CWT	California Water Service	$48.28	$43	(9%)	$1.44	$1.31	$1.55	$1.69	28.6x	(7%)	1.6%	9.0%	5.0%
AVERAGE										**30.8x**				

Source: FactSet, UBS Equity Research

Figure 3: Independent Power Producers

Rating	Ticker	Company	7/16/2020 Price	Price Target	Total Return inc. Div. Yld	UBS 2018A EBITDA	UBS 2019A EBITDA	UBS 2020E EBITDA	UBS 2021E EBITDA	2020 EV/ EBITDA Ratio	2020 Prem/ Disc	2021 EV/ EBITDA Ratio	2021 Prem/ Disc	2019E Net Debt/ EBITDA
Buy	VST	Vistra Energy Corp	$19.40	$31	62%	$2,899	$3,393	$3,287	$3,195	5.7x	(21%)	5.6x	(18%)	3.2x
Buy	NRG	NRG Energy	$33.84	$41	22%	$2,001	$1,977	$1,914	$1,813	4.1x	(43%)	4.0x	(41%)	2.2x
MID-CYCLE MEDIAN										**7.2x**		**6.8x**		

Source: FactSet, UBS Equity Research

Figure 4: Regulated Utilities & Power 1Q20 Earnings Summary

U.S. companies in US$ Cdn companies in C$ CUP in US$		Quarterly					Annual					
Company	Ticker	Scheduled Reporting Date	2Q20E UBS	2Q20E Consensus	UBS Vs. Consensus	UBS Confidence Indicator[1]	2Q19A Adjusted	2020E UBS	2020E Consensus	UBS Vs. Consensus	Trailing 12 Month	2019A UBS	2020E Guidance
ELECTRIC UTILITIES													
AES Corp	AES	6-Aug	$0.21	$0.26	($0.05)		$0.26	$1.38	$1.42	($0.04)	$1.33	$1.36	$1.32-$1.42
ATCO Ltd (C$)	ACO.x-TSE	30-Jul	$0.55	$0.55	$0.00		$0.68	$2.91	$2.92	($0.01)	$2.85	$3.18	N/A
Alliant Energy	LNT	7-Aug	$0.57	$0.40	$0.17		$0.40	$2.45	$2.44	$0.01	$2.69	$2.33	$2.34-$2.48
Ameren Corp	AEE	7-Aug	$0.85	$0.84	$0.01		$0.72	$3.47	$3.45	$0.02	$3.29	$3.35	$3.40-$3.60
American Electric Power	AEP	6-Aug	$1.08	$0.99	$0.09		$1.00	$4.30	$4.31	($0.01)	$4.16	$4.24	$4.25-$4.45
Canadian Utilities Ltd (C$)	CU-TSE	30-Jul	$0.35	$0.38	($0.03)		$0.46	$2.04	$2.02	$0.02	$2.05	$2.23	N/A
Caribbean Utilities Corporation Ltd	CUP.USD-TSE	31-Jul	$0.19	$0.18	$0.01		$0.24	$0.69	$0.74	($0.04)	$0.77	$0.84	N/A
CMS Energy	CMS	3-Aug	$0.48	$0.36	$0.12		$0.33	$2.68	$2.62	$0.06	$2.57	$2.49	$2.64-$2.68
Consolidated Edison	ED	6-Aug	$0.52	$0.54	($0.02)		$0.58	$4.25	$4.40	($0.15)	$4.28	$4.38	$4.15-$4.35
Dominion Energy	D	31-Jul	$0.78	$0.73	$0.05		$0.77	$3.50	$4.38	($0.88)	$4.22	$4.13	$4.25-$4.60
DTE Energy	DTE	28-Jul	$1.51	$1.16	$0.35		$0.99	$6.61	$6.57	$0.05	$6.35	$6.30	$6.47-$6.75
Duke Energy	DUK	10-Aug	$1.00	$1.02	($0.02)		$1.12	$5.07	$5.14	($0.07)	$4.83	$5.05	$5.05-$5.45
Edison International	EIX	28-Jul	$1.16	$1.16	($0.00)		$1.58	$4.45	$4.46	($0.01)	$4.28	$4.70	$4.32-$4.62
Emera Inc (C$)	EMA-TSE	12-Aug	$0.52	$0.58	($0.06)		$0.54	$2.76	$2.80	($0.04)	$2.43	$2.60	N/A
Entergy Corp	ETR	29-Jul	$1.30	$1.24	$0.06		$1.22	$5.62	$5.56	$0.06	$5.75	$5.33	$5.45-$5.75
Evergy, Inc (2)	EVRG	w/o 8/3 Est	$0.63	$0.67	($0.04)		$0.57	$3.06	$3.09	($0.03)	$2.94	$2.89	N/A
Eversource Energy	ES	31-Jul	$0.75	$0.78	($0.03)		$0.72	$3.67	$3.65	$0.02	$3.52	$3.46	$3.60-$3.70
Exelon Corp	EXC	4-Aug	$0.45	$0.45	$0.00		$0.60	$2.98	$3.06	($0.08)	$3.07	$3.22	$2.80-$3.10
FirstEnergy Corp	FE	24-Jul	$0.53	$0.55	($0.02)		$0.61	$2.50	$2.49	$0.01	$2.50	$2.58	$2.40-$2.60
Fortis Inc (C$)	FTS-TSE	30-Jul	$0.57	$0.58	($0.01)		$0.54	$2.66	$2.65	$0.01	$2.54	$2.55	N/A
Hawaiian Electric Industries	HE	30-Jul	$0.40	$0.38	$0.02		$0.39	$1.61	$1.95	($0.34)	$1.90	$1.99	$1.90-$2.10
Hydro One Ltd (C$)	H-TSE	11-Aug	$0.32	$0.27	$0.05		$0.26	$1.37	$1.39	($0.02)	$1.33	$1.41	N/A
NextEra Energy	NEE	24-Jul	$2.49	$2.49	$0.00		$2.35	$9.08	$9.08	$0.00	$8.69	$8.37	$8.70-$9.20
OGE Energy Corp	OGE	6-Aug	$0.50	$0.50	$0.00		$0.50	$2.17	$2.19	($0.02)	$2.16	$2.16	$2.08-$2.18
PG&E Corp	PCG		$0.84	$0.94	($0.10)		$1.10	$1.41	$1.45	($0.04)	$3.52	$3.93	N/A
Pinnacle West Capital Corporation	PNW	w/o 8/3 Est	$1.55	$1.36	$0.19		$1.28	$4.85	$4.83	$0.02	$5.16	$4.77	$4.75-$4.95
PNM Resources	PNM	31-Jul	$0.50	$0.40	$0.10		$0.35	$2.16	$2.19	($0.03)	$2.34	$2.16	$2.16-$2.26
Portland General	POR	31-Jul	$0.34	$0.25	$0.09		$0.28	$2.44	$2.39	$0.04	$2.54	$2.39	$2.20-$2.50
PPL Corporation	PPL	8/7 Est	$0.57	$0.56	$0.01		$0.58	$2.40	$2.46	($0.05)	$2.41	$2.37	$2.40-$2.60
Public Service Enterprise Group	PEG	31-Jul	$0.59	$0.62	($0.03)		$0.58	$3.31	$3.37	($0.06)	$3.25	$3.28	$3.30-$3.50
Sempra Energy	SRE	5-Aug	$1.65	$1.19	$0.46		$1.38	$7.45	$7.15	$0.30	$7.78	$6.78	$7.20-$7.80
Southern Company	SO	30-Jul	$0.64	$0.69	($0.05)		$0.79	$3.20	$3.15	$0.05	$3.03	$3.11	$3.10-$3.22
WEC Energy Group	WEC	4-Aug	$0.67	$0.67	($0.00)		$0.74	$3.75	$3.74	$0.01	$3.61	$3.58	$3.71-$3.75
Xcel Energy	XEL	30-Jul	$0.49	$0.48	$0.01		$0.46	$2.77	$2.76	$0.01	$2.62	$2.64	$2.73-$2.83
Average			**$0.75**	**$0.71**	**$0.04**		**$0.73**	**$3.38**	**$3.42**	**($0.04)**	**$3.43**		
WATER UTILITIES													
American States Water Company	AWR		$0.70	$0.63	$0.07		$0.59	$2.25	$2.27	($0.02)	$2.75	$2.03	N/A
American Water Works Company	AWK	6-Aug	$0.99	$0.95	$0.04		$0.94	$3.85	$3.85	$0.00	$4.25	$3.63	$3.79-$3.89
Essential Utilities	WTRG	6-Aug	$0.26	$0.24	$0.02		$0.37	$1.58	N/A	N/A	$1.27	$1.48	$1.53-$1.58
California Water Service Group	CWT	30-Jul	$0.51	$0.64	($0.13)		$0.37	$1.55	$1.51	$0.03	$2.27	$1.31	N/A
SJW Group	SJW		$0.70	$0.70	$0.00		$0.50	$2.34		$2.34	$2.65	$2.03	N/A
Average			**$0.63**	**$0.62**	**($0.01)**		**$0.57**	**$2.31**	**$2.54**	**$0.01**	**$2.64**		
IPPS - Adjusted EBITDA not EPS	**US$mlns**												
NRG Energy	NRG	TBA	$543	$528	$15		$469	$1,986	$1,967	$19	N/A		$1,900-$2,100
Vistra Energy	VST	5-Aug	$819	$749	$70		$707	$3,444	$3,409	$35	N/A		$3,285-$3,585

1. UBS Confidence Indicator: Green = high confidence in estimate vs. consensus; Red = low confidence in estimate vs. consensus; Yellow = mid confidence in estimate vs. consensus
2. UBS estimates exclude corporate owned life insurance.
3. UBS estimates reflected above remove the estimated NRG Yield assets results from prior and current quarter and consensus for comparison purposes as they were sold on 8/31/18

Source: FactSet, company filings, UBS Equity Research

Regulated Utilities 2Q20 preview

Focus Stocks this Quarter

DTE Energy. Management will likely provide an update on the electric rate freeze until 2022 and the LEAP expansion which we expect is on track to go into service his quarter.

Duke Energy. In the investor call following Q2 earnings, DUK will have an opportunity to update investors on the financial impact of the ACP abandonment decision; highlighting the potential for higher spending at the Piedmont subsidiary to source replacement capacity. Also, we expect a regulatory update, both on the recent GRC decision in Indiana and the ongoing GRC in North Carolina. With an number of parties signing on to settlements that stipulate an ROE and equity layer in North Carolina, we see most contentious element of this case being the potential to earn a return on the deferred balance of coal ash remediation expenses. Should the PSC ultimately decide not to allow a return on that balance, we estimate ongoing EPS will be impacted by $0.10/share.

Evergy Inc. The Strategic Operations Committee recommendations to the Board are due July 30 and the Board decision August 17 so the timing will be interesting. We expect EVRG to continue delivering cost cuts at the higher end of the 6-9% reduction range.

PG&E Corp. With the company's first quarterly call out of bankruptcy we look for a calendar update and additional financial guidance. We also expect a discussion on preparations for fire season which has so far started without much impact.

Pinnacle West Capital. We expect an update on the general rate case following Staff testimony August 3 and the results of the August 4 primary as 3 seats on the Arizona Corporation Commission are up this year (Chairman Burns who is term-limited, Commissioner Dunn who is not running and Commissioner Marquez-Peterson).

Public Service Enterprise Group. We expect PEG to provide updates on cost cutting efforts embedded in their reiteration of annual guidance on the 1Q 2020 conference call and the COVID-19 impacts on volumes seen in 2Q 2020. We believe investors will be focused on management's updates around the energy efficiency spending program in New Jersey, and any prospects for settlement on the Transmission ROE at FERC.

Sempra Energy. We expect Sempra to report $1.65/share for 2Q 2020, well ahead of consensus estimates of $1.19. We also expect management to reiterate the 2020 eps guidance range of $7.20 - $7.80, which was recently increased from $6.70-$7.50 after closing the sales of the South American businesses. On the call management could also update 2021 guidance. Current 2021 guidance (on a GAAP basis) was provided during the March 2020 Analyst Day at $7.50-$8.10 commensurate with the original Adjusted EPS guidance for 2020 of $6.70-$7.50. Other items of interest will be an update on COVID impacts, particularly at IEnova, and the status of the last remaining permit for ECA LNG Phase 1.

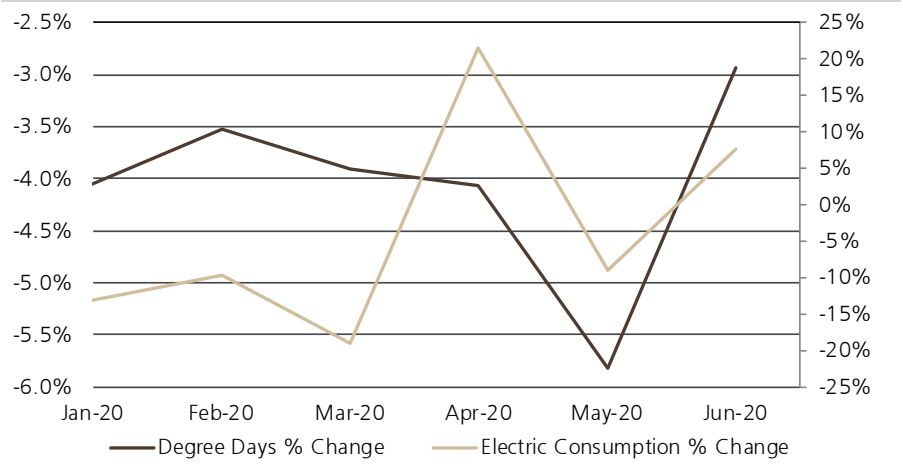
Southern Company. We expect the market to be focused on an update on the Vogtle new nuclear construction project for schedule and budget and any COVID-19 impacts to productivity.

Weather

Weather was positive in 2Q'20 as degree days rose 9% above normal and 12% above Q2'19. Weather was most favorable in the Midwest and Northeast versus Q2'19 and all regions experienced an increase in degree days.

From an electric consumption standpoint electric sales declined 4.1% in April, 5.8% in May and 2.9% in June versus 2019 including weather. We believe this was in line or better than expectations in company guidance.

Figure 5: 2Q Change in Weather versus Electric Consumption



Source: NOAA, EIA, UBS

Figure 6: Q2'20 Weather and Sales Comparisons

		Retail Sales Growth YoY										
		YTD			Deg Days vs '19		2Q'20		Deg Days vs Normal		2Q'20	
State	Decoupled?	April	April	March	May	June	VS. 2Q'19	Rank	May	June	VS. 2Q'19	Rank
Connecticut	Yes	-6.0%	-7.0%	-9.6%	12.2%	17.6%	21.1%	16	17.6%	52.2%	18.7%	2
Maine	No	-7.1%	-3.7%	-9.0%	-13.8%	10.3%	-2.3%	42	4.6%	5.3%	4.6%	42
Massachusetts	Yes	-3.5%	-5.4%	-6.0%	2.7%	71.0%	24.2%	11	7.0%	36.6%	12.9%	19
New Hampshire	No	-4.7%	-3.1%	-3.5%	-3.2%	45.9%	9.9%	27	10.1%	33.8%	10.6%	27
Rhode Island	Yes	-7.6%	-1.1%	-3.2%	0.7%	8.8%	16.1%	19	9.4%	50.0%	14.7%	14
Vermont	Yes	-4.7%	-7.6%	-4.0%	7.6%	27.0%	13.8%	21	21.2%	59.0%	18.5%	4
New Jersey	No	-5.6%	-3.8%	-8.8%	44.8%	19.6%	41.5%	2	16.7%	29.7%	15.6%	11
New York	Yes	-4.1%	-3.6%	-4.5%	22.5%	60.3%	28.7%	7	12.5%	27.6%	12.6%	21
Pennsylvania	No	-7.3%	-5.4%	-12.4%	50.0%	7.9%	36.8%	3	19.0%	23.5%	13.0%	18
Illinois	Yes	-5.0%	-7.1%	-7.8%	19.0%	37.2%	21.0%	18	5.6%	23.5%	10.2%	30
Indiana	Yes	-6.1%	-12.8%	-7.4%	23.1%	21.0%	23.5%	13	8.5%	15.5%	11.3%	26
Michigan	No	-6.8%	-15.9%	-8.3%	27.2%	43.4%	21.7%	15	15.3%	-3.3%	10.3%	28
Ohio	Partial	-5.1%	-6.1%	-9.6%	47.7%	13.4%	34.6%	4	16.0%	21.2%	13.6%	17
Wisconsin	No	-4.0%	-7.0%	-4.8%	1.4%	15.3%	7.5%	30	9.7%	-1.1%	6.5%	35
Iowa	No	-2.3%	-2.8%	-6.8%	-3.7%	14.9%	8.9%	28	9.8%	21.6%	12.9%	20
Kansas	No	-5.8%	-6.8%	-7.3%	-3.0%	42.9%	22.9%	14	0.5%	30.0%	14.2%	15
Minnesota	Yes	-3.9%	-7.3%	-6.2%	-13.7%	11.6%	0.6%	37	5.6%	-6.2%	6.7%	34
Missouri	No	-5.4%	-4.6%	-8.2%	2.2%	27.3%	23.7%	12	1.7%	17.7%	12.5%	23
Nebraska	No	-2.5%	-2.6%	-5.3%	-13.3%	32.4%	13.5%	23	9.1%	32.4%	16.3%	8
North Dakota	No	2.6%	5.7%	2.7%	-12.6%	4.4%	3.9%	34	14.7%	-2.7%	12.1%	24
South Dakota	No	-3.9%	-4.3%	-7.0%	-16.5%	14.7%	2.2%	35	6.8%	7.1%	9.2%	31
Delaware	Yes	-5.1%	-0.3%	-7.8%	19.7%	3.3%	29.8%	6	38.6%	32.6%	19.2%	1
District of Columbia	Yes	-7.9%	-8.0%	-16.8%	-9.3%	5.5%	14.5%	20	24.4%	18.1%	13.8%	16
Florida	No	1.4%	3.4%	3.3%	-16.0%	-6.2%	-3.8%	43	4.2%	7.8%	16.6%	7
Georgia	No	-3.0%	-8.5%	-2.6%	-23.0%	-3.7%	-10.2%	47	19.0%	4.0%	6.3%	36
Maryland	No	-7.7%	-1.9%	-13.1%	22.6%	-3.8%	31.6%	5	24.5%	19.4%	15.3%	13
North Carolina	Yes	-3.4%	-8.1%	-4.7%	-10.8%	3.0%	1.8%	36	41.4%	11.5%	18.3%	5
South Carolina	No	-2.9%	-10.4%	-0.2%	-26.3%	-0.8%	-12.2%	50	22.9%	4.1%	10.2%	29
Virginia	No	-5.9%	-1.5%	-6.1%	12.0%	6.0%	26.5%	9	37.9%	20.1%	17.7%	6
West Virginia	No	-4.6%	0.1%	-10.6%	61.2%	3.7%	46.2%	1	30.6%	4.9%	16.0%	9
Alabama	No	-3.1%	-8.5%	-2.7%	-20.4%	-6.5%	-10.5%	48	16.5%	7.5%	6.0%	37
Kentucky	No	-4.7%	-7.1%	-7.7%	15.2%	0.8%	26.7%	8	19.3%	4.1%	12.1%	25
Mississippi	No	-1.7%	-2.9%	0.5%	-15.6%	-1.7%	-7.8%	45	16.9%	4.1%	5.3%	40
Tennessee	No	-4.0%	-6.6%	-3.4%	4.0%	3.7%	13.7%	22	28.6%	4.0%	15.5%	12
Arkansas	No	-3.9%	-5.9%	-5.4%	-19.9%	6.0%	0.1%	38	-2.0%	3.8%	4.7%	41
Louisiana	No	-0.5%	1.2%	1.1%	-16.4%	-7.4%	-8.5%	46	3.8%	-1.6%	6.0%	38
Oklahoma	No	-3.1%	-5.1%	-1.6%	-6.1%	22.1%	21.1%	17	0.5%	14.1%	15.9%	10
Texas	Partial	1.0%	3.1%	3.0%	0.0%	3.5%	4.1%	33	14.3%	5.5%	12.6%	21
Arizona	No	-1.5%	-1.1%	-3.4%	100.0%	-1.0%	25.8%	10	5.7%	-7.7%	-4.5%	46
Colorado	No	-0.3%	-4.0%	-1.8%	-39.9%	-10.9%	-10.8%	49	-24.1%	-18.9%	-11.8%	47
Idaho	Yes	0.1%	2.6%	-3.2%	4.9%	23.5%	10.6%	26	3.4%	8.5%	5.5%	39
Montana	No	-4.3%	3.4%	-8.8%	-7.8%	17.3%	7.7%	29	3.7%	-0.4%	8.1%	33
Nevada	Yes	0.6%	-6.8%	2.1%	-0.5%	-13.3%	12.2%	24	-35.4%	-24.8%	-20.0%	49
New Mexico	No	2.5%	-4.0%	3.9%	-32.1%	12.8%	-1.7%	39	-32.1%	-8.6%	-16.4%	48
Utah	No	-0.3%	-4.3%	1.6%	-27.3%	24.6%	-2.1%	41	-11.3%	-3.6%	-3.1%	45
Wyoming	No	-4.8%	-11.0%	-6.5%	-26.7%	-21.9%	-6.4%	44	-4.8%	-27.0%	-1.0%	44
California	Yes	-3.5%	-4.4%	-2.3%	-37.8%	6.6%	5.7%	32	-41.2%	-29.1%	-21.5%	50
Oregon	Partial	-2.1%	-2.0%	-0.7%	14.2%	14.3%	6.0%	31	9.0%	29.0%	8.8%	32
Washington	Yes	-4.2%	-3.2%	-6.1%	21.5%	18.5%	11.4%	25	-3.5%	15.3%	2.7%	43
Hawaii	No	-0.3%	-13.7%	4.3%	-3.1%	-2.0%	-2.0%	40	20.4%	17.0%	18.6%	3

Source: EIA, NOAA, UBS

Electric Utilities

AES Corp

We estimate Q2'20 EPS of $0.21 versus $0.26 last year. We assume a -$0.04/share impact from COVID globally of the $0.06-$0.07/share the company identified on the Q1 call. We do not see a material impact from sensitivities. A knowable driver is the absence of the Ohio rider which we estimate is -$0.01/share. We look forward to an update on where AES stands with S&P, renewable PPA origination and the company's progress to reduce coal generation to 30% of total by year-end.

Alliant Energy

We estimate an increase in LNT's EPS to $0.57 versus $0.40 last year. We estimate a strong comparison due to rate relief at IP&L and WP&L (+$0.16/share) and the first half of 2020 tax timing from wind production credits. We estimate this added $0.06/share in Q2'20 versus the $0.08/share in Q1'20. We estimate a small net negative impact from the combination of weather normalized sales and cost cuts. We expect LNT to discuss progress on the Wisconsin rate freeze proposal and solar filing.

Figure 7: LNT Q2'20 EPS Drivers

Q2'19	$0.40
Weather to Normal	$0.02
Weather Below Normal	$0.01
IP&L & WP&L Rates	$0.16
Tax timing - PTCs	$0.06
O&M	$0.03
Interest Expense	-$0.01
Dilution	-$0.02
Depreciation/other	-$0.03
Weather Normalized Demand	-$0.05
Q2'20 Estimate	$0.57

Source: Company reports, FactSet, UBS Equity Research

Ameren Corp

We forecast EPS for AEE of $0.85 versus $0.72 last year. Weather likely helped offset the impact of lower demand. Ameren assumes a -$0.10/share impact from lower Ameren Missouri sales in 2020 (-7%: +2.5% Residential, -15% Commercial and -10% Industrial). The absence of a Callaway outage likely added $0.08/share. We estimate a mark-to-market of the Illinois formula distribution ROE is a -$0.03/share impact versus 2019.

Figure 8: AEE Q2'20 EPS Drivers

Q2'19	$0.72
Weather to Normal	$0.06
Weather versus Normal	$0.05
Callaway Outage	$0.08
Missouri Rates	$0.02
IL Rate base Growth	$0.01
Interest Expense	-$0.01
IL Electric Distribution ROE (7.3% vs. 8.8%)	-$0.03
Demand	-$0.05
Q2'20 Estimate	$0.85

Source: Company reports, FactSet, UBS Equity Research

American Electric Power

We forecast AEP EPS of $1.08 versus $1.00 last year. The absence of a transmission true-up at AEP Transco is a -$0.08/share impact absent a similar development. At the 2019 EEI conference AEP identified $0.19/share of cost cuts at the Vertically Integrated Utilities and $0.14/share at the T&D Utilities which will help offset a demand reduction. Overall we expect T&D utility rates will be slightly higher net of the absence of the legacy rider in Ohio.

Figure 9: AEP Q2'20 Earnings Drivers by Segment

Q2'19	$1.00
Vertically Integrated ($0.50 v. $0.38)	
Weather to Normal	$0.01
Weather vs Normal	$0.02
Operations and Maintenance	$0.07
Transmission	$0.05
Rates	$0.03
Other	-$0.01
Load	-$0.02
Depreciation	-$0.03
T&D Utilities ($0.31 v. $0.27)	
Transmission	$0.04
Operations and Maintenance	$0.03
Rates	$0.02
Depreciation	-$0.02
Tax Carrying Charge	-$0.03
AEP Transmission ($0.25 v. $0.31)	-$0.06
Generation & Marketing ($0.07 v. $0.06)	$0.01
Corp and Other (-$0.05 v. -$0.02)	-$0.03
Q2'20 Estimate	$1.08

Source: Company reports, FactSet, UBS Equity Research

ATCO Ltd

We expect ATCO Ltd to report 2Q 2020 adjusted eps of C$0.55 vs. C$0.55 consensus estimates and C$0.68 last year. The largest negative drivers in the quarter are the asset divestitures of the Alberta Power Line and the Canadian competitive generation assets. Further, we expect lower earnings contributions from Neltume Ports on economically driven lower trade volumes, slightly higher corporate expenses, and lower earnings year on year at the Australian gas distribution utility on lower ROE and flat CPI adjustor. Partially offsetting these negative drivers will be higher earnings at the Structures business driven by LNG Canada completing the manufacturing phase and rate base growth at the electric distribution and Canadian gas utilities.

Figure 10: ATCO Ltd. 2Q 2020 Drivers

2Q 2019 EPS	**$ 0.68**
2Q 2019 Cons. Adj. Earnings	78
Naltume Ports	(2)
Corporate Drag	(2)
Canadian Utilities	(3)
S&L	4
Sale of Power & Alberta Power Line	(8)
Australia lower RB growh/ROE/CPI	(4)
2Q 2020 Cons. Adj. Earnings	**63**
Shares	114.3
2Q 2020 EPS	**$ 0.55**

Source: UBS Equity Research Estimates

Canadian Utilities

We expect Canadian Utilities to report 2Q 2020 adjusted eps of C$0.35 vs. consensus estimates of C$0.35 and C$0.38 last year. Results will be driven by the sale of the Alberta Power Line and the Canadian generation assets, higher corporate expenses year on year, and lower earnings at the Australian gas utility business on lower rate base growth, lower allowed ROE, and a lower CPI adjustor year on year. This will be mostly offset by rate base growth at the electric distribution and Canadian gas utilities.

Caribbean Utilities

We expect Caribbean Utilities to report 2Q 2020 eps of $0.19 vs. consensus estimates of $0.18, and $0.24 last year. The biggest driver of year on year results will be lower electric volumes due to a significant decline in by air and by sea tourism visits to Grand Cayman. This will be partially offset by lower O&M as a result of lower volumes as well as cost discipline.

CMS Energy

We expect an increase for CMS' EPS to $0.48 versus $0.33 last year. Weather and cost cuts likely helped offset the impact of lower demand due to COVID. NOAA data shows a 24% increase in degree days from last year and 11% above normal. Michigan manufacturing returned in May and retail in June at or ahead of the company's plan. MISO load was -15% in April and gradually recovered to flat in July including weather. Cost cuts included the company's CE Way, employee benefits and COVID-related impacts like mileage reimbursement.

Figure 11: CMS Q2 EPS Drivers

Q2'19	$0.33
Weather to Normal	$0.06
Weather	$0.10
O&M reinvestment	$0.06
Gas Rates	$0.06
Pension	$0.02
Enterprises and Enerbank	$0.01
Debt and Dilution	-$0.02
Demand	-$0.07
Depreciation, Interest and Other	-$0.07
Q2'20 Estimate	$0.48

Source: Company reports, FactSet, UBS Equity Research

Consolidated Edison

We forecast ED EPS of $0.52 versus $0.58 last year. We do not expect ED to move off its 2020 EPS guidance reduction of $0.15/share to $4.15-$4.35. We assume lower results at Consolidated Edison Company of New York ($0.41 versus $0.46) which is decoupled but the lower EPS reflects the costs of doing work with social distancing which raised costs. CECONY and other New York investor owned utilities filed comments with the New York Public Service Commission to: 1) Allow for deferral of net costs of COVID-19; 2) Establish mechanisms to mitigate cash flow stress like riders and 3) Declare COVID-19 a pandemic crisis that justifies excusing a utility from meeting a rate plan performance metric.

Dominion Energy

We expect Dominion Energy to report adjusted 2Q EPS of $0.78/share; this is modestly below the mid-point of the original guidance for the quarter of $0.75-$0.85/share and includes earnings from both the company's midstream and ACP assets. We expect that in conjunction with its Q3 earnings release (later in the year), Dominion will restate earnings from the first and second quarter to reflect the discontinued nature of those midstream and pipeline operations, consistent with its restated guidance for 2020 of $3.37-$3.63 and 2021 of $3.85-$3.90.

Year/Year second quarter earnings will benefit from continued investment in Dominions regulated business lines, higher capacity revenues in PJM, lower depreciation expense due to the early retirement of coal plants and life extension of nuclear plants, and very modestly lower interest expenses. These benefits will be offset by lower earnings from Cove Point, lower capacity earnings at the Millstone nuclear plant and equity dilution. Our earnings forecast assumes that any negative impact from the Covid-19 economic slowdown will be offset by lower O&M expenses, and that below normal weather in the quarter will have a negative earnings impact..

We expect Dominion's second quarter investor call will focus on the future goals of the company; its increasing focus on regulated earnings, an improving balance sheet, renewable generation development and zero carbon and methane emissions by 2050. In this context we expect the refreshed EPS and dividend growth target of 6.5% and 6% respectively, to be reiterated.

Figure 12: Dominion Energy Q2'20 EPS Drivers

Q2'19	$0.75
Weather - Weaker vs. normal	-$0.02
Regulated Investment Growth	$0.07
Capacity - New Gen	$0.04
Nuclear & Asset life Extension	$0.02
Interest Expense	$0.00
Cove Point - Lower Ownership	-$0.03
Millstone - Lower capacity revenues	-$0.01
Equity Dilution	-$0.04
Covid-19 - Demand Shift/O&M Savings	$0.00
Q2'20 Estimate	$0.78

Source: UBS Equity Research, Company Reports, FactSet

DTE Energy

We forecast lower EPS of $1.51 versus $0.99. Overall, DTE seems on track for the year. We expect favourable weather versus last year (+$0.05/share) and normal (+$0.16/share) benefitted the second quarter result. The company likely saw a higher mix of residential sales which provides for a greater impact from a rise in degree days. DTE Electric recovered the impacts of 2 rate cases. Share based incentive comp was a -$0.18/share impact in Q1 due to a lower stock price but recovered in Q2. DTE is progressing with the LEAP expansion to the Blue Union expansion which they expect to complete in Q3. Lower demand from DTE Electric from waste coal REF sales could impact the Power & Industrials business.

Figure 13: DTE Q2'20 EPS Drivers

Q2'19	$0.99
DTE Electric weather	$0.18
DTE Electric sales	-$0.17
DTE Electric rate case recovery	$0.20
DTE Electric Share based incentive comp	$0.11
DTE Electric O&M	$0.08
DTE Gas weather	$0.03
DTE Gas rate base	$0.03
GS&P - similar to 1Q'20	$0.12
Power & Industrials - lower utility waste coal to DTE Electric	-$0.01
DTE Energy Trading	$0.02
Corp & Other	$0.01
Dilution (192M versus 182M)	-$0.08
Q2'20 Estimate	$1.51

Source: Company reports, FactSet, UBS Equity Research

Duke Energy

We expect Duke Energy to report adjusted 2Q'20 EPS of $1.00 vs. a weather adjusted Q2'19 result of $1.04. The most significant variable (and source of uncertainty) in Q2'20 earnings will be the impact of the Covid-19 related economic shutdown and the related O&M savings the company can realize as an offset. Our estimate assumes a negative EPS impact of $0.19 (reflects residential demand +5%, commercial demand -15%, industrial demand -20%) offset by O&M savings of $0.12. Beyond the impact of lower demand in the quarter, higher rates, investment in renewables and the gas LDC business will be offset by higher depreciation, interest and equity dilution.

We expect DUK's investor call will focus on the company's regulatory calendar (Indiana & North Carolina), potential need for additional capital spending at its gas LDC (following the cancelation of ACP) and the potential outcome of the Governors upcoming clean energy plan.

Figure 14: Duke Energy Q2'20 EPS Summary

Q2'19	$1.04
Weather impact	$0.01
Demand Impact of Covid-19 Shut down	-$0.19
O&M Savings to Offset Covid-19 Impact	$0.12
FL/NC/SC rates & riders	$0.05
Gas LDC & Pipeline (net)	$0.01
Wholesale Contracts & Renewables	$0.02
Depreciation & Interest Expense	-$0.05
Equity Dilution	-$0.01
Q2'20 Estimate	$1.00

Source: UBS Equity Research, Company Reports, FactSet

Edison International

We forecast EPS of $1.16 versus $1.58 last year. Our EIX jurisdictional revenue impact includes the absence of a $0.20/share benefit from a revenue true-up from the rate case along with an attrition year impact. EIX also likely experienced higher costs related to insurance and its wildfire plan and we do not expect a similar year-on-year impact to O&M (-$0.30/share) as we are looking for in this quarter.

Figure 15: Edison International Q2'20 EPS Summary

Q2'19	$1.58
California Jurisdictional Revenue	$0.06
FERC Transmission Revenue	$0.04
Depreciation	-$0.02
Financing	-$0.03
O&M	-$0.30
Corporate Expenses	-$0.01
Dilution (378M vs. 331M avg shrs)	-$0.16
Q2'20 Estimate	$1.16

Source: Company reports, FactSet, UBS Equity Research

Emera Inc

We expect Emera Inc. to report 2Q 2020 adjusted eps of C$0.52 vs. C$0.58 consensus estimates and C$0.54 last year. Normalizing the C$0.54 in 2Q 2019 for the Emera Maine asset sale yields C$0.49. Drivers off of this normalized level last year will by rate base growth in Florida, slightly better results in Nova Scotia, and positive impacts from FX due to a stronger USD/CAD year over year. Mostly offsetting these positive drivers will be lower results at Emera Energy due to lower natural gas price volatility, the $12mln one time regulatory decision impact at New Mexico Gas in 2Q 2019, and slightly higher corporate expenses and share dilution.

Figure 16: Emera Inc. 2Q 2020 Drivers

2Q 2019	**$**	**0.54**
Maine Asset Sale	$	(0.05)
2Q'19 Normalized	**$**	**0.49**
FL Electric	$	0.03
Emera Energy	$	(0.02)
Gas Utes & Infra	$	0.04
Canadian	$	0.01
One-Time NM Reg. Dec.	$	(0.04)
FX	$	0.03
Other/Parent	$	(0.02)
4Q 2019	**$**	**0.52**

Source: UBS Equity Research Estimates

Entergy Corp

We expect Entergy Corp. to report adjusted 2Q'20 EPS of $1.30 vs. a weather adjusted Q2'19 result of $1.29. Second quarter earnings will benefit from a step up in regulated earning related the company's formulaic rate plans and tracking mechanisms, offset by higher depreciation, interest and tax expense and equity

dilution. We estimate that slowdown associated with the Covid-19 pandemic could impact earnings by up to $0.15 in the quarter (retail +4%, commercial -15%, industrial -10%) but that some portion of that will be offset by O&M cost reductions (we assume $0.11).

We expect ETR will affirm its 2020 full year earnings guidance of $5.45-$5.75, its EPS CAGR through '22 of 5-7% and its plans for a fall investor day when it will expand the current three year forward look that includes both EPS and capital spending plans to a five year look forward.

Figure 17: Entergy Q2'20 EPS Summary

ETR - Earnings Walk Q2'19-Q2'20				Q2'19
EPS as reported Q2'19				$1.35
Adjustments (weather benefit)				($0.06)
Q2'19 Operating EPS				$1.29
	Annual Impact (mm)	After Tax Q2 (mm)	Per Share	
E - LA Saint Charles SCPS	$110.0	$13.75	$0.07	
E - MS FRP ($33/$18 net of D&A)	$18.0	$3.38	$0.02	
E - LA FRP	$25.0	$4.69	$0.02	
E - MS Chowtaw	$59.0	$11.06	$0.06	
E - NO Rate Case	(15.00)	(2.81)	(0.01)	
E - AR FRP	$57.0	$10.69	$0.05	
AMI Annual Rider	$20.0	$3.75	$0.02	
E - TX TCRF	$17.0	$2.13	$0.01	
E-LA Lake Charles Power Station	$108.0	$13.50	$0.07	
E-MS FRP	$23.8	$2.98	$0.01	$0.31
	Annual Impact			
Annual Guidance from ETR:	(EPS)		Qtrly Impact	
Regulated Utility:				
O&M	$0.05		($0.01)	
Nuclear Refuel Expense	$0.05		$0.02	
Depreciation Expense	($0.70)		($0.18)	
Net Interest Expense (wgted in 2H)	($0.40)		($0.08)	
Effective Income Tax	($0.15)		($0.05)	
Share Count	($0.14)		($0.04)	($0.33)
Parent & Other:				
Effective Tax Rate	$0.07		$0.02	
Share Count	$0.03		$0.01	$0.03
Covid-19 Related Damand Loss			($0.15)	
O&M Savings			$0.11	($0.04)
Projected Weather Benefit				$0.04
Q2 2020 EPS Estimate				$1.30

Source: UBS Equity Research, Company Reports, FactSet

Eversource Energy

We expect Eversource Energy to report 2Q'20 EPS of $0.75 vs $0.70 in the prior year quarter (adjusted for a $0.04 gain on landfill gas investments). Q2'20 EPS will benefit from continuing investment in the regulated utility business, the transmission system and the gas LDC business (through pipeline replacement). Higher depreciation, property tax and interest will be a modest drag on earnings for the quarter. We expect ES will reiterate its full year earnings guidance $3.60-$3.70, EPS growth rate of 5-7% and capital spending plans.

On the investor call following the earnings release we expect ES to update investors on ongoing regulatory proceedings including its New Hampshire general rate case, the approval of its Columbia Gas acquisition and the RFP process addressing grid modernization in Connecticut.

Figure 18: Eversource Energy Q2'20 EPS Drivers

Q2'19	$0.70
Regulatory actions (Nstar/CL&P/PSNH)	$0.06
Transmission investment	$0.03
Gas pipe trackers	$0.01
O&M/Depreciation/Tax	-$0.02
Weather (NH)	$0.01
Equity Dilution	-$0.04
Q1'20 Estimate	$0.75

Source: UBS Equity Research, Company Reports, FactSet

Evergy Inc.

We forecast EPS of $0.63 versus $0.57 last year excluding the impact of income from corporate owned life insurance. Above normal weather and cost cuts will offset the impact of lower weather normalized sales. EVRG's guidance for O&M cuts is 6-9% from $1.187B and we assume the higher end of the range. On the financing side we see an impact from the issuance of $1.6B of parent debt.

Figure 19: EVRG Q2'20 EPS Drivers

Q2'19 Estimate	$0.57
Weather to Normal	$0.04
Weather	$0.04
Weather Normal Sales	-$0.08
O&M	$0.09
KCP&L refinancing and term loan	$0.01
Other	-$0.01
Depreciation	-$0.02
Interest on $1.6B parent debt	-$0.02
Share buyback	$0.01
Q2'20 Estimate	$0.63

Source: NOAA, Company reports, FactSet, UBS Equity Research

Exelon Corp

We expect Exelon to report 2Q 2020 adjusted EPS of $0.45 vs. $0.45 consensus and $0.60 last year. Drivers at ExGen are expected to be poorer market and portfolio conditions, volume degradation from COVID-19 dislocations particularly at the Constellation C&I retail segment, higher nuclear refueling outages year on year, and lower capacity prices for two of the three months of the quarter. These negative drivers will be partially offset by incrementally higher ZEC revenues and lower O&M. At the utilities we expect a drag from the distribution ROE formula in Illinois and volumes at PECO, which will be more than offset collectively by weather at PECO, distribution investment at ComEd, the distribution rate increase at BGE and rate increases at PHI.

Figure 20: Exelon 2Q 2020 Drivers

2Q 2019	**$**	**0.60**
ExGen		
Lower O&M	$	0.06
NDT Fund Losses	$	(0.02)
ZEC Revenues	$	0.02
Market & Portfolio Conditions	$	(0.10)
Nuclear Outages	$	(0.02)
Capacity Revenue	$	(0.11)
ComEd		
Distribution Formula Rate Timing	$	(0.02)
Distribtution Investment	$	0.02
PECO		
Volumes/Weather	$	(0.03)
BGE		
Distribution Rate Increases	$	0.03
PHI		
Rate Increases	$	0.02
Corporate		
Other	$	0.01
1Q 2020	**$**	**0.45**

Source: UBS Equity Research Estimates

FirstEnergy Corp.

We forecast $0.53 of EPS versus $0.61 last year. FE previously provided a guidance range of $0.48-$0.58/share. We do not expect weather had a significant impact across FE's service territory and the final quarter of the expiration of the Ohio distribution modernization rider is -$0.06/share. We estimate that other riders contributed from Ohio and Pennsylvania $0.02/share. The company incurred interest expense for the Energy Harbor payment but is now a fully regulated utility.

Figure 21: FE Q2'20 EPS

Q2'19	$0.61
Normal Weather	$0.01
Weather Normalized Distribution Deliveries	-$0.02
Ohio Distribution Modernization Rider	-$0.06
Other Rider Recovery	$0.02
O&M Reduction	$0.01
Other Financing	-$0.01
Depreciation	-$0.01
General Taxes	-$0.01
Transmission Growth	$0.02
Transmission O&M	-$0.01
Parent and Transmisison Financing	-$0.02
Q2'20 Estimate	$0.53

Source: Company reports, FactSet, UBS Equity Research

Fortis Inc.

We expect Fortis Inc. to report 2Q 2020 adjusted eps of C$0.57 vs. C$0.58 consensus estimates and C$0.54 last year. Drivers year on year will be rate base growth at the western Canadian utilities, rate base growth at ITC, rate design timing and rate base growth at Central Hudson and slightly better results at energy infrastructure with better rainfall in Belize and slightly better margins at Aitken Creek storage. Offsetting these positive drivers are higher weighted average shares from the C$1.2Bln equity issuance completed in late 2019, and slightly lower results at UNS. Results at UNS will be driven by higher costs year on year on yet in rate base given the ongoing rate case in Arizona, and lower volumes related to coronavirus dislocations. These negative drivers are mostly offset by warmer weather and the partial reversal of the pension loss recorded in 1Q 2020.

Figure 22: Fortis Inc. 2Q 2020 Drivers

2Q 2019	**$**	**0.54**
Western CA Elec & Gas	$	0.03
US Transmission - ITC	$	0.03
Central Hudson	$	0.02
Energy Infrastructure	$	0.02
Corp & Other	$	-
UNS Energy	$	(0.01)
Wtd. Avg. Shares	$	(0.06)
2Q 2020	**$**	**0.57**

Source: UBS Equity Research Estimates

Hawaiian Electric

We expect HE to report adjusted 2Q'20 EPS of $0.40 vs. $0.39 in the prior year quarter. Earnings in the quarter will be driven by the regulated utility, with growth through the tracking and recovery mechanisms and O&M efficiency, offset only

modestly by higher depreciation expense. We expect HE's American Savings Bank subsidiary will report lower earnings than in the prior quarter ($0.10 vs. 0.14) due to the challenged economic environment in the state of Hawaii (closed to tourists till September). American Savings bank will report earnings on the evening of July 30.

We expect HE will reiterate its full year utility earning guidance of $1.46-$1.54, but will not reinstate earnings guidance for American Savings Bank given the continued economic uncertainty in the state. Further, we expect an update on the ongoing regulatory proceedings (PBR), cost saving initiatives and capital spending plans.

Figure 23: Hawaiian Electric Q2'20 earnings summary

Q2'19 - Utility	$0.30
Regulatory actions (RAM/MPIR etc.)	$0.06
O&M efficiency	$0.01
Depreciation	-$0.01
Q2'20 Estimate	$0.36
Earnings Composition	
Utility	$0.36
Bank	$0.10
Hold Co. & Other	-$0.06
Q2'20 Estimate	$0.40

Source: UBS Equity Research, Company Reports, FactSet

Hydro One

We expect Hydro One to report 2Q 2020 adjusted eps of C$0.32 vs. C$0.27 consensus and C$0.26 last year. Results will be mainly driven by strong weather in May and June driving peak demand load higher which impacts transmission segment earnings. OM&A expenses are also likely to be lower given higher vegetation management and storm cost expenses in 2Q 2019 as well as stand down of work crews in part of April 2020. Some of those lower cost drivers will be partially offset by higher COVID-19 related mitigation costs. Revenues will also be up year on year related to the transmission rate order from the Ontario Energy Board, and the one-time regulatory dispositions and catch up items to be booked this quarter as a result.

Figure 24: Hydro One Estimates and Actual Results 2Q 2020 vs. 2Q 2019

C$mlns	2Q 2019A	2Q 2020E
Revenue Net of Purch. Power	760	814
OM&A Costs	267	259
D&A	221	221
Finance Charges	117	119
Income Taxes	(6)	15
Other/NonCont/Pref. Divs	6	7
Net Income to Common	155	193
Shares Outstanding	595	595
Reported EPS	$ 0.26	$ 0.32
Items	-	-
Adj. NI	155	193
Shares Outstanding	595	595
Adjusted EPS	**$ 0.26**	**$ 0.32**

Source: UBS Equity Research Estimates

NextEra Energy

We expect NextEra Energy to report 2Q 2020 adjusted eps of $2.49 vs. $2.49 consensus and $2.35 last year. Given the move of transmission from the corporate segment to the Energy Resource segment the comparable segment break-out for 2Q 2020 is $0.97 at Energy Resources and $0.01 at Corporate & Other. Drivers in the quarter will be rate base investments at FPL and at Gulf Power. From a retail sales perspective vs. the prior two year average was +5.4% in April and (2.4%) in May as coronavirus dislocations on volumes were not as large as expected and significantly warmer weather (particularly in April) offset some of the negative volume impacts. At the end of last quarter FPL had a reserve balance of $744mln. At Energy Resources the drivers will be new investment and better results at existing resources given the 92/93% wind resource in 2Q 2019. Offsetting these positive impacts will be a drag from customer supply and trading and an outage at Seabrook. At Gulf we expect largely flat year on year results and at Corporate & Other we expect increased interest expense given debt issuance at the parent of $1.25Bln in April at 2.75%, and $2Bln in May at 2.25%. There will also be some share dilution year on year given equity unit share issuances in September 2019 and February 2020.

OGE Energy

We forecast EPS of $0.50 versus $0.50 last year. From a GAAP basis OGE's remaining 2020 results will include an offsetting $0.26/share consolidating tax adjustment benefit for the remainder of the year related to the Enable write-down. We do not include that in our EPS estimates. Below normal weather and lower demand likely kept results similar to Q2'19. Rate case recovery and cost cuts likely helped OGE.

Figure 25: OGE Q2'20 EPS Summary

Q2'19	$0.50
Weather to Normal	$0.07
Weather	-$0.03
Rates	$0.09
O&M	$0.02
Interest Expense	-$0.01
Depreciation	-$0.05
Sales	-$0.08
ENBL	-$0.01
Q2'20 Estimate	$0.50

Source: Company reports, FactSet, UBS Equity Research

PG&E Corp.

We estimate Q2'20 EPS forecast of $0.84 versus $1.10 last year. The company will report earnings and should provide 1 or more years of annual EPS and potentially net income guidance. We estimate 695M shares outstanding using an average method and reflecting 2 trading days post close of the block equity (97% at 647M and the remaining 3% at the 2153M maximum) versus 529M last year. Other drivers are rate base (+$0.02/share and energy efficiency (+$0.01/share) as positives. We estimate negative drivers of unrecoverable interest and legacy O&M.

Figure 26: PCG Q2'20 EPS Summary

Q2'19	$1.10
Rate base Growth	$0.02
Energy Efficiency	$0.01
Timing of Taxes	-$0.01
Unrecoverable interest/other	-$0.02
Shares outstanding (695M vs. 529M)	-$0.26
Q2'20 Estimate	$0.84

Source: Company reports, FactSet, UBS Equity Research

Pinnacle West Capital

We forecast $1.55 of EPS versus $1.28 last year. Weather which impacted residential demand and cost cuts led the quarter. The impact of May weather (194 versus 107 degree days) is an important driver. PNW disclosed that the impact from March 13 to May 26 was -$0.14/share versus the company's initial expectation and that a 1% change in sales is $0.16-$0.20/share on an annual basis. PNW disclosed that residential sales rose 4% and commercial and industrial sales fell 4% versus 2019 from May 13 to June 16. There was 1 fewer planned outage and we expect PNW worked to offset the impact of lower demand through cost cuts.

Figure 27: PNW Q2'20 EPS Summary

Q2'19	$1.28
Weather to Normal	$0.22
Weather versus Normal	$0.05
O&M	$0.13
Pension and Other	$0.06
Other	$0.01
Sales	$0.01
LFCR	-$0.01
Interest	-$0.01
Depreciation and Taxes	-$0.03
Demand	-$0.16
Q2'20 Estimate	$1.55

Source: Company reports, FactSet, UBS Equity Research

PNM Resources

We expect PNM Resources to report Q2'20 EPS of $0.50 vs. $0.44 in the prior year quarter. Better weather in 2Q'20 is expected to offset the negative impact of the Covid-19 related shift in demand (-$0.02 in both April & May), along with rate base growth and the absence of a San Juan maintenance outage. Interest expense, depreciation and property have a modestly negative impact on the quarter. In conjunction with the disclosure of its earnings release date (July 31), PNM affirmed its annual EPS guidance of $2.16-$2.26 (targeting the mid-point).

On its investor call we expect PNM will update investors on its ongoing proceeding in New Mexico to replace the power provided by the San Juan coal plant (decision deadline is October 1), the potential to retire the Four Corners generation station and any possible updates to the capital spending plan.

Figure 28: PNM Resources Q2'20 EPS Sumary

Q2'19	$0.44
Retail rate phase in (PNM & TNMP)	$0.05
Retail load growth (PNM & TNMP)	$0.00
Weather improvement	$0.00
O&M improvement	$0.00
Depreciation & property tax	-$0.05
Interest Expense	$0.00
San Juan Outage Costs	$0.04
Transmission/Renewables/AFUDC	$0.02
Q2'20 Estimate	$0.50

Source: UBS Equity Research, Company Reports, FactSet

Portland General Electric

We forecast $0.34 of EPS versus $0.28 last year. Weather conditions were slightly below normal in POR's region with heating degree days down 13% and cooling degree days up 11%. POR's 1-2% sales baseline would imply a $0.15/share reduction for the balance of the year. The company's guidance on non-fuel O&M

would imply a $0.10-$0.15/share reduction per quarter. Depreciation could fall in the $104-$106M range per quarter using the $410-$430M guidance and $108M in Q1'20. We also expect an impact related to the non-qualified benefit program. POR had no portfolio changes but the recovery in the markets should help reverse some of the -$0.06/share impact in 1Q'20. We expect an update on regulation in Oregon on the investor call although no resolution on the COVID-19 docket until 2022.

Figure 29: POR Q2'20 EPS Summary

Q2'19	$0.28
Weather to Normal	$0.04
Weather Normalized Demand	-$0.07
Non-Fuel Operations and Maintenance	$0.13
Employee Benefits	$0.03
Depreciation	-$0.02
PCAM to the Baseline	-$0.05
Q2'20 Estimate	$0.34

Source: Company reports, FactSet, UBS Equity Research

PPL Corporation

We expect lower EPS of $0.57 versus $0.58 last year. In general F/X hedges (86% hedged at 1.55x) and small benefits from weather in Kentucky and the U.K. helped to offset the pandemic impacts and dilution. PPL continues to benefit from returns on transmission investment Pennsylvania.

Figure 30: PPL Q2'20 EPS Summary

Q2'19	$0.58
Kentucky weather versus normal	$0.01
Weather normalzized KY sales	-$0.03
F/X 1.51x '20 vs 1.36x '19 Pound/US$	$0.03
Kentucky Rate Case	$0.02
Other Expenses	-$0.01
Transmission	$0.01
U.K. weather	$0.01
Other U.K.	-$0.02
Dilution (770M versus 730M shares)	-$0.02
Q2'20 Estimate	$0.57

Source: Company reports, FactSet, UBS Equity Research

Public Service Enterprise Group

We expect Public Service Enterprise Group to report adjusted eps of $0.59 vs. $0.62 consensus and $0.58 last year. At PSE&G we expect positive drivers of continued rate base growth, better weather year on year, lower distribution O&M, and better pension and OPEB. Partially offsetting these positive drivers are lower volumes as a result of coronavirus dislocations, and higher D&A, interest expense, and taxes. At PEG Power we expect positive drivers related to NJ ZECs for a full quarter in 2020 vs. 2019, lower O&M on cost controls, and lower D&A as a result of the extension of the Peach Bottom operating license to 80 years and the sale of

the Hudson and Mercer retired coal generation stations in January to Hilco Redevelopment Partners. Bridgeport Harbor 5 also went into service year on year increasing volumes at PEG Power all else equal. More than offsetting these positive drivers will be volume declines related to coronavirus dislocations and lower capacity prices in April and May, while price for the new capacity year took effect in June. At corporate and other we expect slightly higher taxes and slightly higher interest expense relate the $800mln in term loans in March and April.

Figure 31: PEG 2Q 2020 Drivers

PEG Consolidated	2Q 2019A	2Q 2020E
	$ 0.58	**$ 0.59**
PSE&G		
2Q 2019	**$ 0.45**	
Transmission	$ 0.06	
Weather/Load	$ (0.02)	
Gas Margin	$ 0.01	
Distribution O&M	$ 0.02	
D&A, Int.	$ (0.02)	
Pension, OPEB	$ 0.02	
Taxes & Other	$ (0.02)	
2Q 2020	**$ 0.50**	
PSEG Power		
2Q 2019	**$ 0.13**	
ZECs	$ 0.02	
Capacity Prices	$ (0.05)	
Re-Contracting Mkt	$ (0.01)	
Volume	$ (0.02)	
O&M	$ 0.06	
Int. Exp.	$ (0.01)	
Lower Gas Sendout	$ (0.01)	
1Q 2020	**$ 0.11**	
Enterprise/Corporate		
2Q 2019	**$ -**	
Int. Exp/Taxes	$ (0.02)	
2Q 2020	**$ (0.02)**	

Source: UBS Equity Research Estimates

Sempra Energy

We expect Sempra Energy to beat the quarter and report ongoing adjusted eps of $1.65 vs. $1.19 consensus and $1.10 last year. The big beat will be driven by a shift in seasonality of the utility earnings given the delayed CPUC rate order last year which will impact both SDG&E, and SoCalGas. Further SDG&E will also have rate base growth at transmission and one-time benefits of ~$60mln from the

CPUC tax memo account decision (as disclosed on page 48 in 1Q'20 10-Q). One slight offset at SDG&E will be wildfire related amortization. At SoCalGas, in addition to the impacts of the CPUC rate order we expect a one- time benefit of ~$60mln similar to SDG&E also related to the CPUC tax memo account decision. In Texas we expect year on year rate base growth driving results higher by ~$40mln, with minimal coronavirus disruption in the 2Q in Texas. For South America, the assets were divested in the quarter, however, Peru will have a one-month contribution to results and Chile will have a 3 month contribution to results, leaving overall results down ~$30mln year over year. In Mexico results will be lower given Peso appreciation vs. the USD and a drag to capex deployment and volumes related to COVID-19. We see higher results at Sempra LNG & Midstream by ~$30mln related to an additional 2 months of Cameron Train 2 in service offset by higher liquefaction project development costs. At Parent & Other we expect a reversal of the year over year pension and OPEB loss recorded in 1Q 2020 and slightly lower interest expense as Peru sale proceeds began to pay down debt in the quarter.

Southern Company

We expect Southern Company to report adjusted eps of $0.64 vs. $0.69 consensus, their $0.65 guidance and $0.80 last year. Drivers in the quarter will be coronavirus volume impacts only partially offset by O&M cost controls as those programs got started in the quarter and will have more impact in the second half of the year. The southeast also did not have the positive weather of most of the rest of the country so we expect a negative weather drag vs. the warmer than normal weather in 2Q 2019. There will also be a slight drag at Southern Power related to the divestiture of the Nacogdoches and Mankato power plants. At corporate & other we expect higher interest expense and share dilution. These negative drivers will be offset by some cost control impact on non-fuel O&M and the year on year retail revenue impacts from the Georgia rate case decisions in December 2019.

Figure 32: Southern Company 2Q 2020 Drivers

2Q 2019	$	0.80
Retail Sales	$	(0.06)
Retail Rev. Impacts	$	0.05
Weather	$	(0.08)
Wholesale Operations	$	-
Other Op. Revenues	$	-
Non-Fuel O&M	$	0.04
Int. Exp. D&A, Other	$	(0.07)
Income Taxes	$	-
SO Power	$	(0.02)
SO Company Gas	$	-
Parent & Other	$	(0.01)
Increase in Shares	$	(0.01)
2Q 2020	$	0.64

Source: UBS Equity Research Estimates

WEC Energy Group

We expect WEC to report adjusted eps of $0.67 vs. $0.67 consensus estimates and $0.74 last year. We see drivers year on year of lower volumes due to coronavirus economic disruptions and higher interest expense, D&A and lack of fuel band earnings in 2Q 2020 vs. 2Q 2019. These negative drivers will be mostly offset by efficiencies in O&M year on year, slightly better results at energy infrastructure from Coyote Ridge and the incremental 10% ownership stake in Upstream Wind, and slightly better results at ATC transmission due to the FERC ROE decision and rate base growth. Weather was also better year over year.

Xcel Energy

We expect Xcel Energy to report adjusted 2Q'20 earnings of $0.49 vs. $0.47 in the prior year quarter. Our estimate assumes load loss associated with the Covid-19 related economic shut down reduce earnings by $0.11 in the quarter, offset by $0.05 of lower O&M. This assumption is consistent the with company's 'base case' scenario which assumes a total annual EPS impact of $0.17, and we spread the offsetting projected O&M savings assumption (4-5% of prior year) over the three remaining three quarters of the year as an offset. Q2 EPS benefit from higher regulated rates and AFUDC earnings which offset higher depreciation, property tax and interest expense. We expect XEL will maintain its 5-7% EPS growth target, and 2020 EPS guidance of $2.73-$2.83.

On the investor call following the earnings release we expect XEL to provide some additional colour around its Minnesota filing to both pull forward capital spending plans and extend its current rate case stay out agreement. Hearings in this process are scheduled for July 29 to discuss the process and procedure. To date, none of the company's other jurisdictions have followed Minnesota in exploring a potential acceleration of capital spending in order to drive additional economic growth and employment.

Figure 33: Xcel Energy Q2'20 EPS Summary

Q2'19			$0.47
	Base Case Annual	Quarterly Impact	
Load Loss - 6%	($0.17)	($0.11)	
O&M Savings - 4.5% (After Tax)	$0.15	$0.05	
Est. Qtrly Impact of Covid-19 Shutdown			($0.06)
MN/ND/SD/NM revenue step-up			$0.04
Property tax up/AfUDC down			$0.04
Q2'20 Estimate			$0.49

Source: UBS Equity Research, Company Reports, FactSet

Water Utilities

American Water Works.

We expect American Water Works to report adjusted 2Q'20 EPS of $0.99 vs. $0.94 in the prior year quarter (which included both a negative $0.05 weather impact and $0.03 benefit from the sale of a legacy investment). Quarterly earnings should benefit from higher rates (achieved through regulatory proceedings and formulaic step increases), infrastructure charges and favorable spring weather.

These benefits will likely be offset by higher depreciation and interest expenses. On its investor call, we expect AWK will reiterate it 7-10% EPS CAGR guidance, capital spending plans ($8.8-$9.4 billion through '24), full year earnings guidance (GAAP $3.85-$3.95/operating $3.79-$3.89) and developments in both its regulated and market based businesses.

American States Water

We expect AWR to report adjusted 2Q'20 EPS of $0.70 vs. $0.64 in the prior year quarter (after adjusting for the retroactive impact of a CPUC decision: $0.08). Year over year earnings growth is attributable to rate base investment (second step increase in CA rates effective 1/1/20), demand growth and modestly lower depreciation expense (offset by higher administrative & general expense). In conjunction with its quarterly earnings release, we expect AWR will update investors on the impact of the Covid-19 pandemic (memorandum account), its contracted services business and regulatory schedule in California (a GRC may be filed by the time of the earnings release).

California Water

We expect CWT to report adjusted 2Q'20 EPS of $0.51 vs the prior year quarter of $0.35. Without a final general rate case decision (PD may come by the end of July), we expect there will be no year over year revenue increase. Our projected step up in earnings is derived from a reversal of the Q1 charges associated with the loss on benefits adjustment and the pension expense that we attribute to the recovery of the broader market. These benefits may be offset by higher depreciation and operating expense. Absent a decision in the pending general rate case around the contested revenue adjustment mechanisms, we believe this quarter results will be similar in character to those of the first quarter, that is somewhat distorted vs. normal. That said it is possible that we will see a proposed decision in the general rate case prior to the earnings release.

SJW Group

We expect SJW to report adjusted ongoing 2Q'20 EPS of $0.70 vs $0.58 from the prior year quarter. Q2'20 earnings will benefit from the rate base growth and investment, and the close of the Connecticut Water acquisition (October '19). In conjunction with its earnings release we expect SJW will update investors on its water production costs, ongoing regulatory calendar and the memorandum account it has established to manage costs associated with the ongoing Covid-19 pandemic. SJW updated in annual guidance on its first quarter call to a range of $1.95-$2.05, we do not expect any change or adjustment to this guidance after what is largely considered a shoulder quarter for California water utilities.

Essential Utilities

We expect Essential Utilities to report adjusted 2Q'20 EPS of $0.26 vs. the prior year quarter (pre Peoples Gas acquisition and excluding acquisition related costs) of $0.37. This estimate is consistent with the company's annual guidance of $1.53-$1.58 and its expectations for earnings dispersion across the year (35-45% in Q1/10-20% in Q2/10-20% in Q3/25-35% in Q4). While annual guidance is largely theoretical given the timing of the Peoples Gas deal close and its inclusion in earnings at a assumed level, Q2 will be the first full quarter for the whole entity and should provide investors will useful insight (albeit in a slow quarter for a gas LDC) of the company's earnings power. Earnings drivers for the quarter include positive weather (warm & dry spring season), rate increases across the company's

operating jurisdictions, somewhat lower expenses associated with 'work from home' environment.

In conjunction with its earnings release, we expect WTRG will update investors on the integration of its Peoples Gas acquisition, its pending acquisition of DELCORA (and the timing of the associated equity) and other potential M&A activity (Chester Water Authority, Norristown etc.). We also expect an update on the company's 'catch-up' repairs tax adjustment filing in Pennsylvania and pending federal infrastructure legislation.

Independent Power Producers

NRG Energy

We expect NRG Energy to report ongoing Adjusted EBITDA of $533mln vs. $528mln consensus estimates and $469mln last year. We expect drivers you over year to be incremental EBITDA from the Stream retail acquisition, continued margin enhancement at the retail business and warmer weather year on year. This warmer weather is likely to offset any coronavirus bad debt or volume related impacts in the quarter, which we expect to be less impactful overall than originally estimated in March.

On the 1Q 2020 earnings call update, NRG indicated that they were 98% hedged in the East/West segment for the balance of 2020 and had the integrated hedge in ERCOT through retail. For 2022, hedging levels were 22% in the East/West segment at the time of the 1Q 2020 earnings call.

We are also updating our annual Adjusted EBITDA estimates on a mark to market basis to $1,986/$1,840/$1,737mln from $1,914/$1,813/$1,773mln for '20/21/22 respectively.

Vistra Energy

We expect Vistra Energy to report ongoing Adjusted EBITDA of $819mln vs. $749mln consensus estimates, and $707mln last year. We expect operational performance improvement cost cutting initiatives (OPIs) to begin to show impact in the quarter and to largely if not completely offset the impact of lower capacity revenues for the non-ERCOT generation businesses. We expect ERCOT results will be higher by ~$50mln year-year as that segment also captures OPIs and we do not expect bad debts to be a high as anticipated by management on the 1Q call, at least in 2Q 2020 given that Texas did not significantly lock down. Further the capture of ~$60mln in the guidance walk on the 1Q conference call discussed by management was largely in 1Q but there will be some residual impact carried into the 2Q period. At retail we expect that results will be higher year over year related to the acquisitions of both the Crius and Ambit retail businesses. This will not be damped by mild weather as in 1Q and will somewhat shift the seasonality of results for Vistra more toward 1Q, 2Q, and 4Q and away from 3Q.

On the 1Q 2020 earnings call update, VST indicated that they were 100% hedged across the non-natural gas generation fleet and 97% hedged at the gas fleet for the balance of 2020. In 2020 hedging levels were 72% at the non-natural gas fleet an 36% at the natural gas fleet for 2021, with the largest open position at the natural gas fleet in ERCOT and PJM.

We are also updating our annual Adjusted EBITDA estimates on a mark to market basis to $3,444/$3,087 /$3,076mln from $3,287/$3,195/$3,074mln for '20/21/22 respectively.

Figure 34: Vistra Energy Adj. EBITDA – 2Q 2019A vs. 2Q 2020E

US$mlns	2Q 2019A	2Q 2020E	Variance
Retail	293	355	62
ERCOT	156	206	50
PJM	167	167	-
NY/NE	91	91	-
MISO	1	1	-
Non-Seg Ops	(1)	(1)	-
Asset Closure	-	-	-
Total	**707**	**819**	**112**

Source: UBS Equity Research Estimates

Figure 35: Actual Power Price Comparisons ($/MWh)

ISO	Hub	2Q '20	2Q '19	Change
ISO NE	Internal Hub	19.07	24.02	(4.96)
NYISO	Zone G	15.54	20.98	(5.44)
PJM	AEP-Dayton	18.60	24.38	(5.78)
PJM	Eastern	15.89	22.48	(6.58)
PJM	N Illinois	15.90	22.19	(6.29)
PJM	PSEG	16.12	21.54	(5.41)
PJM	Western	18.01	24.07	(6.06)
MISO	Indiana	20.24	25.23	(4.99)
MISO	Michigan	21.00	25.67	(4.67)
ERCOT	North	16.45	25.09	(8.64)
ERCOT	Houston	18.66	26.28	(7.62)
ERCOT	West	15.04	23.34	(8.30)
CAISO	NP15	21.15	21.18	(0.04)
CAISO	SP15	19.31	21.64	(2.33)

Source: S&P Global Market Intelligence, UBS Equity Research Estimates

Figure 36: Power Price Comparisons & Spark Spread Trends ($/MWh)

Period	ISO	Hub	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7
Q220	ISO NE	Internal Hub	$ 9.93	$ 10.85	$ 10.88	$ 11.47	$ 13.18	$ 12.02	$ 12.46
Q219	ISO NE	Internal Hub	$ 10.92	$ 12.49	$ 11.90	$ 8.72	$ 5.71	$ 6.54	$ 6.20
		Change	$ (0.99)	$ (1.64)	$ (1.02)	$ 2.75	$ 7.47	$ 5.48	$ 6.25
Q220	PJM	Eastern	$ 12.27	$ 13.50	$ 13.86	$ 14.32	$ 15.04	$ 15.52	$ 15.56
Q219	PJM	Eastern	$ 13.60	$ 12.36	$ 11.82	$ 11.69	$ 11.24	$ 11.12	$ 11.54
		Change	$ (1.33)	$ 1.14	$ 2.05	$ 2.63	$ 3.80	$ 4.40	$ 4.01
Q220	PJM	Western	$ 14.35	$ 15.87	$ 15.92	$ 16.16	$ 16.56	$ 16.69	$ 16.91
Q219	PJM	Western	$ 14.47	$ 15.50	$ 14.61	$ 14.53	$ 14.28	$ 13.66	$ 14.08
		Change	$ (0.12)	$ 0.37	$ 1.32	$ 1.63	$ 2.28	$ 3.03	$ 2.83
Q220	ERCOT	Houston	$ 33.20	$ 22.13	$ 20.05	$ 19.38	$ 18.82	$ 17.92	$ 16.11
Q219	ERCOT	Houston	$ 22.74	$ 22.67	$ 20.44	$ 17.41	$ 15.01	$ 12.05	$ 9.39
		Change	$ 10.46	$ (0.54)	$ (0.39)	$ 1.97	$ 3.81	$ 5.87	$ 6.72

Source: S&P Global Market Intelligence, UBS Equity Research Estimates

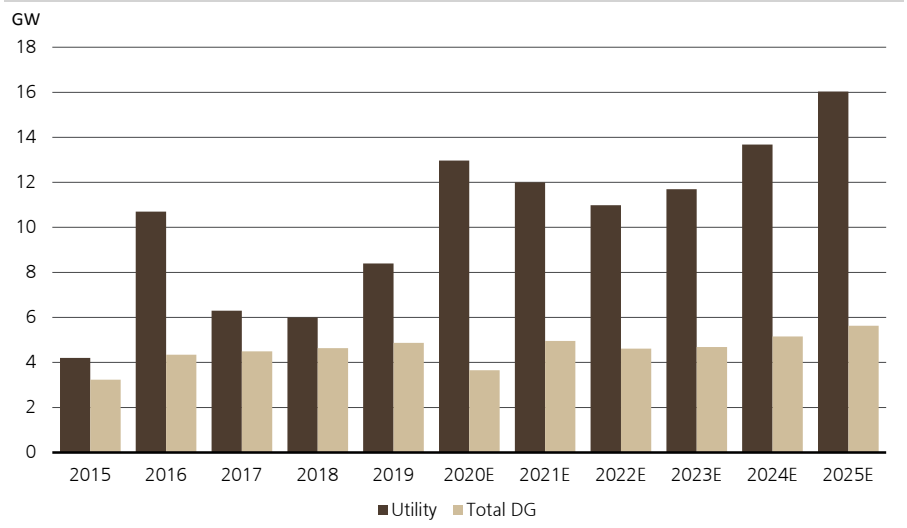
Alternative Energy 2Q20 preview

Key issues for the quarter

We expect 2Q20 results calls to focus on 1) Strength of the post-COVID recovery in distributed solar demand 2) potential policy support following the election and 3) RUN/VSLR deal impact on supply chains and potential to drive adoption of residential storage. We expect the market to look past trough 2Q actuals which are likely to be noisy; FSLR consensus revenue estimate dispersion is at the widest since 3Q17.

Our top pick in our Alternative Energy coverage is Generac (GNRC, Buy, PT $145) with exposure to accelerating residential solar + storage demand. See our GNRC initiation here.

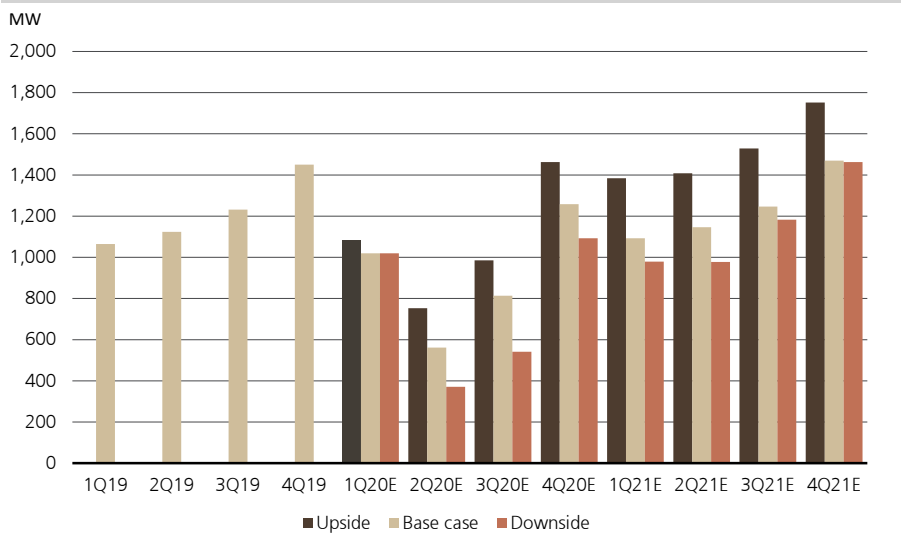
Figure 37: U.S. new solar installations (GW)



Source: EIA, IRENA, SEIA, Wood Mackenzie, UBS estimates

Recent comments from RUN indicate demand potentially tracking closer to our upside case for a 33% y/y 2Q decline in distributed solar demand.

Figure 38: U.S. distributed solar demand – quarterly forecast



Source: EIA, SEIA, Wood Mackenzie, UBS estimates

Company specific focus areas

- **FSLR**: We expect a 2Q20 loss per share of $0.04 driven by lower systems segment contribution from project sale timing delays. Consensus 2Q20 adj. EPS is currently $0.30. FSLR previously pulled 2020 financial guidance but maintained module production guidance of 5.9GW indicating confidence in manufacturing execution. Uncertainty of systems sales remains driven by timing rather than quantity. Management flagged a sequential quarterly decline in module ASP with 1Q20 having benefitted from safe harbor demand. UBSe 2Q20 module ASP is $0.36/watt.

- **SPWR**: 2Q20 revenue guide of $290-330mn implies down 27-36% q/q & down 32-40% y/y. Adj. EBITDA guidance is negative $40-20mn. We expect a sequential recovery in earnings after 2Q but note SPWR has over 50% market share in the new home solar market which could be a drag in 2H20. On the 16 July Maxeon analyst day management highlighted the Maxeon spin remains on track to close in 3Q20. Preliminary Maxeon results were provided for 2Q20 revenue of $160-170mn, down 40% y/y at the midpoint driven by 8 week production shut downs. We expect Maxeon to continue to focus on deploying a base of premium-quality modules while driving faster growth through expanding sales of lower-cost modules produced by the TZS JV in China. Maxeon currently arranged financings provide enough liquidity to cover the expected $385mn investment in capacity expansion through 2022.

- **CSIQ**: 2Q20 guidance is 2.5-2.7GW module shipments, $630-680mn revenue, and gross margin 18.5-20.5%. 2020 shipment guidance 10-12GW. We see risk of industry overcapacity potentially dragging on profit margins into 2H20. Key uncertainty for utility scale solar exposure remains project sale timing and price. Project revenue has comprised 24% of total net sales over the last 5 years. We look for an updated on CSIQ's prior suspension of its share repurchase program.

- **JKS**: 2Q20 guidance is 4.2-4.5GW shipments, $1.1-1.18bn revenue, and 16-18% gross margin. 2020 shipment guidance is 18-20GW. We forecast module ASP declining ~10% 2Q20 q/q with margin pressure persisting through 2020.

JKS management is targeting cost reductions to offset ASP pressure and maintain ~flat margin to 2Q20.

- **RUN**: RUN's latest commentary implies 2Q20 deployments better than the previous 30% y/y decline expectation. Our 2Q20 deployment estimate is 77MW, -25% y/y. We expect focus on the conference call around potential impacts on the inverter supply chain following RUN's acquisition of VSLR. Based on our analysis of California distributed solar data, RUN installs have historically use a ~50/50 mix of SEDG and ENPH inverters with VSLR primarily using ENPH equipment.

- **SEDG**: 2Q20 revenue guidance of $305-335mn implies a decline of 22-29% q/q. The 2Q guidance is well ahead of ENPH's 2Q revenue guide for a 37-44% q/q decline. SEDG noted a 33% y/y decline in U.S. installations in April and we see likely sequential improvement in May-June. 2Q20 gross margin guidance of 30-32% reflects margin pressure driven by higher European sales mix, with a U.S./Europe margin differential of 450bps, partially offset by 200bps margin improvement on reduced air shipments.

- **GNRC**: We forecast 2Q20 adj. EPS of $0.68, reflecting -43% y/y growth driven by a 40% y/y 2Q decline in C&I segment sales. GNRC provided only directional 2Q guidance for a modest sequential decline in net sales (UBSe $449mn) and adj. EBITDA margin (UBSe 15.7%). Our focus will be on customer adoption of Clean Energy products and GNRC's progress in shifting its manufacturing to Vietnam (which we expect to have largely been completed in June). See our recent initiation here.

- **HASI**: Long-term core EPS growth guidance of 2-6% off a 2017 baseline remains intact implying core EPS of $1.43 in 2020 at the midpoint. We model 2Q20 core EPS of $0.33.

- **ORA**: We forecast 2Q20 adj. EPS of $0.39 and adj. EBITDA of $98mn reflecting typical seasonality of electricity generation. ORA 2020 guidance is revenue $710-740mn and adj. EBITDA $400-415mn. The Puna plant re-start previously pushed to 4Q20 and we look for an update on progress toward completing permitting & necessary transmission upgrades. The emerging market assets continue to be a source of concern. Trade receivables reached $169mn, and DSO is at 93 days, up from 73 days in 1Q19. See our read-throughs from California Public Utility Commission's latest Integrated Resource Plan here.

- **TPIC**: We expect 2Q20 line utilization of 70% driven by Juarez & Matamoros COVID-19 related shutdowns. 2Q20 UBSe adj. EBITDA is $22mn. We expect cumulative 2020-2021 wind demand to remain intact with the impact to TPIC earnings being one of timing. In addition, customer pushout of blade transitions could help mitigate the COVID related earnings impact to 2020 by reducing TPIC's blade transition costs.

Figure 39: Alternative Energy key estimates

		Quarterly				Annual		
Company	Ticker	Scheduled Reporting Date	2Q20E UBS	2Q20E Consensus	UBS Vs. Consensus	2020E UBS	2020E Consensus	UBS Vs. Consensus
ALTERNATIVE ENERGY								
Hannon Armstrong	HASI	29-Jul est.	$0.33	$0.32	$0.01	$1.50	$1.47	$0.04
Generac	GNRC	30-Jul	$0.68	$0.88	($0.20)	$4.18	$4.38	($0.20)
First Solar	FSLR	30-Jul est.	($0.04)	$0.32	($0.36)	$3.39	$2.82	$0.58
Ormat Technologies	ORA	4-Aug	$0.39	$0.39	($0.00)	$1.74	$1.77	($0.04)
Sunpower	SPWR	4-Aug est.	($0.30)	($0.38)	$0.08	($0.27)	($0.44)	$0.17
SolarEdge	SEDG	5-Aug est.	$0.74	$0.53	$0.21	$4.22	$3.06	$1.16
TPI Composites	TPIC	5-Aug est.	$0.04	($0.23)	$0.27	$0.35	$0.41	($0.05)
SunRun	RUN	6-Aug est.	($0.01)	$0.07	($0.08)	($0.23)	$0.15	($0.37)
Canadian Solar	CSIQ	13-Aug est.	($0.13)	($0.06)	($0.07)	$2.47	$2.91	($0.44)
Jinko Solar Holding Company	JKS	20-Aug est.	$0.98	$0.66	$0.32	$3.77	$3.61	$0.16

Source: Company reports, FactSet, UBS research estimates.

Environmental Services 2Q20 preview

Progress on recovery in waste volumes

We expect relatively upbeat 2Q20 conference call as the recovery in municipal solid waste appears to be firmly underway. At the UBS Industrial and Transportation conference in early June, Management's noted continued w/w improvements in commercial waste volumes & landfill tons following the bottom in April. In addition, WCN pre-announced high-level results on 9 July driving a 4% increase in our 2Q20 revenue estimate.

As we approach the election we expect increased focus on potential for higher corporate tax rates. Broadly, every 1% increase in the corporate tax rates (from 21% to 22%) drives a 0.6% decrease in MSW FCF.

Re-issuing 2020 guidance

We expect most of the waste names will re-issue 2020 guidance with 2Q20 results. In our view, names best positioned to exceed expectations are nationally diversified players (WM, RSG, WCN) that were likely able to mitigate the impact of the relatively more restrictive COVID-19 shutdowns in the U.S. Northeast. For CVA, CLH, and ECOL waste volumes expected to recover sequentially after 2Q20 but likely to ramp more slowly than for the MSW haulers.

Figure 40: Environmental Services business exposures

Metric 2020E	WM	RSG	WCN	ADSW	CWST	CVA
2020 revenue ($bn)	14.9	9.6	5.3	1.5	0.7	1.9
N. American market share	24%	16%	9%	2%	1%	3%
Geographic						
U.S. Northeast	22%	18%	22%	26%	100%	47%
U.S. South	24%	34%	17%	36%	0%	33%
U.S. Midwest	23%	20%	12%	38%	0%	7%
U.S. West	24%	28%	33%	0%	0%	10%
Canada/other	7%	0%	16%	0%	0%	3%
Total	100%	100%	100%	100%	100%	100%
Revenue composition						
Residential collection	17%	19%	21%	25%	17%	0%
Commercial collection	22%	25%	26%	23%	18%	0%
Industrial collection	15%	18%	14%	15%	17%	0%
Total collection	54%	62%	61%	63%	52%	0%
Other operations						
Transfer	9%	11%	12%	10%	9%	10%
Disposal	19%	20%	20%	21%	18%	56%
Recycling	7%	3%	1%	1%	5%	5%
E&P	1%	2%	4%	1%	2%	0%
Other operations	10%	2%	2%	4%	14%	29%
Total	100%	100%	100%	100%	100%	100%
Cost composition						
SGA as % of revenue	10.4%	10.3%	10.0%	11.6%	11.9%	5.1%
Opex as % of revenue	62%	62%	-85%	64%	70%	75%

Source: Company reports, UBS Research estimates

Figure 41: UBSe, Consensus, prior guidance table

		Original 2020 guidance				
Ticker	Metric	Low	Mid	High	UBSe	Consensus
WM						
	Price		2.5%		1.1%	
	Volume		1.5%		-7.4%	
	Adj. EBITDA ($bn)	4.56	4.61	4.66	4.14	4.05
	FCF ($bn)	2.15	2.20	2.25	2.82	1.81
	Capex ($bn)	1.70	1.75	1.80	1.65	1.59
RSG						
	Price		3.0%		1.1%	
	Volume	0.8%	0.9%	1.0%	-7.0%	
	Sales growth	4.3%	4.6%	5.0%	-6.4%	-3.4%
	Adj. EBITDA ($bn)	3.05	3.08	3.10	2.65	2.73
	Adj. EPS	3.48	3.51	3.53	2.51	2.79
	Adj. EBITDA ($bn)	3.05	3.08	3.10	2.65	2.73
	FCF ($bn)	1.18	1.20	1.23	1.01	1.03
	Capex ($bn)		1.20		1.16	1.13
WCN						
	Sales ($bn)	5.73	5.75	5.78	5.35	5.34
	Adj. EBITDA ($bn)	1.76	1.77	1.79	1.61	1.58
	Net income ($mn)	653	661	668	522	630
	FCF ($bn)	975	988	1000	899	850
CWST						
	Price	3.5%	4.0%	4.5%	3.0%	
	Volume	-0.5%	0.0%	0.5%	-8.2%	
	Sales ($mn)	800	808	815	735	757
	Adj. EBITDA ($mn)	170	172	174	151	152
	Net income ($mn)	35	37	39	18	24
	FCF ($mn)	60	62	64	46	51
	Capex ($mn)		113		101	102
CVA						
	Adj. EBITDA ($mn)	415	430	445	390	402
	FCF ($mn)	100	120	140	16	74
CLH						
	Adj. EBITDA ($mn)	545	565	585	466	449
	FCF ($mn)	210	225	240	207	175
ECOL						
	Adj. EBITDA ($mn)	230	240	250	198	184
	Adj. EPS	1.65	1.89	2.12	0.91	0.70
	FCF ($mn)	81	94	106	72	50
	Capex ($mn)	90	93	95	79	68

Source: FactSet, company reports, UBS research estimates. Note: UBSe for WM reflects partial year contribution from ADSW acquisition. All companies have withdrawn original 2020 guidance in light of COVID-19 pandemic.

Company specific focus areas

- **WM**: WM's well-diversified national exposure should help mitigate the most severe of the shutdown impacts on the U.S. Northeast (22% of revenue) and Canada (7% of revenue). WM's acquisition of ADSW is now expected to close 3Q20. WM expects to redeem ~$3bn of outstanding senior notes issued in May 2019 under the redemption provision that the deal be closed by 14 July 2020. Assuming refinancing at current rates we see a potential ~$27mn annual interest savings and $1.20/sh share price accretion at a 5% FCF yield.

- **RSG**: We forecast 2Q20 volumes down 14% y/y and adj. EBITDA of $596mn. RSG had previously disclosed 40% decremental EBITDA margin on the entire company driven by declines in high margin small container and landfill volumes. At our UBS Industrials & Transportation conference in early June, management highlighted continued improvement in volumes through May and expectations for a good June result. In addition, the company has seen no material change in DSO to-date.

- **WCN**: WCN pre-announced high level 2Q results. See our note here. 2Q revenue declined 4.7% y/y ($1.3bn; +1.5% to consensus) with adj. EBITDA margin down 90-100bps y/y ($392-394mn; +6.8% to consensus at mid-point). WCN highlighted same store solid waste revenue down 5.3% y/y and down 1.3% y/y excluding Canada and the U.S. Northeast. In addition WCN closed $50mn in new annualized revenue of new tuck-ins. We had previously expected a pause on acquisition spending in 2Q-3Q20. We expect WCN to re-issue formal 2020 guidance with the 2Q20 results and see FY2020 revenue tracking above the $5.25bn baseline provided previously.

- **ADSW**: ADSW will not be hosting an earnings conference call given the announced acquisition by WM. We do not expect the stock to trade on results given expected near-term acquisition closure.

- **CWST**: CWST's Northeast footprint suggests a more muted recovery than that experienced by WCN (and likely other nationally diversified players). We forecast 2Q20 volumes to decline 15% y/y. Our 2Q20 adj. EBITDA is $35mn, down 13% y/y. As of the 1Q results call, CWST expected a 150-200bps negative headwind to adj. EBITDA margin from COVID-19. Excluding M&A, the April y/y revenue impacts by product line were: Residential: 0%, Commercial -9.3%, Roll-off -26%, Disposal -14.4%, Resource Solution +1%. CWST noted a sequential up-tick from trough demand in late-April and May.

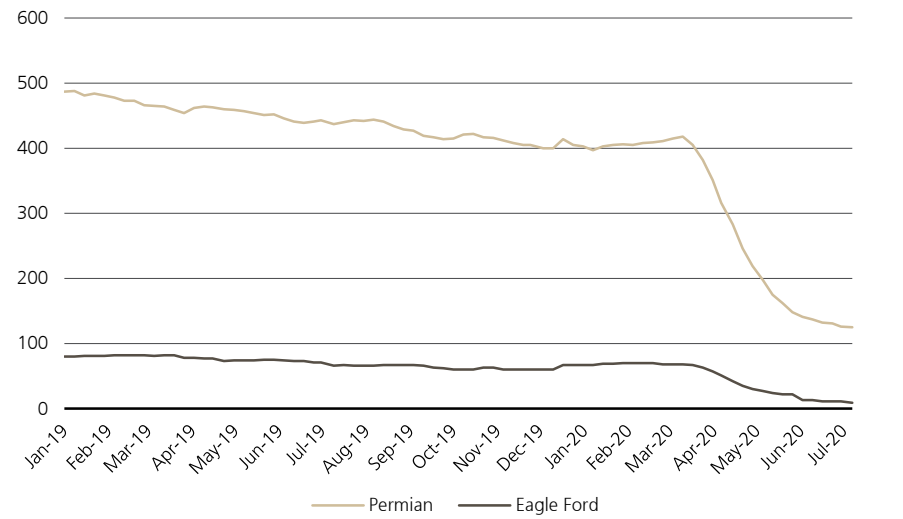
- **CVA**: Given CVA's Northeast concentration we expect a relatively slower recovery ramp than for the large national solid waste names, however we expect waste volumes for CVA have continued to improve off of April lows. Our 2Q20 adj. EBITDA is $68mn, down 28% y/y. Management previously highlighted April tip fee pricing down $4-6 per blended tip fee ton, or approximately 7-10% vs. 2Q19 averages and ~$5mn per month impact. See our recent upgrade of CVA to Buy here.

- **CLH**: We forecast 2Q20 adj. EBITDA of $92mn, -39% y/y. We see CLH's Safety Kleen segment taking the brunt of COVID related impacts, with segment revenue down 30% y/y in April but improving sequentially through June. CLH has completed ~$50mn of decontamination work related to COVID-19. As of 1Q20 CLH had closed half of its refinery capacity to reduce fixed costs and we

look for an update on potentially restarting these assets. Expect management to issue revised guidance with the 2Q results.

- **ECOL:** We forecast 2Q20 adj. EBITDA $39mn, ~flat y/y despite contribution from the NRCG acquisition. April & May likely reflecting trough months with the recovery in earnings underway in June. For the ES segment, management had previously flagged base business declines (~30% of revenue) of 10-15% y/y in April and likely similar May impact. Rig count has yet to find a bottom indicating pressure on ECOL's E&P waste revenues continuing to worsen in 3Q. ECOL has energy waste landfill exposures in the Permain (avg. 2Q rig count down 55% y/y) and Eagle Ford (avg. 2Q rig count down 63%) basins.

Figure 42: North America rig count



Source: Baker Hughes, UBS Research

Figure 43: Environmental Services EPS estimates

		Quarterly				Annual		
Company	Ticker	Scheduled Reporting Date	2Q20E UBS	2Q20E Consensus	UBS Vs. Consensus	2020E UBS	2020E Consensus	UBS Vs. Consensus
ENVIRONMENTAL SERVICES								
Clean Harbors	CLH	29-Jul est.	$0.07	($0.00)	$0.07	$0.99	$0.85	$0.14
Advanced Disposal Services	ADSW	30-Jul	($0.02)	($0.01)	($0.01)	$0.02	$0.14	($0.12)
Covanta Holding Corp	CVA	30-Jul	($0.24)	($0.19)	($0.05)	($0.34)	($0.29)	($0.05)
Waste Management	WM	30-Jul	$0.74	$0.77	($0.04)	$3.49	$3.68	($0.19)
Casella Waste System	CWST	3-Aug	$0.05	$0.05	($0.00)	$0.44	$0.52	($0.08)
US Ecology	ECOL	5-Aug est.	$0.22	($0.02)	$0.24	$1.24	$1.12	$0.12
Republic Services	RSG	6-Aug	$0.47	$0.56	($0.09)	$2.51	$2.79	($0.28)
Waste Connections	WCN	6-Aug	$0.49	$0.54	($0.06)	$2.36	$2.38	($0.02)

Source: Company reports, FactSet, UBS research estimates.

Figure 44: Environmental Services EBITDA estimates ($mn)

		Quarterly				Annual		
Company	Ticker	Scheduled Reporting Date	2Q20E UBS	2Q20E Consensus	UBS Vs. Consensus	2020E UBS	2020E Consensus	UBS Vs. Consensus
ENVIRONMENTAL SERVICES								
Clean Harbors	CLH	29-Jul est.	106	93	14.2%	474	447	6.0%
Covanta Holding Corp	CVA	30-Jul	68	77	-11.5%	381	403	-5.5%
Advanced Disposal Services	ADSW	30-Jul	93	87	7.2%	374	390	-4.2%
Waste Management	WM	30-Jul	908	922	-1.5%	4,141	4,067	1.8%
Casella Waste System	CWST	3-Aug	35	33	5.5%	151	153	-1.3%
US Ecology	ECOL	5-Aug est.	49	39	24.4%	211	184	14.4%
Republic Services	RSG	6-Aug	596	608	-2.0%	2,652	2,729	-2.8%
Waste Connections	WCN	6-Aug	393	376	4.6%	1,609	1,576	2.1%

Source: Company reports, FactSet, UBS research estimates.

Valuation Method and Risk Statement

Our valuation methodology for North American utilities is price to earnings based. The adjustments applied fall into 6 categories. These are as follows: 1) Group Valuation Bias: Flowing from our valuation work comparing Baa corporate yields to group dividend yields and RU price to earnings ratios to those for the S&P 500, we incorporate a positive or negative adjustment to our group multiple representing the gap we calculate to the nearest 5%; 2) Growth Adjustment: We adjust our valuations based on the growth quartile each utility occupies. First quartile receives a 5% premium, second quartile a 2% premium, third quartile a 2% discount and fourth quartile a 5% discount; 3) Regulatory Adjustment: Our valuation adjustments for regulation are based on our proprietary Regulatory Rankings. First quartile jurisdictions receive 5%, second quartile 2%, third quartile -2% and fourth quartile -5%; 4) Earnings Consistency Adjustment: For companies that fall in the top quartile of % Time Beat/Meet, we include +5%; 5) Multi Utility Diversified Valuation: For multi utilities (those with more than 15% diversified or foreign earnings), we perform a sum-of-parts analysis applying business/region appropriate valuations to those diversified businesses; 6) One-off Adjustments: In special situations, we value risk on an issue specific basis. Common areas where we apply such an adjustment include: ESG advantage, large project construction risk, legal risk, and announced M&A completion risk. We identify the following risk factors for the sector overall: rising interest rates; regulatory and policy risks; operational risks; construction risks; cybersecurity risk to the transmission grid and/or customer data, and extreme weather events.

Our valuation methodology for the IPPs is based on mid-cycle EV/EBITDA multiples of 7.2x on UBSe 2020 EBITDA, UBSe 2020 Net Debt, the NPV of hedges and any NOLs discounted to the current year at 8%, and UBSe 2020 share count.

Our valuation methodology for the Alternative Energy space is based on a variety of metrics including P/BV, EV/EBITDA, P/E, and retained equity value per share. Our target multiples are derived from historical group averages with adjustments for expected growth rates, leverage, and earnings growth confidence. We identify the following risks for the sector: Demand for new renewable installations has historically been volatile around changes in state and federal policy, and we expect this volatility to continue. In addition, margins for product manufacturers can be impacted by swings in raw materials pricing and the overall level of energy prices.

Our valuation methodology for the Environmental Services space is based on EV/EBITDA with adjustments made to the target EV/EBITDA multiple based on relative growth rates, Free Cash Flow (FCF) conversion, expected earnings stability, and the general level of risk and our confidence in future earnings estimates. We identify the following risks for the sector: Housing remains a key driver of incremental municipal solid waste volume growth, and a slowdown in new housing starts could put downward pressure on sales growth. In addition, pricing tends to follow GDP growth, and a slowdown in economic growth could drive lower ability to raise pricing driving potential contraction in margins. For more industrial-exposed names, swings in commodity prices can impact the overall level of waste-generating activity, contributing to earnings volatility.

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Buy	FSR is > 6% above the MRA.	49%	32%
Neutral	FSR is between -6% and 6% of the MRA.	39%	30%
Sell	FSR is > 6% below the MRA.	13%	20%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 June 2020.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Advanced Disposal Services Inc[3, 5, 13, 16, 19]	ADSW.N	Neutral (CBE)	N/A	US$30.16	16 Jul 2020
AES Corp[16]	AES.N	Buy	N/A	US$14.88	16 Jul 2020
Alliant Energy Corp[16]	LNT.O	Neutral	N/A	US$49.73	16 Jul 2020
Ameren Corp[16]	AEE.N	Buy	N/A	US$76.79	16 Jul 2020
American Electric Power Inc[7, 16]	AEP.N	Buy	N/A	US$85.09	16 Jul 2020
American States Water Co[16]	AWR.N	Sell	N/A	US$77.59	16 Jul 2020
American Water Works Co[16]	AWK.N	Neutral	N/A	US$138.32	16 Jul 2020
ATCO Ltd	ACOx.TO	Buy	N/A	C$42.31	16 Jul 2020
California Water Service Group[16]	CWT.N	Sell	N/A	US$48.28	16 Jul 2020
Canadian Solar Inc[6c, 7, 13, 16, 20a]	CSIQ.O	Neutral (CBE)	N/A	US$22.80	16 Jul 2020
Canadian Utilities Ltd	CU.TO	Neutral	N/A	C$34.41	16 Jul 2020
Caribbean Utilities Corp	CUPu.TO	Sell	N/A	US$15.49	16 Jul 2020
Casella Waste Systems Inc[16]	CWST.O	Neutral	N/A	US$53.39	16 Jul 2020
Clean Harbors Inc[16, 20b]	CLH.N	Neutral (CBE)	N/A	US$60.25	16 Jul 2020
CMS Energy Corp[4, 5, 6a, 16]	CMS.N	Neutral	N/A	US$60.33	16 Jul 2020
Consolidated Edison Inc[16]	ED.N	Neutral	N/A	US$71.84	16 Jul 2020
Covanta Holding Corp[4, 16]	CVA.N	Buy	N/A	US$9.69	16 Jul 2020
Dominion Energy Inc[7, 16]	D.N	Buy	N/A	US$76.95	16 Jul 2020
DTE Energy Co[16]	DTE.N	Buy	N/A	US$109.70	16 Jul 2020
Duke Energy Corp[7, 16]	DUK.N	Buy	N/A	US$81.07	16 Jul 2020
Edison International[7, 16]	EIX.N	Buy	N/A	US$56.09	16 Jul 2020
Emera Inc	EMA.TO	Buy	N/A	C$55.94	16 Jul 2020
Entergy Corp[7, 16]	ETR.N	Buy	N/A	US$98.33	16 Jul 2020
Essential Utilities Inc[16]	WTRG.N	Neutral	N/A	US$43.88	16 Jul 2020
Evergy, Inc[16]	EVRG.N	Neutral	N/A	US$61.41	16 Jul 2020
Eversource Energy[7, 16]	ES.N	Neutral	N/A	US$85.81	16 Jul 2020
Exelon Corp[7, 16]	EXC.O	Buy	N/A	US$38.06	16 Jul 2020
First Solar Inc[16]	FSLR.O	Buy	N/A	US$59.03	16 Jul 2020
FirstEnergy Corp[16]	FE.N	Buy	N/A	US$41.29	16 Jul 2020
Fortis Inc[16]	FTS.TO	Buy	N/A	C$54.10	16 Jul 2020
Generac Holdings Inc[16]	GNRC.N	Buy	N/A	US$132.54	16 Jul 2020
Hannon Armstrong Sustainable Infra[16]	HASI.N	Neutral	N/A	US$32.37	16 Jul 2020
Hawaiian Electric Industries Inc[16]	HE.N	Sell	N/A	US$37.00	16 Jul 2020
Hydro One	H.TO	Sell	N/A	C$27.26	16 Jul 2020
JinkoSolar Holding Co Ltd[13, 16, 20a]	JKS.N	Neutral (CBE)	N/A	US$19.86	16 Jul 2020
NextEra Energy Inc[4, 6a, 7, 16]	NEE.N	Buy	N/A	US$268.38	16 Jul 2020
NRG Energy Inc[7, 16]	NRG.N	Buy	N/A	US$33.84	16 Jul 2020
OGE Energy Corp[16]	OGE.N	Buy	N/A	US$31.90	16 Jul 2020
Ormat Technologies Inc[16]	ORA.N	Neutral	N/A	US$61.53	16 Jul 2020
PG&E Corp[7, 16, 20b]	PCG.N	Buy (CBE)	N/A	US$9.02	16 Jul 2020
Pinnacle West Capital Corp[7, 16]	PNW.N	Neutral	N/A	US$80.56	16 Jul 2020

Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
PNM Resources Inc[7, 16]	PNM.N	Buy	N/A	US$39.13	16 Jul 2020
Portland General Electric Co[16]	POR.N	Neutral	N/A	US$42.32	16 Jul 2020
PPL Corp[16]	PPL.N	Buy	N/A	US$25.85	16 Jul 2020
Public Service Enterprise Group[7, 16]	PEG.N	Buy	N/A	US$52.91	16 Jul 2020
Republic Services Inc[13, 16]	RSG.N	Buy	N/A	US$84.60	16 Jul 2020
Sempra Energy[7, 16]	SRE.N	Buy	N/A	US$122.63	16 Jul 2020
SJW Group[4, 16]	SJW.N	Neutral	N/A	US$63.02	16 Jul 2020
SolarEdge Technologies Inc[16, 20a]	SEDG.O	Neutral (CBE)	N/A	US$164.75	16 Jul 2020
Southern Co[6b, 7, 13, 16]	SO.N	Neutral	N/A	US$53.74	16 Jul 2020
SunPower Corp[16, 20a]	SPWR.O	Neutral (CBE)	N/A	US$9.79	16 Jul 2020
Sunrun Inc[16, 20a]	RUN.O	Neutral (CBE)	N/A	US$36.65	16 Jul 2020
TPI Composites Inc[16]	TPIC.O	Buy	N/A	US$26.25	16 Jul 2020
US Ecology Inc[16]	ECOL.O	Buy	N/A	US$32.89	16 Jul 2020
Vistra Energy Corp[2, 4, 6a, 16]	VST.N	Buy	N/A	US$19.40	16 Jul 2020
Waste Connections Inc[16]	WCN.N	Buy	N/A	US$100.04	16 Jul 2020
Waste Management Inc[3, 16]	WM.N	Buy	N/A	US$107.46	16 Jul 2020
WEC Energy Group Inc[16]	WEC.N	Neutral	N/A	US$87.76	16 Jul 2020
Xcel Energy Inc[16]	XEL.O	Neutral	N/A	US$64.99	16 Jul 2020

Source: UBS. All prices as of local market close.
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Q2 2019 Earnings Preview

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Regulated Utilities:
Our Q2'19 EPS estimates are 3% below consensus and 3% below Q2'18. Weather conditions were below normal in every region of the country with the upper Midwest and West most impacted (CMS, EVRG, PNM, PNW) although conditions in the Southern U.S. improved YoY which we expect helped ETR exceed consensus, and should also be helpful to NEE and SO. Due to the timing of rate case revenue EIX likely also beat consensus and the company could discuss their contribution to the wildfire insurance fund and the legislation on their call. Canadian utilities likely miss consensus with mild weather for CU, FTS and H, and EMA capped on ROE in NS despite better weather.

Power:
Our expectations for Adj. EBITDA are similar to 1Q where we see NRG results of $486mln below current consensus due to annual estimates not being seasonally weighted enough to 3Q, whereas we see VST results of $718mln above consensus due to estimates not being seasonally weighted enough away from 3Q. Overall results should not be significantly impacted by the lower power prices year on year as NRG was 93%/82% hedged in ERCOT/PJM as of the 1Q call and VST was 100% hedged to natural gas and 94% hedged to heat rate in ERCOT and 94%-95% hedged in the northeast as of the 1Q call. Despite forward curves being lower management should discuss on the call the offsetting effects of expanding retail margins. In addition to discussion of these sensitivities, investors are likely to focus on integration of the Crius acquisition for VST, implementation of the retail lite strategy for NRG, and any updates on target leverage and use of FCF, as well as the upcoming PJM capacity auction.

Alternative Energy: Waiting for 2H19
We expect muted 2Q19 results given most companies in the space point towards a 2H19 ramp in demand and earnings. 2Q19 should be a small loss for FSLR (Buy) before the ramp in Series 6 volume and transition cost declines. 2H19E adj. EPS of $3.18/sh compares to 1H19E adj. loss per share of $0.67/sh. Similarly, we expect TPIC (Buy) y/y EBITDA ramp to begin in 3Q19 as 1H19 was impacted by one-off labor and production issues. We see potential upward guidance revisions for 2019 module shipments, particularly for the Chinese exposed names CSIQ and JKS.

Environmental Services: Headwinds make 2019 guidance increases unlikely
We expect the focus to be on two headwinds: 1) a 64% YTD decline in recycled fiber pricing and 2) a 10% YTD decline in Permian Basin E&P rig count. However, 2019 guidance is likely to be maintained across the group, in our view, driven by strong core MSW price and volume and incremental M&A offsetting the commodity headwinds. WCN (Buy) remains our top pick.

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Figure 1: Electric Utilities Universe

Rating	Ticker	Company	7/19/2019 Price	Price Target	Total Return inc. Div. Yld	UBS 2018A EPS	UBS 2019E EPS	UBS 2020E EPS	UBS 2021E EPS	2020 P/E Ratio	2020 Prem/ Disc	2021 P/E Ratio	2021 Prem/ Disc	Current Dividend Yield	5 Yr EPS Growth	5 Yr DPS Growth	Regulatory Quartile
Neutral (CBE)	PCG	PG&E Corp	$17.79	$24	35%	$4.00	$3.27	$1.90	$2.39	9.4x	(53%)	7.4x	(60%)	0.0%	-4.9%	0.0%	4th
Buy	ACO	ATCO Ltd. (C$)	$43.29	$54	28%	$3.10	$3.22	$3.29	$3.43	13.2x	(32%)	12.6x	(30%)	3.7%	3.8%	6.1%	4th
Buy	PPL	PPL Corporation	$30.17	$36	25%	$2.38	$2.40	$2.54	$2.52	11.9x	(40%)	12.0x	(36%)	5.5%	3.1%	0.9%	2nd
Buy	DUK	Duke Energy	$88.45	$105	23%	$4.72	$4.97	$5.27	$5.57	16.8x	(16%)	15.9x	(15%)	4.3%	5.2%	2.0%	1st
Buy	EXC	Exelon	$47.57	$56	21%	$3.12	$3.19	$3.14	$3.14	15.1x	(24%)	15.2x	(19%)	3.0%	1.7%	5.3%	3rd
Buy	D	Dominion Energy	$76.85	$89	21%	$4.05	$4.22	$4.40	$4.65	17.5x	(12%)	16.5x	(11%)	4.8%	5.2%	4.3%	1st
Buy	FE	FirstEnergy Corp	$43.49	$50	18%	$2.60	$2.47	$2.53	$2.60	17.2x	(14%)	16.7x	(10%)	3.5%	1.9%	3.7%	2nd
Buy	NEE	NextEra Energy	$209.73	$240	17%	$7.70	$8.43	$9.08	$9.84	23.1x	16%	21.3x	14%	2.4%	7.9%	10.0%	1st
Buy	PEG	Public Service Ent Group	$60.18	$68	16%	$3.12	$3.22	$3.62	$3.54	16.6x	(16%)	17.0x	(9%)	3.1%	5.2%	5.0%	2nd
Buy	FTS	Fortis Inc (C$)	$51.62	$58	16%	$2.51	$2.54	$2.73	$2.93	18.9x	(2%)	17.6x	(3%)	3.5%	6.1%	6.0%	3rd
Buy	ES	Eversource Energy	$76.77	$86	15%	$3.25	$3.46	$3.67	$3.87	20.9x	5%	19.8x	6%	2.8%	5.9%	5.9%	2nd
Buy	AEP	American Electric Power	$90.28	$100	14%	$3.94	$4.10	$4.39	$4.75	20.5x	3%	19.0x	2%	3.0%	6.1%	7.0%	1st
Neutral	CU	Canadian Utilities Ltd (C$)	$35.80	$39	14%	$2.24	$2.21	$2.28	$2.38	15.7x	(18%)	15.1x	(17%)	4.6%	3.0%	5.4%	4th
Neutral	ED	Consolidated Edison	$87.24	$96	13%	$4.33	$4.33	$4.70	$4.87	18.6x	(7%)	17.9x	(4%)	3.4%	4.7%	3.0%	4th
Buy	EIX	Edison International	$70.17	$77	13%	$4.09	$4.49	$4.36	$4.58	16.1x	(19%)	15.3x	(18%)	3.5%	3.4%	0.2%	4th
Neutral	PNW	Pinnacle West Capital Corp	$93.59	$103	13%	$4.54	$4.94	$5.28	$5.60	17.7x	(11%)	16.7x	(10%)	3.2%	6.9%	6.0%	4th
Neutral	DTE	DTE Energy	$128.79	$141	12%	$6.30	$6.29	$6.56	$6.96	19.6x	(1%)	18.5x	(1%)	2.9%	4.8%	7.0%	1st
Buy	ETR	Entergy Corp	$105.60	$115	12%	$6.29	$5.30	$5.51	$5.82	19.2x	(3%)	18.1x	(3%)	3.4%	-0.1%	2.3%	2nd
Buy	EMA	Emera Inc (C$)	$54.02	$58	12%	$2.87	$2.79	$2.82	$3.02	19.1x	(1%)	17.9x	(1%)	4.4%	3.5%	4.3%	1st
Neutral	AEE	Ameren Corp	$75.98	$83	12%	$3.37	$3.25	$3.52	$3.92	21.6x	9%	19.4x	4%	2.5%	5.4%	6.0%	2nd
Buy	SRE	Sempra Energy	$140.05	$150	10%	$5.57	$5.89	$6.99	$7.55	20.0x	1%	18.6x	(0%)	2.8%	8.9%	8.1%	3rd
Neutral	SO	Southern Company	$55.27	$58	9%	$3.07	$3.03	$3.22	$3.36	17.2x	(13%)	16.5x	(12%)	4.5%	4.0%	3.2%	1st
Neutral	OGE	OGE Energy Corp	$42.74	$45	9%	$2.12	$2.11	$2.33	$2.45	18.3x	(8%)	17.5x	(6%)	3.4%	4.3%	7.0%	3rd
Neutral	CUP	Caribbean Utilities Corp Ltd	$16.35	$17	8%	$0.78	$0.82	$0.85	$0.93	19.1x	(1%)	17.6x	(3%)	4.3%	6.7%	5.7%	3rd
Neutral	AES	AES Corp.	$17.22	$18	8%	$1.22	$1.33	$1.46	$1.61	11.8x	(41%)	10.7x	(43%)	3.2%	8.0%	6.0%	2nd
Neutral	CMS	CMS Energy	$58.26	$61	7%	$2.33	$2.51	$2.68	$2.90	21.7x	9%	20.1x	8%	2.6%	6.8%	7.0%	1st
Neutral	XEL	Xcel Energy	$60.77	$63	6%	$2.47	$2.60	$2.77	$2.95	22.0x	11%	20.6x	10%	2.7%	5.7%	6.0%	2nd
Neutral	WEC	WEC Energy Group	$86.31	$87	4%	$3.34	$3.54	$3.74	$3.97	23.1x	16%	21.8x	17%	2.7%	6.0%	6.2%	1st
Neutral	EVRG	Evergy	$60.79	$61	3%	$2.67	$2.83	$3.07	$3.27	19.8x	(0%)	18.6x	(0%)	3.1%	5.7%	6.2%	3rd
Neutral	PNM	PNM Resources	$49.62	$50	3%	$2.00	$2.16	$2.24	$2.38	22.2x	12%	20.8x	12%	2.3%	5.0%	9.3%	4th
Neutral	LNT	Alliant Energy	$49.93	$49	1%	$2.19	$2.26	$2.49	$2.56	20.1x	1%	19.5x	5%	2.8%	4.6%	6.0%	2nd
Sell	POR	Portland General	$54.61	$52	(2%)	$2.37	$2.48	$2.60	$2.74	21.0x	6%	20.0x	7%	2.8%	5.0%	6.0%	3rd
Sell	H	Hydro One Ltd (C$)	$23.34	$21	(6%)	$1.35	$1.35	$1.30	$1.34	18.0x	(10%)	17.4x	(7%)	4.2%	2.5%	4.7%	4th
Sell	HE	Hawaiian Electric Industries	$44.31	$35	(18%)	$1.85	$1.95	$2.05	$2.16	21.6x	9%	20.5x	10%	2.9%	5.0%	3.2%	4th
Overall Average (unnormalized, inc. Gas Midstream)										18.8x		17.8x					
Electric Utility Normalized (including Gas Midstream)										19.9x		18.6x					

Source: FactSet, UBS Equity Research

Figure 2: Water Utilities Universe

Rating	Ticker	Company	7/19/2019 Price	UBS Price Target	Total Return inc. Div. Yld	UBS 2018A EPS	UBS 2019E EPS	UBS 2020E EPS	UBS 2021E EPS	2021E P/E Ratio	2021E Prem/ Disc	Current Dividend Yield	5 Yr EPS Growth	5 Yr DPS Growth
Buy	AWK	American Water	$114.98	$123	9%	$3.30	$3.57	$3.85	$4.17	27.5x	0%	1.6%	8.2%	10.0%
Neutral	SJW	SJW Group	$64.77	$64	1%	$2.51	$2.14	$2.34	$2.49	26.0x	(5%)	1.9%	2.6%	7.0%
Buy	WTR	Aqua America	$41.00	$42	5%	$1.41	$1.48	$1.58	$1.68	24.5x	(11%)	2.1%	6.4%	7.0%
Sell	CTWS	Connecticut Water Service	$69.57	$67	(2%)	$2.29	$2.39	$2.53	$2.77	25.1x	(8%)	1.8%	6.7%	5.0%
Sell	CWT	California Water Service	$52.60	$44	(15%)	$1.44	$1.39	$1.61	$1.70	30.9x	13%	1.5%	5.7%	5.0%
Sell	AWR	American States Water	$76.02	$57	(24%)	$1.73	$1.98	$2.08	$2.20	34.6x	26%	1.4%	7.8%	6.0%
AVERAGE										27.4x				

Source: FactSet, UBS Equity Research

Figure 3: Independent Power Producers

Rating	Ticker	Company	7/19/2019 Price	Price Target	Total Return inc. Div. Yld	UBS 2018A EBITDA	UBS 2019E EBITDA	UBS 2020E EBITDA	UBS 2021E EBITDA	2020 EV/ EBITDA Ratio	2020 Prem/ Disc	2021 EV/ EBITDA Ratio	2021 Prem/ Disc	2019E Net Debt/ EBITDA
Buy	VST	Vistra Energy Corp	$21.83	$35	63%	$2,760	$3,292	$3,212	$2,654	5.4x	(25%)	6.1x	(10%)	2.9x
Buy	NRG	NRG Energy	$35.14	$46	31%	$2,001	$1,970	$1,821	$1,906	5.8x	(20%)	5.2x	(24%)	2.2x
MID-CYCLE MEDIAN										7.2x		6.8x		

Source: FactSet, UBS Equity Research

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Figure 4: Regulated Utilities & Power 2Q19 Earnings Summary

U.S. companies in US$ Cdn companies in C$ CUP in US$		Quarterly						Annual				
Company	Ticker	Scheduled Reporting Date	2Q19E UBS	2Q19E Consensus	UBS Vs. Consensus	UBS Confidence Indicator[1]	2Q18A Adjusted	2019E UBS	2019E Consensus	UBS Vs. Consensus	Trailing 12 Month	2019E Guidance
ELECTRIC UTILITIES												
AES Corp	AES	6-Aug	$0.25	$0.28	($0.03)		$0.25	$1.33	$1.33	($0.00)	$1.22	$1.28-$1.40
ATCO Ltd	ACO.x-TSE	25-Jul	$0.61	$0.61	($0.00)		$0.53	$3.22	$3.11	$0.11	$3.29	N/A
Alliant Energy	LNT	1-Aug	$0.43	$0.45	($0.02)		$0.43	$2.26	$2.25	$0.00	$2.19	$2.17-$2.31
Ameren Corp	AEE	2-Aug	$0.75	$0.78	($0.03)		$0.97	$3.25	$3.26	($0.01)	$3.31	$3.15-$3.35
American Electric Power	AEP	25-Jul	$0.97	$0.99	($0.02)		$1.01	$4.10	$4.13	($0.03)	$4.14	$4.00-$4.20
Canadian Utilities Ltd	CU-TSE	25-Jul	$0.40	$0.43	($0.03)		$0.39	$2.21	$2.18	$0.03	$2.31	N/A
Caribbean Utilities Corporation Ltd	CUP.USD-TSE	2-Aug	$0.21	$0.21	$0.00		$0.21	$0.82	$0.79	$0.02	$0.84	N/A
CMS Energy	CMS	25-Jul	$0.32	$0.46	($0.14)		$0.48	$2.51	$2.50	$0.01	$2.05	$2.47-$2.51
Consolidated Edison	ED	1-Aug	$0.54	$0.59	($0.05)		$0.61	$4.33	$4.35	($0.02)	$4.27	$4.25-$4.45
Dominion Energy	D	31-Jul	$0.76	$0.79	($0.03)		$0.86	$4.22	$4.19	$0.03	$3.91	$4.05-$4.40
DTE Energy	DTE	24-Jul	$1.17	$1.20	($0.03)		$1.36	$6.29	$6.24	$0.05	$6.29	$5.97-$6.33
Duke Energy	DUK	6-Aug	$0.98	$0.98	$0.00		$0.93	$4.97	$4.92	$0.06	$4.71	$4.80-5.20
Edison International	EIX	25-Jul	$1.21	$1.09	$0.12		$0.85	$4.49	$4.67	($0.18)	$4.31	$4.72-$4.92
Emera Inc	EMA-TSE	12-Aug	$0.52	$0.55	($0.03)		$0.48	$2.79	$2.85	($0.07)	$2.98	N/A
Entergy Corp	ETR	31-Jul	$1.40	$1.36	$0.04		$0.83	$5.30	$5.29	$0.02	$6.57	$5.10-$5.50
Evergy, Inc	EVRG	7-Aug	$0.58	$0.69	($0.11)		$0.90	$2.83	$2.90	($0.06)	$2.36	$2.80-$3.00
Eversource Energy	ES	31-Jul	$0.78	$0.75	$0.03		$0.76	$3.46	$3.46	($0.00)	$3.39	$3.40-$3.50
Exelon Corp	EXC	1-Aug	$0.59	$0.65	($0.06)		$0.71	$3.19	$3.14	$0.05	$2.92	$3.00-$3.30
FirstEnergy Corp	FE	23-Jul	$0.58	$0.61	($0.03)		$0.62	$2.47	$2.51	($0.04)	$2.55	$2.45-$2.75
Fortis Inc	FTS-TSE	2-Aug	$0.56	$0.61	($0.05)		$0.59	$2.54	$2.62	($0.08)	$2.51	N/A
Hawaiian Electric Industries	HE	2-Aug	$0.44	$0.45	($0.01)		$0.42	$1.95	$1.95	$0.00	$1.92	$1.85-$2.05
Hydro One Ltd	H-TSE	9-Aug	$0.26	$0.29	($0.03)		$0.33	$1.35	$1.46	($0.12)	$1.37	N/A
NextEra Energy	NEE	24-Jul	$2.31	$2.29	$0.02		$2.11	$8.43	$8.40	$0.03	$8.18	$8.00-$8.50
OGE Energy Corp	OGE	8-Aug	$0.52	$0.52	($0.00)		$0.55	$2.11	$2.14	($0.03)	$2.05	$2.05-$2.20
PG&E Corp	PCG	26-Jul	$1.16	$0.99	$0.17		$1.16	$3.27	$3.81	($0.54)	$4.13	N/A
Pinnacle West Capital Corporation	PNW	8-Aug	$1.37	$1.55	($0.18)		$1.48	$4.94	$4.85	$0.09	$4.56	$4.75-$4.95
PNM Resources	PNM	2-Aug	$0.37	$0.49	($0.12)		$0.53	$2.16	$2.12	$0.04	$1.77	$2.10-$2.18
Portland General	POR	2-Aug	$0.52	$0.51	$0.01		$0.51	$2.48	$2.45	$0.03	$2.48	$2.35-$2.50
PPL Corporation	PPL	6-Aug	$0.55	$0.58	($0.03)		$0.55	$2.40	$2.43	($0.03)	$2.36	$2.30-$2.50
Public Service Enterprise Group	PEG	30-Jul	$0.58	$0.64	($0.06)		$0.64	$3.22	$3.26	($0.03)	$3.17	$3.15-$3.35
Sempra Energy	SRE	2-Aug	$1.17	$1.21	($0.04)		$1.35	$5.89	$6.04	($0.15)	$5.89	$5.70-$6.30
Southern Company	SO	31-Jul	$0.72	$0.72	$0.00		$0.80	$3.03	$3.02	$0.01	$2.81	$2.98-$3.10
WEC Energy Group	WEC	5-Aug	$0.70	$0.72	($0.02)		$0.73	$3.54	$3.51	$0.02	$3.41	$3.48-$3.52
Xcel Energy	XEL	1-Aug	$0.52	$0.54	($0.02)		$0.52	$2.60	$2.62	($0.02)	$2.51	$2.55-$2.65
Average			**$0.73**	**$0.75**	**($0.02)**		**$0.75**	**$3.35**	**$3.38**	**($0.02)**	**$3.32**	
WATER UTILITIES												
American States Water Company	AWR	TBA	$0.58	$0.55	$0.03		$0.44	$1.98	$1.97	$0.01	$1.73	N/A
American Water Works Company	AWK	31-Jul	$0.89	$0.93	($0.04)		$0.83	$3.57	$3.59	($0.02)	$3.31	$3.54-$3.64
Aqua America	WTR	6-Aug	$0.32	$0.38	($0.06)		$0.37	$1.48	$1.39	$0.09	$1.40	$1.45-$1.50
California Water Service Group	CWT	1-Aug	$0.41	$0.37	$0.04		$0.37	$1.39	$1.40	($0.02)	$1.53	N/A
Connecticut Water Service	CTWS	TBA	$0.68	$0.68	$0.00		$0.59	$2.39	$2.36		$2.22	N/A
SJW Group	SJW	24-Jul	$0.63									
Average			**$0.59**	**$0.58**	**($0.00)**		**$0.52**	**$2.16**		**$0.02**		
IPPS - Adjusted EBITDA not EPS	**US$mlns**											
NRG Energy	NRG	7-Aug	$486	$597	($111)		$517	$2,010	$2,023	($13)	N/A	$1,850-$2,050
Vistra Energy	VST	2-Aug	$718	$688	$30		$653	$3,210	$3,347	($137)	N/A	$3,220-$3,420

1. UBS Confidence Indicator: Green = high confidence in estimate vs. consensus; Red = low confidence in estimate vs. consensus; Yellow = mid confidence in estimate vs. consensus

2. Not meaningful. UBS estimate and company guidance reflect UPO-only earnings.

3. UBS estimates reflected above remove the estimated NRG Yield assets results from prior and current quarter and consensus for comparison purposes as they were sold on 8/31/18

Source: FactSet, company filings, UBS Equity Research

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Regulated Utilities 2Q19 preview

Key Calls this Quarter

AES Corp. We expect a discussion of development in Vietnam of 450 TBTU of LNG capacity and 2 GW of combined cycle gas or projects totalling $3B. The projects could come on-line in the 2023-2025 timeline. AES would look to use partner equity in the project while still growing net income up to $100M in our estimation.

Alliant Energy. With intervenor testimony in the IP&L rate case 8/1 the company may be in a position to comment. An update on 2020 equity needs will wait until the third quarter call.

Ameren Corp. We expect a discussion on Missouri renewables and financing needs. We raised our assumption for 2019 equity need to $700M from $500M due to the acquisition of an incremental 400 MW if wind.

American Electric Power. Management could discuss the North Central Wind Energy facilities at SWEPCO and PSO which total 1,485 MW and represent $2B in rate base. The company could use up to 50% equity to finance these projects which would provide for $0.07-$0.10/share of accretion. Another topic is the numerous rate cases in which the company is involved including Arkansas, Indiana, Michigan, and Texas.

CMS Energy. Despite a light Q2'19 ($0.32E versus $0.48 last year) we believe there is a reasonable bridge to 2019 guidance of $2.47-$2.51 due to the absence of reinvestment spending in 2018 which could add $0.23/share along with contingency.

DTE Energy. We look for a discussion of how the company thinks about the company's 5 year forecast at the Gas, Pipelines & Storage segment and plans to spend $4-$5B.

Edison International. With wildfire legislation having passed in California the company could raise its forecast of capital needs for its contribution to the wildfire insurance fund from the $1.5B equity need discussed on the first quarter call. EIX stands out as one of the potential beats versus consensus due to $0.22/share of rate relief.

Emera Inc. We expect EMA to spend time on the call on August 12 discussing the Maine intervenor testimony filed in the pending EmeraMaine sale to ENMAX at the Maine Public Service Commission on August 5 and provide an update on the process.

FirstEnergy. We expect FE to maintain 2019 EPS guidance of $2.45-$2.75 but following a Ohio Supreme Court decision they are collecting the Distribution Modernization Rider subject to refund.

OGE Energy. We expect investors to revive the issue of dividend payout although we do not necessarily expect news beyond the previously stated policy of 10% annual growth in the dividend through 2019.

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Weather

Weather was broadly milder year over year in the second quarter, with weather in all regions below normal and the country 4% below normal on degree days. Regionally the West North Central Region, Middle Atlantic, and East North Central region experienced the fewest degree days versus normal for the quarter, while the Pacific region and the Southeast had the closest to normal weather experience. Year over year, the Middle Atlantic, Mountain, Pacific, and East North Central regions were down the most, while the East & West South Central regions were actually better year on year and the West North Central region was flat.

Figure 5: 2Q19 Regional Degree Days

Q2'19 Degree Days (April , May, June)	2Q19	2Q18	2Q Normal	2Q19 vs. 2Q18	2Q19 vs. Normal
New England	927	966	1,055	-4%	-12%
Middle Atlantic	749	885	945	-15%	-21%
East North Central	858	961	1,072	-11%	-20%
West North Central	947	951	1,232	0%	-23%
South Atlantic	883	747	900	18%	-2%
East South Central	809	758	960	7%	-16%
West South Central	961	880	1,073	9%	-10%
Mountain	756	886	823	-15%	-8%
Pacific	693	811	741	-15%	-6%
United States	4,882	4,778	5,073	2%	-4%

Source: NOAA, UBS

We also looked at the states that had the biggest shifts in year-on-year weather. We sorted them on the largest percentage change although 2Q degree days are not that significant in some areas.

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Figure 6: Top 10/Bottom 10 States' Change in Degree Days

Q2'19 Degree Days	2Q19	2Q18	2Q Normal	2Q19 vs. 2Q18	2Q19 vs. Normal
Oregon	62	47	29	32%	114%
Washington	62	53	28	17%	121%
Delaware	436	373	264	17%	65%
Alabama	771	697	568	11%	36%
Maryland	407	368	263	11%	55%
Florida	1,234	1,120	1,010	10%	22%
Louisiana	959	894	838	7%	14%
Georgia	713	678	516	5%	38%
Mississippi	776	743	657	4%	18%
South Carolina	760	737	550	3%	38%
Kansas	323	590	395	-45%	-18%
Utah	94	173	144	-46%	-35%
Illinois	193	356	256	-46%	-25%
North Dakota	108	203	124	-47%	-13%
Minnesota	115	232	143	-50%	-20%
Wyoming	33	74	60	-55%	-45%
Colorado	59	155	60	-62%	-2%
Michigan	69	182	156	-62%	-56%
Wisconsin	61	182	133	-66%	-54%
Maine	6	25	29	-76%	-79%

Source: NOAA, S&P Global Market Intelligence, UBS

Electric Utilities

- **AES.** We expect flat EPS in Q2'19 at $0.25 and the company's growth to be more back-end loaded this year with OPGC II in India coming on line in the second quarter and renewable capacity funded by tax equity in the fourth quarter. Otherwise the Changuinola outage in Panama is a negative driver though in guidance as are asset sales. On the positive side we expect similar drivers to Q1'19 like cost cuts, the Dominican Republic and the U.S. utilities. Despite a light first half AES is in position to make the full year due to start-ups of new renewable capacity primarily in the United States and of the OPGC II coal plant in India.

Figure 7: AES 2019 Earnings Drivers

	2019E	Q1'19A	Q2'19E	Q3'19E	Q4'19E	Comments
Prior Year Start		$0.28	$0.25	$0.35	$0.36	
Asset Sales		-$0.04	-$0.03	-$0.01	-$0.01	
Tax rate		$0.01	$0.01	$0.00	-$0.01	30% for the year
Dominican Republic				$0.02		Absence of outage
Argentina			-$0.01			
Panama			-$0.01			Hydro, outage
Panama, Colon				$0.01	$0.01	Tank vs. floating storage
OPGC II			$0.01	$0.01	$0.01	Start-up of operations
Renewables				$0.03	$0.03	Start-up of operations
Parent Interest		$0.01	$0.01			
SBUSs Other		$0.02				
Sensitivities, F/X			$0.01	$0.01		Interest rates
Other			$0.01			
UBS 2019 Forecast	$1.33	$0.28	$0.25	$0.42	$0.39	
Tax rate 2018			36%	28%	24%	

Source: Company reports, Factset, UBS Equity Research

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- **ACO.** We see ATCO Ltd earnings in line with 2Q'18 at C$0.61. Year over year earnings drivers will be from the S&L business segment where seasonally the largest contributions are in the 2nd and 4th quarters. S&L growth to the full year run rate is expected to be more back-end loaded in 2019 due to the ramp at construction facilities as work force has begun ramping up in the quarter. Year on year, earnings are likely to be higher at S&L vs. 2Q'18 related to the close of the Mexico acquisition in late February. The production factory in Chile was completed in 2Q'18 and could contribute year over year. Sanctioning of new projects related to LNG Canada, Coastal GasLink, and the Silvertip Mine, among others are still ramping up and likely to contribute more in the back half of the year vs. the 2Q. The Naltume Ports acquisition was closed in September 2018 and will be a year on year contributor at the expected run rate of about C$4mln/qtr. Given the ownership stake in Canadian Utilities, earnings will also be impacted by the drivers discussed for that company, which are provided below.

- **LNT.** We see LNT's Q2'19 EPS flat at $0.43 versus $0.43 in Q2'18. The absence of above normal weather in Q2'18 is -6 cents and weather was below normal this year. Rate relief at WP&L should add 5 cents and interim rate relief at IP&L could add 8 cents. IP&L wind going into service at the end of March could add 2 cents. Negative drivers are depreciation and interest expense including $600M at IP&L at rates of 3.0-3.6%.

Figure 8: LNT Q2'19 EPS Drivers

	Q2'19E	Q1'19A	Q2'18A
IP&L	$0.26	$0.23	$0.22
WP&L	$0.19	$0.28	$0.17
Utils & Corp	$0.45	$0.52	$0.41
ATC	$0.03	$0.03	$0.03
Non-utility	-$0.03	-$0.02	-$0.01
Total	$0.43	$0.53	$0.43
Shares MM	238	237	232

Q2'18	$0.43
Weather to normal	-$0.06
Weather below normal	-$0.02
IP&L interim rates	$0.08
WP&L rates	$0.05
IP&L wind in service	$0.02
IP&L depreciation	-$0.02
Interest expense-unregulated	-$0.02
Interest expense-regulated	-$0.02
Q2'19	$0.43

Source: Company reports, Factset, UBS Equity Research

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- **AEE.** We look for a decline in AEE's EPS in Q2'19 to $0.75 from $0.97. A normalized Q2'18 is $0.74 with normal weather (-$0.19/share), Callaway outage timing (-$0.09/share) and Missouri taxation (+$0.04/share). Otherwise we see $0.02 from Ameren Transmission rate base growth and $0.03 from Ameren Illinois Electric and Gas growth offset by -$0.04 for below normal June weather in Missouri and other expenses of -$0.02/share.

Figure 9: AEE Q2'19 EPS Drivers

Q2'18	$0.97
Weather to normal	-$0.19
(10 year not 30 year average)	
Callaway	-$0.08
Missouri taxation	$0.04
Normalized Prior Year	$0.74
Q2'19 Drivers	
Ameren Transmission rate base	$0.02
Ameren Illinois rate base	$0.03
Ameren Illinois electric ROE impact	-$0.01
Below normal weather, other	-$0.04
Q2'19	$0.75

Source: Company reports, Factset, UBS Equity Research

- **AEP.** We expect a small decline in AEP's EPS in Q2'19 to $0.97 from $1.01. We expect a decline of $0.12 to normal weather. Rate relief likely added $0.09/share or $0.06 to Vertically Integrated and $0.03 to T&D Utilities. O&M and depreciation increases reduced EPS by $0.05 or more.

Figure 10: AEP Q2'19 Earnings Drivers by Segment

	Q2'19E	Q1'19A	Q2'18A	
Adjusted Earnings	$0.97	$1.19	$1.01	Earnings Drivers
Vertically Integrated	$0.50	$0.63	$0.56	Normal weather -12 cents
				Rates +6, D&A -3, O&M -1
T&D Utilities	$0.23	$0.32	$0.23	Rates +3 cents, O&M -1, D&A
AEP Trans Holdco	$0.26	$0.25	$0.21	
Gen & Marketing	$0.04	$0.09	$0.05	
Corp & Other	-$0.06	-$0.10	-$0.04	

Source: Company reports, Factset, UBS Equity Research

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- **CMS.** We see a decline in CMS' EPS in Q2'19 to $0.32 from $0.48. Michigan experienced below normal weather versus an $0.11/share positive in Q2'18. Carrying costs that we expect the company can pick-up in electric and gas rate case recovery such as depreciation, interest and taxes was potentially a -$0.05/share impact or more. We also look for a decline at CMS Enterprises from lower sales and revenue. Positives include rate case margins (25% of revenue) which add $0.06/share and other items. We believe the company can meet EPS guidance due to reinvestment in 2018.

Figure 11: CMS Q2'19 EPS Drivers

	2019E	Q1'19A	Q2'19E	Q3'19E	Q4'19E	Comments
Prior Year Start		$0.86	$0.48	$0.59	$0.40	
Weather		$0.08				
Storm Costs		-$0.10				
O&M reinvestment				$0.07	$0.16	Absence of '18 impact
Rates & Investment		$0.03				
Usage, Enterprises & Other		-$0.12				
Weather to normal			-$0.11	-$0.12	-$0.01	Absence of '18 impact
Weather			-$0.03			
Rate case recoverable costs (D&A, interest)			-$0.05			
Debt, parent dilution			-$0.01			
Enterprises sales and revenue			-$0.04	$0.04	$0.04	
Gain on asset sales			$0.03			
Electric Rate Case			$0.06	$0.06	$0.06	
Gas Rate Case					$0.13	Effective 10/1
Taxes			-$0.02			
Other			$0.01	$0.01	$0.01	Charitable, other
UBS 2019 Forecas	$2.48	$0.75	$0.32	$0.65	$0.79	

Source: Company reports, Factset, UBS Equity Research

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- **CU.** We expect investors on the conference call to want to discuss the potential use of proceeds given the company's announced sale of the Alberta Power business and the Alberta Power Line. We anticipate that management will reiterate the focus to potentially target utility or utility like infrastructure or long term contracted assets that would provide not only adequate capital returns but also geographic diversity outside of Alberta. For scale once the asset sales are closed we would expect acquired assets could range in the C$1 – C$3Bln range and that the higher end of that range could require preferred equity financing. A larger scale transaction would be possible but management would likely seek a financial partner in such a scenario. For the quarter we expect earnings of C$0.40 versus C$0.39 last year. We anticipate that management will report the Alberta Power and Alberta Powerline segments as assets held for sale, but include them in both reported and adjusted earnings. The quarterly results will be most impacted by significantly lower Alberta power prices in the C$30/MWh range due to mild June and July weather vs. warm weather in 2Q '18. Regulatory decisions in Alberta for the transmission and pipeline segments will be +C$2mln year on year, and the electric transmission application order will book make up revenue of ~C$13mln for 2018 and ~C$4mln for Q1'19 as well as the Q2'19 impacts in the quarter. Other topics of interest for the call will be the IT common matters decision and how that ties to the sale of IT services in as well as the approval of the Hanna transmission project.

- **CUP.** We expect Caribbean utilities to report an in-line quarter at $0.21. Year over year drivers will be increased usage from economic growth mostly driven by likely increased overnight tourism visits and increased financial sector activity. In 1Q'19 customer growth was 2% year on year with 5% usage growth leading to 4% sales growth overall. Year over year the revised rates for large commercial demand customers that were awarded in June 2018, as well as the 1.8% rate increase under the RCAM mechanism will have an impact. Further we expect slight reductions in financing and operating costs year on year.

- **ED.** We see lower EPS for ED in Q2'19 at $0.56 versus $0.61 last year. 3 considerations are: 1) Steam added 3 cents in Q2'18 which unlikely to occur; 2) Stagecoach earnings sharing steps down to 50% from 60% starting 6/6; and 3) An increase in the stock price has a negative impact on the mark to market which was -4 cents as a reference in Q1'19. In Q2'18 CECONY earned a 9.6% ROE although comp mark-to-market could contribute to reducing that to 9.0% which would be a -3 cent reduction. Other drivers include a reduction in the Clean Energy Businesses ($0.06 versus $0.09) potentially offset by cost control.

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Figure 12: ED Q2'19 EPS Summary

	Q2'19E	Q1'19A	Q2'18A	Earnings Drivers
CECONY	$0.45	$1.28	$0.48	Q2'18 was 9.6% ROE and 48% equity ratio equity dilution, comp -3
O&R	$0.02	$0.10	$0.02	
CEBs	$0.06	-$0.04	$0.09	
CET	$0.04	$0.04	$0.04	StageCoach 50% of Crestwood not 60% start 6/6
Parent	$0.00	$0.01	-$0.02	
Total	$0.54	$1.39	$0.61	Reflects share dilution
Shares MM	327	322	311	

Source: Company reports, Factset, UBS Equity Research

D. We expect D to report adjusted EPS of $0.76 vs. consensus of $0.79, and 2Q'18 results of $0.86. The guidance range for the quarter is $0.70-$0.80. Negative yr/yr drivers include a Millstone refueling outage (historical cost range is $0.07-$0.09), share dilution (approx. $0.16), assets sales and more normal weather. Positive yr/yr drivers include the earnings contribution from the Southeast Energy Group ($0.18 before financing considerations) and rate base earnings growth. Beyond the earnings and regular business report, we expect investors to focus on updates around the Atlantic Coast Pipeline and Supply Header. While an order from the 4th Circuit addressing the biological opinion is expected in early August (90 days after oral arguments), the more important US Supreme Court decision on whether to take up the case won't be issued till late 2019.

- **DTE.** We forecast lower EPS for DTE in Q2'19 at $1.17 versus $1.25 last year. We see 3 adjustments in Q2'18 which are: 1) Weather was $0.17 above normal and this year was unseasonably cold; 2) There will be 1.5 months of the DTE Electric rate increase which we forecast as a 25% margin and 3) Rate base expenses are up to -$10M after-tax per quarter for DTE Electric and DTE Gas combined. We also see some impact from the absence of NEXUS AFUDC and depressed volumes.

Figure 13: DTE Q2'19 EPS and Net Income Summary (Dollars in Millions)

	Q2'19E	Q1'19A	Q2'18A	Earnings Drivers
DTE Electric	$150	$147	$163	Weather -$31M to normal and Q2 was cold Rate relief +$30M; Rate base costs -$10M
DTE Gas	$10	$151	$14	Volume weighted impact $47M rate increase rate-base costs -$3M; tax timing reveral -$10M
GS&P	$50	$48	$60	Lower volumes; absence of AFUDC but on track
P&I	$33	$26	$43	1/3 of result to guidance
Corp & Other	-$35	-$3	-$41	1/3 of result to guidance
Energy Trading	$5	$5	$8	
DTE Energy	$214	$374	$247	
EPS	$1.17	$2.05	$1.36	
Shares MM	182	182	181	

Source: Company reports, Factset, UBS Equity Research

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- **DUK.** We expect DUK to report adjusted EPS of $0.98 vs. consensus of $0.98 and 2Q'18 results of $0.93. Earnings in the quarter should benefit from better than normal weather, load growth, new rates (SC) and incremental rate base (Citrus County & Rosamont). Midstream will show modest growth (AFUDC) and the commercial renewables segment should show a marked improvement over Q1 as the shape of earnings from that segment adjust. Beyond earnings and guidance, we expect investors to focus on legislative and coal ash updates from North Carolina, the Atlantic Coast Pipeline and the legal appeal of the rate decision in South Carolina.

- **EIX.** We forecast Q2'19 EPS for EIX of $1.21 versus $0.85 last year. The big driver is $0.22 from the general rate case which is the company discussed on the Q1'19 investor call. We also expect for the regulatory lag on non-fuel O&M recovery to dissipate. Other positives include transmission rate base growth and lower financing costs. At Edison Energy and Parent we assume -$0.05 versus -$0.06 last year.

Figure 14: Southern California Edison Q2'19 EPS Summary

Q2'18 SCE	$0.91
Rate case	$0.22
O&M	$0.08
Financing	$0.05
FERC	$0.03
D&A & other	-$0.03
Q2'19 SCE	$1.26

Source: Company reports, Factset, UBS Equity Research

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- **EMA.** We expect EMA to report C$0.52 vs. C$0.48 last year. Drivers will be the sale of the New England generation assets year over year and mild weather outside the Southeast will be a drag on results in Maine and on the remaining energy segment. In 2Q'18 the power plants has a pre-interest allocation earnings of C$13.5mln. Interest expense at the plants allocated to corporate was C$6mln. Maine should show better results year on year given non-recurring storm expenses in 2Q'18. Further Maine received a distribution rate increase of US$15.7mln in July of 2018. At Nova Scotia Power, weather has been colder than normal which is a driver of demand for electric heat. However, upside is limited from strong weather as a result of a capped ROE sharing mechanism at 9.25%, which is 25bps above the allowed ROE of 9%. As a result, earnings in 2Q will not be as strong as weather might otherwise indicate. In Florida, unlike most of the United States, weather was favorable vs. last year with the warmest May on record and the tail end of June was also warm. The solar under the SOBRA program now has 405MWs earning returns vs. 145MWs booking AFUDC last year. FX average is also approximately 1.33 vs. 1.29 year on year and each +0.01 in FX is about +C$0.01/share to EMA. On the call we expect investors to be focused on the approval process for the sale of Emera Maine and the management take on the intervenor testimony which will be filed on August 6, vs. the earnings call date of August 12.

- **ETR.** We expect ETR to report adjusted EPS of $1.40 vs. consensus of $1.39 and 2Q'18 results of $1.23. Weather for the quarter should be positive vs. normal, but below last year, while rate increases in Arkansas and Louisiana and rate base growth in Louisiana (St. Charles power station) should all represent yr/yr growth. Our estimate assumes a ratable allocation of targeted O&M savings over the remainder of the year, but we recognize that the actual realization of these savings could be uneven. We expect ETR will update investors on its continued exit from the EWC business, the various proceedings at the regulated entities and any residual impact from the recent hurricane.

- **EVRG.** We forecast Q2'19 Adjusted EPS of $0.58 versus $0.90 pro-forma last year. Weather conditions made a significant swing in the quarter from $0.22/share above normal last year to below normal this year. Deferred taxes was a negative driver as well. Another negative is a reduction in pro-forma merger transaction costs under accounting rules which is a $35-$36M pre-tax change (Q2'18 10-Q p. 66). Positive drivers include plant shutdowns at the end of 2018 (Montrose and Sibley), merger synergies and the share buyback.

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Figure 15: EVRG Q2'19 EPS Drivers

	Q2'19E	Q1'19A	Q2'18A	Earnings Drivers
Pro-forma, adjusted	$0.58	$0.44	$0.90	
Weather to normal	-$0.22	$0.05	$0.22	
Weather	-$0.02			Cooling days 14% below normal
Rates	$0.00	$0.05		
O&M, absence w-off	$0.03	$0.05		
O&M	-$0.10			Reduction in pro-forma transaction costs
D&A	-$0.01	-$0.08		Schedule changes offset in revenue
Tax Rate	-$0.19	-$0.01	$0.19	Change in deferred taxes
Bill Credits	$0.01			3 months versus 5 months
Severance		$0.06		
Plant shutdowns	$0.06			Sibley (400 MW) and Montrose (330 MW)
Merger Synergies	$0.07			
Share buyback	$0.04			
Shares Quarter Ended	247	252		
Avg Shares-MM	250	253	272	
GAAP				
EPS	$0.58	0.39	0.56	
Shares-MM	250	253	181	

Cooling Degree Days	Q2'19	Norm	Q2'18
Missouri	322	354	569
Kansas	323	395	590
Total	645	749	1159
Q2'19 vs.		-14%	-44%

Source: NOAA, Company reports, Factset, UBS Equity Research

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- **ES.** We expect ES to report adjusted EPS of $0.78 vs. consensus of $0.77 and 2Q'18 results of $0.76. We look for ES to benefit modestly from the 2018 CL&P rate case implementation, the transmission rate base true up that occurs in the second quarter, ongoing cost control efforts, the investment portfolio mark and the Nstar Electric rate increase. Offsetting these benefits will be the impact of decoupling at Yankee Gas, higher property tax and interest expense, and the loss of generation earnings. We expect the investor call to focus on incremental growth opportunities (GridMod spending in CT/Mass/NH, offshore wind, water M&A), and changes in regulatory personnel.

- **EXC.** We expect EXC to report $0.59 v. $0.71 last year. Overall this expectation is below the mid-point of the company's $0.55-$0.65 2Q'19 guidance range provided on the 1Q'19 conference call. Factors not incorporated into the guidance range at the time were mild weather impacts at the non-decoupled utilities, especially PECO. Further, the planned outage at the Salem nuclear plant lasted approximately 30 days beyond likely initial projections which would have increased costs by ~$30mln on pre-tax basis. NDT will also likely be a drag quarter over quarter as of the $0.07 of NDT gains in 2018, $0.05 were recorded in 2Q'18. Milder weather is unlikely to impact the nuclear fleet all that much as run times were likely around-the-clock regardless although it could have some small impact on the much smaller non-nuclear generation fleet. Power prices and spreads are lower year on year, however, financial and retail hedging as well as the zero emission credits in New York, New Jersey, and Illinois will protect the majority of the nuclear fleet from significant volatility in EBITDA.

- **FE.** We forecast Q2'19 EPS of $0.58 versus $0.62 last year. Weather to normal was -3 cents versus last year and conditions were below normal this year. The absence of a renewable energy credit is a -3 cent item too. Offsetting that is cost cuts and rate base growth. This compares to the company's $0.55-$0.65 guidance for the quarter.

Figure 16: FE Q2'19 EPS (Dollars in Millions)

	Q2'19E	Q1'19A	Q2'18A	Earnings Drivers
Adjusted Earnings	$0.58	$0.67	$0.62	
Regulated Distribution	$0.50	$0.62	$0.55	Weather -3 cents to normal and below normal in 2019; renewable credit reversal -3 cents, D&A -1 to -2 cents, FE Tomorrow +1 cents
Regulated Transmission	$0.21	$0.19	$0.19	+2-3 cents of rate base growth
Corporate/Other	-$0.13	-$0.13	-$0.12	

Source: Company reports, Factset, UBS Equity Research

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- **FTS.** We expect that consistent with Q1'19 reporting Fortis will report results excluding mark to market impacts from the Aitken Creek storage facility and adjust prior periods to exclude them as well. As a result 2Q '18 will be restated to C$0.59. For the current quarter we expect lower earnings year on year of C$0.56 mainly driven by significantly milder weather in Arizona. Further 2Q'18 included nonrecurring items related to the positive hydrology impacts in Belize and the Hurricane Irma insurance receipts. Offsetting this will be rate base and sales growth as well as positive timing impacts related to the timing of plant outages in Arizona. Lastly, the sale of the Waneta hydroelectric plant will have a greater than anticipated drag on the quarterly results as the majority of earnings contribution was seasonally in the second quarter. We expect that on the call investors will be focused on execution of any potential incremental capital projects that could increase or extend current growth rates, and any updates on the Federal Energy Regulatory Commission transmission ROE review process and the ongoing rate case for Tucson Electric Power in Arizona.

- **HE.** We expect HE to report adjusted EPS of $0.44 vs. consensus of $0.45 and 2Q'18 results of $0.42. Yr/Yr earnings will benefit from interim rates at Maui Electric ($12.2mm; effective Aug '18) and the interim recovery mechanism (MPIR) for the Schofield project. We expect Bank earnings to benefit from asset sales and lease expirations at some point this year (3-5 cents) but believe these will be one time benefits. We expect the earnings conference call to focus on the regulatory climate and proceedings in Hawaii, and capital spending opportunities.

- **H.** We expect H to report C$0.26 v. C$0.32 last year, mainly driven by milder weather year on year. Peak loads in Ontario in May were down 20% year on year and overall peak loads were down 9% quarter over quarter. Further, there were significant storm costs in Ontario in 2Q'18 which are helpful to earnings as they are capitalized, so lack of storm costs will likely increase O&M year on year given a return to normal work patterns. Further, lack of storms has likely allowed for an acceleration of work related to maintenance and vegetation management which would also increase O&M year on year. Further, interest expense will tick a bit higher given the term out of C$1.5Bln in debt issued in April 2019, composed of C$700mln at 2.54% due 2024, C$550mln at 3.02% due 2029, and C$250mln at 3.64% due 2050. On the call we expect investor focus to be on any improvement in controllable costs, the recently announced changes to the Board of Directors, and any insights into the status of the change out of several senior management positions, and how new CEO Mark Poweska's strategy for the company continues to evolve.

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- **NEE.** We expect NEE to report $2.31 v. $2.28 last year. Year over year we anticipate drivers at FPL to be new investment growth (+$0.07). The acquisition of Gulf Power will also be additive year on year (+$0.10). At NEER, results will be driven by growth for existing assets (+$0.08) and increased earnings due to new investments related to execution of the backlog (+$0.05). Offsetting these positive drivers will be share dilution (-$0.05), and lower results at Corp & Other (-$0.12). We expect not much of an update informationally on the conference call versus the recently held Analyst Day in New York. Investors will be focused on any updates on wind backlog at NEER, and any insights into the further integration efforts for recently acquired Gulf Power.

- **OGE.** We forecast a decline in Q2'19 EPS at OGE to $0.52 from $0.55 last year. The absence of above normal weather is -5 cents and we estimate the impact of below normal conditions (particularly June) in Oklahoma was -2 cents. That said July has started off well and OGE is on track for the year.

Figure 17: OGE Q2'19 EPS Summary

OGE EPS Summary			
	Q2'19E	Q1'19A	Q2'18A
OGE	$0.52	$0.24	$0.55
OG&E	$0.41	$0.14	$0.46
OGE Energy Holdings	$0.12	$0.12	$0.11
Hold Co.	-$0.01	-$0.01	-$0.02

OG&E Earnings Drivers	
Q2'18	$0.46
Weather to normal	-$0.05
Below normal	-$0.02
Rate design	$0.01
AFUDC/D&A	-$0.01
Interest expense	$0.01
O&M	$0.01
Q2'19	$0.41

Source: Company reports, Factset, UBS Equity Research

- **PCG.** PCG will report Q2'19 EPS results on July 26 and we see $1.16 versus $1.16 last year. Tax timing is a regular driver for the company that nets to zero for the year. The company began to record formula rates for the 2020 transmission rate case on May 1. PG&E requested a 12.5% ROE. There was not a nuclear outage in the quarter.

Figure 18: PCG Q2'19 EPS Summary

PCG Q2'18	$1.16
Tax timing	-$0.05
Non-fuel O&M	-$0.02
Shares	-$0.01
Rate base	$0.04
Reduction in insurance	$0.04
PCG Q2'19	$1.16

Source: Company reports, Factset, UBS Equity Research

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- **PNM.** We expect PNM to report adjusted EPS of $0.37 vs consensus of $0.49 and 2Q'18 results of $0.53. Our estimate is consistent with guidance issued by the company of $0.36-$0.38 on 7/12 which reflects substantially milder temperatures in the service territory during the second quarter. We expect investor attention will focus on the company's earning profile through the remainder of the year, weather trends that have been observed quarter to date and the contributing factors to the revised annual guidance.

- **PNW.** We expect PNW to report Q2'19 EPS of $1.37 versus $1.48 last year. There are some significantly negative drivers including a decline in cooling degree days 28% from 2018 and 30% versus normal (about 130 days). In Q1 PNW had 1.0% weather normalized sales growth which could continue. Other drivers include several timing related items versus last year like pension and transmission income. PNW also provides guidance on quarterly outage spending.

Figure 19: PNW Q2'19 EPS Summary

Q2'18	$1.48
O&M	$0.10
Sales	$0.02
LFCR	$0.01
Interest	$0.01
Depreciation	-$0.02
Outage O&M	-$0.03
Transmission	-$0.04
Pension	-$0.05
Weather	-$0.11
Q2'19	$1.37

Source: Company reports, Factset, UBS Equity Research

- **POR.** We forecast flat EPS in Q2'19 of $0.52 versus $0.51 last year. The absence of plant O&M should add 4-5 cents and normal weather conditions adds 2 cents. We don't see much of a story here for the quarter.

Figure 20: POR Q2'19 EPS Summary

Q2'18	$0.51
Weather	$0.02
Carty	$0.03
Plant O&M maintenance	-$0.04
Rate case	$0.03
Q2'19	$0.52

Source: Company reports, Factset, UBS Equity Research

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- **PPL.** We expect flat EPS for PPL in Q2'19 at $0.55 versus $0.55 last year. At a high level we see +3 cents from F/X hedges (1.41x UK sterling to US dollar) for the company's U.K. utility and Kentucky rate relief offset by non-fuel O&M and weather.

Figure 21: PPL Q2'19 EPS Summary

	Q2'19E	Q1'19A	Q2'18A	Earnings Drivers
EPS	$0.55	$0.70	$0.55	
Pennsylvania	$0.11	$0.16	$0.11	Weather -1 cent, Transmission +1
Kentucky	$0.12	$0.17	$0.12	Rates +2 cents, weather -1
U.K.	$0.37	$0.42	$0.36	F/X +3 cents, O&M -2 cents
Other	-$0.03	-$0.05	-$0.04	
Shares MM	728	723	698	

Source: Company reports, Factset, UBS Equity Research

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- **PEG.** We expect PEG to report $0.58 v. $0.65 last year. One of the key drivers will be timing related to tax reform impacts for excess deferred income taxes. This factor was +$0.05 in 1Q'19 and we expect that to reverse out in 2Q'19. On the PEG Power side both the Keys Energy Center and Sewaren 7 were put into service in late 2Q '18 and will add 1,300MWs of capacity to the generation fleet for the majority of the quarter year over year. Zero Emission Credits were also put into place in New Jersey in April 2018 and will be a positive driver of results as they will have a full quarter of impact in 2Q'19. However this positive impact is likely to be mostly offset by lower capacity prices year over year as prices reset on the June 1 capacity year. Last year capacity prices were $205/MW-day on 9,600MWs of capacity while this year pricing as of June 1 was $115/MW-day on 9,000MWs of capacity. Capacity prices in New England were also lower ($2.31/kW-month vs. $3.14/kW-month) despite capacity being +500MWs for the new capacity year. Re-contracting will also be a headwind to results as PEG management indicated a $3/MWh drag although because of seasonal impacts we expect a lower drag on results in 2Q than the ($0.08) seen in 1Q'19. Off-system sales for gas will be lower year over year due to milder weather, and results will be impacted by outage timing as the planned outage at the Salem nuclear facility extended by a likely 30 days beyond projected timelines. However, the Salem plant is only 50% owned by PEG whereas Hope Creek had an outage in 2Q'18 and that plant is 100% owned by PEG. D&A and interest expense are projected to tick higher due to the new plant in service. At the utility we expect the transmission formula rate to be +$0.03 year on year, and despite the distribution rate increase settled on Nov 1 expect that to not have large impacts in 2Q given seasonality of load. Changes to OPEB will add roughly +$0.01 as in 1Q'19 and there will be some incremental benefit from the operating contract at LIPA booked in parent & other. Interest expense will be up slightly at parent and other for the $750mln at 2.875% in debt issued on June 1 slightly offset by the retirement of $350mln at LIBOR +80bps earlier in the quarter.

- **SRE.** We expect SRE to report $1.17 v. $1.21 last year mainly driven by continued drag related to the GRC decision in California. A final decision would be retroactive to 1/1/19 but cannot be booked until received. Our latest expectation for GRC resolution in year-end 2019. We expect interest expense to be slightly higher given issuances of $400mln at SDE&G and $390mln at SoCalGas at around 4%. Offsetting the drag somewhat are likely to be increased earnings for the pipeline program and energy efficiency awards. At Oncor results should be higher year on year related to the close of the InfraREIT transaction on 5/16, although volumes are likely to be lower on milder weather in ERCOT. At South America there were no one-time items in 2Q'18 although there will likely be an FX drag year on year. In Mexico the Peso averaged 19.9 to the USD at 2Q'19 vs. 18.3 at Q2'18 versus hedged levels of 20.72. The TDN plant is uncontracted into the SoCal market and SP15 pricing is down year over year. Renewables will have negligible to no impact in the quarter as the transaction with AEP is now closed. LNG and midstream will continue to be a little bit of a drag on results as expected until the completion of the Cameron LNG facility. We expect corporate and other to be roughly in-line with 1Q'19. There will likely be slightly higher interest expense related to $700mln in debt issuance at 7.5% year over year and the proceeds from the storage and wind sale of $500mln paid off short term debt at a 2.5% - 3% rate.

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- **SO.** Southern reported $0.80 in 2Q'18 and issued guidance for 2Q'19 on their first quarter call of $0.71 versus our estimate of $0.72. The main drivers year over year will be the divestitures of the Florida assets to NextEra Energy. In 1Q'19 this was a ($0.11) year over year impact, and we anticipate about a ($0.09) impact in 2Q'19. Another significant driver will be weather as April was significantly milder than normal, May was a touch warmer than normal, and June was cooler than normal all vs. warmer than normal weather last year. Management may be able to shift O&M timing to mitigate some of the negative impact of cooler weather. PowerSecure in Puerto Rico was a ($0.03) drag in Q1 '19 and we would expect a slightly smaller drag in 2Q'19. Higher share count will also be a year on year negative driver. We expect lower interest expense year on year given the debt retired with the proceeds of the Florida assets sales, and expect sales and rate base growth to also be positive drivers in the quarter. On the call we expect investors will be focused on the ongoing Vogtle new nuclear project (the Georgia PSC staff comments on the project rebasing are due the same day as the earnings call), as well as other regulatory matters in Georgia. While the integrated resource plan will be settled by the time of the call, most of the financial implications of the IRP will be determined within the context of the Georgia Power general rate case which was filed at the beginning of the month. Hearings for the GRC begin on September 30th and we expect the biggest discussion points to be around return on equity and coal ash mitigation spending and recovery. We see the Atlanta Gas Light rate case as less potentially contentious and view the Mississippi Power rate case to be filed in November potentially positive given two of the three commissioners in that state have decided to not stand for reelection.

- **WEC.** We expect WEC to report toward the low end of their 2Q'19 guidance range of $0.70-$0.72 at $0.70 vs. $0.73 last year and consensus estimates of $0.72. Weather will be a driver as both heating degree days and cooling degree days are down year over year, and 2Q'18 results included a +$0.04 impact for above normal weather. Upstream Wind and Bishop Hill have come online year over year and Presque Isle's retirement will save about $40mln in O&M on an annualized basis although that will be weighted away from the 2Q shoulder period. The RICE units came on-line at the end of March and will be $8-$10mln additive to O&M year over year. Management guided to a 3%-4% reduction in O&M in 2019 vs. 2018 but that could be lumpy throughout the year vs. a normalized +$0.02 per quarter. ATC also had a non-recurring charge in 2Q'18 of $3.7mln on a FERC Audit which will be +$0.01 year on year. There were several debt issuances year on year, and at the Hold Co. there was $350mln issued at 3.1% due 2022 while late in '18 $250mln was retired at 1.65%, which will be a slight increase in interest expense year over year.

- **XEL.** We expect XEL to report adjusted EPS of $0.52 vs. consensus of $0.54 and 2Q'18 results of $0.52. Yr/yr earnings should benefit from higher rates in Minnesota/Colorado/New Mexico, and improved O&M management vs. Q1'19. These benefits will be offset by weather which we estimate was either close to, or below normal during the quarter (vs. a $0.04 benefit in Q2'18).

Water Utilities

Following a traditionally slow start to the year, water use and capital investment tends to pick up for the group in the second and third quarter. We expect earnings growth at AWR as a result of new rates and higher Contracted Services. AWK will

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continue to benefit from the Pivotal acquisition, and rate increases. Both WTR and SJW results will be negatively impacted by share dilution, while CWT and CTWS will report largely in line with consensus.

- **AWR.** We expect AWR to report adjusted EPS of $0.58 vs consensus of $0.55 and 2Q'18 results of $0.44. Growth in the quarter is driven by modest growth at the Water utility (new rates), and higher earnings at Contracted Services.

- **AWK.** We expect AWK to report adjusted EPS of $0.89 vs consensus of $0.93 and 2Q'18 results of $0.83. Rate increases are expected to provide growth in the quarter, offset by slightly higher expenses. The Pivotal acquisition, which closed after 1Q'18 should contribute to be a positive year-over-year variance.

- **WTR.** We expect WTR to report adjusted EPS of $0.32 vs consensus of $0.38 and 2Q'18 results of $0.37. Quarter over quarter earnings growth is driven by rate increases and normal customer growth, which will be more than offset by share dilution. We expect a gain in the quarter associated with the closing of an interest rate hedge ($11mm gain) to be adjusted out of given its one time nature. An ALJ recommendation in the company's pending acquisition is expected by the end of August, with a final PSC decision in late October.

- **CWT.** We expect CWT to report adjusted EPS of $0.41 vs consensus of $0.37 and 2Q'18 results of $0.37. Quarterly earnings benefit from higher rates in CA, WA and HI, that will be somewhat offset by higher expenses. This year is the third year of CQT's rate case cycle in CA, which usually generates the largest gap in cost recovery.

- **CTWS.** We expect CTWS to report adjusted EPS of $0.68 vs consensus of $0.68 and 2Q'18 results of $0.59. Earnings in the quarter will benefit from rate increases in Connecticut and Maine. Our estimates exclude the impact of merger related costs.

- **SJW.** We expect SJW to report adjusted EPS of $0.63 vs consensus of $0.56 and 2Q'18 results of $0.72. Earnings in the quarter benefit from higher rates in California, however, this benefit is more than offset by higher expenses and share dilution.

Independent Power Producers

- **NRG.** We expect NRG to report adjusted EBITDA of $486mln vs. $843mln last year and the main driver of the results to be the asset sales of renewables, NYLD, and the South Central assets year over year. We do believe consensus is too high as estimates continue to not be seasonally weighted enough to the third quarter which is not fully reflected of NRG's more ERCOT heavy business mix post asset dispositions. Further, booking generation to retail transfer pricing on an expected average basis over the course of the year, naturally weights earnings to the third quarter. While actual power prices were significantly lower year over year, we expect NRG's matched generation and retail book to have significantly reduced volatility of EBITDA in the quarter. Forward curves are also lower by $2-$4/MWh which lowers the mark to market of EBITDA forecasts in future years. However, key to the conference call will be discussion of the expansion of retail margins as generation margins decline and the true sensitivity of future year's EBITDA to changes in the forward curves. Disclosed hedging levels for NRG at 1Q'19 were 93%/82% in ERCOT/PJM for

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the balance of 2019 and 56%/35% in ERCOT/PJM for 2020. Also on the call management could begin to further discuss the "retail-lite" strategy around contracting assets under purchased power agreements which would further lower volatility of EBITDA and cash flows.

- **VST.** We expect VST to report adjusted EBITDA of $718mln vs. $653mln last year. We believe consensus is too low as the Dynegy acquisition has led to a diversity of the portfolio outside of ERCOT, and therefore less seasonality of results toward the third quarter. Further, given the higher generation prices at which management hedged the third quarter earlier in the year, and the booking of actual transfer price experience between retail and generation throughout the year, we expect this year to have greater retail margins in Q1,Q2, and Q4 and thinner retail margins in Q3. This was discussed in detail by management on the 1Q'19 conference call. While VST is more exposed than NRG to the reduction in power prices on the forward curve given their 50% retail to generation match, we also expect management to address the lower volatility of EBITDA and cash flows to forward curve changes than in the past given in place hedging and offsetting expansion of retail margins. Hedging disclosures on the 1Q'19 call showed for ERCOT 100%/100% for natural gas; 94%/52% for heat rates for '19/20 respectively. Outside of ERCOT hedge levels were 74%/94%/95% and 37%/32%/67% on volumes in '19/20 for MISO/CAISO, NENY, and PJM respectively. On the call investors will also likely focus on the recent close of the Crius acquisition and what incremental factors management has learned since owing the business.

Figure 22: Power Price Comparisons ($/MWhr)

ISO	Hub	2Q '19	2Q '18	Change
ISO NE	Internal Hub	24.02	31.02	(6.99)
NYISO	Zone G	20.98	28.52	(7.54)
PJM	AEP-Dayton	24.38	34.94	(10.57)
PJM	Eastern	22.48	29.92	(7.44)
PJM	N Illinois	22.19	26.08	(3.89)
PJM	PSEG	21.54	27.95	(6.41)
PJM	Western	24.07	33.76	(9.69)
MISO	Indiana	25.23	33.16	(7.93)
MISO	Michigan	25.67	32.20	(6.52)
ERCOT	North	25.09	27.76	(2.67)
ERCOT	Houston	26.28	28.08	(1.79)
ERCOT	West	23.34	22.60	0.73
CAISO	NP15	21.18	24.56	(3.37)
CAISO	SP15	21.64	24.87	(3.23)

Source: S&P Global Market Intelligence, UBS Equity Research

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Figure 23: Spark Spread Rate Trends ($/MWh)

Period	ISO	Hub	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7
Q219	ISO NE	Internal Hub	$ 10.92	$ 12.49	$ 11.90	$ 8.72	$ 5.71	$ 6.54	$ 6.20
Q218	ISO NE	Internal Hub	$ 11.70	$ 11.51	$ 12.28	$ 10.45	$ 10.67	$ 8.00	$ 8.53
		Change	$ (0.78)	$ 0.97	$ (0.38)	$ (1.73)	$ (4.96)	$ (1.47)	$ (2.33)
Q219	PJM	Eastern	$ 13.60	$ 12.36	$ 11.82	$ 11.69	$ 11.24	$ 11.12	$ 11.54
Q218	PJM	Eastern	$ 16.40	$ 14.33	$ 15.30	$ 15.28	$ 15.04	$ 14.21	$ 13.97
		Change	$ (2.80)	$ (1.97)	$ (3.48)	$ (3.59)	$ (3.80)	$ (3.09)	$ (2.42)
Q219	PJM	Western	$ 14.47	$ 15.50	$ 14.61	$ 14.53	$ 14.28	$ 13.66	$ 14.08
Q218	PJM	Western	$ 16.73	$ 18.05	$ 18.63	$ 18.35	$ 17.96	$ 17.42	$ 17.17
		Change	$ (2.25)	$ (2.55)	$ (4.03)	$ (3.81)	$ (3.68)	$ (3.77)	$ (3.09)
Q219	ERCOT	Houston	$ 22.74	$ 22.67	$ 20.44	$ 17.41	$ 15.01	$ 12.05	$ 9.39
Q218	ERCOT	Houston	$ 30.04	$ 23.69	$ 22.11	$ 19.84	$ 16.66	$ 14.49	$ 10.59
		Change	$ (7.30)	$ (1.02)	$ (1.67)	$ (2.43)	$ (1.65)	$ (2.44)	$ (1.21)

Source: S&P Global Market Intelligence, UBS Equity Research

Alternative Energy 2Q19 preview

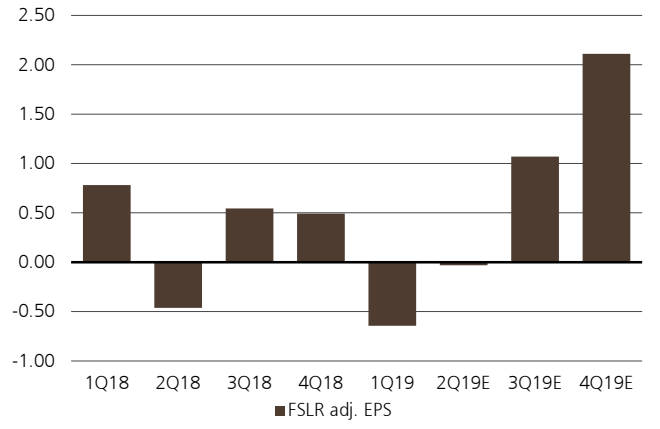
Key issues for the quarter

For Buy rated FSLR and TPIC we expect relatively weak 2Q19 results ahead of an inflection in y/y and sequential earnings growth in 3Q19.

FSLR is nearing the end of its manufacturing transition to Series 6, which is expected to drive increased production capacity and margin expansion. Despite ~breakeven EPS for FSLR being flagged on the 1Q earnings call we expect volatility in the stock on results.

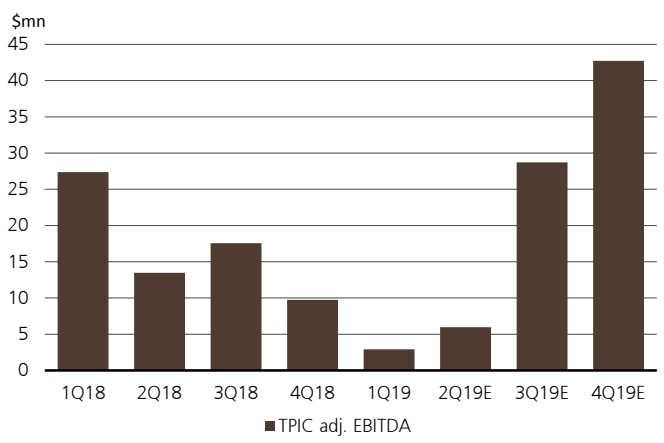
For TPIC, the company was impacted by one-off labor and production issues in 1H19 which offset the positive tailwind from manufacturing line transitions and startups. We model a significant earnings ramp starting in 2H19 through 2020, but expect 2Q19 adj. EBITDA of just $6mn, down 56% y/y. We expect a key focus to be on maintained 2020 financial targets.

Figure 24: FSLR 2018-2019 quarterly adj. EPS



Source: Company reports, UBS estimates

Figure 25: TPIC 2018-2019 quarterly adj. EBITDA



Source: Company reports, UBS estimates

For the module manufacturers we expect stronger than previously expected China solar demand in 2019 to support potential upward guidance revisions for 2019

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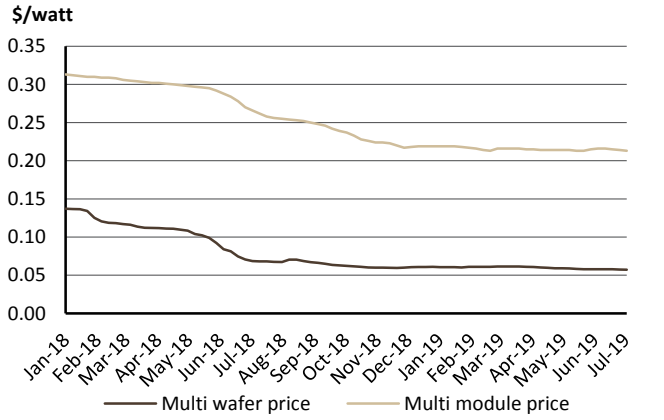
module shipments, particularly for the Chinese exposed names CSIQ and JKS. Please see China Utilities Analyst Alex Liu's recent note: NEA: 50GW solar projects to start construction in 2019.

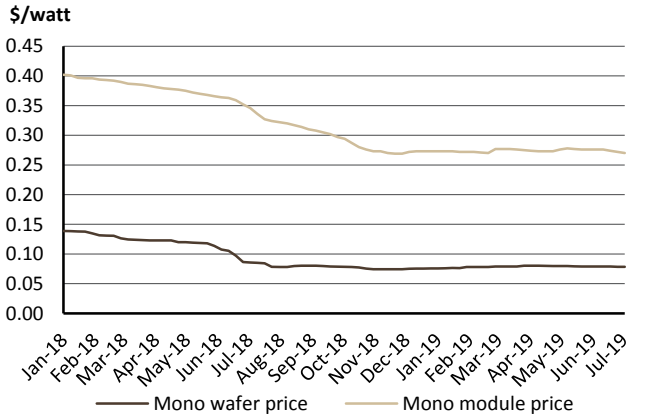
Commodity multi silicon module pricing declined just 1% q/q in 2Q19 while multi silicon wafer pricing declined 3.7% over the same period. Pricing for mono silicon modules increased 0.4% q/q, while mono wafer pricing increased 1.9% q/q suggesting continued strong demand for high efficiency solar products. We expect the increased input costs for mono wafer to result in potential 2Q19 margin pressure for JKS which has a relatively larger proportion of capacity dedicated to mono. Please see: Downgrade to Neutral.

Figure 26: Multi silicon wafer and module ASP, $/watt



Source: PV Insights, UBS research

Figure 27: Mono silicon wafer and module ASP, $/watt



Source: PV Insights, UBS research

Company specific focus areas

- **FSLR**: We expect a 2Q19 loss of $3mn ($0.03/sh) driven by Series 6 ramp and start up charges, while approximately 75% of Series 6 2019 sales will occur in 2H. Consensus 2Q19 adj. EPS is currently $0.00/sh. We currently forecast 2H19 adj. EPS of $3.18/sh compared to 1H19 adj. EPS of ($0.67)/sh. 4Q19 Series 6 cost per watt is expected to be 30% lower than 1Q19 cost. We also look for an update on FSLR's progress restructuring its EPC organization to ease labor constraints and equipment supply issues. As of the 1Q19 earnings call FSLR had sold 50% of 1Q21 capacity with new bookings in the mid-$0.30/watt range. We expect strength in bookings demand for 2021 deliveries could increase the likelihood of FSLR converting its 3rd Malaysia manufacturing facility to Series 6, a development we would view positively.

- **SPWR**: We expect a slowdown in 2Q19 residential solar installations in the CA market driven by abnormally wet weather. SPWR's residential business is relatively more weighted to the CA market compared to other national installers as a result of its leading share in the CA new homes market. SPWR had previously guided to 60-70MW of residential deployments for 2Q19 and 280-310MW deployments for the full year. We expect a key focus will be on any development in potential sources of funding for both NGT manufacturing capacity expansion and safe harboring of modules to capture the full 30% investment tax credit in 2020 and beyond as SPWR had expected to begin executing on financings in 2H19.

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- **CSIQ**: 2Q19 guidance is for 1.95-2.05GW module shipments, $970-1,010mn revenue, and 13-18% gross margin (16-18% excluding impact of low margin Mustang solar project sale). We see potential upward bias to 2019 guidance which is currently 7.4-7.8GW module shipments, and revenue $3.5-3.8bn due to China National Energy Administration's announcement that it expects 50GW of solar to begin construction in 2019. See: NEA: 50GW solar projects to start construction in 2019. We also look for an update on the status of CSIQ CEO Dr. Shawn Qu's medical leave of absence. Yan Zhuang, SVP, COO, and President of the MSS segment has stepped in as acting CEO.

- **JKS**: JKS has secured 70% of orders for 2H19 providing relatively good demand visibility for the rest of the year. JKS is well positioned to benefit from stronger solar demand from China in 2H19 driven by finalization of 2019 solar subsidy policy. However, we expect gross margin to be lower than the 16.6% 1Q19 margin due to ongoing manufacturing capacity expansion and a higher contribution from lower-margin sales in the China market. We expect 2019 capex of $450mn for mono wafer and PERC cell capacity expansion. 2Q19 guidance is for shipments of 3.2-3.3GW and gross margin between 14-15%, with a high level of confidence given JKS reported 1Q19 earnings on 28 June.

- **RUN**: We expect abnormally wet weather in CA to contribute to a sluggish 2Q for residential solar installations, however RUN is less exposed to the CA market than peer SPWR. RUN previously provided 2Q19 deployment guidance of 102-104MW and FY2019 deployment growth guidance growth of 16-18%. RUN highlighted 100% y/y growth in the Brightbox storage business in 2019. The ramp in storage is likely to continue to drive higher customer acquisition cost given the higher entry price for solar with attached storage. For more on RUN's battery storage strategy in our note: Value stacking residential storage.

- **SEDG**: Focus will be on the status of SEDG's manufacturing ramp in a new Vietnam facility which is expected to provide tariff-free inverter supply to the North America market. 2Q19 guidance was previously provided for revenue $310-320mn, gross margin of 32-34%, and solar product gross margin of 33-35%. We expect revenue from the acquired SMRE, Kokam, and Gamatronic businesses will see gradual sequential q/q revenue growth in 2019 from supply chain and channel sales improvements, and guidance implies 2Q19 non-solar revenue of $20mn. By YE19 we expect acquired revenues to comprise less than 10% of sales.

- **HASI**: Long term core EPS growth guidance of 2-6% off a 2017 baseline remains intact implying core EPS of $1.37 in 2019 at the midpoint. We model 2Q19 core EPS of $0.34.

- **ORA**: We forecast 2Q19 adj. EPS of $0.36 and adj. EBITDA of $90mn reflecting typical seasonality of electricity generation. 2Q results are also expected to include $4mn of business interruption insurance proceeds related to the Puna plant. Current 2019 guidance is for revenue of $720-742mn and adj. EBITDA of $370-380mn.

- **TPIC**: Slower than expected replacement hiring and training time in Mexico has led to production delays and triggered significant liquidated damages which are expected to continue through 3Q19 (included in the $25mn Mexico related reduction). We model a significant earnings ramp starting in 2H19 through 2020, but expect 2Q19 adj. EBITDA of just $6mn, down 56% y/y. We expect a key focus to be on maintained 2020 financial targets.

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Figure 28: Alternative Energy key estimates

Company	Ticker	Quarterly				Annual		
		Scheduled Reporting Date	2Q19E UBS	2Q19E Consensus	UBS Vs. Consensus	2019E UBS	2019E Consensus	UBS Vs. Consensus
ALTERNATIVE ENERGY								
Sunpower	SPWR	July 30 est.	($0.16)	($0.16)	$0.00	($0.30)	($0.42)	$0.12
Hannon Armstrong	HASI	Aug 2 est.	$0.34	$0.34	$0.00	$1.39	$1.39	($0.00)
SolarEdge	SEDG	Aug 2 est.	$0.77	$0.83	($0.06)	$3.09	$3.18	($0.09)
First Solar	FSLR	Aug 6 est.	($0.03)	($0.00)	($0.03)	$2.51	$2.44	$0.06
TPI Composites	TPIC	Aug 7	($0.23)	($0.19)	($0.04)	$0.06	$0.02	$0.04
Ormat Technologies	ORA	Aug 7 est.	$0.36	$0.33	$0.03	$1.62	$1.68	($0.07)
SunRun	RUN	Aug 7 est.	$0.43	$0.25	$0.18	$1.09	$0.60	$0.49
Canadian Solar	CSIQ	Aug 14 est.	$0.66	$0.35	$0.31	$2.20	$2.41	($0.21)
Jinko Solar Holding Company	JKS	Aug 22 est.	$0.37	$0.28	$0.09	$1.93	$2.79	($0.86)

Source: Company reports, Factset, UBS research estimates.

Environmental Services 2Q19 preview

Key issues for the quarter

We expect the majority of investor questions to be focused on the impact of two headwinds to MSW earnings growth: 1) a 64% YTD decline in recycled fiber pricing and 2) a 10% YTD decline in Permian Basin E&P rig count. 2019 guidance, which is typically set in February, largely reflects a "steady state" outlook and we anticipate management commentary to focus on the incremental headwinds from continued commodity price and drilling activity declines. Broadly we see continued above average acquisition activity in 2019 helping to offset these headwinds.

WCN has already flagged a potential $3-5mn EBITDA headwind per quarter due to the decline in E&P activity and $5mn EBITDA headwind per quarter due to commodity price weakness. WCN has the largest E&P exposure of the MSW group at 5% of revenue followed by WM at ~3%.

MSW 2019 guidance is typically updated with 2Q19 results, however given these headwinds we see a bias towards reaffirming existing guidance rather than the historically common beat-and-raise.

We remind investors that MSW was able to overcome a 2018 ~50% y/y decline in recycling prices due to strong underlying macro conditions supporting the ~95% of revenue from the core disposal business. See: UBS Evidence Lab Inside: Housing survey read-throughs for waste volumes, March 2019.

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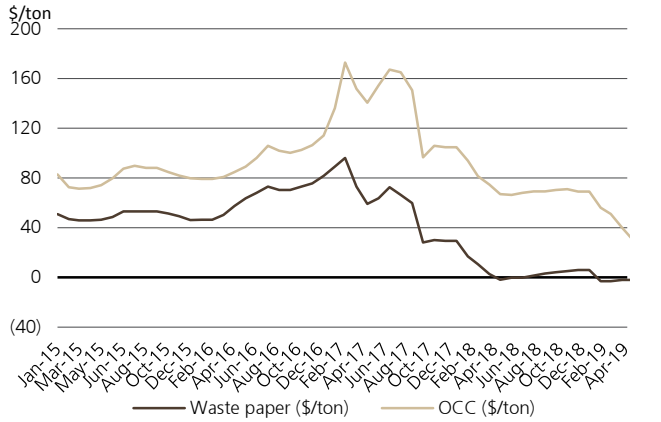
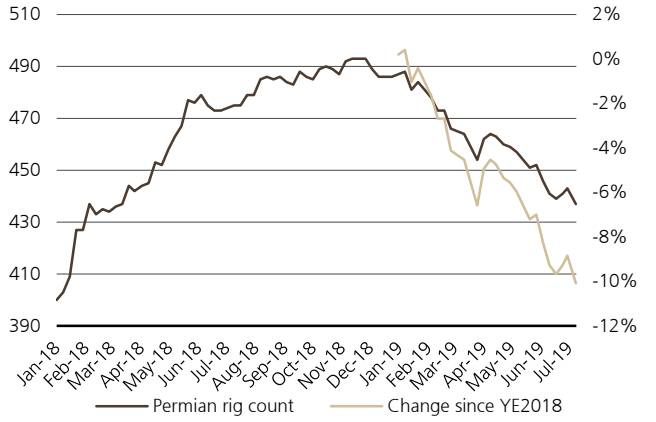
Figure 29: Recycled commodity pricing, $/ton



Source: RISI, UBS Research

Figure 30: U.S. Permian E&P rig count



Source: Baker Hughes, UBS Research

Figure 31: Environmental Services business mix

Metric 2019E	WM	RSG	WCN	ADSW	CWST	CVA
2019 revenue ($bn)	15.5	10.5	5.4	1.6	0.7	1.9
N. American market share	26%	17%	9%	3%	1%	3%
Geographic						
U.S. Northeast	22%	18%	22%	26%	100%	47%
U.S. South	24%	34%	17%	36%	0%	33%
U.S. Midwest	23%	20%	12%	38%	0%	7%
U.S. West	24%	28%	33%	0%	0%	10%
Canada/other	7%	0%	16%	0%	0%	3%
Total	100%	100%	100%	100%	100%	100%
Revenue composition						
Residential collection	16%	19%		25%	17%	0%
Commercial collection	22%	25%		23%	18%	0%
Industrial collection	15%	18%		15%	17%	0%
Total collection	53%	62%	60%	63%	52%	0%
Other operations						
Transfer	9%	11%	10%	10%	9%	10%
Disposal	19%	20%	20%	21%	18%	58%
Recycling	8%	3%	2%	1%	7%	5%
E&P	3%	2%	5%	1%	2%	0%
Other operations	8%	2%	3%	4%	12%	27%
Total	100%	100%	100%	100%	100%	100%
Cost composition						
SGA as % of revenue	9.8%	10.4%	11.0%	11.6%	12.8%	6.2%
Opex as % of revenue	62%	61%	58%	64%	68%	75%

Source: Company reports, UBS research estimates

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Company specific focus areas

- **RSG**: As of the 1Q19 call RSG flagged a $0.07 EPS headwind from recycled commodity pricing assuming current pricing holds. Pricing has since fallen by an additional $15/ton implying potential $0.12/sh total EPS headwind. RSG had previously reiterated 2019 EPS guide of $3.23-3.28 and FCF of $1.125-1.725bn. However the previously increased 2019 M&A spend target of $300mn should help mitigate commodity pricing pressures. RSG's $142mn current YTD spend is expected to contribute $55mn in annualized revenue.

- **WCN**: We revise our 2Q19 adj. EBITDA to $426mn from $436mn previously and our FY2019 adj. EBITDA to $1,708mn from $1,713mn previously. On 4 June WCN flagged 2 potential headwinds to 2Q19 results; first, a $5mn EBITDA headwind from 30% decline in recycled commodity values, second, a $3-5mn EBITDA headwind driven by 10% YTD reduction in E&P rig count.2Q19 guidance was previously provided for revenue of $1,360mn and adj. EBITDA of $434mn. These headwinds are expected to be offset by contribution from acquisitions in 2H19 with WCN still achieving current 2019 adj. EBITDA guidance of $1,705mn. We expect WCN to potentially provide an updated 2019 outlook on the 2Q19 earnings call.

- **CWST**: Since the 1Q19 earnings call CWST has acquired $11.5mn annualized revenue ($18.5mn YTD) and announced an asset purchase agreement to buy RSG waste assets in NY and MA. The asset purchase will add $30mn of annualized revenue and is expected to close by the end of 3Q19. Based on these acquisitions we estimate CWST tracking well ahead of its FY2019 guidance for $152-156mn adj. EBITDA. We forecast 2Q19 adj. EBITDA of $43.3mn (consensus $41.6mn) which should be relatively unaffected by recent commodity price declines given offsetting fees recouped through CWST's SRA program. Recycling adj. EBITDA was up $2mn y/y in 1Q19 driven by these fees.

- **CVA**: We update our 2Q19 adj. EBITDA estimate to $98mn from $112mn previously to reflect a revision to our expected plant maintenance expense in the quarter. The increase in maintenance expense compared to our prior estimate is to account for the impact of the Palm Beach plant which CVA acquired in 4Q18. Maintenance spend is historically heavier in 1H for CVA. Our EPS estimates are revised in-line with the EBITDA change.

- **CLH**: We forecast 2Q19 adj. EBITDA of $151mn or +8.2% y/y, a slowdown from the 15.2% y/y 1Q19 growth due to more difficult y/y comps. We expect earnings to benefit from a business interruption insurance recovery related to CLH's Deer Park facility outage ($3.5mn EBITDA headwind in 1Q19). CLH has been working to reposition some oil inventory to the southern part of U.S. to try to mitigate future shortfalls/transport limitations driven by weather. Closed loop oil sales are tracking to the 15mn gallon target in 2019. Management noted at the UBS Industrials Conference in June that the Environmental Services pipeline was the strongest it has ever been and expect this to drive solid growth through 2020. See: UBS Global Industrials Conference takeaways.

- **ECOL:** We forecast 2Q19 adj. EBITDA of $35mn or +10% y/y driven by contribution from 2018 acquisition activity. ECOL's planned merger with NRCG received FTC antitrust clearance on 16 July and is still subject to approval from both ECOL and NRCG shareholders. The merger faces pushback from certain holders of NRCG's 7.0% Series A Convertible Preferred Stock who have asked NRCG to reconsider the terms for conversion of the preferred stock. We have

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incorporated the contribution from NRCG in our model assuming 31 Dec 2019 deal closure (see: Updating model for NRCG merger).

Figure 32: Environmental Services EPS estimates

Company	Ticker	Quarterly				Annual		
		Scheduled Reporting Date	2Q19E UBS	2Q19E Consensus	UBS Vs. Consensus	2019E UBS	2019E Consensus	UBS Vs. Consensus
ENVIRONMENTAL SERVICES								
Republic Services	RSG	July 25	$0.76	$0.77	($0.01)	$3.27	$3.23	$0.04
Covanta Holding Corp	CVA	July 25	($0.07)	($0.05)	($0.02)	$0.16	$0.22	($0.06)
Waste Connections	WCN	July 29	$0.67	$0.69	($0.02)	$2.71	$2.75	($0.04)
Clean Harbors	CLH	July 31	$0.61	$0.61	($0.00)	$1.77	$1.78	($0.01)
Casella Waste System	CWST	Aug 1	$0.32	$0.27	$0.05	$1.01	$0.85	$0.16
US Ecology	ECOL	Aug 1	$0.58	$0.61	($0.02)	$2.27	$2.24	$0.03

Source: Company reports, Factset, UBS research estimates.

Figure 33: Environmental Services EBITDA estimates ($mn)

Company	Ticker	Quarterly				Annual		
		Scheduled Reporting Date	1Q19E UBS	1Q19E Consensus	UBS Vs. Consensus	2019E UBS	2019E Consensus	UBS Vs. Consensus
ENVIRONMENTAL SERVICES								
Republic Services	RSG	July 25	722	725	-0.4%	2,972	2,955	0.6%
Covanta Holding Corp	CVA	July 25	98	101	-2.8%	444	452	-1.7%
Waste Connections	WCN	July 29	426	431	-1.1%	1,708	1,717	-0.5%
Clean Harbors	CLH	July 31	151	146	3.7%	530	526	0.8%
Casella Waste System	CWST	Aug 1	43	41	3.2%	159	156	2.3%
US Ecology	ECOL	Aug 1	35	36	-3.2%	139	140	-0.5%

Source: Company reports, Factset, UBS research estimates.

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Valuation Method and Risk Statement

Regulated Utilities: Our valuation methodology for the group is price to earnings based. The adjustments applied fall into 5 categories. These are as follows: 1) Group Valuation Bias: Flowing from our valuation work comparing Baa corporate yields to group dividend yields and RU price to earnings ratios to those for the S&P 500, we incorporate a positive or negative adjustment to our group multiple representing the gap we calculate to the nearest 5%; 2) Growth Adjustment: We adjust our valuations based on the growth quartile each utility occupies. First quartile receives a 5% premium, second quartile a 2% premium, third quartile a 2% discount and fourth quartile a 5% discount; 3) Regulatory Adjustment: Our valuation adjustments for regulation are based on our proprietary Regulatory Rankings. First quartile jurisdictions receive 5%, second quartile 2%, third quartile -2% and fourth quartile -5%; 4) Multi Utility Diversified Valuation: For multi utilities (those with more than 15% diversified or foreign earnings), we perform a sum-of-parts analysis applying business/region appropriate valuations to those diversified businesses; 5) One-off Adjustments: In special situations, we value risk on an issue specific basis. Common areas where we apply such an adjustment include: ESG advantage, large project construction risk, legal risk, and announced M&A completion risk. We identify the following risk factors for the sector overall: rising interest rates; regulatory and policy risks; operational risks; construction risks; cybersecurity risk to the transmission grid and/or customer data, and extreme weather events.

Our valuation methodology for the Alternative Energy space is based on a variety of metrics including P/BV, EV/EBITDA, P/E, and retained equity value per share. Our target multiples are derived from historical group averages with adjustments for expected growth rates, leverage, and earnings growth confidence. We identify the following risks for the sector: Demand for new renewable installations has historically been volatile around changes in state and federal policy, and we expect this volatility to continue. In addition, margins for product manufacturers can be impacted by swings in raw materials pricing and the overall level of energy prices.

Our valuation methodology for the Environmental Services space is based on EV/EBITDA with adjustments made to the target EV/EBITDA multiple based on relative growth rates, Free Cash Flow (FCF) conversion, expected earnings stability, and the general level of risk and our confidence in future earnings estimates. We identify the following risks for the sector: Housing remains a key driver of incremental municipal solid waste volume growth, and a slowdown in new housing starts could put downward pressure on sales growth. In addition, pricing tends to follow GDP growth, and a slowdown in economic growth could drive lower ability to raise pricing driving potential contraction in margins. For more industrial-exposed names, swings in commodity prices can impact the overall level of waste-generating activity, contributing to earnings volatility.

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Required Disclosures

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	45%	30%
Neutral	FSR is between -6% and 6% of the MRA.	40%	28%
Sell	FSR is > 6% below the MRA.	15%	20%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 June 2019.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

KEY DEFINITIONS:Forecast Stock Return (FSR) is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months. In some cases, this yield may be based on accrued dividends. **Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium). **Under Review (UR)** Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation. **Short-Term Ratings** reflect the expected near-term (up to three months) performance of the stock and do not reflect any change in the fundamental view or investment case. **Equity Price Targets** have an investment horizon of 12 months.

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Company Disclosures

Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
AES Corp[16]	AES.N	Neutral	N/A	US$17.22	19 Jul 2019
Alliant Energy Corp[16]	LNT.O	Neutral	N/A	US$49.93	19 Jul 2019
Ameren Corp[16]	AEE.N	Neutral	N/A	US$75.98	19 Jul 2019
American Electric Power Inc[7, 13, 16]	AEP.N	Buy	N/A	US$90.28	19 Jul 2019
American States Water Co[16]	AWR.N	Sell	N/A	US$76.02	19 Jul 2019
American Water Works Co[16]	AWK.N	Buy	N/A	US$114.98	19 Jul 2019
Aqua America Inc[16]	WTR.N	Buy	N/A	US$41.00	19 Jul 2019
ATCO Ltd	ACOx.TO	Buy	N/A	C$43.24	19 Jul 2019
California Water Service Group[16]	CWT.N	Sell	N/A	US$52.60	19 Jul 2019
Canadian Solar Inc[6c, 7, 13, 16, 20a]	CSIQ.O	Neutral (CBE)	N/A	US$20.94	19 Jul 2019
Canadian Utilities Ltd	CU.TO	Neutral	N/A	C$35.78	19 Jul 2019
Caribbean Utilities Corp	CUPu.TO	Neutral	N/A	US$16.35	19 Jul 2019
Casella Waste Systems Inc[2, 4, 6a, 16]	CWST.O	Neutral	N/A	US$42.15	19 Jul 2019
Clean Harbors Inc[16]	CLH.N	Neutral	N/A	US$70.99	19 Jul 2019
CMS Energy Corp[16]	CMS.N	Neutral	N/A	US$58.26	19 Jul 2019
Connecticut Water Service Inc[16]	CTWS.O	Sell	N/A	US$69.57	19 Jul 2019
Consolidated Edison Inc[16]	ED.N	Neutral	N/A	US$87.24	19 Jul 2019
Covanta Holding Corp[4, 16]	CVA.N	Neutral	N/A	US$17.54	19 Jul 2019
Dominion Energy Inc[6c, 7, 16, 26a]	D.N	Buy	N/A	US$76.85	19 Jul 2019
DTE Energy Co[7, 16]	DTE.N	Neutral	N/A	US$128.79	19 Jul 2019
Duke Energy Corp[4, 6a, 7, 16]	DUK.N	Buy	N/A	US$88.45	19 Jul 2019
Edison International[7, 16]	EIX.N	Buy	N/A	US$70.17	19 Jul 2019
Entergy Corp[7, 16]	ETR.N	Buy	N/A	US$105.60	19 Jul 2019
Evergy, Inc[16]	EVRG.N	Neutral	N/A	US$60.79	19 Jul 2019
Eversource Energy[7, 16]	ES.N	Buy	N/A	US$76.77	19 Jul 2019
Exelon Corp[7, 16]	EXC.N	Buy	N/A	US$47.57	19 Jul 2019
First Solar Inc[16]	FSLR.O	Buy	N/A	US$66.53	19 Jul 2019
FirstEnergy Corp[16]	FE.N	Buy	N/A	US$43.49	19 Jul 2019
Fortis Inc[7, 16]	FTS.TO	Buy	N/A	C$51.58	19 Jul 2019
Hannon Armstrong Sustainable Infra[2, 4, 6a, 13, 16]	HASI.N	Neutral	N/A	US$27.53	19 Jul 2019
Hawaiian Electric Industries Inc[16]	HE.N	Sell	N/A	US$44.31	19 Jul 2019
Hydro One	H.TO	Sell	N/A	C$23.35	19 Jul 2019
JinkoSolar Holding Co Ltd[13, 16]	JKS.N	Neutral	N/A	US$20.23	19 Jul 2019
NextEra Energy Inc[2, 4, 6a, 7, 16, 26c]	NEE.N	Buy	N/A	US$209.73	19 Jul 2019
NRG Energy Inc[7, 16]	NRG.N	Buy	N/A	US$35.14	19 Jul 2019
OGE Energy Corp[16]	OGE.N	Neutral	N/A	US$42.74	19 Jul 2019
Ormat Technologies Inc[16]	ORA.N	Neutral	N/A	US$63.15	19 Jul 2019
PG&E Corp[7, 16, 20b]	PCG.N	Neutral (CBE)	N/A	US$17.79	19 Jul 2019
Pinnacle West Capital Corp[7, 16]	PNW.N	Neutral	N/A	US$93.59	19 Jul 2019
PNM Resources Inc[7, 16]	PNM.N	Neutral	N/A	US$49.62	19 Jul 2019
Portland General Electric Co[16]	POR.N	Sell	N/A	US$54.61	19 Jul 2019

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
PPL Corp[4, 6a, 6b, 6c, 7, 16]	PPL.N	Buy	N/A	US$30.17	19 Jul 2019
Public Service Enterprise Group[7, 16]	PEG.N	Buy	N/A	US$60.18	19 Jul 2019
Republic Services Inc[13, 16, 26b]	RSG.N	Neutral	N/A	US$87.11	19 Jul 2019
Sempra Energy[4, 6a, 6c, 7, 16]	SRE.N	Buy	N/A	US$140.05	19 Jul 2019
SJW Group[2, 4, 6a, 16]	SJW.N	Neutral	N/A	US$64.77	19 Jul 2019
SolarEdge Technologies Inc[16]	SEDG.O	Buy	N/A	US$63.37	19 Jul 2019
Southern Co[2, 4, 6a, 6b, 7, 16]	SO.N	Neutral	N/A	US$55.27	19 Jul 2019
SunPower Corp[13, 16, 20a]	SPWR.O	Neutral (CBE)	N/A	US$10.99	19 Jul 2019
Sunrun Inc[16, 20a]	RUN.O	Neutral (CBE)	N/A	US$19.77	19 Jul 2019
TPI Composites Inc[16]	TPIC.O	Buy	N/A	US$26.22	19 Jul 2019
US Ecology Inc[16]	ECOL.O	Neutral	N/A	US$62.24	19 Jul 2019
Vistra Energy Corp[2, 4, 6a, 16]	VST.N	Buy	N/A	US$21.83	19 Jul 2019
Waste Connections Inc[16]	WCN.TO	Buy	N/A	C$123.55	19 Jul 2019
Waste Connections Inc[16]	WCN.N	Buy	N/A	US$94.58	19 Jul 2019
WEC Energy Group Inc[16]	WEC.N	Neutral	N/A	US$86.31	19 Jul 2019
Xcel Energy Inc[16]	XEL.O	Neutral	N/A	US$60.77	19 Jul 2019

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date

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bcobrien@aquaamerica.com Ben O'Brien 07/24/19 02:14:58 PM Aqua America Inc

Aqua America Inc

Downgrade to Neutral; Valuation reflects attractive fundamentals & strong prospects; PT to $45

Equities

Americas
Water Utilities

12-month rating	**Neutral** *Prior: Buy*
12m price target	**US$45.00** *Prior: US$42.00*
Price	**US$42.06**

RIC: WTR.N **BBG:** WTR US

Trading data and key metrics

52-wk range	US$42.06-32.37
Market cap.	US$7.50bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	302
Avg. daily value (m)	US$12.3
Common s/h equity (12/19E)	US$2.15bn
P/BV (12/19E)	3.5x
Net debt / EBITDA (12/19E)	5.1x

EPS (UBS, diluted) (US$)

	12/19E			
	From	To	% ch	Cons.
Q1	0.28	0.28	0	0.28
Q2	0.32	0.25	-22	0.25
Q3E	0.47	0.47	0	0.39
Q4E	0.41	0.43	3	0.38
12/19E	1.48	1.48	0	1.41
12/20E	1.58	1.58	0	1.57
12/21E	1.68	1.68	0	1.67

WTR has tightened the valuation gap vs. peers

Since the announcement of the Peoples Gas acquisition (10/18), the completion of the associated equity financing (4/19) and successful progression through its regulatory calendar, WTR has closed the relative valuation gap to its peer group by 25%. While we are raising our valuation target to reflect our confidence in both the business model and management execution, we are lowering our rating to Neutral from Buy to reflect the lower total potential return profile.

Q2 Adjusted EPS in line with market expectations

WTR reported Q2'19 adjusted EPS of $0.37/share vs. UBSe $0.32/sh, consensus $0.38/sh, and 2Q'18 of $0.37/sh. The adjusted EPS excludes merger-related expenses of $11.9mm (net of tax), comprising of a loss on the extinguishment of debt ($18.9mm), transaction related expenses ($12.7mm), a favourable mark-to-market adjustment on the settlement of interest rate swaps ($11mm) and interest income ($7.4mm). Fundamentals of the core business remain strong, with quarter over quarter revenue growth of 3.3%, and relatively flat O&M expenses.

Guidance and growth forecast reiterated; strong acquisition pipeline

In conjunction with its Q2'19 earnings report, WTR reaffirmed its full year earnings guidance of $1.45-$1.50/sh, infrastructure investment target of $550mm for 2019 ($269 invested 1H) and $1.4 billion through 2021, annual rate base growth of 7% and total customer growth of between 2% and 3%. The acquisition pipeline is strong; WTR announced exclusive discussions with the Delaware County Regional Water Control Authority (DELCORA, serves approximately 500,000 people, PA) and the purchase of the Campbell, Ohio water system (3,200 customers). Including DELCORA, the pipeline of potential water and wastewater acquisitions WTR is pursuing has approximately 400,000 customers in four states the company already serves.

Valuation: $45 Price Target

We are raising our PT to $45 from $42. The PT is predicated on a 3% discount to the average water group multiple of 27.4x, applied to our 2021e EPS of $1.68. The modest discount multiple reflects the blended gas/water business model. Our prior PT of $42 was premised on a 3% discount to a group average multiple of 25.2x.

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Highlights (US$m)	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
Revenues	820	810	838	881	921	956	995	1,033
EBIT (UBS)	326	329	337	370	399	425	454	482
Net earnings (UBS)	234	240	251	265	281	299	319	342
EPS (UBS, diluted) (US$)	1.32	1.35	1.41	1.48	1.58	1.68	1.79	1.92
DPS (US$)	0.74	0.79	0.88	0.94	1.00	1.07	1.15	1.23
Net (debt) / cash	(1,891)	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)

Profitability/valuation	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
EBIT margin %	39.7	40.6	40.3	42.0	43.3	44.5	45.6	46.7
ROIC (EBIT) %	9.0	8.4	7.9	8.0	8.0	8.1	8.3	8.4
EV/EBITDA (core) x	16.2	17.0	17.6	19.2	18.4	17.7	17.0	16.1
P/E (UBS, diluted) x	23.9	24.8	25.0	28.3	26.7	25.1	23.5	22.0
Equity FCF (UBS) yield %	0.2	(1.6)	(1.6)	(1.8)	0.2	0.5	0.8	1.2
Net dividend yield %	2.3	2.4	2.5	2.2	2.4	2.6	2.7	2.9

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$42.06 on 07 Aug 2019 16:43 EDT

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UBS Research THESIS MAP a guide to our thinking and what's where in this report

PIVOTAL QUESTIONS

Q: Has WTR's earnings and growth outlook changed, 2019-2021?

We are not changing our '19-'21 earnings estimates of $1.48/$1.58/$1.68/share. These estimates are consistent with WTR's rate base growth target of 7% through 2021, also reflecting the guidance of modest accretion in the first calendar year for the Peoples acquisition. We believe the Peoples acquisition is likely to receive final approval (PA) in the autumn given the close to unanimous settlement with parties to the proceeding (all but 2 parties either signed on, or agreed not to oppose). WTR's absolute growth profile should improve as Peoples rate base growth (8%-10%) outpaces WTR's by 100-300 basis points on the deployment of capital to improve aging infrastructure.

Q: Can WTR be successful as a combined water and gas utility company?

Yes. We believe WTR can successfully lever its regulatory, operating and cost management experience to combine with Peoples Gas while continuing to execute on its infrastructure improvement commitments and customer growth ambitions. Acquisition and integration are key skill-sets that WTR has developed through its ongoing muni acquisition program.

UBS VIEW

WTR's share price reflects the value of its combined regulated water and gas business model. We impute a modest discount of 3% vs. the water peer group average P/E to reflect the premium regulatory jurisdictional exposure, Fair Value profile and blending of a lower multiple for the gas business. 2019 should be a transition year for WTR as it closes the Peoples acquisition (autumn) and concludes the Peoples rate case (autumn). Beginning in 2020, we expect to see continued focus on municipal water acquisitions and possible realization of merger benefits.

EVIDENCE

PA is currently WTR's largest jurisdiction, with ~69% of rate base; therefore the growth outlook in PA tends to be indicative for the company overall. Additional sources of growth include organic customer growth, which averages ~1%/yr and a steady diet of tuck-in acquisitions. In 2019/2020, WTR estimates adding approximately 20k new customers. We estimate the Peoples acquisition to be ~neutral to EPS in 2020 and accretive over time as Peoples rate base growth outpaces WTR's.

WHAT'S PRICED IN?

WTR has tightened the relative valuation gap vs its peers by 25% since announcing the proposed acquisition of Peoples and completing the associated equity financing. Once the Peoples transaction is closed, we look for WTR to trade at roughly a 3% discount to the average Water P/E on 2021e EPS of $1.68, or $45, representing upside of ~12% including the 2.26% dividend yield.

UPSIDE / DOWNSIDE SPECTRUM

Value drivers	Peer Avg. P/E Multiple	Premium/discount	EPS CAGR '19-'21	2021e EPS
$49 upside	29.0x	0.0%	7.0%	$1.70
$45 base	26.5x	-3.0%	6.0%	$1.68
$34 downside	21.0x	0.0%	5.0%	$1.62

Source: UBS

more→

COMPANY DESCRIPTION

Aqua America, Inc. provides regulated utility water and wastewater services to approximately 972,000 customers in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey,...

more →

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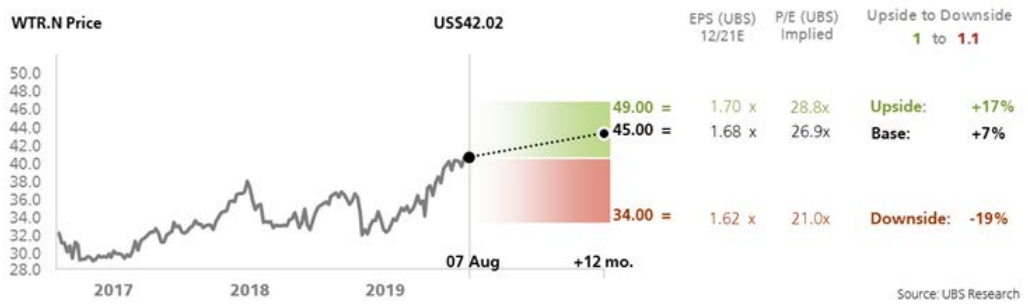
UPSIDE / DOWNSIDE SPECTRUM

return ↑



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$34 downside	21.0x	0.0%	5.0%	$1.62

Source: UBS

Risk to the current share price is heavily skewed (1:1.1) to the upside

Upside (US$49): Our upside scenario is predicated upon a 0% premium applied to a 29.0x P/E multiple, which reflects the average small cap peer group multiple. We also assume the 2019–2021 earnings growth rate is 100 basis points higher than our base case estimates, matching the rate base growth forecast proposed by the company.

Base (US$45): Our base case is predicated upon a 3% discount applied to the average water utility P/E multiple on WTR standalone 2021e EPS. We estimate the Peoples acquisition could be neutral to ~$0.03 accretive to 2021e EPS. The 3% discount reflects the net of: 5% discount to account for the water group average multiple near historical highs relative to the broad market, 5% premium for WTR's regulatory jurisdiction ranking, 6% premium for the seven Fair Market Value states in which WTR operates, and a 9% discount to reflect the impact of 30% of earnings derived from lower multiple gas assets.

Downside (US$34): Our downside scenario is predicated on the trough absolute average water utility P/E experienced since 1/1/18. We also assume the 2019–2021 earnings growth rate is 100 basis points lower than our base case estimates which would reflect a failure to execute on incremental tuck in acquisitions.

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COMPANY DESCRIPTION

return ↑

Aqua America, Inc. provides regulated utility water and wastewater services to approximately 972,000 customers in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana, and Virginia. Operations in Pennsylvania account for approximately 52% of revenues and 74% of net income. Aqua Resources provides unregulated services such as operating and maintenance contracts with municipal authorities and other parties, as well as water and wastewater line repair service, Aqua Infrastructure provides unregulated raw water supply services for firms in the natural gas drilling industry.

)

Industry outlook

Infrastructure spending and consolidation will continue to be the underlying drivers of industry growth for the next 5-10 years. Capital spending should remain at or near peak levels for the next 12 months, and is forecast to remain elevated through at least 2020. We would expect water utilities to follow the pattern of electric utilities with a bias toward upward revision in the spending forecast. Factors that could increase the pace of consolidation include broader adoption of fair value legislation, enhanced focus on water quality and accountability standards, or macro trends that instigate budgetary pressures or risk-off strategies at the municipal level. We expect conservation and efficiency to continue to reduce the trend of water usage nationally, and drought could be a disruptive event regionally.

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Forecast returns

Forecast price appreciation	+7.0%
Forecast dividend yield	2.3%
Forecast stock return	+9.3%
Market return assumption	6.6%
Forecast excess return	+2.7%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 3% discount to the 2021 average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 9% discount to reflect impact of lower P/E associated with gas earnings.

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	45%	30%
Neutral	FSR is between -6% and 6% of the MRA.	40%	28%
Sell	FSR is > 6% below the MRA.	15%	20%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 June 2019.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
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UBS Securities LLC: Daniel Ford, CFA; Paul Cole.

Company Disclosures

Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Aqua America Inc[16]	WTR.N	Suspended	N/A	US$41.15	06 Aug 2019

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date
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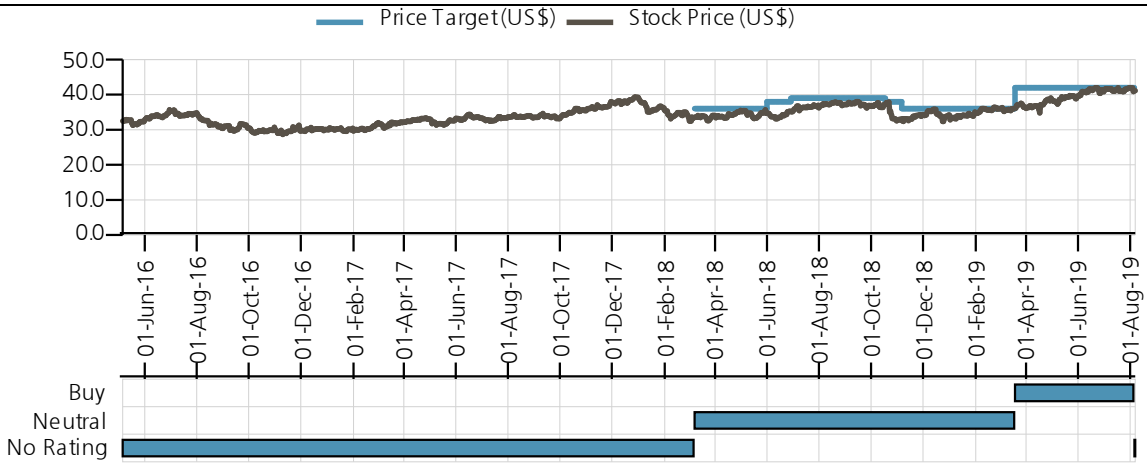
Aqua America Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2016-05-06	32.49	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy
2019-08-06	41.15	-	No Rating

Source: UBS; as of 06 Aug 2019

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bcobrien@aquaamerica.com Ben O'Brien 08/08/19 12:39:05 PM Aqua America Inc

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First Read

Aqua America Inc

PA PUC ALJ recommends approval of Peoples Natural Gas Co. acquisition

Equities

Americas
Water Utilities

12-month rating	**Neutral**
12m price target	**US$45.00**
Price (28 Oct 2019)	**US$44.90**

RIC: WTR.N **BBG:** WTR US

Trading data and key metrics

52-wk range	US$46.58-32.37
Market cap.	US$8.01bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	322
Avg. daily value (m)	US$14.2
Common s/h equity (12/19E)	US$2.15bn
P/BV (12/19E)	3.7x
Net debt / EBITDA (12/19E)	5.1x

EPS (UBS, diluted) (US$)

	12/19E	
	UBS	Cons.
Q1	0.28	0.28
Q2	0.25	0.37
Q3E	0.47	0.43
Q4E	0.43	0.38
12/19E	1.48	1.41
12/20E	1.58	1.59
12/21E	1.68	1.71

Final PUC decision expected late 2019/early 2020

In an opinion issued on 10/28, the Pennsylvania Public Utility Commission (PUC) Administrative Law Judge (ALJ) recommended approval of the Peoples Natural Gas Company acquisition by Aqua America. All parties to the proceeding will now have 30 days to file exceptions and reply exceptions before final PUC action either in December or early 2020. We expect the analyst day that the company had tentatively planned to follow the merger close in early December will now get pushed out in line with the revised consideration schedule.

The Goodwin and Tombaugh gathering system

A point of contention through the consideration process is the treatment of the Goodwin and Tombaugh gathering system. The ALJ approval recommends that the bare steel pipeline system be replaced within 7 years (starting 3 months after merger close) at a cost of $120mm (which will be recovered through base rates). Offsetting this cost, all ratepayers will receive a $13mm bill credit by the end of 2019.

Q3'19 earnings report scheduled for 11/4

We expect WTR to report Q3'19 earnings of $0.47/share vs. prior year earnings of $0.44/share. Quarter-over-quarter earnings growth is driven by rate increases, normal customer growth and acquisitions. We expect the company will address the ongoing Peoples acquisition process, the DELCORA approval process as well as further M&A plans on the conference call following the earnings release.

Valuation:

We believe the ALJ recommendation to approve the Peoples acquisition should be well received by investors as it moves this process closer to completion. We are maintaining our Neutral rating and $45/share price target.

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Paul Cole
Analyst
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Highlights (US$m)	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
Revenues	820	810	838	881	921	956	995	1,033
EBIT (UBS)	326	329	337	370	399	425	454	482
Net earnings (UBS)	234	240	251	265	281	299	319	342
EPS (UBS, diluted) (US$)	1.32	1.35	1.41	1.48	1.58	1.68	1.79	1.92
DPS (US$)	0.74	0.79	0.88	0.94	1.00	1.07	1.15	1.23
Net (debt) / cash	(1,891)	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)

Profitability/valuation	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
EBIT margin %	39.7	40.6	40.3	42.0	43.3	44.5	45.6	46.7
ROIC (EBIT) %	9.0	8.4	7.9	8.0	8.0	8.1	8.3	8.4
EV/EBITDA (core) x	16.2	17.0	17.6	20.2	19.3	18.6	17.8	16.9
P/E (UBS, diluted) x	23.9	24.8	25.0	30.2	28.5	26.8	25.1	23.4
Equity FCF (UBS) yield %	0.2	(1.6)	(1.6)	(1.7)	0.2	0.5	0.8	1.1
Net dividend yield %	2.3	2.4	2.5	2.1	2.2	2.4	2.6	2.7

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$44.90 on 28 Oct 2019 19:47 EDT

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Forecast returns

Forecast price appreciation	+0.2%
Forecast dividend yield	2.2%
Forecast stock return	+2.4%
Market return assumption	6.6%
Forecast excess return	-4.2%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 3% discount to the 2021E average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 9% discount to reflect impact of lower P/E associated with gas earnings.

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Buy	FSR is > 6% above the MRA.	45%	29%
Neutral	FSR is between -6% and 6% of the MRA.	40%	29%
Sell	FSR is > 6% below the MRA.	15%	21%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 September 2019.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Aqua America Inc[16]	WTR.N	Neutral	N/A	US$44.90	28 Oct 2019

Source: UBS. All prices as of local market close.
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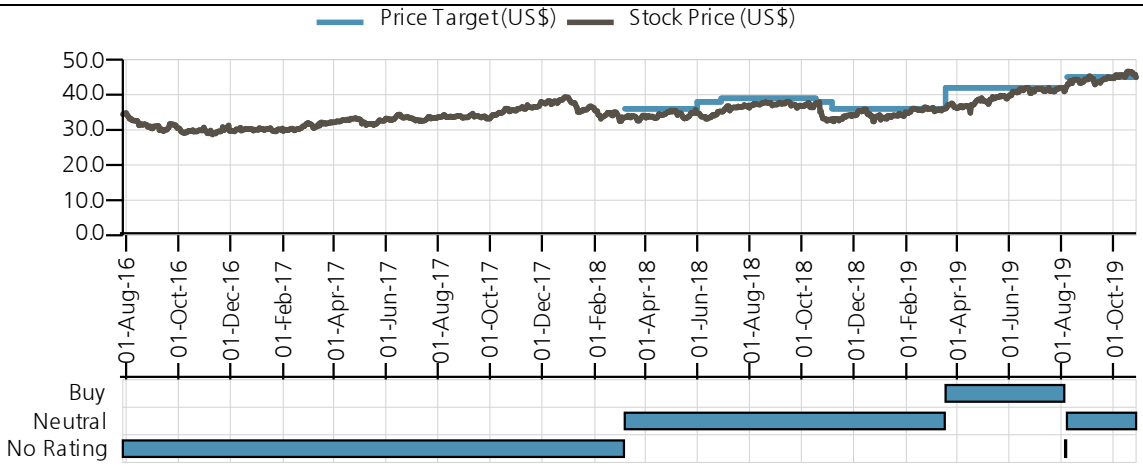
Aqua America Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2016-07-28	34.39	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy
2019-08-06	41.15	-	No Rating
2019-08-08	42.47	45.0	Neutral

Source: UBS; as of 28 Oct 2019

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This report is intended exclusively for:
bjdingerdissen@ aquaamerica.com

First Read

Aqua America Inc

3Q'19 GAAP $0.38; Ex-transaction $0.48

Q: How did the results compare vs expectations?

A: 3Q'19 GAAP EPS of $0.38 vs. 3Q'18 of $0.44; on an ex-transactional basis (excluding Peoples related dilution & costs), operating EPS of $0.48 was ahead of UBS and consensus estimates of $0.47 & $0.38 respectively.

Q: What were the most noteworthy areas in the results?

A: Net income increased in the quarter ($88.5mm vs. 78.2mm in Q3'18) helped by higher rates, customer and volume growth, offsets included growth related costs

Q: Has the company's outlook/guidance changed?

A: Operating EPS guidance (ex: Peoples dilution & expense) for '19 of $1.45-$1.50; Cap-ex for '19 ($550), and through '21 ($1.4 bill.); rate base CAGR (7%); customer growth (between 2-3%); Peoples closing date (late'19/early '20) all reaffirmed.

Q: How would we expect investors to react?

A: Noisy quarterly report; investor focus remains on the pending approval and close of the Peoples & DELCORA acquisitions; potential analyst day with updated guidance.

Key metrics ($)

	Consensus estimates	UBS estimates	Actual	% diff vs. consensus
GAAP Earnings	$0.38	$0.47	$0.37	0.0%

Source: Factset, UBS Equity Research, Aqua American Q3 Earnings Press Release

Equities

Americas

Water Utilities

12-month rating	**Neutral**
12m price target	**US$45.00**
Price (04 Nov 2019)	**US$43.56**

RIC: WTR.N **BBG:** WTR US

Trading data and key metrics

52-wk range	US$46.58-32.37
Market cap.	US$7.77bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	326
Avg. daily value (m)	US$14.5
Common s/h equity (12/19E)	US$2.15bn
P/BV (12/19E)	3.6x
Net debt / EBITDA (12/19E)	5.1x

EPS (UBS, diluted) (US$)

	12/19E	
	UBS	Cons.
Q1	0.28	0.28
Q2	0.25	0.37
Q3E	0.47	0.38
Q4E	0.43	0.35
12/19E	1.48	1.39
12/20E	1.58	1.58
12/21E	1.68	1.71

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Highlights (US$m)	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
Revenues	820	810	838	881	921	956	995	1,033
EBIT (UBS)	326	329	337	370	399	425	454	482
Net earnings (UBS)	234	240	251	265	281	299	319	342
EPS (UBS, diluted) (US$)	1.32	1.35	1.41	1.48	1.58	1.68	1.79	1.92
DPS (US$)	0.74	0.79	0.88	0.94	1.00	1.07	1.15	1.23
Net (debt) / cash	(1,891)	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)

Profitability/valuation	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
EBIT margin %	39.7	40.6	40.3	42.0	43.3	44.5	45.6	46.7
ROIC (EBIT) %	9.0	8.4	7.9	8.0	8.0	8.1	8.3	8.4
EV/EBITDA (core) x	16.2	17.0	17.6	19.7	18.9	18.1	17.4	16.5
P/E (UBS, diluted) x	23.9	24.8	25.0	29.3	27.6	26.0	24.3	22.7
Equity FCF (UBS) yield %	0.2	(1.6)	(1.6)	(1.7)	0.2	0.5	0.8	1.2
Net dividend yield %	2.3	2.4	2.5	2.2	2.3	2.5	2.6	2.8

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$43.56 on 04 Nov 2019 19:34 EST

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Forecast returns

Forecast price appreciation	+3.3%
Forecast dividend yield	2.3%
Forecast stock return	+5.6%
Market return assumption	6.6%
Forecast excess return	-1.0%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 3% discount to the 2021 average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 9% discount to reflect impact of lower P/E associated with gas earnings.

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Buy	FSR is > 6% above the MRA.	45%	29%
Neutral	FSR is between -6% and 6% of the MRA.	40%	29%
Sell	FSR is > 6% below the MRA.	15%	21%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 September 2019.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

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UBS Securities LLC: Daniel Ford, CFA; Paul Cole.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Aqua America Inc[16]	WTR.N	Neutral	N/A	US$43.56	04 Nov 2019

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date
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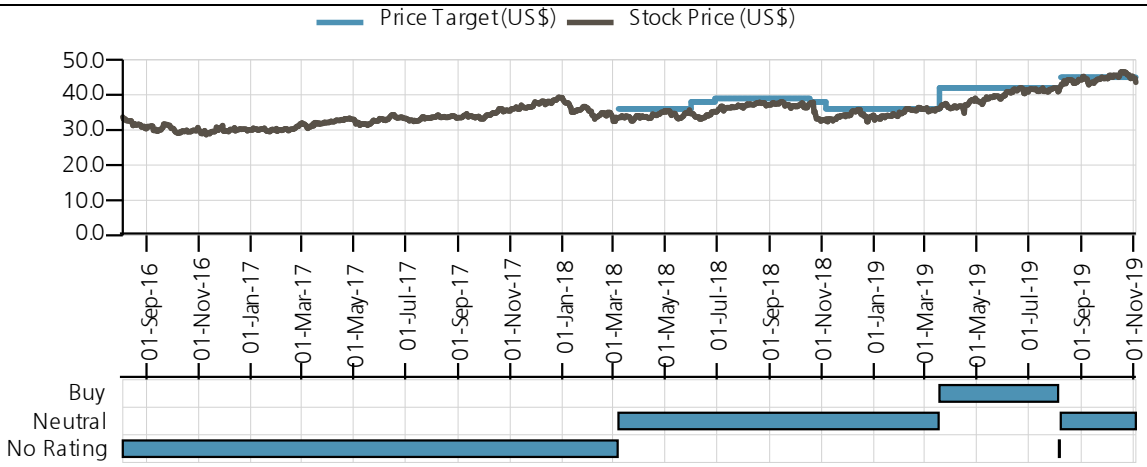
Aqua America Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2016-08-04	33.72	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy
2019-08-06	41.15	-	No Rating
2019-08-08	42.47	45.0	Neutral

Source: UBS; as of 04 Nov 2019

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First Read

Essential Utilities Inc

Q4/2020 Adj. EPS in-line; '21 guidance unchanged

Q: How did the results compare vs expectations?

A: In line. WTRG reported Q4/full year 2020 adjusted EPS of $0.46/$1.58. These results are in line with consensus and UBS estimates of $0.45/$1.57 and $0.45/$1.58, respectively, and are above prior period results of $0.28/$1.47. Full year 2020 EPS guidance was $1.53-$1.58 (top end).

Q: What were the most noteworthy areas in the results?

A: Full year results benefited from the acquisition of Peoples Gas (customer credits are excluded from the adjusted results), higher rates and volume growth (driven by favorable weather and work-from-home orders). Vs. the prior year fourth quarter, results benefited from the Peoples Gas acquisition, higher rates and volume growth.

Q: Has the company´s outlook/guidance changed?

A: Earnings guidance for 2021 is unchanged at $1.64-$1.69. The projected EPS CAGR is 5-7% through 2023, driven by water rate base growth of 6-7% and gas rate base growth of 8-10%. WTRG currently has six signed purchase agreements for additional water and wastewater systems serving approximately 227,000 customers/$438mm of rate base, including the DELCORA system. WTRG has rate proceedings pending in Virginia and Indiana.

Q: How would we expect investors to react?

A: In line. On the investor call, we are looking for an update on the DELCORA (and other) acquisitions, the catch-up repairs tax proceeding, and the performance of both the Peoples Gas and Texas based subsidiaries through the recent polar vortex event.

Key Metrics ($)

	Consensus estimates	UBS estimates	Actual	% diff vs. UBS
Q4 Adj. EPS	$0.45	$0.45	$0.46	+2.2%
2020 Adj. EPS	$1.57	$1.58	$1.58	0.0%

Source : UBS Equity Research, FactSet, Company Reports

Equities

Americas

Water Utilities

12-month rating	**Neutral**
12m price target	**US$45.00**
Price (24 Feb 2021)	**US$44.09**

RIC: WTRG.N **BBG:** WTRG US

Trading data and key metrics

52-wk range	US$50.31-32.65
Market cap.	US$7.99b
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	411
Avg. daily value (m)	US$19.1
Common s/h equity(12/20E)	US$2.35b
P/BV(12/20E)	4.8x
Net debt to EBITDA(12/20E)	4.0x

EPS (UBS, diluted) (US$)

	12/20E	
	UBS	Cons.
Q1	0.60	0.60
Q2	0.29	0.29
Q3	0.23	0.23
Q4E	0.45	0.45
12/20E	1.58	1.54
12/21E	1.68	1.67
12/22E	1.79	1.79

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Highlights(US$m)	12/17	12/18	12/19	12/20E	12/21E	12/22E	12/23E	12/24E
Revenues	810	838	881	1,049	956	995	1,033	1,072
EBIT (UBS)	329	337	370	527	425	454	482	512
Net earnings (UBS)	240	251	265	403	299	319	342	365
EPS (UBS, diluted) (US$)	1.35	1.41	1.48	1.58	1.68	1.79	1.92	2.05
DPS (net) (US$)	0.79	0.88	0.91	0.97	1.04	1.11	1.19	1.27
Net (debt) / cash	(2,121)	(2,376)	(2,670)	(2,744)	(2,931)	(3,066)	(3,186)	(3,293)
Profitability/valuation	**12/17**	**12/18**	**12/19**	**12/20E**	**12/21E**	**12/22E**	**12/23E**	**12/24E**
EBIT (UBS) margin %	40.6	40.3	42.0	50.3	44.5	45.6	46.7	47.7
ROIC (EBIT) %	8.4	7.9	8.0	10.6	8.1	8.3	8.4	8.6
EV/EBITDA (UBS core) x	17.0	17.6	18.7	15.6	18.4	17.6	16.7	16.2
P/E (UBS, diluted) x	24.8	25.0	27.3	28.4	26.7	25.0	23.4	21.9
Equity FCF (UBS) yield %	(1.6)	(1.6)	(1.8)	1.7	0.5	0.8	1.1	1.5
Dividend yield (net) %	2.4	2.5	2.2	2.2	2.3	2.5	2.7	2.8

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$ 44.09 on 24-Feb-2021

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Forecast returns

Forecast price appreciation	+2.1%
Forecast dividend yield	2.4%
Forecast stock return	+4.4%
Market return assumption	5.1%
Forecast excess return	-0.7%

Company Description

Essential Utilities, Inc. provides regulated water and wastewater services to approximately 3m people in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana, and Virginia and distributes natural gas to approximately 2m people in western Pennsylvania, West Virginia and Kentucky. WTRG's water operations represent approximately $5.5bn of rate base value, while its gas distribution operations represent approximately $2.5bn of rate base. Growth is generated by infrastructure investment (pipes, plants, etc.), strategic M&A (water/ wastewater) and management of private water systems.

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events. Our price target is premised upon a 7% discount to the 2021E average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 7% premium to reflect operations in six Fair Market Value states, and 14% discount to reflect impact of lower P/E associated with gas earnings.

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	51%	31%
Neutral	FSR is between -6% and 6% of the MRA.	37%	29%
Sell	FSR is > 6% below the MRA.	12%	18%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 31 December 2020.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
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UBS Securities LLC: Daniel Ford, CFA, Paul Cole.

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Company Name	Reuters	12-month rating	Price	Price date
Essential Utilities Inc[16]	WTRG.N	Neutral	US$44.09	24 Feb 2021

Source: UBS. All prices as of local market close.
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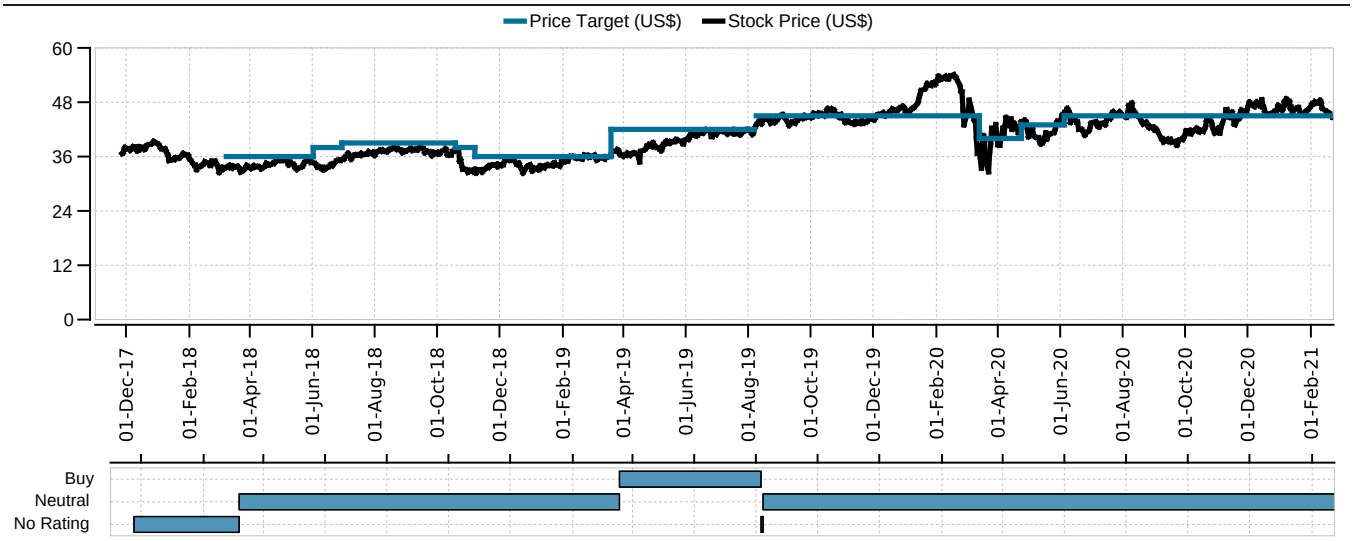
Essential Utilities Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2017-11-24	36.57	-	No Rating
2018-03-08	33.52	36.00	Neutral
2018-06-01	34.71	38.00	Neutral
2018-06-29	35.18	39.00	Neutral
2018-10-18	37.23	38.00	Neutral
2018-11-06	32.59	36.00	Neutral
2019-03-19	36.12	42.00	Buy
2019-08-06	41.15	-	No Rating
2019-08-08	42.47	45.00	Neutral
2020-03-13	38.43	40.00	Neutral
2020-04-23	42.62	43.00	Neutral
2020-06-04	44.51	45.00	Neutral

Source: UBS; as of24-Feb-2021

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First Read

Essential Utilities Inc

Q4/2019 Adj. EPS & 2020 Guidance

Q: How did the results compare vs expectations?

A: Q4/full year EPS adjusted for transaction costs and equity dilution $0.34/$1.47 vs. consensus/UBSe $0.31/$1.48 - $0.37/$1.48; prior year $$0.31/$1.41.

Q: What were the most noteworthy areas in the results?

A: Yr/yr results improved due to higher rate & surcharge revenues, commentary suggests that O&M (absent transactions costs) increased in line with expectations.

Q: Has the company's outlook/guidance changed?

A: Illustrative guidance for 2020 of $1.53-$1.58 vs consensus $1.58; EPS growth CAGR off '19 adjusted base through '22 of 5-7%; rate base growth for water, 6-7% and gas, 8-10% through '22; and infrastructure investment through '22 of $2.8 bill.

Q: How would we expect investors to react?

A: Subject to incremental detail at the investor day, we expect a muted reaction to earnings and growth guidance that is modestly lower than current consensus.

Key metrics ($)

	Consensus estimates	UBS estimates	Actual	% diff vs. consensus
Q4 Adj. EPS	$0.31	$0.37	$0.34	+9.6%
2019 Adj. EPS	$1.48	$1.48	$1.47	-0.6%

Source: FactSet, UBS estimates, Essential Utilities Press Release

Equities

Americas

Water Utilities

12-month rating	**Neutral**
12m price target	**US$45.00**
Price (26 Feb 2020)	**US$50.31**

RIC: WTRG.N **BBG:** WTRG US

Trading data and key metrics

52-wk range	US$54.07-34.82
Market cap.	US$8.98bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	419
Avg. daily value (m)	US$20.5
Common s/h equity (12/19E)	US$2.15bn
P/BV (12/19E)	4.2x
Net debt / EBITDA (12/19E)	5.1x

EPS (UBS, diluted) (US$)

	12/19E	
	UBS	Cons.
Q1	0.28	0.28
Q2	0.37	0.37
Q3	0.46	0.48
Q4E	0.37	0.31
12/19E	1.48	1.48
12/20E	1.58	1.57
12/21E	1.68	1.68

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Highlights (US$m)	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
Revenues	820	810	838	881	921	956	995	1,033
EBIT (UBS)	326	329	337	370	399	425	454	482
Net earnings (UBS)	234	240	251	265	281	299	319	342
EPS (UBS, diluted) (US$)	1.32	1.35	1.41	1.48	1.58	1.68	1.79	1.92
DPS (US$)	0.74	0.79	0.88	0.94	1.00	1.07	1.15	1.23
Net (debt) / cash	(1,891)	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)

Profitability/valuation	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
EBIT margin %	39.7	40.6	40.3	42.0	43.3	44.5	45.6	46.7
ROIC (EBIT) %	9.0	8.4	7.9	8.0	8.0	8.1	8.3	8.4
EV/EBITDA (core) x	16.2	17.0	17.6	22.0	21.0	20.2	19.3	18.3
P/E (UBS, diluted) x	23.9	24.8	25.0	33.9	31.9	30.0	28.1	26.3
Equity FCF (UBS) yield %	0.2	(1.6)	(1.6)	(1.5)	0.2	0.4	0.7	1.0
Net dividend yield %	2.3	2.4	2.5	1.9	2.0	2.1	2.3	2.4

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$50.31 on 26 Feb 2020 18:41 EST

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Forecast returns

Forecast price appreciation	-10.6%
Forecast dividend yield	2.0%
Forecast stock return	-8.6%
Market return assumption	6.2%
Forecast excess return	-14.8%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 3% discount to the 2021 average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 9% discount to reflect impact of lower P/E associated with gas earnings.

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	44%	32%
Neutral	FSR is between -6% and 6% of the MRA.	41%	29%
Sell	FSR is > 6% below the MRA.	15%	20%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 31 December 2019.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Essential Utilities Inc[16]	WTRG.N	Neutral	N/A	US$50.31	26 Feb 2020

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date
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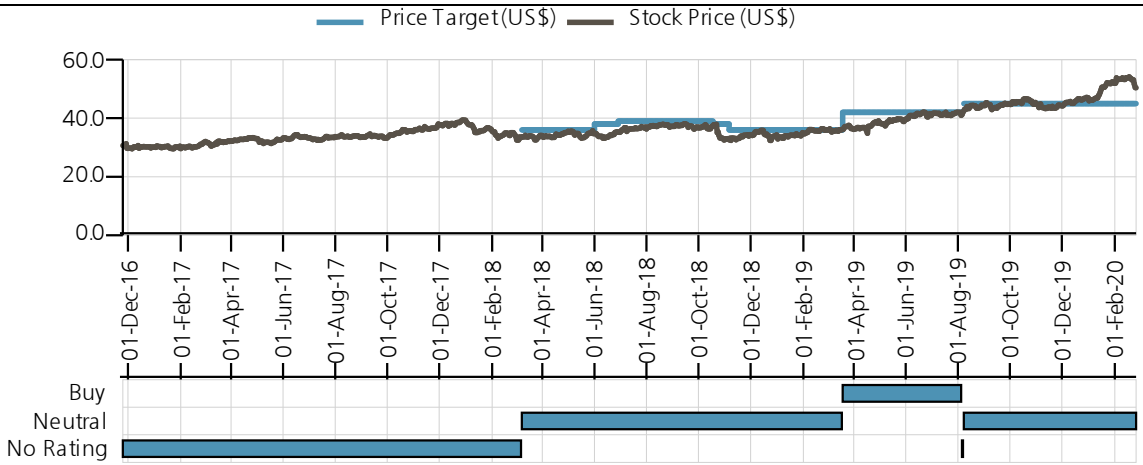
Essential Utilities Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2016-11-25	30.6	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy
2019-08-06	41.15	-	No Rating
2019-08-08	42.47	45.0	Neutral

Source: UBS; as of 26 Feb 2020

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This report is intended exclusively for:
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First Read

Essential Utilities Inc

Q2'20 EPS $0.29 vs. UBSe $0.26, Consensus $0.22

Q: How did the results compare vs expectations?

A: Better. WTRG reported Q2'20 EPS of $0.29 vs. the prior year quarter of $0.25. UBS and consensus expectations for the quarter were $0.26 and $0.22, respectively.

Q: What were the most noteworthy areas in the results?

A: Vs. the prior year qtr, revenues increased due to the addition of Peoples Gas, higher rates, weather derived volumes and customer growth. Residential water sales were +10% quarter over quarter, while commercial & industrial sales were -16% and -11% respectively. O&M expenses in the quarter rose as a result of the Peoples Gas combination, but were helped by the absence of transaction & integration costs.

Q: Has the company's outlook/guidance changed?

A: Full year '20 guidance of $1.53-$1.58 unchanged, as is the EPS CAGR of 5-7%, rate base growth of 6-7% in water and 8-10% in gas, and projected infrastructure spending of $2.8 billion. Guidance for EPS dispersion across the year is unchanged.

Q: How would we expect investors to react?

A: Better EPS & affirmation of guidance should be well received by investors.

Key metrics ($)

	Consensus estimates	UBS estimates	Actual	% diff vs. consensus
EPS	$0.22	$0.26	$0.29	+26.0%

Source: UBS Equity Research, FactSet, Essential Utilities Inc.

Equities

Americas

Water Utilities

12-month rating	**Neutral**
12m price target	**US$45.00**
Price (05 Aug 2020)	**US$44.69**

RIC: WTRG.N **BBG:** WTRG US

Trading data and key metrics

52-wk range	US$54.07-32.65
Market cap.	US$7.97bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	415
Avg. daily value (m)	US$17.8
Common s/h equity (12/20E)	US$2.25bn
P/BV (12/20E)	3.5x
Net debt / EBITDA (12/20E)	5.1x

EPS (UBS, diluted) (US$)

	12/20E	
	UBS	Cons.
Q1	0.60	0.60
Q2E	0.26	0.22
Q3E	0.27	0.26
Q4E	0.45	0.47
12/20E	1.58	1.48
12/21E	1.68	1.66
12/22E	1.79	1.80

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Highlights (US$m)	12/17	12/18	12/19	12/20E	12/21E	12/22E	12/23E	12/24E
Revenues	810	838	881	921	956	995	1,033	1,072
EBIT (UBS)	329	337	370	399	425	454	482	512
Net earnings (UBS)	240	251	265	281	299	319	342	365
EPS (UBS, diluted) (US$)	1.35	1.41	1.48	1.58	1.68	1.79	1.92	2.05
DPS (US$)	0.79	0.88	0.94	1.00	1.07	1.15	1.23	1.32
Net (debt) / cash	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)	(3,378)

Profitability/valuation	12/17	12/18	12/19	12/20E	12/21E	12/22E	12/23E	12/24E
EBIT margin %	40.6	40.3	42.0	43.3	44.5	45.6	46.7	47.7
ROIC (EBIT) %	8.4	7.9	8.0	8.0	8.1	8.3	8.4	8.6
EV/EBITDA (core) x	17.0	17.6	18.7	19.2	18.5	17.7	16.8	16.3
P/E (UBS, diluted) x	24.8	25.0	27.3	28.4	26.7	25.0	23.3	21.8
Equity FCF (UBS) yield %	(1.6)	(1.6)	(1.8)	0.2	0.5	0.8	1.1	1.5
Net dividend yield %	2.4	2.5	2.3	2.2	2.4	2.6	2.8	2.9

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$44.69 on 05 Aug 2020 18:42 EDT

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Forecast returns

Forecast price appreciation	+0.7%
Forecast dividend yield	2.3%
Forecast stock return	+3.0%
Market return assumption	5.1%
Forecast excess return	-2.1%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 3% discount to the 2021 average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 9% discount to reflect impact of lower P/E associated with gas earnings.

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	49%	32%
Neutral	FSR is between -6% and 6% of the MRA.	39%	30%
Sell	FSR is > 6% below the MRA.	13%	20%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 June 2020.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Essential Utilities Inc[16]	WTRG.N	Neutral	N/A	US$44.69	05 Aug 2020

Source: UBS. All prices as of local market close.
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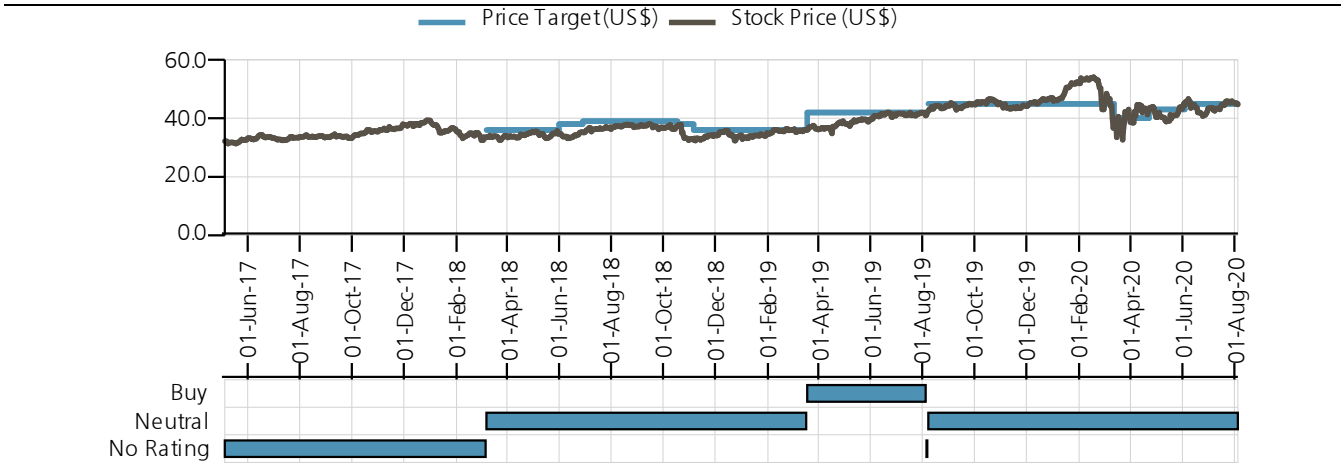
Essential Utilities Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2017-05-05	32.16	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy
2019-08-06	41.15	-	No Rating
2019-08-08	42.47	45.0	Neutral
2020-03-13	38.43	40.0	Neutral
2020-04-23	42.62	43.0	Neutral
2020-06-04	44.51	45.0	Neutral

Source: UBS; as of 05 Aug 2020

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U.S. Capital Advisors®

USCA Friday Midstream Recap

May 7, 2021

- **Earnings – ET, LNG, TRGP, DCP, MPLX, EPD, AWK, WMB, NS, ENB, TRP, ENLC, ALTM, SMLP, WTRG, ETRN, PAA**
- **Earnings Themes**
- **WMB Sequent Purchase**

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Please see important disclosures beginning on page 10

Earnings – ET, LNG, TRGP

- **ET:** *Uh…well…Positive…I guess.* Would call this the beat to beat all beats in the history of Midstream. Almost all in the Intrastate segment as ET noted a $1.5B benefit from higher storage margins and a $1.1B benefit from higher gas sales and retained fuel revenues. Some offsets, but a net ~$2.4B positive impact for the year. EBITDA guidance increased by the amount of the storm benefit plus another $100mm to a new midpoint of $13.1B (not including impact of ENBL merger). ***And we think that could move higher given they have not booked all the storm gains due to some disputes with counterparties.*** We estimate the one-time windfall worth 80c/unit to ET, after factoring in units issued for ENBL transaction.
- **ET (cont'd):** ET reduced debt by $3.7B during Q1. We estimate that the storm windfall lowered by just over 0.2x, and that the full $3.7B debt pay down reduced leverage by 0.34x. We're guessing it is enough to take them off negative credit outlooks. Growth capex +$150mm, to $1.6B on combo of new Permian Bridge project (rich gas line), several smaller project additions and some acceleration of '22 spend into '21. ***Finally, just a darn good conference call, emphasizing the things they did during Uri to keep gas flowing (as opposed to the windfall), talking head-on about improving ESG metrics, and exuding lots of confidence about the outlook for their base business.***
- **LNG:** *Positive.* Monster 40% EBITDA beat vs. consensus, another guidance raise, and new accelerated schedule for SPL Train 6 (now H1'22 vs. prior H2'22). Unlike monster EBITDA beat in Q2'20, this was not driven by an acceleration of revenue recognition from cancelled cargoes, but rather a reflection of the volatile LNG and gas markets in Q1. For second quarter in a row, raised EBITDA guidance by $200mm to new range of $4.3-$4.6B. ***Biggest elements of most recent guidance revision include a roughly $1/mmbtu improvement on the 50 TBtus of open capacity as of last ccall (~$50mm) and 30+ TBtus of new production added to the 2021 forecast at a ~$3/mmbtu margin (~$100mm).***
- **TRGP:** *Positive.* Also a monster EBITDA beat and full year EBITDA guidance raise. Raise in line with Q1 beat plus impact of higher assumed commodity prices in guidance. Adj EBITDA $516mm, a 20%+ beat vs. USCA/street at $401mm/$418mm. Raised full year EBITDA guidance by $125mm, or 7%, to midpoint of $1.85B. ***Bulk of raise appears to be related to Q1 outperformance (~$100m in aggregate composed of a $30mm net Uri benefit combined with unquantified cost savings and non-storm related NGL marketing),*** as we estimate the higher commodity price assumptions are worth ~$25mm of the raise. Leverage now expected to be 4x at year-end vs. prior 4.25x.

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Earnings – DCP, MPLX, EPD, AWK, WMB

- **DCP:** *Positive.* DCP finally firmed up Uri impacts as a ~$60mm hit to Q1, bringing EBITDA down to $275mm, a 10% beat vs. USCA/Street. ***Implies ex-weather impact, EBITDA would have been ~$335mm, which would have been a record quarter and beaten pre-Uri street estimates of ~$300mm.*** Real driver of beat was G&A costs of $38mm, down ~$25mm from 2020 quarterly average. FCFaD of $89mm beat vs. USCA's $45mm on higher EBITDA and $19mm lower capex. No change to full year guidance.
- **MPLX:** *Positive.* Adjusted EBITDA +6%/5% vs. USCA/Street, driven by better-than-expected G&P results (higher NGL prices & lower opex). ***Repurchased $155mm of common units in Q1 (introduced $1B buyback program in Q3'20).*** Liquidity includes $24mm in cash and $2.7B available through their revolving credit facility.
- **EPD:** *Neutral.* Big beat, but largely offset in our view by bits and pieces in release about y/y declines in Eagle Ford and Permian. About $250mm storm benefit. No change to capex guidance, and LT capital run rate of $1.5-$2.0B/yr. Think spread/marketing margin >$500-$600mm for the year. ***Opened kimono a little more on energy transition.*** Doing deep dive review on carbon technologies, review of evolutionary technologies, including hydrogen, and looking at sequestering their own carbon and plastics recycling. ***Waiting for clarification on Biden tax policy before pulling trigger on buybacks.***
- ***AWK:*** *Neutral.* In line quarter and no change to recently issued guidance. ***Remain confident that sale of NY assets will close.*** Delay does not impact timing for equity issuance. Filed rate case in WV (5% of revenues) in April, requesting a $32mm revenue increase with a 10.5% ROE. 10-Q noted a subsidiary, American Water Resources, received a subpoena from the U.S. Attorney's Office for the Eastern District of NY seeking information about their operations and contractor network in the New York City area. Company does not believe the investigation will have a material adverse effect on them.
- **WMB:** *Neutral.* Beat EBITDA by $100mm or 7%, but all on winter storm benefits. Raised '21 guidance by $100mm, but one-time storm/other impacts were ~$126mm, so same amount as beat. Leverage 4.2x and expected to end year at that level, down from prior 4.25x. ***WMB is now below their 4.25x Debt/EBITDA target. Market looking for guide posts on capital allocation, but WMB still reviewing internally.*** FCF after dividends and capex $104mm vs. $(47)mm in Q1'20. ***Announced purchase of Sequent Energy, a gas marketing firm,*** from SO for $110mm, including $60mm of working capital. We find that a bit of a head scratcher – see below for more. Should hear something over the next 30-60 days on E&P partner to develop recently acquired Haynesville and Wamsutter properties.

Earnings – NS, ENB, TRP, ENLC, ALTM

- **NS:** *Neutral.* Quarterly EBITDA 3% light vs. consensus on the winter storm, but full year guidance unchanged. ***Raised expectations for Permian 2021 volume exit rate from ~475 mbpd to 500 mbpd*** and expect refined product system at ~100% of pre-pandemic levels for remainder of 2021. Reiterated expectation for 2021 EBITDA to be comparable to 2020 ($723mm) when adjusted for the sale of Texas City assets (USCAe ~$10mm of EBITDA). Will publish first sustainability report later this year.
- **ENB:** *Neutral.* EBITDA largely in line and no change to guidance. Continue to progress on small wind and solar projects, but nothing that moves the needle in a meaningful way. ***Ballpark, would say ~75% of questions on ccall focused on energy transition.*** Segments pretty much inline except: 1) Green Power, with a $34mm or 28% beat vs. USCA, but all on a one-time promote fee; and 2) Energy Services, with a $75mm loss vs. USCA at breakeven, on the lack of basis and quality diffs. ***ENB now expects Energy Services to record a loss in 2021.*** Expect mainline throughput to average 2.8 mmbb/d in 2021 (USCA at 2.8), but expect Q2 to average 2.6 mmbpd due to higher refinery and upgrader maintenance.
- **TRP:** *Neutral.* Adjusted EBITDA in line with consensus. Large KXL impairment taken in Q1, but expected. ***No update on expected costs or timing delays associated with Coastal GasLink project.*** US Gas Pipes was a C$63mm beat vs. USCA (6%) on Columbia Gas implementing new rates effective Feb 1 as a result of the rate case filed in 2020 (new rates remain subject to refund pending outcome of rate case). Power and Storage was a C$47mm beat (35%), though drivers unclear.
- **ENLC:** *Neutral.* EBITDA beat both USCA and street, but otherwise messy quarter with sizeable beats and misses at the segment level from disparate Uri impacts. Announced $60mm acquisition of Amarillo Rattler (~$11mm book value) for expected 6x 2022 EBITDA multiple. Net, net OK had largest negative impact from Uri which, combined with roll-off of $17mm MVC in Q1, led to segment profit declining 46% vs. Q1'20. ***Also laid out various GHG reduction targets – notably, targeting net zero emissions by 2050.*** Interim targets include 30% reduction in methane emissions by 2024 and 30% reduction in CO2e emissions by 2030 (both relative to 2020 baseline).
- **ALTM:** *Neutral.* Quarterly EBITDA essentially in line, with lower EBITDA from JVs offset by a $7.2mm power credit (assuming as a result of Uri) and higher G&P volumes and margins (~$3mm). Modest 2% increase in EBITDA guidance midpoint. ***Raised midpoint of EBITDA guidance $5mm from $250mm to $255mm on higher G&P volumes and Q1 performance.*** Raised G&P volume expectations to 370-410 mmcf/d from 360-400. New volume guidance incorporate two completed DUCs in Q1 and five DUCs expected to be completed in Q2.

Earnings – SMLP, WTRG, ETRN, PAA

- **SMLP:** *Neutral.* Quarterly EBITDA and DCF beats offset by unchanged guidance and lower volumes across the board. Gas volumes -7% vs. Q4'20 and flat y/y. Bakken crude volumes -8% from Q4 and -34% from Q1'20. Reduced revolver debt by $55mm in Q1, and are ***working on a holistic solution to refinance 2022 senior notes (~$234mm) and revolver ($802mm drawn at March 31).*** Double E Pipeline: $4.6mm investment in pipeline during the first quarter and expect credit facility to fund the majority of remaining capital commitment. Expect completion to be at or below $425mm, gross and in-service by 4Q'21.
- **WTRG:** *Neutral.* EBITDA, at $312mm a 2% beat vs. USCA's $305mm. Net Income $184mm, a 7% beat vs. USCA's $171mm, with incremental beat on higher Other Income and lower effective tax rate. 2021 guidance unchanged. Expect to file rate case in PA in 2H'21. ***Continue to be adamant they will close DELCORA acquisition.***
- **ETRN:** *Slight negative.* Earnings beat, but largely on non-cash derivative gain and slight, 1% earnings guide up, but once again delayed MVP in service and raised cost estimate. ***Pushed MVP in-service date to summer 2022 and raised cost estimate to $6.2B (was $5.8-$6.0B)*** due to requested extensions of review time for permits from VA and WV. ETRN's portion is $3.1B, of which $2.3B has been spent to date. Positive news was that GPOR has agreed to honor their gathering contracts with ETRN.
- **PAA:** *Slight negative.* Earnings beat, but no change to full year EBITDA guidance and ***very weak Q2 and Q3 guidance relative to street likely to make investors nervous. Partially offset by further capex cuts (-$65mm) and thus higher expected free cash flow (+$100mm).*** No buybacks during Q1. Guidance for Q2'21 of ~$452mm vs. street $520mm/USCA $478mm. Guidance for Q3'21 of $516mm, vs. street $544mm/USCA $528mm. Have said up to 25% of FCF after dividends could be used for buybacks, but emphasized that could be lower as you have to take into account EBITDA lost from the asset sales.

Earnings Themes

- **Very Positive Sentiment:** What a difference a year makes – really two ends of the spectrum vs. May 2020. Management sounds so upbeat about prospects for their business and their balance sheets – you can hear it in their voices and that's despite the over-arching energy transition theme. It sets up well for 2022.
- **Winter Storm Uri Largely a Big Windfall:** Some massive, needle-moving beats, with only some slight negatives. Some longer-term implications as generators/utilities forced to contract for more firm storage/transportation.
- **So '21 Guidance Higher…:** Haven't tabulated the numbers yet, but definitely will see a nice tick up in '21 consensus driven not just by Uri, but more confidence in commodity prices and volumes.
- **…And Much More FCF:** This week was a blur, but gut feel is that almost every company we cover (ex Canadians) generated FCF after dividends and capex. Have been waiting on this for a long time and have to say it is so nice to see.
- **Plus Debt Reductions:** Also think we are going to see, in aggregate, a very nice step down in debt for the group, with companies achieving or having near-term visibility to long sought-after coveted debt targets.
- **Buybacks Taking a Backseat for Now:** Which means buybacks are on the back burner for now, with the exception of MPLX. We still think 2022 is the year of the buyback, assuming we don't see yet another black swan event.
- **Capex Guidance Largely in Check:** Market has been worried about capex creep, but we just didn't see it (so far). A little higher at ET, but with a >$2B storm benefit, you deserve to go out and buy a new pair of shoes.
- **Meaningful Cost Reductions:** Companies have been tackling costs for the last two years, but they are still coming down nicely. Unsure how much of this quarter's O&M declines were due to storm-induced lower volumes and how much was true cost reductions. And we are in the camp that inflation is about to take off. Love the cost cutting, but watching the outlook closely.
- **Energy Transition:** Dominated some of the calls (ENB) and missing from others (PAA), but each quarter you can see companies making a little more progress on getting their hands around potential opportunities. Way too early for meaningful investment, although we would not be surprised to see some smaller acquisitions over the next 12 months.

WMB Sequent Purchase

- **News:** WMB announced they are buying Sequent Energy from SO for $110mm, including $60mm of working capital. Closing is expected in Q3. Normally we wouldn't write about a $110mm acquisition for a $30B market cap company, but this is interesting.
- **Who is Sequent?:** Gas marketing company formed in 2001 within AGL Resources (former Georgia utility). Sequent, based in Houston, is the 6th largest gas marketer in North America (based on Q4'20 volumes). As part of their business they have contracts for ~1.1 Bcf/d of firm transportation capacity on interstate gas pipelines or up to 5.8 Bcf/d when you include where they are listed as an agent of the shipper. And they have ~15 Bcf of contracted gas storage, or up to 38 Bcf when you include where they are listed as an agent.

Top NA Gas Marketers (Q4'20)

Company	Bcf/d
BP	16.8
Macquarie Energy	11.8
Shell	10.6
Tenaska	10.0
Conoco Phillips	8.3
Sequent	6.9
Direct Energy	6.6
Mercuria Energy	4.8
J. Aron	4.7
Morgan Stanley	4.4

Sequent Contracted Volumes

Pipeline	Transportation Contracts (mmcf/d)			Storage Contracts (Bcf)		
	As Shipper	As Agent	Total	As Shipper	As Agent	Total
Texas Eastern		950	950			
Transcontinental	120	814	934		15.0	15.0
Rockies Express		900	900			
Tennessee Gas	145	610	755		3.1	3.1
ANR Pipeline		683	683	3.0		3.0
Natural Gas Pipeline Company	134	205	339	7.0	1.1	8.1
East Tennessee Natural Gas	75	128	203			
Northern Border	196		196			
Columbia Gas	22	153	175			
Enable Gas	150		150			
Gulf South		96	96	3.2	1.1	4.4
Southern Star				2.1		2.1
National Fuel Gas Supply					2.3	2.3
Other	221	166	387			
Total	**1,062**	**4,705**	**5,767**	**15.4**	**22.7**	**38.0**

Source: S&P Global, SNL, USCA

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WMB Sequent Purchase, cont'd

- **WMB Ccall Comments:** WMB currently markets ~1 Bcf/d, so this will propel them to a top five-ish position. They expect Sequent to generate ~$20-$30mm of EBITDA/yr.
- **SO Call Comments:** On their earnings call last week, SO announced they were selling Sequent and provided some metrics. "We probably tie up something on average like $200mm worth of working capital so we have to provision for that within our credit facilities and then because of the gross revenue or gross sales associated with that business in forward positions probably something like another $800mm worth of parental support." "If you look at Sequent even prior to when Southern made the acquisition say from 2010 forward, they've averaged ~$40mm in net income. They had two years – one was $260mm and one was $163mmn where they really blew out earnings. Other than that the earnings were near zero." In Q1'21, Sequent generated ~$200mm of net income.
- **Our Thoughts:** ***Sounds like WMB is buying Sequent not because they see some step change in gas volatility or marketed volumes, but because they want maximize commercial opportunities by having a better understanding of daily gas market dynamics.*** Because Sequent has always been owned by a utility, in our view, it has been more de-risked than traditional gas marketing businesses. That said, marketing businesses have scorched more than just a handful of companies, and we are a bit jaded by covering WMB in early 2000s, when multiple downgrades in their debt created a marketing-driven liquidity crisis that almost sent them into bankruptcy. Yes, WMB is a very, very different company today, but that memory is still fresh, so we are in a show-me mode on this acquisition.

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Midstream Link Library

Below are links to PDF versions of our recent Friday Notes, as well as other USCA Midstream publications.

Recent Friday Notes

- OKE, MMP, CEQP Earnings, Money Flows, Frac Efficiency and Oil Supply Growth, 914 Data, NGL Data Points 4.30.21
- KMI Earnings, Storage Stats, Proxy Tidbits 4.23.21
- Misc Tidbits, EIA DPR Data 4.16.21
- DAPL Decision, Refresh on Permian Gathering Data 4.9.21
- Clean Energy SPACtivity, Clean Energy Money Flows, Energy Money Flows, Panhandle Rate Case, 914 Data, NGL Data Points 4.1.21
- Misc. Tidbits, Midstream Headcount 3.12.21
- EPD Analyst Day, Money Flows, FCF to EV Analysis, 914 Data, NGL Data Points 3.5.21
- Earnings Recaps, Earnings Themes, Misc Tidbits, AWK Analyst Day, Fun with 13-Fs, Short Interest 2.26.21
- Earnings Recaps, ET Acquisition of ENBL, Texas Deep Freeze 2.19.21
- Earnings Recaps, Solving the Permian Pipe Problems, Coalition for RNG Fireside Chat, RDS Strategy Day 2.12.21

Other Publications

- USCA Q1'21 Midstream Earnings Preview 4.20.21
- Tracking Midstream Returns 3.31.21
- USCA Q4'20 Earnings Recap 3.10.21
- KMI Analyst Meeting Preview 1.22.21
- Initiating Coverage of WTRG 1.21.21
- Initiating Coverage of AWK 1.21.21
- USCA Q4'20 Earnings Preview 1.20.21
- USCA Q3'20 Earnings Recap 11.19.20
- USCA Q3'20 Earnings Preview 10.14.20
- Initiating Coverage of WES 8.31.20

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For C-Corps, our price targets are based on a sum-of-the parts analysis. In our sum of the parts analysis, we value various business segments on a multiple of forward year(s) EBITDA, with multiples ranging from ~3x to ~12x. The spectrum reflects a wide range of contract lives, commodity sensitivity, volume risk, customer risk, cash flow visibility, growth outlook, etc. LP units are valued at our LP price target. GP values are determined by allocating a proportionate share of the consolidated equity value commensurate with the percent of total distributions the GP receives. We then net out C-Corp level debt and add back in forward year GP distributions received.

MLPs
For MLPs, our price targets are also based on a sum-of-the parts analysis. We value various business segments on a multiple of forward year(s) EBITDA, with multiples ranging from ~4x to ~13x. The spectrum range reflects a wide range of contract lives, commodity sensitivity, volume risk, customer risk, cash flow visibility, growth outlook, etc. We then net out forward year debt and minority interest to arrive at a consolidated equity value. From there we allocate equity value to the MLP based on the proportionate share of distributions the LP receives and add back in forward year distributions to be received.

MLP yield refers to the cash distributions paid out by the MLP, part of which may be treated as a return of capital rather that interest or capital gains.

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Overweight/Buy	29	60%	Overweight/Buy	2	7%
Hold	19	40%	Hold	2	11%
Underweight/Sell	0	0%	Underweight/Sell	0	0%

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Flash Comment

Utilities

Utility & Infrastructure Daily

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Quick thoughts from Wells Fargo Securities, LLC Utility & Infrastructure Team:

Utilities

Aqua America (WTR/Market Perform)(Reeder) – Yesterday afternoon (9/17), WTR announced that an asset purchase agreement was signed with the Delaware Country Regional Water Quality Control Authority (DELCORA) to purchase the municipal authority's wastewater assets for $276.5M. The agreement marks the culmination of a roughly two month exclusivity period between the two parties to explore a combination, which WTR discussed on the Q2 call in early August. The transaction is subject to Pennsylvania Public Utilities Commission (PaPUC) approval and would more than double WTR's existing 128,000 wastewater connections by adding the equivalent of 165,000 retail customers across 42 Southeast PA municipalities. While the purchase price is a bit north of DELCORA's $220-240M net PP&E value, WTR does not expect the transaction to create any goodwill which seems to suggest that the PaPUC will be asked to approve the deal under the state's fair market value (FMV) law. We expect PaPUC approval could take roughly 12 months and then once the deal closes, another 2-3 years before WTR is able to earn a return on the equity portion of the $276.5M rate base commensurate with the remainder of the water/wastewater business. In addition, we believe DELCORA could add as much as $150M of capex to our prior 2019-23 water capex (ex. M&A) forecast of $2.3B. In terms of equity needs, we think WTR could need to raise an additional $150-175M in 2020 & beyond (likely through establishment of an at-the-market program per management's Q2 call comments) with the bulk needed when the deal closes in 2H'20. Net-net, we believe minimal accretion is likely in 2020 with the DELCORA deal eventually adding roughly $0.05, or 2-3%, to EPS power by 2023. As a reminder, our current WTR 2019-23E EPS (pro forma for the pending Peoples deal but excluding any potential uplift from the planned election of repairs tax deduction at Peoples) are $1.32, $1.57, $1.68, $1.78 & $1.90.

Bigger picture, we are extremely encouraged by WTR's ability to find and get the deal signed with DELCORA for three reasons. First, it shows that management has not taken their eye off growing the regulated water/wastewater business despite the pending move into the gas LDC (local distribution company) business nor has the move into gas soured counterparties willingness to transact with WTR. Second, it further demonstrates that municipals are willing to come to the M&A negotiating table as a way to solve impending challenges. For DELCORA it was an estimated $1.2B of capital investment needed through 2041 which included a substantial amount to comply with Environmental Protection Agency (EPA) mandates to resolve combined sewer overflow problems – rather than put the burden on customer bills, DELCORA plans to place the sales proceeds into a trust to create a "rate stabilization plan" that should help offset those capital needs and save the average retail customer $1,400. Third, the addition of a substantial wastewater presence in Southeast PA could open the door to additional wastewater growth opportunities in the region, much the way WTR expanded its water footprint to the greater Philadelphia suburbs in the 1990s and perhaps to those same communities where the company already serves water.

Please see page 3 for rating definitions, important disclosures and required analyst certifications.
All estimates/forecasts are as of 09/18/19 unless otherwise stated. 09/18/19 05:35:12 ET

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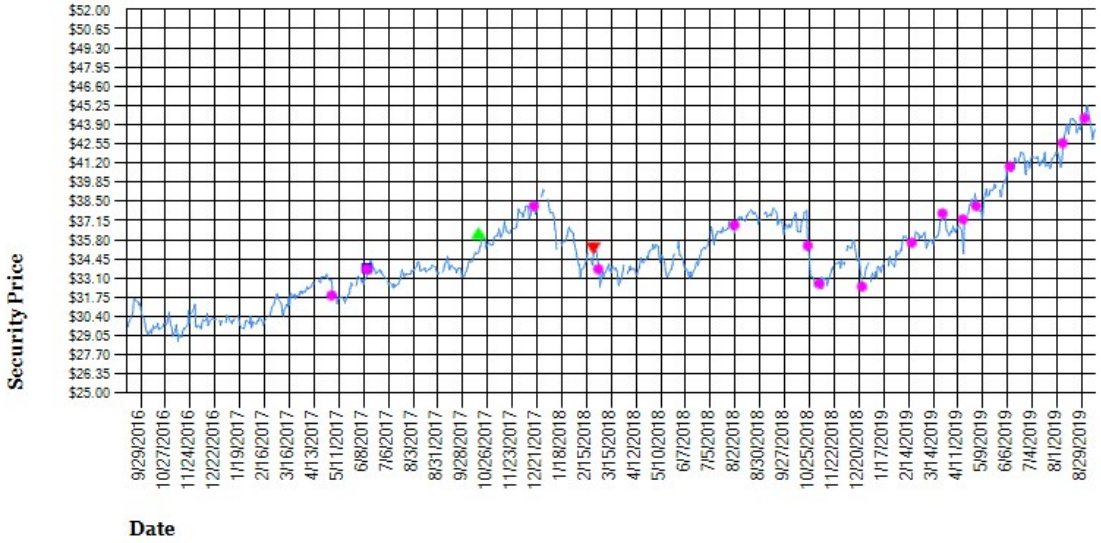
Aqua America, Inc. (WTR)/Market Perform (2)
Price as of 9/17/2019: $43.90
FY 19 EPS: $1.32
FY 20 EPS: $1.57
Shares Out.: 215.7 MM
Market Cap.: $9,469.23 MM

Rating Basis Information:
WTR Thesis: We are attracted to WTR's strong fundamentals - a proven EPS growth strategy, a growing rate base, constructive regulation, efficient operations and a strong balance financial profile. Our Market Perform rating reflects valuation considerations in light of WTR's pending agreement to acquire Peoples (a gas utility) and the associated P/E multiple, regulatory and deal execution/integration related risks.

DISCLOSURE APPENDIX

Required Disclosures

Aqua America, Inc. (WTR) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	9/13/2016		Kalton				
	9/13/2016	NA	2	NE	31.00	33.00	29.73
●	5/4/2017	31.70	2	NE	32.00	34.00	31.73
■	6/13/2017		Reeder				
●	6/13/2017	33.62	2	35	NE	NE	33.62
▲●	10/19/2017	35.30	1	40	NE	NE	36.03
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Outperform/Buy	SR	Suspended
2	Market Perform/Hold	NR	Not Rated
3	Underperform/Sell	NE	No Estimate

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M=Market Weight: Industry expected to perform in-line with the relevant broad market benchmark over the next 12 months.
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As of: September 18, 2019

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Flash Comment

Utilities

Utility & Infrastructure Daily

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Quick thoughts from Wells Fargo Securities, LLC Utility & Infrastructure Team:

Utilities

Essential Utilities (WTRG/Overweight) (Reeder) - We admittedly missed the ruling by Judge Dozor in the Court of Common Pleas of Delaware County last Monday (12/28). In what we consider to be a very positive development, the judge ruled in favor of DELCORA and WTRG on both matters disputed by Delaware County - the validity of the asset purchase agreement as well as the ability to put the proceeds of the $277M sale into a trust to be used to stabilize ratepayers' bills in the years ahead (keep increases to 3% annually so long as the fund is solvent while ensuring WTRG earns its authorized ROE). While Delaware County has indicated an intention to continue to argue its case as part of the pending PaPUC regulatory approval process (has yet to decide whether to appeal Judge Dozor's ruling), we believe the 12/28 ruling clears the way for WTRG to close the DELCORA deal by Q2'21.

We find it unlikely that the PaPUC will be overly sympathetic to Delaware County's contention that the $277M agreed to sales price that was blessed by the prior County Council undervalues the fair market value (FMV) of the system. It is our understanding that DELCORA struck that price during exclusive negotiations with WTRG in '19 perhaps knowing that it might be less than a closer to $400M price tag defensible by PA's FMV legislation. Rather the lower sales price would serve as a balancing act to help keep the subsequent rate increases to DELCORA customers manageable as WTRG recovers the FMV of the initial investment as well as the roughly $700M of capital investments required by 2028 to keep the system viable. Further, we believe the PaPUC's FMV approval process if anything is geared to protect against the opposite – a utility overpaying FMV and then trying to socialize those higher costs across its entire customer base.

We look towards WTRG's 1/11 investor event for additional insights into getting the deal across the finish line as well as the expected longer-term benefits. As we have previously opined, we believe the DELCORA deal represents material long-term value (that is not currently reflected in the share price!) given meaningful capex needs that fall beyond the current 5-year forecast as well as the likely substantial wastewater tuck-in deals that could transpire in the area. In other words, we believe the DELCORA deal should, at a minimum, allow WTRG to continue to target a 5-7% EPS CAGR through the end of the decade.

Infrastructure

Brookfield Infrastructure (BIP/BIPC)(Overweight) & Brookfield Renewable (BEP/BEPC)(Equal Weight) (Reeder) – Brookfield Asset Management (BAM/Not Covered) along with institutional partners made a public offer before the open on 1/4 to acquire the remaining units of one of its publicly traded

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All estimates/forecasts are as of 01/05/21 unless otherwise stated. 01/05/21 08:12:41 ET

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vehicles, Brookfield Property Partners L.P. (BPY/Not Covered), that it does not already own for $16.50/unit or a roughly 15% premium to the 12/31 close. We touched base with a Brookfield Infrastructure contact to confirm our suspicions – this situation is very much unique to BPY and should not be viewed as a potential read-through to either BEP/BEPC or BIP/BIPC. BAM has expressed frustration with the public valuation of BPY's underlying assets since prior to the onset of the pandemic and the stock's underperformance over the last 10 months, ostensibly related to longer term concerns regarding the health of the commercial real estate market, has only exacerbated that frustration. This contrasts to BEP/BEPC and BIP/BIPC which have been warmly embraced by investors, particularly (1) in the wake of the pandemic, (2) amidst the secular shifts towards renewables and infrastructure investment strategies and (3) following the creation of c-corp share classes in '20. As such, investors should not be thinking a potential take-private offer could be coming from BAM for either Brookfield Infrastructure or Brookfield Renewable absent a meaningful, and what we would consider an unexpected, re-rating down in the respective unit/share prices.

Acronyms:

DELCORA – Delaware County Regional Water Quality Control Authority

PaPUC – Pennsylvania Public Utility Commission

Essential Utilities, Inc. (WTRG)/Overweight
Price as of 1/4/2021: $46.19
FY 20 EPS: $1.58
FY 21 EPS: $1.65
Shares Out.: 245.2 MM
Market Cap.: $11,325.79 MM

Brookfield Infrastructure Partners L.P. (BIP)/Overweight
Price as of 1/4/2021: $49.49
FY 20 FFO/sh: $3.08
FY 21 FFO/sh: $3.50
Shares Out.: 465.0 MM
Market Cap.: $23,012.85 MM

Brookfield Infrastructure Corporation (BIPC)/Overweight
Price as of 1/4/2021: $70.29
FY 20 FFO/sh: $3.08
FY 21 FFO/sh: $3.50
Shares Out.: 465.0 MM
Market Cap.: $32,684.85 MM

Brookfield Renewable Partners LP (BEP)/Equal Weight
Price as of 1/4/2021: $44.26
FY 20 FFO/sh: $1.35
FY 21 FFO/sh: $1.43
Shares Out.: 646.0 MM
Market Cap.: $28,591.96 MM

Brookfield Renewable Corporation (BEPC)/Equal Weight
Price as of 1/4/2021: $57.95
FY 20 FFO/sh: $1.35
FY 21 FFO/sh: $1.43
Shares Out.: 464.0 MM
Market Cap.: $26,888.8 MM

Rating Basis Information:

WTRG Thesis: Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived and near-term regulatory risk is low as both the water and gas utilities completed rate cases in 2019), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

BIP Thesis: We believe attractive roughly 10% FFO/unit and 8% distribution/unit CAGRs are achievable over the next 5-years driven by a robust capital backlog and a savvy management team that has shown a consistent ability to execute and be good stewards of investor capital. In addition, we are drawn to BIP's diversified business mix – both strategically and geographically – as well as the highly regulated/contracted cash flow profile. We believe the near-term pressures from COVID-19 economic fallout, the strong U.S. dollar, etc. will be offset in the long run by value creating M&A opportunities, some of which may result from pandemic related disruptions in global equity and debt markets.

BIPC Thesis: We believe attractive roughly 10% FFO/unit and 8% distribution/unit CAGRs are achievable over the next 5-years driven by a robust capital backlog and a savvy management team that has shown a consistent ability to execute and be good stewards of investor capital. In addition, we are drawn to BIPC's diversified business mix – both strategically and geographically – as well as the highly regulated/contracted cash flow profile. We believe the near-term pressures from COVID-19 economic fallout, the strong U.S. dollar, etc. will be offset in the long run by value creating M&A opportunities, some of which may result from pandemic related disruptions in global equity and debt markets.

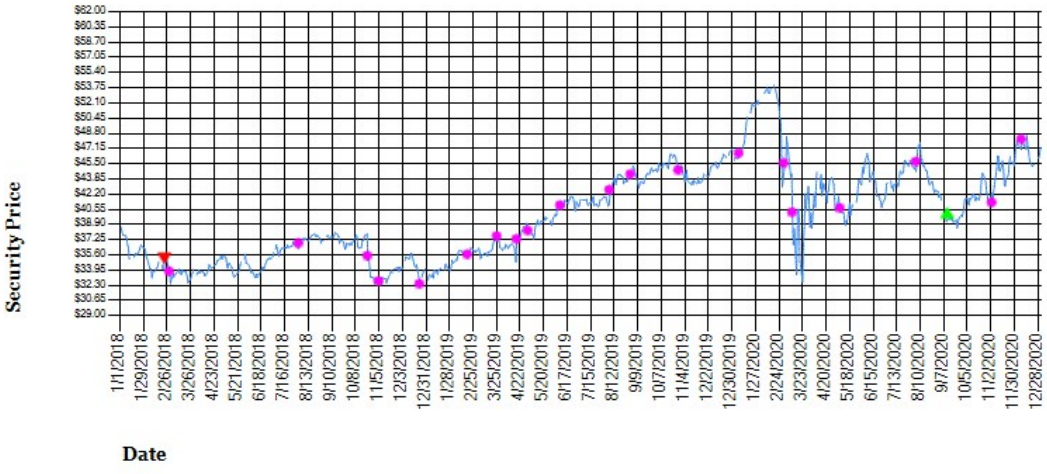
BEP Thesis: We consider BEP – as one of the few sizeable, publicly traded, pure play global renewable companies – to be a compelling way for investors to gain exposure to the decades-long global transformation towards carbon-free electric generation and growing ESG investing mantra. BEP is led by a proven management team with a track record of efficiently deploying (and recycling) capital across the portfolio. BEP's conservative philosophy of amassing a well-diversified global portfolio of predominantly contracted, carbon-free generation assets that are backed by an investment grade balance sheet and healthy cash flows results in a relatively low risk profile versus other renewable asset owners/developers. We believe units of BEP offer investors attractive long-term total return potential comprised of at least 7% FFO/unit growth and a roughly 3% yield with mid-to-upper single digit distribution/unit growth. That said, our Equal Weight rating reflects current valuation considerations.

BEPC Thesis: We consider BEPC – as one of the few sizeable, publicly traded, pure play global renewable companies – to be a compelling way for investors to gain exposure to the decades-long global transformation towards carbon-free electric generation and growing ESG investing mantra. BEPC is led by a proven management team with a track record of efficiently deploying (and recycling) capital across the portfolio. BEPC's conservative philosophy of amassing a well-diversified global portfolio of predominantly contracted, carbon-free generation assets that are backed by an investment grade balance sheet and healthy cash flows results in a relatively low risk profile versus other renewable asset owners/developers. We believe shares of BEPC offer investors attractive long-term total return potential comprised of at least 7% FFO/share growth and a 2.0-2.5% yield with mid-to-upper single digit distribution/share growth. That said, our Equal Weight rating reflects current valuation considerations.

DISCLOSURE APPENDIX

Required Disclosures

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	1/1/2018		Reeder				
	1/1/2018	NA	1	43	NE	NE	38.65
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51
●	3/2/2020	43.01	2	45	NE	NE	45.44
●	3/11/2020	44.41	2	48	NE	NE	40.03
●	5/7/2020	40.49	2	42	NE	NE	40.53
●	8/6/2020	45.56	2	45	NE	NE	45.56
▲	9/14/2020	39.35	1	45	NE	NE	39.82
●	11/4/2020	41.19	1	47	NE	NE	41.19
●	12/10/2020	47.70	1	52	NE	NE	48.02

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Source: Wells Fargo Securities, LLC estimates and Reuters data

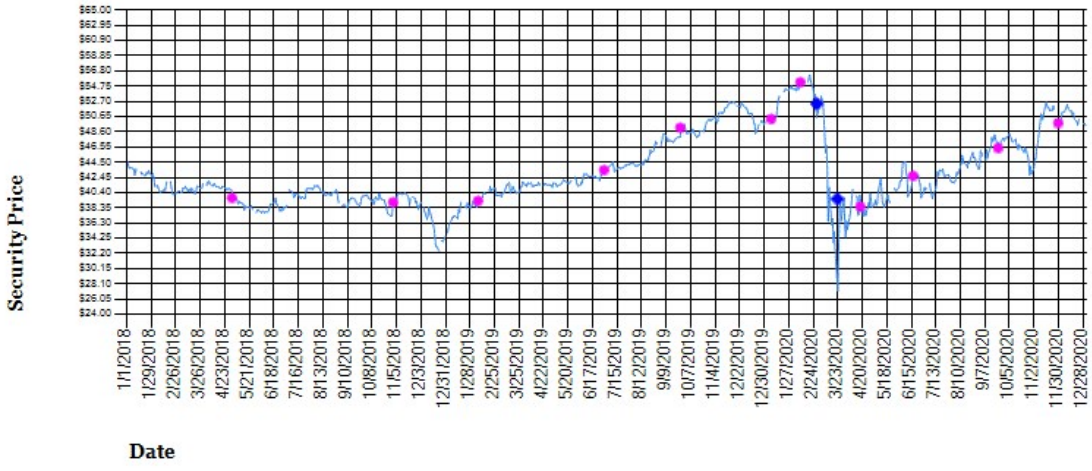
Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

Brookfield Infrastructure Partners L.P. (BIP) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	1/1/2018		Reeder				
	1/1/2018	NA	1	47	NE	NE	44.64
●	5/2/2018	39.59	1	46	NE	NE	39.57
●	11/2/2018	38.89	1	44	NE	NE	38.83
●	2/7/2019	39.20	1	46	NE	NE	39.15
●	7/1/2019	43.47	1	49	NE	NE	43.32
●	9/27/2019	49.30	1	54	NE	NE	49.05
●	1/8/2020	50.15	1	56	NE	NE	50.15
●	2/11/2020	55.03	1	60	NE	NE	55.05
◆●	3/2/2020	52.10	SR	NE	NE	NE	52.10
◆●	3/26/2020	38.23	1	50	NE	NE	39.22
●	4/20/2020	40.06	1	47	NE	NE	38.29
●	6/19/2020	42.49	1	48	NE	NE	42.46
●	9/23/2020	46.18	1	51	NE	NE	46.14
●	12/1/2020	49.61	1	56	NE	NE	49.61

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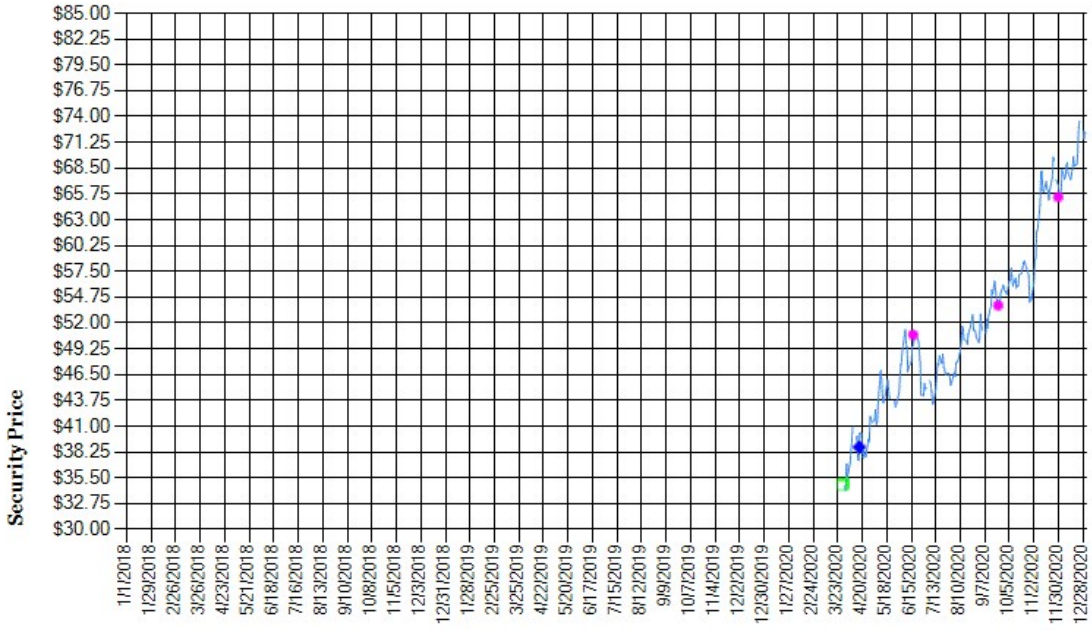
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

Brookfield Infrastructure Corporation (BIPC) 3-yr. Price Performance



Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
3/31/2020		Listed on NYSE, TSX exchanges				
4/19/2020		Reeder				
4/20/2020	40.27	1	47	NE	NE	38.47
6/19/2020	50.00	1	53	NE	NE	50.59
9/23/2020	53.58	1	57	NE	NE	53.66
12/1/2020	65.18	1	70	NE	NE	65.18

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Source: Wells Fargo Securities, LLC estimates and Reuters data

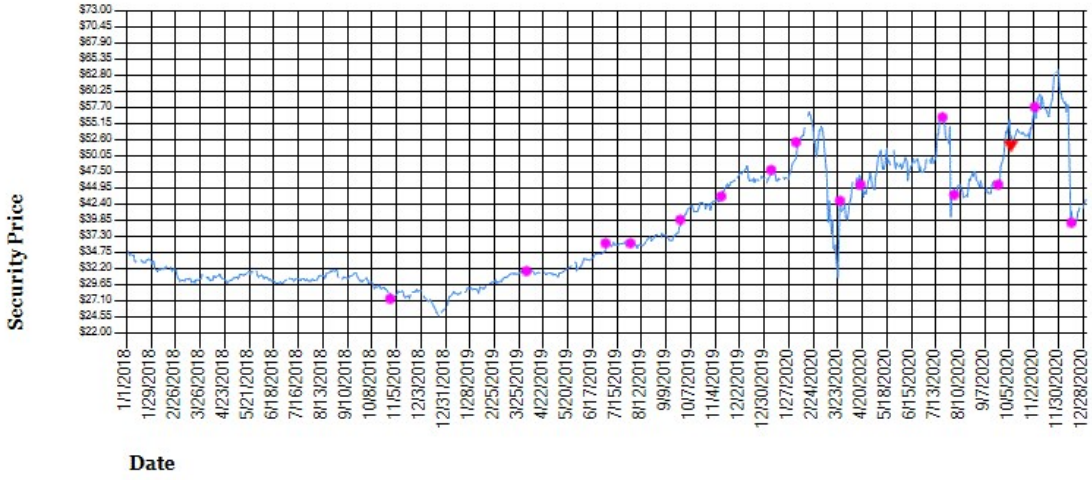
Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

Brookfield Renewable Partners LP (BEP) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	1/1/2018		Reeder				
	1/1/2018	NA	1	37	NE	NE	34.92
●	10/31/2018	27.48	1	34	NE	NE	27.25
●	4/4/2019	31.46	1	36	NE	NE	31.46
●	7/3/2019	36.03	1	38	NE	NE	35.99
●	7/31/2019	35.91	1	39	NE	NE	35.85
●	9/27/2019	39.24	1	42	NE	NE	39.70
●	11/12/2019	43.39	1	46	NE	NE	43.27
●	1/8/2020	47.44	1	51	NE	NE	47.44
●	2/6/2020	52.20	1	57	NE	NE	52.02
●	3/26/2020	41.54	1	47	NE	NE	42.75
●	4/20/2020	46.95	1	52	NE	NE	45.22
●	7/22/2020	55.90	1	60	NE	NE	55.90
●	8/4/2020	44.81	1	48	NE	NE	43.50
●	9/23/2020	44.95	1	50	NE	NE	45.27
▼●	10/8/2020	53.11	2	53	NE	NE	51.27
●	11/5/2020	55.91	2	55	NE	NE	57.50
●	12/16/2020	41.14	2	40	NE	NE	39.31

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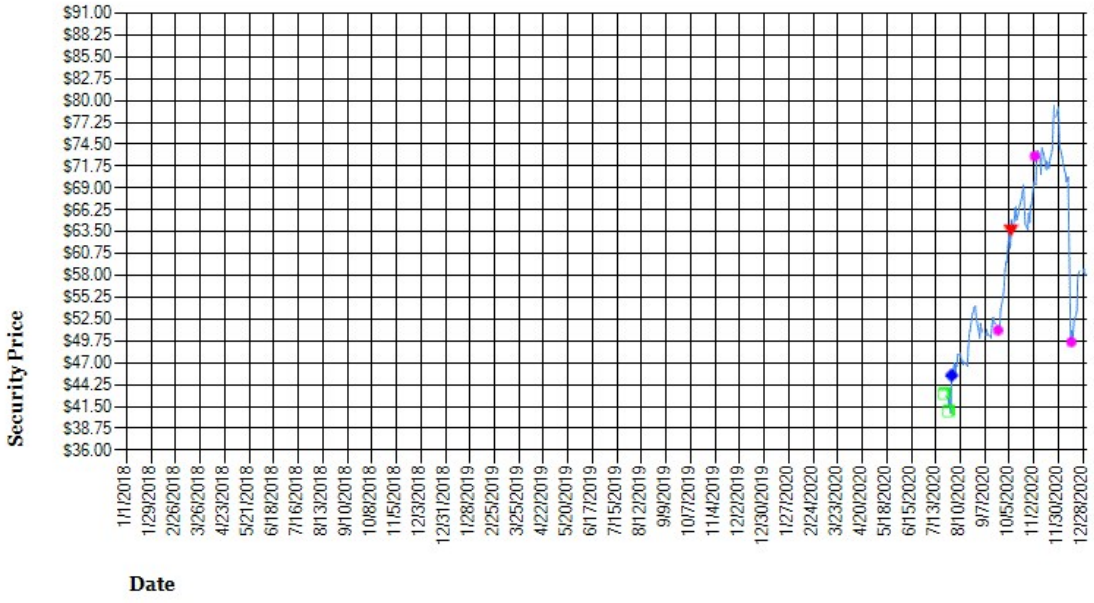
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

Brookfield Renewable Corporation (BEPC) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
▫	7/24/2020		begins when issued trading				
▫	7/30/2020		beings trading after unit split (1 for 4) from BEP shares				
	8/3/2020		Reeder				
◆	8/4/2020	47.00	1	51	NE	NE	45.17
●	9/23/2020	51.15	1	55	NE	NE	50.91
▼●	10/8/2020	64.98	2	60	NE	NE	63.43
●	11/5/2020	69.42	2	62	NE	NE	72.87
●	12/16/2020	51.06	2	47	NE	NE	49.46

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Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

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- ▫ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

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WTRG: Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.
BIP: Key risks, in our view, include prolonged economic fallout from the COVID-19 outbreak, the potential for a strategic misstep, foreign exchange risks, exposure to foreign governments, regulatory/contract risks and capital markets risks.
BIPC: Key risks, in our view, include prolonged economic fallout from the COVID-19 outbreak, the potential for a strategic misstep, foreign exchange risks, exposure to foreign governments, regulatory/contract risks and capital markets risks.
BEP: Key risks, in our view, include prolonged economic fallout from the COVID-19 outbreak, the potential for a strategic misstep, foreign exchange risks, exposure to foreign governments, contract risks and capital markets risks.
BEPC: Key risks, in our view, include prolonged economic fallout from the COVID-19 outbreak, the potential for a strategic misstep, foreign exchange risks, exposure to foreign governments, contract risks and capital markets risks.

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2=Equal Weight: Total return on stock expected to be 0-10% over the next 12 months. HOLD
3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

VOLATILITY RATING
V=A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: January 5, 2021

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WELLS FARGO SECURITIES

Essential Utilities, Inc.

WTRG: ALJ Recommendation a Setback but DELCORA Deal Far from Dead

Reiterate Overweight

Overweight/$52

Water Utilities

Company Note

- **Key Points.** The ALJ recommendation in the pending DELCORA deal was posted to the PaPUC website on 1/12. It recommends denial as (1) ongoing litigation regarding DELCORA's ability to transfer assets under the asset purchase agreement and (2) failure to attach the rate stabilization plan to the application make it too difficult to make an informed recommendation regarding if the deal is in the public interest. WTRG plans to file objections. This is no doubt a setback but in no way does it appear to kill the DELCORA deal. For starters, it does not necessarily convey the PaPUC commissioners' view (the PaPUC order is due by 3/26). We believe there is still a reasonable pathway to approval – perhaps through settlement – however it could push deal closure beyond early Q2'21. Reiterate Overweight.
- **Ongoing Litigation.** These lawsuits are separate from the 12/28 ruling in favor of DELCORA/WTRG regarding the APA's validity and ability to put the $210M of net proceeds into a trust. Rather five of the 49 municipalities served by DELCORA (represent 9% of annual revenues) have not yet consented to the transfer of the assets and/or assignment of contracts to WTRG – though WTRG reached a settlement on 1/8 with one (Trainer) resolving its issues. Three of the munis (SWDCMA, Lower Chichester and Upland) filed lawsuits in early November in the Delaware County Court of Common Pleas.
- **Path Forward.** At this time it is unclear to us what the path forward would be if settlements are not reached with the remaining four munis and/or the section of the APA that contemplated such a scenario is not upheld/enforced. Can they be carved out of the deal? Once those issues are resolved, the reasonableness of the purchase price under PA's FMV law as well as the public interest determination can be made. The ALJ indicates a new application should be filed to reflect those updates along with the rate stabilization plan and tariff provisions outlining the bill credit mechanism to limit customers' rate increases to a 3% compound annual maximum (so long as the trust remains solvent). If a new application is indeed required, we believe it would push the potential closing date to late '21 or early '22.
- **Reiterate Overweight.** First, getting the $277M DELCORA deal closed is more important than the timing. The near-term EPS impact is minimal. The strategic value is longer-term, including the fact that the bulk of DELCORA's $700M capex needs through '28 fall in the 2026-28 period. Second, our Overweight thesis is not solely predicated on DELCORA closing. As previously stated, though the DELCORA deal is highly supportive of WTRG's growth aspirations, we consider the future to be bright without it, driven by elevated pipeline infrastructure investment needs for the foreseeable future supplemented by municipal M&A trends. We believe relatively low risk, regulated EPS growth of at least 6% is achievable and that rate of growth would simply be enhanced if DELCORA closes.

$ EPS	2019A	2020E Curr.	2020E Prior	2021E Curr.	2021E Prior
Q1 (Mar.)	0.28	0.60 A	NC	0.67	NC
Q2 (June)	0.37	0.29 A	NC	0.25	NC
Q3 (Sep.)	0.48	0.23 A	NC	0.25	NC
Q4 (Dec.)	0.34	0.46	NC	0.50	NC
FY	1.47	1.58	NC	1.67	NC
CY	1.47	1.58		1.67	
FY P/EPS	31.9x	29.7x		28.1x	
Rev.(MM)	890	1,931		2,055	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile
Adjusted EPS excludes items considered non-recurring.
WTRG expects 2021 adjusted EPS of $1.64-1.69 range and targets a 5-7% EPS CAGR through 2023 off the 2019 adjusted base of $1.47.
WTRG expects 2020 adjusted EPS at the top end of the $1.53-1.58 range.

Ticker	WTRG
Price Target/Prior:	**$52/NC**
Price (01/13/2021)	**$46.88**
52-Week Range:	$30-55
Shares Outstanding: (MM)	245.2
Market Cap.: (MM)	$11,495.0
S&P 500:	3,809.84
Avg. Daily Vol.:	923,308
Dividend/Yield:	$1.00/2.1%
LT Debt: (MM)	$5,277.4
LT Debt/Total Cap.:	53.2%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	7.0%
CY 2021 Est. P/EPS-to-Growth:	4.0x
Last Reporting Date:	11/03/2020 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Please see page 3 for rating definitions, important disclosures and required analyst certifications. All estimates/forecasts are as of 01/14/21 unless otherwise stated. 01/14/21 05:39:16 ET

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Acronyms:

ALJ – Administrative Law Judge
APA – Asset Purchase Agreement
DELCORA – Delaware Country Regional Water Quality Control Authority
FMV – Fair Market Value
PaPUC – Pennsylvania Public Utility Commission
SWDCMA – Southwest Delaware County Municipal Authority

Price Target

Price Target: $52 from NC

Our $52/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.80. For WTRG's water utility multiple, we ascribe a roughly 5% discount to the 21E multiple we use for AWK (34-34.5X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The roughly 5% discount reflects a modestly lower earnings growth rate (we forecast roughly 7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 17.0-17.5X (based on ATO, NWN, OGS & SR) and then apply a roughly 10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive PA regulatory framework. Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

Investment Thesis

Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived and near-term regulatory risk is low as both the water and gas utilities completed rate cases in 2019), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

Company Description

Headquartered in Bryn Mawr, PA, Essential Utilities (WTRG) - formerly Aqua America - is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTRG's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total water customer base and nearly 70% of consolidated water rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio.

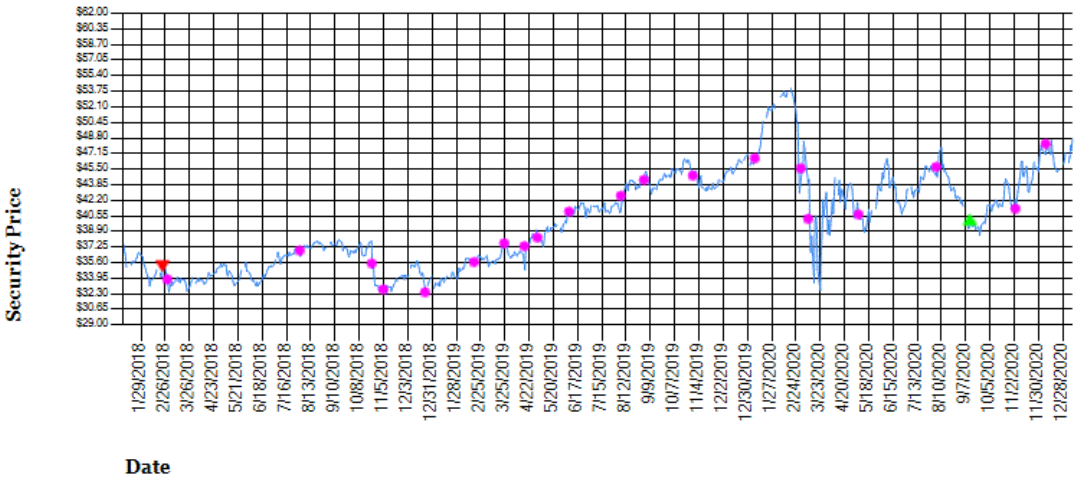
In March 2020, WTRG closed on the acquisition of Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, WTRG paid 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to other gas utility transactions at the time. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

Regulated operations account for more than 99% of consolidated revenues. Consolidated EPS is expected to be driven roughly 70% by water utility operations with the gas utility contributing the remaining 30%.

In February 2020, the new name Essential Utilities, Inc. and new ticker WTRG became effective. Prior, the company was known as Aqua America Inc. and traded under the ticker WTR.

Required Disclosures

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	1/8/2018		Reeder				
	1/8/2018	NA	1	43	NE	NE	37.71
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51
●	3/2/2020	43.01	2	45	NE	NE	45.44
●	3/11/2020	44.41	2	48	NE	NE	40.03
●	5/7/2020	40.49	2	42	NE	NE	40.53
●	8/6/2020	45.56	2	45	NE	NE	45.56
▲	9/14/2020	39.35	1	45	NE	NE	39.82
●	11/4/2020	41.19	1	47	NE	NE	41.19
●	12/10/2020	47.70	1	52	NE	NE	48.02

*Effective December 7, 2019, Wells Fargo Securities' Equity Research modified its ratings definitions. Complete definitions of current ratings can be found below. For information related to prior ratings definitions, please contact equityresearch1@wellsfargo.com.

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

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WTRG: Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

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As of: January 14, 2021

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Company Update — February 25, 2021

Water Utilities

Essential Utilities, Inc. (WTRG)

WTRG: Recent Weakness Provides Attractive Entry Point – We Remain Bullish on WTRG's LT Growth Prospects

Our Call

We believe the recent weakness provides an attractive entry point as the fundamental narrative has not changed. Since 1/8, shares of WTRG are down 11%. This trails "larger cap" water utility peers (-0% to -8%), gas LDCs (+6%) & S&P Utilities (-5%). We reiterate our Overweight rating and $52/sh price target (29X our 22E). WTRG's YE'20 update was consistent with the mid-January guidance event including '21 diluted EPS guidance of $1.64-1.69 (cold YTD weather has Peoples off to a strong start), a 5-7% EPS CAGR target through '23 and $3B of capex over the 2021-23 period which will drive underlying 6-7% water and 8-10% gas rate base CAGRs. Our 21-25E EPS remain $1.67, $1.80, $1.93, $2.07 & $2.20. Our forecast results in an EPS CAGR near the upper end of WTRG's 5-7% range which we believe is reasonable given strong underlying rate base growth driven by accelerated pipeline replacement needs and a municipal M&A strategy that continues to gain momentum.

A Very Healthy Municipal Deal Pipeline. Following a solid 2020 ($63M of deals), 2021 is shaping up to be even better (signed $90M of new deals in 2020). Besides the $277M DELCORA deal, WTRG has five other signed APA's which will add $161M in rate base – includes four separate chunky wastewater deals (East Whiteland, PA $55M; Lower Makefield, PA $53M; Bourbonnais, IL $32M; Williston Township, PA $17.5M). In addition there is the $12M purchase of Shenandoah, PA's water assets – the borough council approved the deal in late November and the APA is still being finalized. WTRG's deal development pipeline remains robust and management continues to express optimism that activity will start ramping up in the years ahead in the four states that only somewhat recently adopted FMV legislation (NC & OH in '18; TX in '19; VA in '20). Our model reflects primarily announced deal closures over the 2020-22 period plus a $75M/year placeholder in '23 & beyond. This could prove conservative if the recent pace continues.

Big Picture DELCORA Thoughts. We believe the deal will close as discussed in greater detail later in this note. Getting DELCORA across the finish line is more important than the timing of it given the longer-term strategic value it represents. Beyond the $277M rate base pick up at closure (expected early Q2'21), we are attracted to (1) the $700M of capital investments – $25-50M/year for typical repair/replace work plus roughly $300M over the 2026-28 period related to DELCORA's treatment plant – as well as (2) the likely substantial wastewater tuck-in deals that could transpire in the area. But our Overweight thesis is not solely predicated on DELCORA closing. We believe relatively low risk, regulated EPS growth in the 5-7% range is achievable without driven by pipeline replacement needs and municipal M&A momentum. That rate of growth would simply be enhanced if DELCORA closes as it should allow WTRG to extend it through the end of the decade and perhaps even raise it.

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Rating	Overweight
Ticker	**WTRG**
Price Target/Prior:	**$52.00/NC**
Upside/(Downside) to Target	**19.6%**
Price (02/25/2021)	**$43.49**
52 Week Range	$30.40 - 52.00
Shares Outstanding	245,271,727
Market Cap (MM)	$10,667
Enterprise Value (MM)	$16,023
Average Daily Volume	979,436
Average Daily Value (MM)	$43
Dividend (NTM)	$1.00
Dividend Yield	2.3%
Net Debt (MM) - last reported	$5,357
ROIC - Current year est.	9%
3 Yr EPS CAGR from current year (unless otherwise noted)	7%

$ EPS	2020A	2021E Curr.	2021E Prior	2022E Curr.	2022E Prior
Q1 (Mar)	0.60 A	0.67 E	NC	-	NC
Q2 (Jun)	0.29 A	0.25 E	NC	-	NC
Q3 (Sep)	0.23 A	0.25 E	NC	-	NC
Q4 (Dec)	0.46 A	0.50 E	NC	-	NC
FY	1.58 A	1.67 E	NC	1.80 E	NC
P/E	27.6x	26.1x		24.1x	

ROIC - Current year est.: ROIC is actually ROE Source: Company Data, Wells Fargo Securities estimates, and Refinitiv.
NA = Not Available, Volatility = Historical trading volatility

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Next PA Rate Cases

WTRG does not have any major rate-setting procedures pending. The next PA water & wastewater rate case filing is expected around mid-'21 while the next gas one might be made in late '22. While WTRG's PA rate cases can never be overlooked given the meaningful % of rate base represented (more than 70% on the water/wastewater side), the utility has a long history of reaching constructive outcomes via settlement agreements. In addition, despite the pandemic-related economic challenges faced by many ratepayers that has led to heightened rate sensitivity in some states, the PA regulatory environment has upheld its constructive reputation – includes the recent NI rate case outcome as well as the ALJ recommendation in the pending AWK case which honors the 10/30 settlement agreement.

Peoples Repairs Tax Deduction Settlement

Management noted that a verbal settlement has been reached with intervenors that will give back 100% of the catchup benefits to ratepayers over a 5-year period. This contrasts with WTRG's proposal where 40% of the benefits would have been shared directly with ratepayers through surcredits on bills and the remaining 60% used as an increasing income tax expense offset over the 2023-25 period in order to avoid implementing a gas base rate increase prior to 1/1/2026. We view the move as goodwill gesture on WTRG's part to help provide customers with some additional bill relief as they deal with the economic impacts of the pandemic. As noted above, we expect Peoples next base rate filing could occur in late '22.

A Deeper Dive Into The DELCORA Approval Process

Since the ALJ recommendation for denial of the $277M deal was posted to the PaPUC website on 1/12, a few developments have occurred.

(1) **Delaware County on 1/21 appealed the 12/28 decision** by Judge Barry Dozor in the Court of Common Pleas of Delaware County. Recall, Judge Dozer ruled against Delaware County's two claims and in favor of DELCORA and WTRG regarding the validity of the asset purchase agreement as well as the ability to put the net proceeds of roughly $200M from the sale into a trust to be used to stabilize ratepayers' bills in the years ahead.

(2) **Settlements have been reached with two more of the municipalities** that had not yet consented to the transfer of the assets and/or assignment of contracts to WTRG from DELCORA and each has discontinued its Complaint in the Court of Common Pleas of Delaware County. One was SWDCMA which constitutes ~5% of DELCORA's annual revenues or the bulk of the 9% represented by all of the holdouts. That leaves only two remaining (the Townships of Edgmont and Lower Chichester) out of the 49 total municipalities served. Discussions remain ongoing and the parties do not oppose the PaPUC approving the DELCORA transaction with the condition that these contractual issues be resolved prior to closing.

(3) **WTRG and DELCORA withdrew the proposed customer assistance bill payment that the ALJ recommendation concluded was a "rate stabilization" plan**. Rather than show it as a credit against the amount due on wastewater bills, DELCORA customers will get the $200M of net benefits from the transaction through direct mail, quarterly payments.

We continue to believe the DELCORA deal will eventually be approved by the PaPUC and close. For starters, the ALJ recommendation does not necessarily convey the PaPUC commissioners' views. That point was highlighted just recently in the constructive conclusion of NI's rate case despite an ALJ recommendation to deny the requested increase altogether. Approval just may take some additional time beyond WTRG's early Q2'21 target. We cannot rule out the potential need to re-file the PaPUC application and/or extend the current statutory timeframe beyond the 3/26 deadline. With only four of the five PaPUC commissioner chairs filled right now, it is possible a 2-2 stalemate occurs.

But under the assumption the ALJ recommendation is consistent with where commissioner heads were in mid-January, WTRG has largely addressed the concerns expressed, in our opinion. Recall, ALJ rationale for denial was that (1) ongoing litigation regarding DELCORA's ability to transfer assets under the asset purchase agreement and (2) WTRG's failure to attach the rate stabilization plan to the application make it too difficult to make an informed recommendation regarding if the deal is in the public interest.

We believe the 12/28 Court of Common Pleas order combined with the additional municipal settlements (and likely two future ones) should allow the reasonableness of the purchase price under

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PA's FMV law as well as the public interest determination to be made by the PaPUC. Reaching a settlement with Delaware County – an outcome that management continues to strive for, possibly even after the 3/26 PaPUC decision deadline – that results in dismissal of the appeal would seemingly de-risk the conclusion even further. Finally, the withdrawal of the "rate stabilization" plan should make the ALJ's concern on that point moot.

Acronyms Used:

ALJ – Administrative Law Judge

APA – Asset Purchase Agreement

DELCORA – Delaware Country Regional Water Quality Control Authority

FMV – Fair Market Value

PaPUC – Pennsylvania Public Utility Commission

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Price Target Basis and Risk

Price Target for WTRG: $52.00 from NC

Our $52/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.80. For WTRG's water utility multiple, we ascribe a roughly 5% discount to the 21E multiple we use for AWK (34X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The roughly 5% discount reflects a modestly lower earnings growth rate (we forecast roughly 7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 18.0-18.5X (based on ATO, NWN, OGS & SR) and then apply a roughly 10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive PA regulatory framework.

Risk for WTRG

Key downside risks include adverse regulatory decisions, issues with the Peoples gas deal integration and earnings accretion, missteps with regards to the M&A strategy and execution as well as potential anti-gas sentiment and ESG concerns stemming from the ownership of a gas utility.

Investment Thesis

WTRG

Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived and near-term regulatory risk is relatively low as both the water and gas utilities completed rate cases in 2019), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

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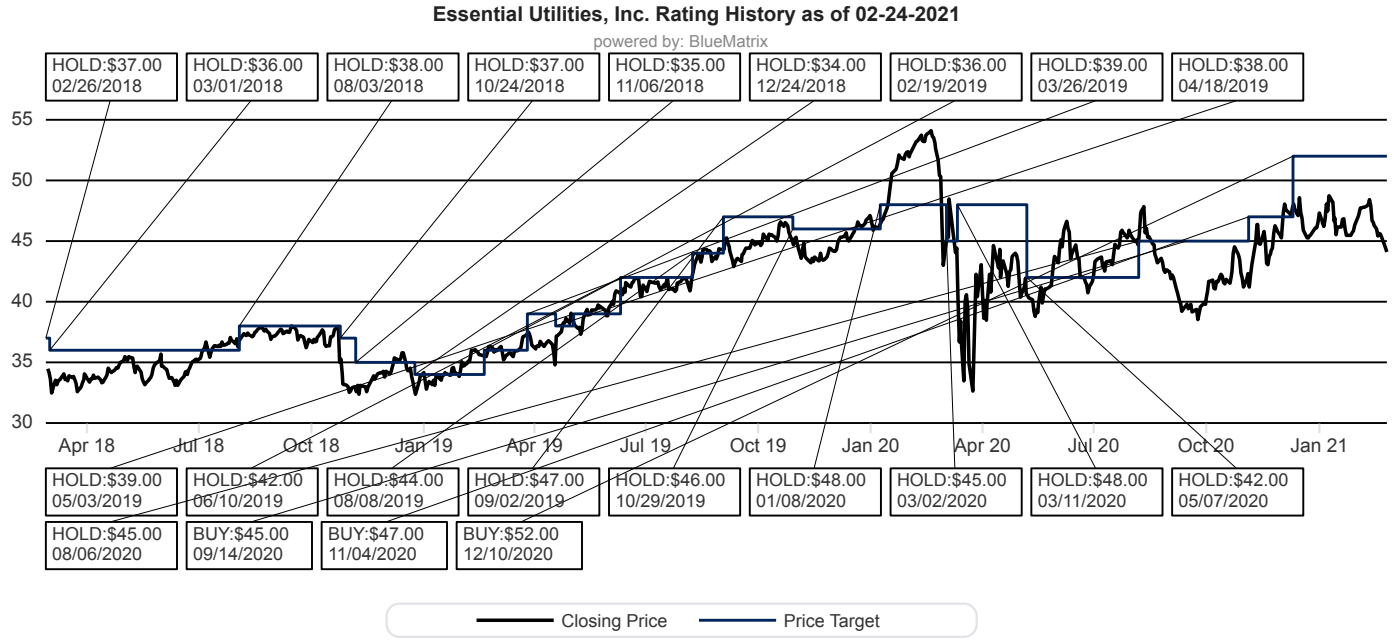

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2=Equal Weight: Total return on stock expected to be 0-10% over the next 12 months. HOLD

3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

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WELLS FARGO SECURITIES

Flash Comment

Utilities

Utility & Infrastructure Daily

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Jonathan Reeder, Senior Analyst (314) 875-2052
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Quick thoughts from Wells Fargo Securities, LLC Utility & Infrastructure Team:

Utilities

Aqua America (WTR/Market Perform)(Reeder) – We had the chance to catch up with WTR regarding the company's disclosure yesterday (6/12) that a settlement agreement was filed with the PA Public Utilities Commission (PaPUC) in the Peoples merger approval docket (A-2018-3006061). Because there is an outstanding issue between two of the intervenors that prevented a unanimous settlement from being reached – relates to the preferred path forward for a 1,600 customer system – the remainder of the docket must play out as scheduled so that the PaPUC can decide the issue. This is what pushes the expected close of the merger into fall 2019. It is our understanding that the settlement agreement does not address any Peoples revenue requirement issues. Rather the appropriate revenue requirement going forward will be determined as part of the pending Peoples rate case. This could include (1) the potential election and treatment of repairs tax deduction at Peoples (discussed on the Q1'19 earnings call) and (2) the potential to realize (and retain) any merger synergies. We continue to expect a constructive outcome in the Peoples rate case later this year and believe the potential election of repairs tax deduction could be a powerful bargaining chip for the utility as settlement discussions take place. Rate case hearings are scheduled to begin June 18.

In terms of our EPS outlook, as we stated yesterday (6/12), the delayed merger close is likely to negatively impact our current 19E EPS of $1.37 which was predicated on a mid-'19 close. Our preliminary analysis suggests pushing it to the end of Q3'19 could have up to a ($0.10) impact. Importantly, we do not have any reason to believe at this point that our 20-23E of $1.56, $1.66, $1.78 & $1.90 are not still within reason. Given the multiple moving parts in '19 related to the merger and rate relief, we believe investors should focus on '20 & beyond for a better sense of WTR's ongoing EPS power. Our '20 & beyond outlook is predicated on earned ROEs at both the water and gas utilities of 10-10.5%.

Aqua America, Inc. (WTR)/Market Perform (2)
Price as of 6/12/2019: $41.12
FY 19 EPS: $1.37
FY 20 EPS: $1.56
Shares Out.: 178.1 MM
Market Cap.: $7,323.47 MM

Please see page 3 for rating definitions, important disclosures and required analyst certifications.
All estimates/forecasts are as of 06/13/19 unless otherwise stated. 06/13/19 05:27:05 ET

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Rating Basis Information:
WTR Thesis: We are attracted to WTR's strong fundamentals - a proven EPS growth strategy, a growing rate base, constructive regulation, efficient operations and a strong balance financial profile. Our Market Perform rating reflects valuation considerations in light of WTR's pending agreement to acquire Peoples (a gas utility) and the associated P/E multiple, regulatory and deal execution/integration related risks.

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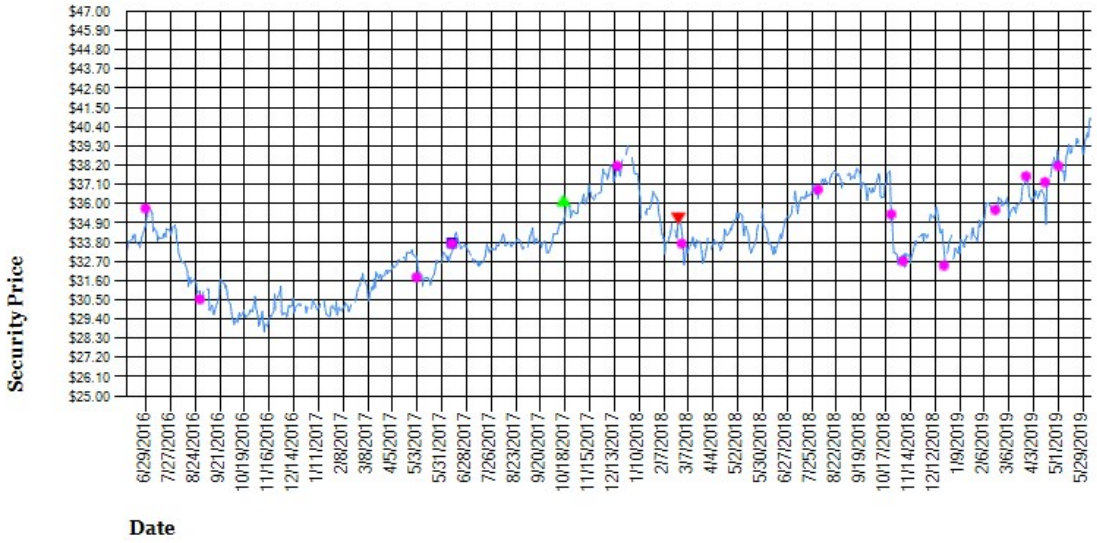
Aqua America, Inc. (WTR) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	6/7/2016		Kalton				
	6/7/2016	NA	2	NE	33.00	34.00	33.21
●	6/30/2016	35.39	2	NE	35.00	36.00	35.66
●	8/31/2016	30.38	2	NE	31.00	33.00	30.41
●	5/4/2017	31.70	2	NE	32.00	34.00	31.73
■	6/13/2017		Reeder				
●	6/13/2017	33.62	2	35	NE	NE	33.62
▲●	10/19/2017	35.30	1	40	NE	NE	36.03
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Outperform/Buy	SR	Suspended
2	Market Perform/Hold	NR	Not Rated
3	Underperform/Sell	NE	No Estimate

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SECTOR RATING
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As of: June 13, 2019

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Aqua America, Inc.

WTR: EPS Outlook Updated As ALJ Recommends Approval Of Peoples Acquisition

Market Perform/$46

Water Utilities
Market Weight

Earnings Estimate Revised Down

- **EPS Outlook Updated As Peoples Merger Close Timing Comes Into Focus.** The assigned Administrative Law Judge (ALJ) to the Peoples merger docket issued the long awaited recommended decision (RD) on 10/28. ALJ Long's RD not only approves WTR's acquisition of the Peoples Companies but adopts the non-unanimous settlement agreement in its entirety. This includes the proposed $120M investment over a 7-year period to update the deteriorated 1,700 customer, 368 mile Goodwin and Tombaugh (G&T) gathering system and replace the existing bare steel pipe as well as a one-time $13M rate credit offered by WTR to partially offset this cost. WTR and the seven other settling parties, including key intervener Office of Consumer Advocate (OCA), support updating the G&T system as the preferred path forward and socializing those costs across Peoples entire customer base whereas the PaPUC's Bureau of Investigation & Enforcement (I&E) and Office of Small Business Advocate believe those customers that cannot be updated economically should be abandoned and forced to convert to an alternative energy source. In fact, ALJ Long goes as far as to characterize the remediation of the G&T system as the most significant benefit of the transaction.

  As we previously discussed, parties have 30 days from the RD to file exceptions and it is likely that the PaPUC (Pennsylvania Public Utilities Commission) may take at least 30 days after that to render a final decision (absent the parties reaching unanimous settlement in light of the ALJ's RD). As such, WTR now anticipates a December 2019 or early 2020 close. We are encouraged by the ALJ's RD and anticipate the PaPUC is likely to ultimately adopt the RD.

  We lower our 19E EPS to $1.19 from $1.32 to reflect an assumed YE'19 close by removing the roughly two months of Peoples net income benefit from our previously assumed end of October '19 deal close. In addition, we made a few other tweaks to our model, primarily related to external financing assumptions including correcting an error that overstated some cash inflows in 2019. As a result, we adjust our 2020-23E EPS down modestly to/from $1.57/$1.58, $1.70/$1.71, $1.80/$1.82 & $1.92/$1.94. This results in a 6.5-7.0% EPS CAGR. As a reminder, our outlook continues to exclude any potential uplift from the planned election of repairs tax deduction at Peoples in 2020. We reiterate our Market Perform rating but lower our 12-18 month price target to $46/share from $47 to reflect lower peer multiples since our last update.

$ EPS	2018A	2019E Curr.	2019E Prior	2020E Curr.	2020E Prior
Q1 (Mar.)	0.29	0.28 A	NC	NE	
Q2 (June)	0.37	0.35 A	NC	NE	
Q3 (Sep.)	0.44	**0.39**	**0.40**	NE	
Q4 (Dec.)	0.31	**0.19**	**0.30**	NE	
FY	1.41	**1.19**	**1.32**	**1.57**	**1.58**
CY	1.41	1.19		1.57	
FY P/EPS	31.8x	37.7x		28.6x	
Rev.(MM)	838	895		1,979	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile
WTR's 2019 ongoing diluted EPS guidance of $1.45-1.50 excludes ALL Peoples related impacts. Our estimates are pro-forma Peoples, ex costs to complete.

Ticker	WTR
Price Target/Prior:	**$46/$47**
Price (10/28/2019)	**$44.90**
52-Week Range:	$32-47
Shares Outstanding: (MM)	215.7
Market Cap.: (MM)	$9,684.9
S&P 500:	3,022.55
Avg. Daily Vol.:	1,029,020
Dividend/Yield:	$0.94/2.1%
LT Debt: (MM)	$2,749.0
LT Debt/Total Cap.:	40.4%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	7.0%
CY 2019 Est. P/EPS-to-Growth:	5.4x
Last Reporting Date:	08/06/2019 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Price Target

Price Target: $46 from $47

Our $46/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 2.5% discount to our 70% water/30% gas utility hybrid multiple to our 2021E of $1.71. The 2.5% discount reflects merger execution/integration risk. For WTR's water utility multiple, we start with AWK's 2020 P/E multiple of 30.3X (AWK represents the closest publicly traded peer) and apply a 5% discount (given AWK's higher growth rate and best-in-class management team). For WTR's gas utility multiple, we utilize the 2020 pure play gas LDC median of 24.6X. Key risks include regulatory and M&A strategy execution related.

Investment Thesis

We are attracted to WTR's strong fundamentals - a proven EPS growth strategy, a growing rate base, constructive regulation, efficient operations and a strong balance financial profile. Our Market Perform rating reflects valuation considerations in light of WTR's pending agreement to acquire Peoples (a gas utility) and the associated P/E multiple, regulatory and deal execution/integration related risks.

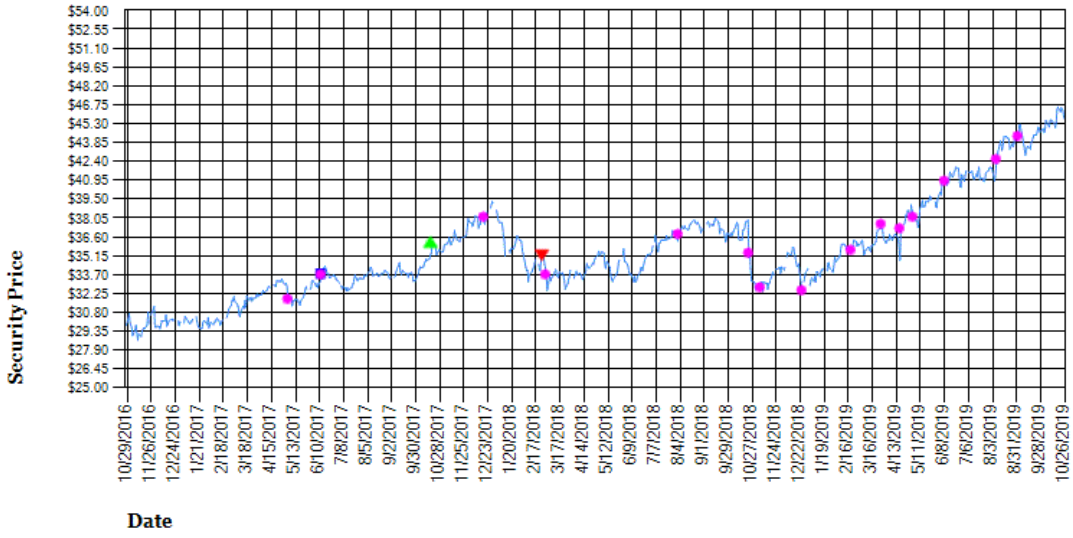
Company Description

Headquartered in Bryn Mawr, PA, Aqua America (WTR) is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTR's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total customer base and nearly 70% of consolidated rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio. Regulated operations account for more than 99% of consolidated revenues.

On 10/23/18, WTR announced a deal to acquire Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, the deal appears to be 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to what we have seen in recent gas utility transactions. WTR expects to close the deal around YE'19, subject to receiving the final necessary regulatory approval from PA. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

Required Disclosures

Aqua America, Inc. (WTR) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	10/26/2016		Kalton				
	10/26/2016	NA	2	NE	31.00	33.00	29.86
●	5/4/2017	31.70	2	NE	32.00	34.00	31.73
■	6/13/2017		Reeder				
●	6/13/2017	33.62	2	35	NE	NE	33.62
▲●	10/19/2017	35.30	1	40	NE	NE	36.03
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Outperform/Buy	SR	Suspended
2	Market Perform/Hold	NR	Not Rated
3	Underperform/Sell	NE	No Estimate

Additional Information Available Upon Request

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SECTOR RATING
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As of: October 29, 2019

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2020 EEI Conference Takeaways

Utilities

- **Key Points.** We hosted virtual meetings with 38 companies at the EEI Financial Conference on November 8-11th. The tone of the conversations were positive with sales recovering nicely and most utilities finding offsets (cost controls and regulatory support) to COVID impacts. Further, the de-carbonization theme was in full force with no shortage of investment opportunities to modernize the electric generation fleet as well as the enabling T&D infrastructure. On the strategic front, conversations centered around the trend toward pure play utility models and interest in M&A, particularly on the LDC side given depressed valuations.
- **Strategic Questions Abound.** This year's conference featured many discussions around strategic options as diversified utilities were asked about transitioning to pure play models and combo electric/gas utilities were asked about their appetite for LDC acquisitions. Among the diversified names, ED and SRE expressed the most openness to strategic moves, in our view. Separately, CNP and OGE were fairly reserved on their comments on ENBL, though we expect to hear more from CNP at the 12/7 analyst day. Companies that are in the midst of divesting or potentially divesting assets (EXC, DTE, PEG, PPL) faced questions about whether they would entertain regulated M&A opportunities post-divestiture (assuming they have greater financial flexibility).

  On the LDC front, reviews were mixed with most mgmt. teams expressing confidence in the long-term business model, but some not willing to add gas to the mix. Companies that expressed the most openness to acquiring LDC systems, in our view, were ALE, BKH, MDU, SO and WEC (not without some cautious language). And for good measure, there was a mid-EEI Reuters report suggesting that NEE made a recent offer for EVRG, which both companies talked down.
- **Optimism on Sales**. Most utilities expressed cautious optimism that C&I sales are coming back and some portion of the uptick in residential could be sustainable given a new working environment. Certain utilities in desirable areas (IDA, NWE and POR, for example) also discussed strong in-migration trends as a result of increased mobility/flexibility in the work place.
- **Guidance Updates.** A few utilities used the EEI conference to update capex/growth forecasts. AEP laid out a robust capex refresh that was heavy on renewables and wires investment (surprise, surprise) and continued to support the 5-7% EPS CAGR. ALE lowered the 2019-2024 EPS CAGR to 4% from 5-7% reflecting COVID impacts and pressure on wind returns. And NWE initiated 2021 EPS guidance and increased the 5-year capex budget, which continues to support the mid-point of the 3-6% EPS CAGR.
- **Company-Specific Takeaways in Body of Note.**

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ALLETE Inc. (ALE/Equal Weight/$58.30) (Akers)

Growth Rate Buckles Under COVID Pressures. ALE is one of the more COVID-exposed companies within our universe because of Minnesota Power's industrial (especially taconite) heavy customer base. Taking various pressures under consideration (electric demand, down-sized transmission project, lower assumed equity issuance price, pressure on wind returns, etc.), mgmt. revised the EPS CAGR to 4% (through '24 off the '19 adjusted base of $3.35) from 5-7%. The growth rate assumes 3% growth at the utility operations and 30% at ALLETE Clean Energy (ACE). The company acknowledged that the 4% CAGR could be conservative should an economic recovery prove faster/stronger than anticipated. On the positive side, ALE is seeing a pickup in steel demand and, importantly, Keetac recently indicated plans to reopen in December, which provides more certainty into 2021, though Verso's future remains unclear. MP filed a request to defer the lost revenue associate with Keetac and Verso – upside to '20E & '21E if approved – and plans to file a general rate case in November '21.

Tone Change on ACE. Mgmt. indicated that ACE is beginning to see pressure on wind returns stemming from increased competition and lower power prices. As a result, the previous target of adding 2-3 wind projects annually may prove challenging. ALE will continue to evaluate wind opportunities, but is also looking at other services, such as solar, storage and grid resiliency as potentially more attractive growth avenues. On the Q3 call, which was during EEI, mgmt. also mentioned the possibility of optimizing the ACE portfolio, which we expect could include asset sales.

Ameren Corporation (AEE/Overweight/$82.37) (Kalton)

Waiting on the CapEx Refresh. EEI is not a big event for AEE as the company provides prompt year EPS guidance and the 5-yr capex refresh in conjunction with Q4 earnings. That being said, we picked up a few tidbits on pending items. First, the renewables RFP in MO is ongoing and it is doubtful that results will be in on time to include in the '21-25 capex refresh – mgmt. is always hesitant to get too far in front of the regulatory approval process in terms of officially adding capital to the base plan. That being said, we think there are plenty of capital investment needs outside the RFP to support a 6%+ EPS CAGR well into the 2020s. As an aside, mgmt. noted that capex spending on technology is up many multiples in MO since the MoPSC approved the PISA mechanism – the reduced regulatory lag allows for improved returns for short lived assets. If/when new MO renewables comes into the fold it remains an open question as to whether it will be purely incremental to the '21-25 plan or whether there will be some capex shifting (factors will include customer rate considerations and financing needs). No new developments on the IL legislative front – mgmt. continues to work with stakeholders as everyone eyes comprehensive energy legislation in the Spring '21 session (and not the Nov. '20 veto session). At issue for AEE are the existing formula rate structure and the allowed ROE methodology for the electric distribution operations and (maybe) the investment rider for the gas utility.

American Electric Power Company, Inc. (AEP/Overweight/$91.15) (Kalton)

New Robust CapEx Plan. While AEP's 5-yr capex refresh ('21-25) was higher than we anticipated ($37B vs. $35B), the underlying drivers were exactly as we expected (wires + renewables). Renewables represents nearly 15% of the planned capex vs. 7% in the original '20-24 capex guidance. Yes, the $2B North Central Wind project was officially added to the capex schedule but other regulated renewables are coming into the fold at AEP's vertically integrated utilities. Renewable additions (owned & PPA) in these jurisdictions are expected to total over 4,600 MW during '21-25 with another 3,400 MW planned for '26-30. As for wires, there is plenty of spend across the board with seams solutions offering potential significant upside in the mid-20s and beyond as transmission grid spend will likely accelerate to better allow for the flow of renewable power across regions. AEP's large geographic footprint combined with strong transmission expertise positions the company for this coming opportunity. All told, the phrase "long capex runway" gets thrown around a lot in the utility sector, but it's clearly appropriate when framing AEP's investment opportunities.

Thoughts on EPS Guidance / Asset Sales. AEP also rolled out initial '21 EPS guidance of $4.51-$4.71, the mid-point of which represents a 6% increase over the '20 EPS guidance mid-point of $4.35 – consistent with AEP's 5-7% EPS CAGR goal. We view the '21 guide as solid but not exceptional (our 21E EPS is $4.70). Notably, the '21 forecasted ROE of 9.0% is a smidge below our estimate of 9.2%. While 20 bps doesn't sound like much, it equates to ~$0.20, or 4%, of EPS power. Keep in mind, the earned ROE guidance heading into '19 was 9.65% and heading into '20 was 9.1% (however, '20 was characterized as a transition year due to a heavy rate case cycle). We think the overall downward trend in allowed ROEs is playing a role in the ROE guidance but it is not the only factor. Mgmt. noted that 30% of the company's capital spend does not have formula or rider rate type recovery, which results in regulatory lag especially as capital spend goes up. This is an area of focus for mgmt. and could result in longer-term

upside if AEP can improve the regulatory frameworks. Last, in our view, there was no discernible change to mgmt.'s thought process around the potential sale of operating utilities. A number of factors go into the calculus including the ability to efficiently recycle capital and the organic growth prospects of the underlying asset (operating utility) in question.

American Water Works (AWK/Equal Weight/$164.37) (Reeder)

If It Ain't Broke, Don't Fix It. This should not come as a shock but management made it clear that the proven strategy and values that have yielded success over the years will continue to be adhered to going forward and it is up to them to continue to execute. Pursuing timely recovery of much needed water/wastewater infrastructure spend while keeping operating costs in check to maintain customer affordability is the core and can lead to attractive 5-7% risk-adjusted EPS growth on its own. Then layer on top a tuck-in acquisition strategy that has gained momentum in recent years and should remain at these elevated levels (if not further accelerate) as (1) states continue to adopt policies to encourage consolidation, (2) COVID and other financial stresses challenge municipal budgets and (3) regulatory requirements make it increasingly difficult to efficiently and effectively operate small-to-mid sized systems. And finally, management is committed to the non-regulated businesses and believe both are complimentary, capital-light ways of augmenting the regulated growth. As such, the 7-10% growth triangle is likely to persist well into the future.

Other Tidbits. Committed To Water/Wastewater. Management believe investors ascribe a high value to the fact that AWK is a pure play water/wastewater utility – and all of the positive long-term fundamentals of the industry like decades long elevated capex needs, consolidation potential, etc. – and is committed to remain that way. The focus is on continuing to build the tuck-in M&A pipeline which is already very strong. Military Marches On. While AWK has won 5 of the last 6 military base awards, the company is by no means resting on its laurels and continues to try to bring value and solutions to the bases under operation to boost its competitive position. AWK is involved in 4 open solicitations, including a Navy base (the first Navy base to embark down the privatization path), and 2 are expected to be awarded within the next 3-6 months. Management indicated the universe of bases yet to be privatized that AWK would be interested in (i.e. sizeable) stands at about 70. External Equity. The plan remains to close the NY American Water cash sale to AQN in Q1 and look to externally raise about $500M of equity in mid-'22. The timing of equity is driven by the rate of capital deployment and would only be accelerated if there is a near-term uptick in municipal deals.

Alliant Energy Corporation (LNT/Overweight/$57.42) (Kalton)

Plenty of Renewables & Distribution. LNT has a wonderfully straightforward story; but there were a couple of nuggets to note from EEI: (1) LNT's recently announced Clean Energy Blueprint in IA includes 400 MW of solar. Notably the solar qualifies for advanced rate making principles including an enhanced ROE (set for the life of the asset). LNT's IA wind farms receive an 11.0% ROE and recent precedent for IA neighbor MidAmerican suggest the solar spend could qualify for a 10.5-10.7% ROE. (2) Both IPL & WPL have been systematically undergrounding their electric distribution systems at a pace of 1.5-2.0% per year and currently sit at 25% undergrounding of LNT's 45,000 mile distribution system (skewed more toward WPL). Given strengthening storms (the recent derecho is an example) and the increasing focus on resiliency/reliability, policymakers may be open to LNT to accelerate the program (it sounds like early days, but mgmt. is evaluating). While we do not expect anything in the near-term, we think this remains an intriguing long—term investment opportunity. At an estimated cost of $100,000-300,000 per mile, we think the undergrounding opportunity is several billion dollars. Again, the work is currently ongoing – but it could be accelerated and be another lever (along with generation transformation) to extend the targeted 6% rate base CAGR well beyond the mid'20s.

AVANGRID (AGR/Overweight/$51.44) (Kalton)

EPS Outlook. Fresh off the heels of AGR's Investor Day, mgmt. helped fill in the blanks on a few of the assumptions underlying the EPS CAGR of 6-8% (off the adjusted '20 EPS base of $2.10) and the '21 & '22 EPS guidance ranges. Our take: we think mgmt. has prudently erred on the side of conservatism particularly as it relates to the regulated utility operations. While the '21-25 guidance contemplates the NY utilities eventually reaching the allowed ROE levels, our sense is that the near-term EPS guidance reflects continued underearning as NYSEG & RG&E continue to ramp up vegetation management spend in order to improve system resiliency. We also think the outlook reflects a pragmatic approach to the pending PNM acquisition taking into account integration risk. However, we believe there could be potential to best AGR's baseline internal goals via (1) the potential for higher capex vs. PNM's current guidance and (2) modest cost savings (sharing of best practices, etc.). In terms of merchant wind pricing,

AGR's near-term guidance reflects flattish power and REC prices of $20-25/MWh and $10/MWh, respectively. Mgmt. remains highly committed to reducing merchant price exposure over time via recontracting.

Offshore Update. Mgmt. remains very excited about AGR's position in the nascent U.S. offshore wind market. In the near-term, Vineyard Wind is one of the three bidders into NY's pending RFP for up to 2,500 MW (AGR owns 50% of Vineyard Wind). The other two bidders are Equinor/BP and Ørsted/ES. Mgmt. noted that Vineyard's bid was for a large amount of capacity given the distance between the company's lease area (off the coast of MA) and NY – the electricity would land onshore in MA and then be wheeled to NY. The winning bid(s) are expected to be announced by YE'20.

Black Hills Corp. (BKH/Equal Weight/$63.63) (Akers)

Next Stop: Growth Rate. BKH plans to provide an EPS growth target in conjunction with the YE update. The company believes there's good line of sight on the gas side given programmatic pipe investments while the electric side can be lumpy depending on IRP/RFP outcomes (likely continue to be somewhat conservative on that front). We expect the growth rate will be in the 5-7% range and we look to the July 2021 IRP filing in WY for additional insight on generation opportunities (could include discussion of carbon capture as WY remains supportive of the coal plants); there's also potential to expand the Renewable Ready subscription program.

ESG & LDCs (and M&A). BKH rolled out plans to reduce GHG emission intensity 70% by 2040 at the electric operations with 50% GHG reductions targeted at the gas utilities by 2035. On the gas side, CO is in the spotlight as there are ongoing discussions – including a recent Commission Informational Meeting – on what the LDCs can do to comply with environmental initiatives. While there are some parties pushing for electrification, BKH appeared encouraged that the utility stakeholders (including electrics) understand the affordability challenges of electrification along with customer choice considerations. As further evidence of the company's comfort with the gas outlook, mgmt. expressed openness to acquisitions within the company's existing jurisdictions. More specifically, BKH would evaluate CNP's AR LDC if it comes up for sale (though the company noted that the service territory is lower growth than its own AR utility).

CenterPoint Energy, Inc. (CNP/Equal Weight/$24.07) (Akers)

What a Difference a Year Makes. We had a very constructive conversation with new CFO Jason Wells. He reiterated that the plan to deliver at the high end of the 5-7% growth rate (off 2020 Utility guidance basis EPS of $1.12-1.20) already contemplates various headwinds/scenarios – these include the 2021 equity dilution headwind, the roll-off of equity returns on transition/securitization bonds at CEHE, one to two LDC sales, and potential strategic alternatives at ENBL that could require more parent debt to be allocated to the utility. Similarly, Mr. Wells confirmed that the $16B capex plan and 10% rate base CAGR already account for the LDC sales (no negative re-basing ahead). On the O&M front, company has already identified meaningful cost cuts for the 2021/2022 time frame and, longer-term, envisions a culture of continuous improvement.

Strategic Update. We look to the 12/7 analyst day for details on the LDCs sale candidates and for insight into the direction on ENBL. On the latter, mgmt. clearly intends for utility earnings to be a bigger piece of the pie over time, but we still think an exchange of shares into a larger MLP (vs. outright cash sale) is a viable option in the review process. Shifting to the LDCs sales, we think a combination of OK, MS, LA and AR could be sale candidates or, on the bigger side, CNP could elect to sell OH. We do not expect the LDCs in TX or IN would be considered given the company's goal to reduce/simplify regulatory jurisdictions and, separately, we suspect MN may be a bit bigger than what CNP needs. The company indicated that the LDC sales are not driven by any long-term electrification concerns and reiterated that their states remain highly supportive of natural gas. That said, having a more electric-centric mix was mentioned as being consistent with the ESG focus, along with making renewable-enabling investments in TX and modernizing the generation fleet in IN (new plan envisions more utility-ownership of renewables).

CMS Energy (CMS/Overweight/$67.01) (Kalton/Reeder)

On Point, As Expected. One did not have to meet with CMS management to know what they would say. And that is not a bad thing! Just the opposite. As CFO Rejji Hayes put it, CMS will give folks "as much certainty on the E as they can and let investors determine the P." It is that de-risked approach to the business – a utility franchise that sports an extensive capex backlog amidst a constructive regulatory backdrop (that is expected to remain steady going forward) and led by a proven management team with a track record of effective cost management in order to deliver consistent 7% EPS growth (why bother even

saying 6-8%!) – that results in an attractive risk-adjusted total return proposition. Then layer on aggressive decarbonization goals for the ESG-friendly crowd and what is there not to like – other than some (not us!) would argue the "P"?

Food For Thought. More COVID Shutdowns. In the event COVID concerns lead to additional restrictions, CMS does not believe commercial & industrial load will be nearly as hard hit as it was in Q2'20 given evidence that businesses have been largely effective at maintaining operations while protecting employees. That said, should headwinds occur that a residential load uptick would not fully offset, you guessed it – costs can be managed! June 2021 IRP Filing. Planning has begun but it does not sound like, at least on a preliminary basis, the plan will look all that different than the prior iteration, even in the context of a potential Biden administration, given CMS's already aggressive stance towards decarbonizing the fleet (0% net emissions by 2040). Management is monitoring storage in terms of both the cost curve decline and increased efficacy but the urgency is not as great as other utilities in terms of balancing the intermittency of renewables given the Ludington Pumped Storage Facility essentially offers CMS more than 1 GW of battery-like capacity. Committed To Non-Regulated. CMS already has a small non-utility earnings mix (~7% with a guide to no more than 10%) which is where some other companies seem to be trying to get. Plus CMS runs the non-utility portion of the portfolio like a utility in terms of the predictability of earnings.

Consolidated Edison Inc. (ED/Equal Weight/$81.72) (Akers)

COVID Impacts. We gained insight into the COVID impacts and impact on guidance. The $0.05 reduction to the top end of the 2020 range (now $4.15-4.30) reflects the continued inability to collect late charges and disconnection/connection fees. The bad debt expense triggered the materiality threshold, which allowed the utilities to book a $50mm deferral, but that was already contemplated in the guidance range. Looking ahead, the company expects commercial fees could resume in Q1 and the timing on residential remains uncertain. ED is seeking approval to defer the lost revenue in a regulatory proceeding, which could provide upside to near-term EPS if approved.

ESG Focus. Mgmt. highlighted opportunities across the platform to advance de-carbonization efforts. These include the EE, EV-enabling and battery storage initiatives at CECONY (not all captured in rate base but all earn returns and, in some cases, incentives), direct investments in renewables at the Clean Energy Business, renewable-enabling electric transmission projects (including offshore wind) and ongoing efforts to reduce emissions from the gas utility operations. ED is also engaging with stakeholders in an effort to allow the utility to invest in large-scale renewables in NY – those discussions are ongoing. Regarding the Clean Energy Business, ED intends to utilize tax equity (a change from prior practice), but continues to see the annual capex run-rate around $400mm. Shifting to the midstream investments, there was no change in tone from the ESG analyst day when mgmt. expressed an openness to divestitures. Specifically to MVP, we sense the company would wait for the project to go online in order to garner a better valuation. Lastly, when asked about potentially acquiring an LDC, mgmt. indicated that it may not be the most attractive opportunity given policy uncertainty going forward, particularly in the Northeast.

DTE Energy (DTE/Overweight/$130.06) (Kalton)

Full Steam Ahead. Post the separation of GSP, DTE has the ability to be one of the fastest growing utilities within our coverage universe as the company targets 5-yr electric and natural gas utility earnings CAGRs of 7-8% and 9%, respectively. When we asked about upside to the already robust $17B regulated utility '21-25 capex plan, mgmt. suggested there was no shortage of capex opportunities and pointed to the company's recent capex refreshes (generally result in 10-20% increases in cumulative 5-yr capex). Switching gears to GSP, mgmt. plans to get out in front of investors as much as possible in front of the planned spin-off in mid '21. CEO Elect David Slater remains excited about the company's organic growth prospects in both the Marcellus and Haynesville shale basins. We also asked whether Spinco would continue to be acquisitive post-spin. It sounds like this remains an open question as mgmt. continues to evaluate the post-spin strategy. In terms of market comparisons for Spinco, DTE views WMB and EQT as most closely resembling Spinco's asset mix/profile, which suggests a valuation range of 8.5-10.0X EV/EBITDA (higher than the 8X multiple assumed in our price target).

Duke Energy (DUK/Equal Weight/$97.31) (Kalton)

Pivoting to Growth. We thought Chair, President & CEO Lynn Good made a highly compelling case for DUK's long-term EPS growth prospects and why it could trend towards the high end of the targeted 4-6% CAGR (off the preliminary '21 EPS base of $5.15). In our view, DUK's messaging to investors has noticeably improved in '20. We point to a focus and execution on cost management along with better

crystallizing (for investors) the long-term generation transformation rate base growth opportunities. Front and center is the recently filed Carolinas IRP, which contemplates substantial spend aimed at decarbonizing DUK's coal heavy generation fleet (hearings are expected to begin in NC during Q2'21). The initial spend is likely to center on solar/battery storage and natural gas-fired generation. Looking beyond the 2020s, the next leg of investment will depend on a number of factors including carbon policies and technology trends. We believe it is at this point that offshore wind could come into the fold (depending upon legislative support) – or not, if it makes more sense to continue down the solar/natural gas path.

Dominion Energy Inc. (D/Equal Weight/$85.68) (Akers)

Execution, Execution, Execution. The message from CEO Bob Blue and CFO Jim Chapman was one of execution with a focus on regulated operations in premium jurisdictions. The company aims to deliver consistent EPS growth aligned with the 6.5% target and appears to be off to a solid start based on the Q3 update. Mgmt. did not express discomfort with the remaining 10-15% of non-utility exposure, noting that it is largely contracted.

Regulatory/Political Update. As it relates to VA, mgmt. acknowledged that it can (and will) get noisy on the political/regulatory front, but highlighted a history of supportive outcomes. The company expects there will be that same opportunity into the 2021 triennial review, particularly given the various items in the toolkit (write-offs, CCROs, etc). The company also expressed cautious optimism heading into the COP process at BOEM given strong local support and project-specific considerations (don't have the same fishery and shipping lane dynamics as other projects); from a timing perspective, being behind other projects may also be beneficial as D can gain insight from others' experience. Shifting to South Carolina, the immediate focus remains on the rate case. Mgmt. indicated nothing out of the ordinary thus far, but acknowledged some uncertainty with recent turnover in the commission (could make it more difficult to settle). Lastly, on the LDCs, D has not seen any anti-gas undertones in the company's service territories and remains very comfortable with those assets in the mix.

Edison International (EIX/Equal Weight/$62.90) (Kalton/Reeder)

Making The Case That Wildfire Risk Is Actually Pretty Low. Management believes the wildfire mitigation plans, Public Safety Power Shutoff policies and improved containment/suppression strategies have vastly reduced the risk of a major California wildfire caused by investor-owned utility equipment. The '19 & '20 wildfire seasons are evidence of that. And planned future mitigation efforts – installing covered conductors, vegetation management with expanded clearances where possible, increasing situational awareness, etc. – should further the cause. Couple the lower event risk with CPUC-sanctioned wildfire insurance programs that are backstopped by the provisions of AB1054, including the liability cap and $21B wildfire fund, means the risk of triggering substantial shareholder liability is pretty low. We note that PCG conveyed a similar message. While this may very well be the case, management acknowledged that it may still take a few more years of benign wildfire seasons for investors, ratings agencies and even insurers to fully recognize the progress that has been made.

Attractive Core Story That Is (Appropriately?) Overshadowed By Wildfire Risk. Excluding the wildfire risk, the underlying EIX story remains attractive with a long runway of transmission and distribution as well as renewable/storage investments needed to support the state's goal to de-carbonize the broad economy. CA regulators have generally been supportive of utility efforts over the years and the framework offers a plethora of cost recovery mechanisms that enable the state's utilities to earn at or above authorized levels. Even the timeliness of CPUC decisions may be improving under President Batjer. EIX's current plan results in a 6.5-7.5% rate base CAGR. Gating factors include the ability to simply execute on all of the work as well as maintain affordability for ratepayers by trying to keep average annual rate increases at or below inflation. Although the average electric bill in CA is roughly 30% below the national average and EIX's bills are roughly 30% lower than in-state peers, O&M efficiency efforts remain a priority.

Emera Inc. (EMA/Equal Weight/$56.24) (Kalton)

Lots Going in FL. Tampa Electric, along with NEE's & DUK's FL electric utilities, are gearing up for base rate filings in 1H'21 for new rates beginning Jan '22. While we consider the FPSC to be a highly constructive regulatory body, rate cases – particularly in the midst of a weak economy – always create a little bit of uncertainty. With that in mind, we view Peoples Gas recent base rate settlement to be a positive date point. Key elements include allowed ROE of 9.9% with an 8.9-11.0% range. This compares with Tampa Electric's current ROE range of 9.25-11.25% - there is an argument to be made that electric

utilities should be awarded a premium ROE to gas LDCs given greater technology risk. Separately, Tampa Electric's growth runway remains robust driven by renewables and reliability spend under the new Storm Protection Plan. On the solar front, Tampa Electric is well into the first 600 MW of planned solar and has an additional 600 MW plus about 30 MW of battery storage planned by '23. Even with these additions, renewables will only represent 12% of Tampa Electric's power supply (natural gas makes up the high majority of the rest). EMA continues to evaluate the optimal resource mix going forward but the full expectation is that solar will grow meaningfully from the 12% level.

News from the North. In late September, Canada Prime Minister Justin Trudeau's Throne Speech (think State of the Union) addressed power transformation and, in particular, the Atlantic Loop transmission project. The Atlantic Loop would bring excess hydro and thermal power from Quebec and New Brunswick, respectively, to Nova Scotia and Newfoundland. If completed, the project would allow Nova Scotia to accelerate the planned retirement of coal generation from 2040 to 2030 (consistent with Canada's target). As a major transmission project that spans multiple regions, Atlantic Loop faces plenty of challenges (including cost allocation). That being said, it also represents a potential meaningful investment opportunity for EMA. Stay tuned!

Entergy Corp. (ETR/Overweight) ($109.83)

Regulatory Updates. ETR's mgmt. team has been making the rounds quite a bit recently between the late September Investor Day, a number of fireside chats in October and the Q3 earnings call. So, we used our EEI meeting to catch up on a few recent developments in what has become a surprisingly straightforward and, in our view, highly compelling rate base growth story. On the regulatory front, ETR recently reached a partial settlement in E-AR's annual FRP filing – the separate request to extend the FRP has a 12/4/20 settlement deadline. In addition, E-LA recently filed a request to extend the company's FRP by three years (through '23) under largely the same terms as the existing FRP (ROE of 9.2%-10.4%). One difference to E-LA's FRP is a proposed distribution recovery mechanism for annual investment in excess of $100mm. Mgmt. stressed that they have a long track record of achieving settlement agreements and we did not get the sense that there were any meaningful roadblocks to prevent settlements in AR & LA (LA is very early in the process). Switching to the pending SERI case at the FERC. ETR does not expect likely commissioner changes at FERC under a Biden administration to have an impact on the resolution (positive or negative). Mgmt. thinks we could gain clarity on the ROE/equity ratio in 1H'21 (already taken into account in ETR's EPS guidance) but the timing of resolution on the broader policy question around uncertain tax positions remains unclear. While mgmt. remains of the opinion that they have a strong argument, should the FERC adopt the ALJ recommendation it presents a $0.15-0.20, or 2-3%, risk to annual EPS power before potential mitigation efforts.

Essential Utilities (WTRG/Overweight/$46.37) (Reeder)

DELCORA Discussion. We devoted a good deal of time to the pending DELCORA transaction as we believe the current share price does not, perhaps appropriately, reflect the considerable long-term benefits from the deal including the meaningful capex needs that fall beyond the current 5-year forecast as well as the likely substantial wastewater tuck-in deals that could transpire in the area. We had three main takeaways. (1) Investors should not rule out the prospects for a settlement in the legal challenge and perhaps optimism in this regard is in part attributable to the confidence that management has conveyed regarding being able to close the deal around the end of Q1'21. (2) Management is pretty comfortable with the PaPUC approval process based on the concerns expressed by the intervening parties as well as previous experience with FMV deal approval in the state. (3) Assuming 1H'21 closure, DELCORA will start earning its full keep in '22 as it will be incorporated in the next PA water/wastewater rate case filing.

Other Notables. Next PA Water Rate Case. Aqua Pennsylvania is likely to file for new rates during 2H'21 with the new rates effective perhaps late 1H'22. Management continues to think PA water rate cases will occur at a 3-year cadence going forward. M&A Strategy. WTRG continues to be focused on bringing other water/wastewater tuck-in deals to bear, including in states beyond PA and IL. OH perhaps offers the most near-term opportunity out of the "new" states. The deal pipeline is robust and water/wastewater tuck-ins are definitely the focus as the company looks to continue to capitalize on the somewhat accelerated pace of municipal deal activity/interest in the sector. Management also reiterated a low (to no?) likelihood of doing another gas deal in the near-term. Guidance Refresh. Finally, the guidance refresh could come as early as January (before the YE2020 call in late February) and is expected to include not only '21 EPS but also refreshes to the 3-year EPS CAGR and capex outlooks.

Evergy, Inc. (EVRG/Overweight/$57.30) (Akers)

Fake News. EVRG issued a statement mid-EEI confirming that there has been no change in strategic direction since the decision to pursue the Sustainability Transformation Plan (STP) and that there is no outstanding offer or bid for the company. That followed a Reuters report that NEE made an offer in the mid-$60s and a statement from Elliott that EVRG should reengage with NEE. For its part, NEE suggested investors not believe everything that shows up in print. All things considered, there's no reason to think there is merit to the Reuters report at this point.

Path Ahead. Mgmt. is focused on executing the STP with a focus on a modern T&D system and kick-starting the ESG aspect of the story, which includes the de-carbonization of the generation fleet. The plan will require supportive regulation, which is a key consideration in the CEO selection process (someone that understands the importance of having strong regulatory relationships) – CEO decision still expected by YE. The cost cutting initiative is also a key component of the story including its role in mitigating customer rate increases. Shifting to capex, we were encouraged to hear that the ~$700mm of renewable (solar) capex in the plan is not dependent on having securitization in place. We look to the 2021 IRP filings for additional insight into the generation outlook.

Eversource Energy (ES/Overweight/$94.42) (Kalton)

CapEx Drivers. We expect ES's upcoming capex refresh in conjunction with Q4 earnings will be more of the same – higher and supportive of a 5-7% EPS CAGR from the base business (ex-offshore wind). ES has already noted a few things that could impact the plan such as (1) the inclusion of Eversource Gas Company of MA (Columbia Gas), which we think could be additive to ES's rate base CAGR, (2) electric transmission including new reliability projects in southeastern MA totaling $175mm and (3) new MA solar legislation that, if passed (likely), would allow NSTAR Electric to develop an additional 230 MW of solar (~$400mm opportunity). It remains unclear whether ES will have clarity on the CT AMI program in time to include it in the refresh. In addition, mgmt. remains optimistic that the MA Grid Mod Plan (2022-2024) will be supportive of AMI. We think the potential CT & MA AMI programs represent a ~1B investment opportunity over a 5-7 year period.

Other Tidbits. (1) Offshore Wind – despite (not unexpected) permitting delays, ES remains bullish on the company's offshore wind program noting that any negative impact of the delays on returns should be mitigated or offset by the positive impact of being able to use larger turbines along with favorable vessel developments afforded by the extra time. In addition, mgmt. thinks President-elect Biden's administration could help speed the process up at BOEM. ES/Ørsted are one of the three bidders participating in NY's offshore wind solicitation for up to 2,500 MW of capacity (a decision is expected by YE'20). While the companies' award in the 1st auction (the 880 MW Sunrise project) bodes well for pending auction, mgmt. emphasized bidding discipline considering there are plenty of other RFPs upcoming in the region (RI, MA, NY). (2) Connecticut – following the public/political outcry to ES's performance in the immediate aftermath of Isaias, it appears that cooler heads are prevailing. PURA's PBR docket will sequence in mid '21 and ES welcomes the opportunity to work under a PBR scheme. ES is also working to insure better storm response with a focus on outage duration and customer communication.

Exelon Corp. (EXC/Overweight/$43.84) (Kalton)

All About the Breakup. EXC's recent proclamation that the company is in fact in the early stages of evaluating separating ExGen from the regulated utility operations took center stage at the company's EEI meetings. We entered the conversation somewhat skeptical that EXC would go down the break-up path nearer-term given our base assumption that IL will pass constructive nuclear-related legislation in the Spring '21 session and that, by doing so, it might prove diplomatically difficult for EXC to immediately turn around and effectuate a spin (or sale). We exited the conversation less skeptical as mgmt. downplayed – to some degree – potential policymaker resistance. In our view, there is a clear industrial logic to separating the businesses (investors prefer pure play regulated utilities, the separated companies will likely have better strategic flexibility, etc.). In addition, once the genie is out of the bottle it is hard to put back. Even though mgmt. was careful to caveat the evaluation process – noting the unique complexities of separating the companies – once the notion is put out into the world the share price embeds an expectation.

IL Clean Energy Update. EXC indicated that there was strong momentum for clean energy legislation heading into the Spring '21 session and noted that, thus far, Gov. Pritzker's carbon price proposal has not seemed to gain much traction. Instead, it sounds like either the Fixed Resource Requirement (FRR) option could still be in play and/or likely changes to the MOPR under a soon-to-be Democrat regime at FERC could provide the Illinois legislature with additional tools to support nuclear. While IL clean energy

legislation conjures up images of Lucy pulling the football away from Charlie Brown, we remain of the strong opinion that the legislature will take the necessary action to keep the state's nuclear fleet operational.

FirstEnergy Corp. (FE/Overweight/$29.79) (Kalton)

A Tough Road Ahead. This was not an easy EEI for FE's mgmt. team coming on the heels of former CEO Chuck Jones' recent termination for code of ethics violations as part of an ongoing internal investigation into FE's potential involvement in the House Bill (HB) 6 bribery scandal. In addition, it sounds like it could be some time before we get clarity on both the pending FBI investigation and FE's internal investigation (mgmt. hoped to have further updates on the internal investigation by the Q4'20 earnings release in early '21). Under this backdrop, we thought Acting CEO Steve Strah did a commendable job in our meeting and came across as very direct and authentic in discussing the serious issues confronting FE. That being said, regaining the trust of FE's constituents (regulators, customers, investors) will not be an easy task and it remains an open question as to whether or not Mr. Strah will be able to pull it off given his lengthy tenure within the company. We also remain mindful that the investigations are ongoing and it is far from clear to what extent FE was involved in the HB 6 scheme – although, Mr. Jones' termination along with several other recent executive terminations and departures from the firm point to some level of wrongdoing.

OH ROEs. FE provided a bit more color on the age-old question of the OH utilities' earned ROE. Per the SEET test (in legislation), FE is allowed to use book equity in the ROE calculation (FE's book equity is higher than equity rate base due to the inclusion of $2.2B of goodwill related to an acquisition in the 1990s). This, along with some other adjustments, helps explain why FE's SEET ROE always results in a lower ROE than what the rate base math suggests. FE plans to provide even more detail in conjunction with the Q4 earnings release. Keep in mind, the OH utilities' current ESP runs through 5/31/24.

Hawaiian Electric Industries (HE/Underweight/$37.05) (Reeder)

Solid Footing Despite COVID. Despite the challenges presented by COVID, particularly in HI where tourism is essentially the lifeblood of the economy, HE is in pretty solid shape and remains focused on helping the state reach the long-term renewables and decarbonization goals. The utility benefits from decoupled rates and COVID expense deferral accounting. The bank's conservative philosophy and strong starting position has allowed it to "bend but not break" under the challenges of COVID. As such, there remains no need for incremental equity at the holding company nor a need for the holding company to invest any capital into the bank, 2021 refinancing needs have been prefunded and HE is committed to maintaining an investment grade structure. As for the dividend, management does not foresee any risk to the current level and reiterated an intent to grow it in-line with earnings over the long-term while maintaining a payout ratio that is commensurate with peers (60-70%).

Here Comes The Sun? The bank's low cost of funds and ability to offset some of the loan loss provision spike with strong mortgage re-financing activities and opportunistic securities sales have kept the bank safely profitable. And management's recent comments regarding the performance of the loan portfolio and the potential for underlying economic conditions to improve as the state recently started re-opening its doors to tourists give reason to believe the worse of the bank could be behind it. While businesses in HI are struggling, customers and the communities served have been resilient, the bank is staying very close to their customers and the high asset quality in the state provide a safeguard. Management reiterated a belief that the bank is well provisioned after Q3 and that the provision is determined based on forward looking information. As such, if tourism gradually returns, another widespread outbreak of COVID is avoided in the coming months (no new shutdowns) and an effective vaccine becomes widely available in '21, it is possible that a good portion of the provision recorded in 2020 could reverse as the economy improves. 76% of deferred loans have already returned to payment and, typically, if there are 6 months of good performance, the loans are eligible to be upgraded and the associated provision reversed.

PBR Me ASAP? The utility continues to believe the transition to a 5-year Performance Based Ratemaking (PBR) framework at some point in '21 will be a net positive in terms of ability to earn close to the allowed ROE. Once implemented, there may be only 30-40 bps of structural regulatory lag remaining. That said, while there seems to be many areas of consensus that have developed amongst parties throughout the PBR proceeding, the devil will be in the details ultimately approved by the commission particularly as they relate to things like how the annual revenue adjustment mechanism works, what the consumer dividend might be and the type and magnitude (collectively up to 100-200 bps of ROE?) of the new performance incentive mechanisms (PIMs). Execution will be critical which also requires cost efficiency improvements, including delivering on the committed $25M of savings by 2022.

IDACORP, Inc. (IDA/Equal Weight/$94.80) (Akers)

Same (Good) Story Near-Term. Mgmt. continues to see strong growth in the Idaho Power Company (IPC) service territory driven by in-migration from surrounding states along with new large load customers. Combined with a strong cost containment efforts, low borrowing costs and creative regulatory solutions, this has allowed IPC to stay out of rate cases while managing to earn reasonable ROEs and deliver on financial targets.

Rate Base Growth Opportunities Brewing Long-Term. Over time, customer growth and coal retirements will drive incremental resource needs. There's also the opportunity for IDA to take over BPA's stake in the Boardman-to-Hemingway (B2H) project and, possibly, to offer a green tariffs that could lead to renewable ownership opportunities over time. Lastly, IDA has been clear that once the new Hells Canyon license is issued (2022 or later), that will result in higher capital and operating expenses. While some of these items could be handled via regulatory solutions (rider-type treatment), the bigger items may require a full vetting in a rate case.

MDU Resources Group, Inc. (MDU/Equal Weight/$24.99) (Akers)

Strategic Update. When asked about the current trend toward pure play models in the utility sector, mgmt. highlighted (1) MDU's general focus on infrastructure, which spans electric/gas utilities, pipelines and construction and (2) a successful track record since divesting the E&P asset. On the M&A front, construction activity has slowed but the company remains active in the pursuit of acquisitions. Mgmt. is also open to adding scale at the regulated utilities including LDCs so long as it makes economic sense (accretive, credit supportive, cost and/or capex levers, etc.). Of note, S&P already raised the FFO/Debt threshold to 22% from 15% due to the non-regulated EBITDA contribution so while utility acquisitions would help the business risk profile, MDU is comfortable with the revised thresholds and, in fact, has a healthy cushion on FFO/Debt.

Construction. Mgmt. disclosed a ~50/50 breakdown between aggregates and vertically integrated activities (hulling, converting to ready-mix, delivering, laying, etc.) within the Materials segment; this is more in-line with peers Summit and Granite vs. pure plays Vulcan and Martin Marietta. Regarding the decline in backlog reported in Q3'20, the company did not appear overly concerned and pointed to the Q1'21 bidding season as the next key data point. Positive drivers include the extension of the FAST Act budget and favorable housing trends. Shifting to Services, mgmt. has been encouraged by the strong performance through the pandemic. While new hospitality projects in Vegas could slowdown, there is line of sight into 2021 from existing projects and, more broadly, MDU is seeing strong growth in the high tech sector, chip manufacturing and data centers along with healthy electric T&D spending trends.

Pipeline. Mgmt. highlighted the largely take-or-pay nature of the pipeline operations and noted that gas volumes are bouncing back in the Bakken (~85% pre-pandemic levels). The company expressed confidence that the revised agreements with shippers on the North Bakken Expansion project are firm and that the project remains on track to secure FERC approval and meet the late '21 in-service target. When asked about threats from de-carbonization, mgmt. expressed skepticism that natural gas can be reasonably replaced on a btu equivalent basis and highlighted gas as a key backstop for renewables.

NextEra Energy (NEE/Overweight/$77.54) (Kalton)

Chasing Our Tails. During EEI, Reuters reported that NEE had made an offer to acquire EVRG for $66/sh. As the story evolved, it became clear that the bid was likely made many months ago while EVRG was in the midst of a strategic evaluation (ultimately, mgmt. and the Board decided not to pursue a sale of the company). For its part, NEE's mgmt. simply indicated that investors should not believe everything they read and intimated that there could be ulterior motives behind the reports. Does NEE remain interested in regulated M&A? Yes, but per our EEI conversation it remains very much a "want" vs. a "need" and the company will only move forward if a transaction checks all the boxes (including EPS accretion factoring in the balance sheet). Looking ahead to '21, the Santee Cooper privatization opportunity in SC remains a possibility as the legislature is expected to take up the issue again in the general session (typically runs through May). Recall, NEE's bid was deemed to be the best option should the legislature decide to sell Santee Cooper. While we tend to think a Santee Cooper privatization is unlikely, it is worth paying attention to heading into '21. We continue to think an acquisition could be immediately 3%+ accretive to EPS and up to 5% within a few years.

NEER is in the Cat Bird Seat. We spent much of our time discussing NEER's competitive advantages along with the overall size of the renewables pie. We always want to remain mindful of the risk of intensifying competition in the renewables arena as energy players increasingly look towards wind & solar

as growth avenues. That being said, we find ourselves agreeing with NEER President John Ketchum in that the company has built such a competitive moat that it will be difficult for newcomers to enter the space and effectively compete. Developing renewables is not as easy as simply buying some equipment and setting up a wind or solar farm. There are all kinds of considerations related to optimal sites, access to transmission, technical expertise, etc. that NEER has spent decades perfecting. Not to mention NEE enjoys enormous scale benefits related to vendor relationships, cost of capital, etc. As for the size of the market – mgmt. continues to believe EIA's projection for 30% wind/solar market share by 2030 as a percent of U.S. power supply (vs. ~10% currently) will prove to be conservative. And green hydrogen has the potential to materially accelerate renewables development looking out beyond '30 – it is clear that NEE sees a lot of potential for hydrogen and we expect (small) announcements on this front will pick up steam in the coming months and years.

NiSource Inc. (NI/Overweight/$24.64) (Akers)

Sensitive to Financing Concerns. No change to the financing plans laid out at the analyst day, but mgmt. was very responsive to concerns on dilution and the equity overhang. We look to the 2021 financing including $600-1,000mm of equity-rich securities (sounds like leaning toward convertibles) as the first major data point informing 2022-2023 block equity needs (currently $500-700mm). Mgmt. also reiterated an openness to portfolio optimization (asset sales) if it is in the best interest of shareholders. We expect the company will take some time to evaluate options and we look to CNP's upcoming LDC sales as a directional data point on gas utility valuations, which could be instructive for NI (and the rest of the combos/LDCs). Separately, we note that NI's financing plans do not include the ongoing $200-300mm of ATM equity needs after 2023 as investments – including the renewable program – are recognized in rates and generate cash.

Perspective on Gas. Mgmt. opined that the valuation de-rating of the LDCs is overdone given both strong demand for the product and readily available low cost supply. The company also sees strong policy support in its remaining service territories and highlighted the high energy content requirements of winter peak energy needs. NI believes it is not a question of whether the distribution pipe system will be used and useful in the future, but rather what will be flowing through the pipes (RNG, hydrogen, etc.).

NorthWestern Corp. (NWE/Overweight/$59.30) (Reeder)

'21 Guidance. Management offered preliminary '21 EPS guidance of $3.40-3.60 but will likely tighten the range to the typical $0.15 variance with the YE'20 report in February. We got the sense the extra $0.05 in the preliminary range was subtracted from what would have otherwise been the bottom end if not for COVID-related uncertainties. The midpoint of the '21 range is 4% above the midpoint of the revised '20 range ($3.30-3.45) but is overall consistent with the original '20 range ($3.45-3.60). It reflects a 0.7-1.0M increase in the diluted average shares out from '20, continued improvement in operating expense levels and decoupling is expected to be implemented at the MT electric utility in mid-'21. Lastly, NWE indicated an expectation that the dividend will be at the upper end of the 60-70% targeted payout ratio – if at 70% while continuing the recent $0.10 annual dividend increase trend, it implies '21 EPS of $3.57.

Capex Budget Increased. NWE rolled out a $2.1B investment plan over the 2021-25 period. The budget represents a $300M increase over the previous 5-year plan and is distributed fairly evenly across the states and utilities (electric vs. gas) relative to each's size. Management characterized the projects as mostly small and relatively low execution risk. The budget is driven by gas and electric transmission and distribution work to accommodate growth across the systems, deal with the shutdown of fossil resources and comply with regulations as well as things like hydro generation facility upgrades and technology (including automated metering infrastructure). The $400M+/year capital plan puts NWE at the midpoint of the 3-6% EPS CAGR target and management noted the growth could be somewhat lumpy based on rate case timing. In addition, it sounds like external equity will be needed fairly regularly to fund the budget and maintain an FFO/Debt ratio in the 14-15% range.

MT Generation Still Upside – And Growing? NWE has bid several projects into the pending 285 MW RFP and reiterated that the $200M capex bogey that they have talked about is based on a level of comfort of what they might win – winning all would be more than $200M. The 3rd party administrator has yet to notify NWE that any of their projects have been eliminated from consideration and management remains confident that their projects are well positioned given the RFP specifications around long duration, flexible capacity. If a NWE project wins, the MT pre-approval process allows AFUDC to be earned as the capital is deployed but then that turns into a cash return with a project-specific ROE once it enters service. The recent termination of the Puget deal (for an increased stake in Colstrip) restores the full 725 MW capacity hole that NWE intends to ultimately fill through multiple RFPs. And the risk of the Colstrip facility shutting down this decade (vs. NWE's 2043 planning assumption) seems elevated, perhaps even more so by

Talen's announcement this week to shut down coal capacity in favor of a more ESG-friendly strategy, which has the potential to add another 222 MW deficit to NWE's MT portfolio.

MT Regulatory Environment. Republicans swept all state offices and the three Montana Public Service Commission (MPSC) elections. While party affiliation has never been a guarantee of constructiveness in MT, we are hopeful that the new MPSC will continue what seemed to be a gradual improvement in the challenging regulatory environment over the last 2 years prior to more recent adverse decisions around COVID expense recovery as well as Colstrip replacement power costs. We also believe it bodes well for the recognition that natural gas needs to play a role in the new generation capacity picture versus some of the Democratic candidates that were more fervent renewables supporters. We were somewhat concerned by the MPSC comments earlier this year around NWE's supply plan perhaps being overly reliant on gas – particularly since we believe NWE's self-build advantages are likely for gas-fired generation.

OGE Energy Corp. (OGE/Overweight/$33.95) (Akers)

Feeling Good. CEO Sean Trauschke struck an optimistic tone on the utility operations, particularly on sales trends. Commercial load flipped to positive in September (vs. year ago period) and mgmt. expects some of the uptick in residential will be sustainable based on work-from-home trends. The company is also bullish on industrial activity and expects Public Authority sales (mostly schools) will pick-up as students return to the classroom. Mgmt. is hopeful that the pre-COVID momentum toward customer growth >1% will return. On the regulatory front, OG&E is focused on executing manageable, straightforward proceedings with a continued focus on customer bills. Lastly, the company plans to file an IRP by October 2021, which could shed light on resource needs. We do not expect any major project revelations, but rather a series of smaller investments (plant conversions to gas and solar additions at the distribution level) along with EE and DR. Overall, things seem to be moving in a positive direction.

Strategic Comments. Mgmt. continues to play its hand close to the vest as it relates to ENBL. The team fully acknowledges the public market dynamics (negative sentiment toward midstream, preference for pure plays) and believes the midstream exposure has overshadowed the utility story. When it comes to potentially selling/swapping into a bigger MLP, OGE considers the aforementioned market/valuation dynamics along with cash flow and credit implications. Separately, when asked about the company's interest in acquiring an LDC (in the context of CNP potentially selling an LDC or two), mgmt. confirmed that gas utilities are not on the company's list.

PG&E Corporation (PCG/Equal Weight/$10.71) (Kalton)

Wildfires Still Top of Mind. First, the lack of a new Safety Certificate from the CPUC remains a little bit disconcerting. That being said, PCG stressed that the prior safety certificate remains in effect until a new one is issued and it is not necessarily uncommon that the issuance has slipped beyond 90 days. In addition, thus far there have been no communications from the CPUC to suggest any major issues with PCG's request. Without a valid Safety Certificate PCG is not afforded the protections of the liability cap under AB1054 (limits wildfire liability to 20% of electric T&D equity rate base, or ~$3B currently). Safety Certificate aside, PCG highlighted substantial progress on wildfire risk mitigation efforts and improvements in the PSPS program vs. '19. Combined with improved containment/suppression strategies, the risk of catastrophic wildfires caused by utility-owned equipment appears to be declining. That being said, we think it may take a few years of benign activity to substantially improve investor confidence. Not surprisingly, mgmt. indicated that the legislature still has little appetite to address the inverse condemnation (IC) doctrine. While AB1054 provides substantial protections, the state's electric utilities still face significant risk relative to utilities in other states as a result of IC. On the capex front, there is no shortage of investment needs as PCG deploys capital to improve grid resiliency, mitigate wildfire risk and support CA's ambitious GHG emission goals. Last, it sounds the like the search for a new CEO is winding down with an announcement expected by YE'20.

Pinnacle West Capital Corp. (PNW/Overweight/$89.59) (Akers)

ACC Profile. The 2020 ACC election resulted in Republican Lea Márquez Peterson retaining her seat with the other two open seats to be filled by Republican Jim O'Connor and Democrat Anna Tovar. It appears that three of the five Commissioners are supportive of a de-carbonization agenda (Peterson, Tovar and sitting Commissioner Kennedy), which aligns with PNW's de-carbonization plan. Favorably, this agenda would appear to conflict with sitting Commissioner (and possible future Chairman) Olson's desire to pursue deregulation. While we reserve judgement until policy discussions are underway and, more so, rate case decisions are issued, our initial view is favorable given both a pro-clean energy and Republican majority. Beyond the ACC make-up, we are encouraged by PNW's focus on improving the company's

position in the state via consensus-building and improved customer service/experience. We think improved regulatory relationships and outcomes would address a key investor concern and allow greater focus on the clean energy growth story, strong balance sheet, effective cost management and strong customer growth.

Rate Case Update. APS filed rebuttal testimony on 11/6 with three key updates: (1) a $15mm reduction to the $184mm rate request reflecting a reduction in the ROE request (to 10.0% from 10.15%), a lower fair value increment (to 0.8% from 1%) and updates to the fuel rates; (2) a proposed Advanced Energy Mechanism (AEM), which would provide rider recovery for clean energy investments and incorporate the DSM and LFCR updates (simplification); and (3) a Coal Community Transition proposal, which is a comprehensive plan to address the Four Corners coal retirement along with various economic development initiatives for the Navajo Nation. It is our understanding that the Navajo Nation is supportive of the coal transition plan along with the AEM. While it is yet to be seen whether other stakeholders support the AEM (key to mitigating regulatory lag and extending the time between rate case filings), we view the updated testimony as an incrementally positive step.

PNM Resources (PNM/Equal Weight/$49.09) (Reeder)

AGR Deal Update. It was not for a lack of effort but we were unable to squeeze out much additional insight regarding how the Avangrid deal (announced 10/21) came about. Management reiterated that a very strategic type of approach was taken to find the right strategic partner for PNM and the communities served. Therefore it was not solely about the price offered. More details will be included in the proxy which is expected to be filed around Christmas. Management believes the prospects of receiving what PNM would deem to be a superior proposal are quite low (again, not just about price) and pretty much shut the door to the prospects of a financial suitor emerging (as was the case in the recent acquisition of PNM's neighbor El Paso Electric) given the need for an acquirer to be strategically aligned. The response to the deal announcement has been positive in NM (governor, legislature, environmental community, etc.) based on AGR's commitment to renewables and the environment and management noted that NM regulators have never turned down a merger application. Both NM and TX are net benefit states and generally those conditions are satisfied by way of rate credits which AGR/PNM stand prepared to offer. Merger approval applications will likely be filed by the end of the month.

Other Business Updates. Constitutional Amendment Passage. The NM regulatory body will be transition to a 3-person appointed commission in 2023 as the amendment passed. Management believes it will not only improve the predictability/stability of the regulatory decisions in the state but also the quality. Therefore, NM has the potential to improve from the commonly held investor notion that the regulatory environment is below average. Four Corners Deal. Management believes NM regulators will be hard pressed to turn down the recently announced deal for PNM to exit Four Corners early given the customer savings associated with it. EPS Power. No real changes in the EPS power of the company looking forward. 2021 EPS power is $2.30-2.40 however PNM will be rolling out guidance in December taking into consideration the latest thoughts around COVID, cost savings and the lack of rate relief or decoupling (both of which were anticipated at one point in '20 to be of help to '21 EPS). Beyond '21, PNM will be deferring to AGR to communicate the growth.

Portland General Electric Company (POR/Equal Weight/$44.57) (Akers)

Mgmt. Bullish on Growth. CFO Jim Lobdell highlighted that growth in POR's service territory has proven resilient with healthy in-migration trends, which may be further helped by COVID as people have more flexibility to work from desirable locations, and continued growth in high tech. This led the company to bring back capex on the Q3 update that was previously removed from the plan. The company still expects 1% sales growth long-term, which could be bolstered by electrification efforts (transportation, but also considering new premise incentives for electric heating, etc.). Separately, Mr. Lobdell spoke of a continued focus on cost controls including greater use of technology and coal unit retirements among a slew of other efforts.

In addition to service territory growth and expense controls, the company's 4-6% EPS growth target is driven by investment in aging infrastructure along with the Wheatridge Renewable Energy Facility. Looking ahead, there could be additional opportunities for generation ownership (upside to the plan) related to one or two RFPs planned for 1H'21 to procure 150 average MW (~450 MW nameplate) of renewables and 700 MW of capacity. Lastly, discussions are ongoing in phase 2 of the Green Future program, which could potentially include utility ownership (TBD).

Regulatory & Other Updates. There was no new information on wildfires (still no evidence that POR's equipment ignited any fires) and the trading loss (investigation ongoing). On the regulatory front, mgmt.

continues to evaluate the timing of the next rate case and highlighted positive data points on the COVID deferral and wildfire deferral, which was approved in ~30 days. While the company still sees 85-90 bps of structural lag related to unrecoverable expenses, there are other areas which could be addressed, such as the PCAM (tightening the deadbands?), storm balancing accounts and the decoupling mechanism, which is set to expire after 2022.

PPL Corporation (PPL/Equal Weight/$29.41) (Kalton)

U.K. Sale & Go-Forward Strategy. The sale of the U.K. utilities continues to progress and mgmt. remains encouraged by the level of interest. An upcoming data point regarding U.K. decarbonization goals will provide parties with guidance into the expected level of long-term investment in the electric distribution systems (arguably a more important driver of value than near-term allowed returns). Timing remains 1H'21 for both the transaction announcement and potential completion given typically quick regulatory approval processes in the U.K. (1-3 months). Post sale, mgmt. is keeping their options open with regard to use of proceeds with share repurchases, regulated M&A (preference towards electric) and additional contracted renewables investment (via Safari Energy) all possibilities.

Kentucky Update. PPL recently filed a notice of intention to file for base rate relief for the KY utilities starting 7/1/21. The filing will include a proposed sur-credit that will be used to mitigate the rate impact on customers via the use of regulatory liabilities. Separately, we spent a good deal of time discussing upside capex opportunities including AMI (a ~$300mm program that PPL intends to revisit with the Kentucky PSC) and generation transformation. The KY utilities own 3,800 MW of coal-fired generation that was developed between 1971-1984 and could be ripe for retirement over the next 10-20 years. PPL characterized the PSC as being most concerned about cost and reliability and is not wedded to fuel type when considering asset replacement proposals. Mgmt. further noted that the economic proposition for solar/battery storage is not quite there (yet).

Public Service Enterprise Group Inc. (PEG/Overweight/$60.88) (Kalton)

Lots to Talk About. (1) Non-nuclear generation sale – mgmt. characterized initial interest in the proposed sale of the fossil fuel generation fleet and solar portfolio as healthy (private equity interest). The solar portfolio is expected to be put up for sale this month with the fossil fuel plants to follow in December. Bids are due in Q1'21 with a sale expected to be announced in mid '21. (2) CEF Filings – mgmt. is optimistic that the New Jersey BPU will bless the $600mm AMI proposal. Conversely, it is unclear to what extent the BPU wants regulated utility involvement in the proposed EV ($300mm) and battery storage ($100mm) programs. Decisions are expected in Q1'21. (3) Stimulus Investment – PSE&G is engaged in early discussions with the BPU Staff around a potential acceleration of Gas System Modernization Program spend and/or electric reliability spend. Should the talks advance, we could see a formal filing within the next 3-6 months. (4) Transmission ROE Discussions – it sounds like the parties (PSE&G, the BPU Staff and the Consumer Advocate) despite being close are currently at a stalemate. From here, either the stalemate breaks or the Staff/Consumer Advocate could launch a formal challenge at FERC (likely a multi-year process). (5) Offshore Wind – PEG expects to make a decision as to whether or not to take up to a 25% interest in Ørsted's 1,100 MW Ocean Wind project by the end of November. We continue to think it is likely that PEG participates. (6) Nuclear – not much new here. PEG has made it clear that the $10/MWh ZEC payment will not be sufficient to keep the company's nuclear units operational longer-term. We expect more clarity on this issue by mid/late '21.

Sempra Energy (SRE/Equal Weight/$133.64) (Akers)

Strategic Capital & LNG. Based on the Q3 call and mgmt. comments at EEI, it appears likely to us that SRE is looking to sell an interest in the LNG portfolio. This would serve two complementary purposes: one, to get an attractive valuation marker for the LNG business; and two, to keep the business mix more heavily weighted toward the regulated utility operations (improves perceived risk profile, which is important to both investors and rating agencies). We do not think a spin of the LNG operations is timely as it provides a competitive advantage to operate under the SRE umbrella. Shifting to Mexico, mgmt. remains bullish long-term while acknowledging challenges presented by the current administration. The company views ECA as a critical asset in Mexico and expressed confidence that the export permit will be received this month with FID by year-end. More broadly, the tone on LNG was constructive as mgmt. indicated that conversations with potential off-takers have picked up and pricing has improved.

Gas in CA. The company expects the friction between SoCalGas and certain environmental interests could continue near-term, but (1) noted that regulatory outcomes have been very supportive of continued investment in the gas infrastructure and (2) expressed confidence that there's a significant long-term role

for the gas LDC infrastructure in a clean energy future (RNG, hydrogen, carbon capture). SoCalGas is making a significant push in RNG and noted that while it appears expensive, costs should be driven down with scale and additional investment (similar to solar and wind in their infancy). We did not get the sense, however, that SRE would look to acquire additional gas utility assets as the company prefers to position the portfolio more directly in alignment with the electrification trend.

Southern Company (SO/Equal Weight/$63.92) (Kalton/Reeder)

The Here and Now. With the finish line nearing on Vogtle Unit 3, it is clear that SO is not taking success for granted. The three risk areas to get to the next major milestone of hot functional testing, in order of increasing importance, are (1) sub-contractor work, (2) bulk electrical work and (3) paperwork – making sure the "as built" condition of the modules conform to the engineering plans so that the requisite ITAACs can be verified by the NRC. If for some reason the inspections, tests, analyses and acceptance criteria (ITAAC) process would uncover the need to submit a license amendment request (LAR), it could potentially take a few weeks to resolve – we believe it is important to note that the NRC is highly supportive of the project as it enters the final stages and has vowed to work expeditiously on their end. That said, management does not believe a LAR is any more likely than some sort of metallurgical condition popping up as the hot functional test ramps up the temperature of the plant components. Overall, management is confident heading into hot functional testing and the overall ability to bring Unit 3 in-service before the end of November '21. And Unit 4 should go better than Unit 3.

Beyond New Nuclear. Assuming the remainder of the new nuclear project goes relatively smoothly, SO is primed to deliver 6%+ EPS growth and this higher growth rate could be fleshed out as part of the YE2020 update. Excluding the "debt only" return penalties imposed by Georgia regulators when the higher price tag and longer schedule had to be recertified, SO has been growing at like 6%. But once both units go online it is projected to add about $200M of net income and generate an additional roughly $800M of cash flow. This should put SO in a position of strength which could include accelerating the dividend growth, upping the capex forecast (assuming rate affordability can be balanced) and/or further improving the credit metrics/rating. In other words, SO could support $8-9B/year of capex without the need to issue equity. A big driver of rate base growth could be early retirement of most of SO's large coal-fired plants and replacing them with renewables and gas as the O&M savings could serve to keep customer bills flat. Embarking on this sort of plan would require the buy-in of AL, GA & MS, including state regulators, and could be propelled forward under a Biden administration with a Republican senate where carbon reduction goals are accelerated.

Growth Outside The Core Regulated Franchises. Three things came up. (1) Renewable deals that meet Southern Power's return hurdles are tough to come by right now. (2) Management did not entirely rule out buying another gas LDC at the right price. (3) SO has clearly been exploring the idea of a synthetic approach to municipal/gov't owned system M&A. SO would lend expertise by operating the system and perhaps even allow access to SO's pool of assets as scale matters in the transition from fossil to zero carbon. This type of approach could overcome the challenge inherent in buying municipal assets including the fact that they are 100% financed with cheap debt and the loss of local ownership.

WEC Energy Group, Inc. (WEC/Equal Weight/$104.43) (Kalton)

Diving Into the '21-25 Capital Plan. Mgmt. provided additional details on the company's '21-25 capital investment plan (called the ESG Progress Plan) – $16.1B plan represents a $1.1B increase from '20-24. The refresh leans more heavily on renewables (25% of the spend) including new regulated solar (800 MW), wind (100 MW) and battery storage (600 MW). The amount of battery storage was a little bit of a surprise to us but mgmt. indicated that the storage integrates nicely into the system. Separately, the contracted renewables bucket (Energy infrastructure) consists of $2.2B of planned investment during the period and incorporates the already announced $400mm Thunderhead project. If WEC executes on the full $2.2B we think Energy Infra's EPS contribution would be ~8% of consolidated EPS in '25, which would still give the company some wiggle room under the 10% threshold (WEC wants to limit non-utility EPS to 10% of total EPS max).

Other Tidbits. (1) Mgmt. indicated that the capital investment plan supports a 5-yr EPS CAGR of just above 6%. Other assumptions underlying this statement include earned ROEs at the allowed levels (little change to allowed ROEs during the period) and equity ratios at the mid-point of the equity ratio ranges of 50-55% for the WI utilities. Optimizing the equity ratio represents a not insignificant EPS opportunity in and of itself. For context, we estimate annual EPS could be $0.10-0.15 higher by '25 if the WI utilities earned the allowed ROEs at a 55% equity layer, which could add 50bps to the 5-yr EPS CAGR. Keep in mind, there is also an opportunity to retain a portion of earnings above the ROE thresholds. Optimizing the WI utilities earnings will depend on a number of factors including future rate case outcomes, sales trends and effective cost management. That being said, the equity ratios provide yet another lever to

help achieve an EPS CAGR toward the upper end of the company's 5-7% goal and/or help offset unforeseen pressures. (2) WEC remains very comfortable with owning gas LDCs and we got the sense they would consider a gas LDC purchase as long as it fit mgmt's famous three criteria: (1) EPS accretive in first full year, (2) credit neutral, and (3) long-term earnings growth prospects consistent with WEC's organic growth. Executive Chairman Gale Klappa suggested that the growth criteria could prove to be an impediment.

Xcel Energy, Inc. (XEL/Equal Weight/$74.69) (Kalton)

CapEx Discussion. Our EEI discussion centered on XEL's recent 5-yr capex refresh for '21-25. As a reminder, the base plan of $22.6B (vs. the '20-24 guidance of $22.0B) results in a rate base CAGR of 6.3% (off the 20E base). In addition, XEL provided a separate analysis including the $1.4B upside related to NSPM's Minnesota Relief & Recovery Proposal consisting of wind repowering ($750mm) and new solar ($650mm). The "incremental" plan would result in a 6.9% rate base CAGR. Mgmt. remains optimistic that the MPUC will approve the spend and noted that the opposition's arguments are consistent with prior arguments in similar proposals (questioning the long-term customer benefits based on NSPM's power price assumptions). Our capex outlook includes the $1.4B of incremental spend. Separately, mgmt. poured cold water on our question as to whether XEL held back other capex from the base plan while NSPM's request is pending – they characterized the base capex plan as fully representing the assessed needs while also pointing out that additional capital tends to come into the plan over time (both traditional capex along with potential PPA buyouts). On the PPA front, mgmt. indicated that while discussions with parties are always ongoing, things tend to heat up around the operating utilities' IRPs.

Hydrogen. We have long viewed XEL as being ahead of the game in terms of long-term system planning and understanding new technology (not to be confused with early adoption as mgmt. carefully considers technology risk and customer rate implications). On that note, mgmt. is evaluating hydrogen as a future fuel source to help bridge the last mile to zero carbon. Our take is that XEL is skeptical that green hydrogen production will be economically attractive and, instead, pointed out that using excess nuclear output from the company's existing nuclear facilities to produce hydrogen could be 1/3 more cost effective. Fun fact: nuclear produced hydrogen is referred to as Purple Hydrogen.

Acronyms

ALJ – Administrative Law Judge
AMI – Advanced Metering Infrastructure
ATM – At the Market
BOEM – Bureau of Ocean Energy Management
BPU – Board of Public Utilities
CCRO – Customer Credit Reinvestment Offset
CEF – Clean Energy Future
CEHE – CenterPoint Energy Houston Electric
COP – Construction and Operations Plan
DR – Demand Response
DSM – Demand-Side Management
ECA – Energía Costa Azul
EE – Energy Efficiency
EIA - Energy Information Administration
ESG – Environmental, Social and Governance
EV – Electric Vehicle
FID – Final Investment Decision
FRP – Formula Rate Plan
FPSC – Florida Public Service Commission
GHG – Greenhouse Gas
IRP – Integrated Resource Plan
LDC – Local Distribution Company
LFCR – Lost Fixed Cost Recovery
LNG – Liquefied Natural Gas
MOPR – Minimum Offer Price Rule
MPUC – Minnesota Public Utilities Commission
MVP – Mountain Valley Pipeline
PBR – Performance Based Ratemaking
PISA – Plant-in-Service Accounting
PPA – Power Purchase Agreement
PURA – Public Utilities Regulatory Authority
REC – Renewable Energy Credit
RFP – Request for Proposals
ZEC – Zero Emission Credit

Required Disclosures

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2020 Utility Symposium Takeaways

Highlighting PEG, WTRG & ATO

Utilities

$	Rating		Price	FY EPS				Price Target	
				2020E		2021E			
Ticker	Curr.	Prior	12/09/20	Curr.	Prior	Curr.	Prior	To	From
Diversified Electric Utilities									
PEG	1	NC	56.89	3.43	NC	3.38	NC	69.00	NC
Natural Gas LDCs									
ATO	1	NC	97.75	4.72A	NCA	5.00	NC	114.00	NC
Water Utilities									
WTRG	1	NC	47.70	1.58	NC	1.65	NC	52.00	47.00

Source: Company data and Wells Fargo Securities, LLC estimates

1= Overweight, 2 = Equal Weight, 3 = Underweight, V = Volatile
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful

- **Summary.** On 12/8 & 12/9, over 35 electric, gas and water utilities participated in virtual investor meetings at the 2020 Virtual Midstream and Utility Symposium. The tone of conversations was quite positive with companies cautiously optimistic on sales growth into 2021 and poised to advance de-carbonization strategies. In the comments below we expand on general industry takeaways and highlight PEG, WTRG (also increase price target) and ATO as timely investment ideas.

- **No Shortage of Investment Opportunities…** Between aging wires and pipes and the push toward de-carbonization, companies touted significant infrastructure investment opportunities with visibility well beyond the 5-year planning horizons. On the electric generation front, a number of utilities are scheduled to file IRPs in 2021 (BKH, CMS, EVRG, NI, OGE, XEL) with most executives pointing to renewables and peaking gas as the most likely resource solutions. In terms of coal retirements, companies generally are not expecting significant pressure from the Biden EPA only because many have already taken steps to accelerate coal retirements. That said, stricter emission regulations could provide greater justification for local stakeholders to accelerate retirements as several companies are still working out the details on recovery of the un-depreciated plant balances with securitization discussions going on in a number of states.
- **…Gating Factor is Customer Rates.** Utilities are always mindful of customer rate pressure, but we sensed a heightened sensitivity in light of COVID-related considerations. Regulators and politicians have pushed back on requested rate increases during the pandemic with the most recent example being the PA ALJ recommendation to deny NI's rate increase along with less overt actions including downward pressure on allowed ROEs (AZ). In response, many utilities are increasing programs to support low income customers and tightening their belts on the O&M front. Should utilities be able to create rate headroom via cost controls, fuel savings (steel for fuel) and, for certain utilities, customer growth, it could support the acceleration of capex and rate base growth.
- **Comments continue on page 2.**

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- **New Technology Roundup.** We continue to sense a greater willingness on the part of the historically risk averse utility sector to embrace new technologies. We think this is being driven by a confluence of factors including (1) real and perceived policy pressure (at the state & federal levels), (2) customer demand for clean energy (both C&I and residential) and (3) the growing influence of ESG investing – is it just us or do company executives sound increasingly apologetic if stated generation resource plans still include coal in 2040? Several utilities indicated the potential to either accelerate or scale-up investments in battery storage (CMS) and EV-related infrastructure (DTE, XEL). And, in a mini eyebrow raising move, on 12/8 NEE acquired eIQ Mobility, a provider of software solutions to help assess fleets for a potential transition to electricity or hydrogen fuel. NEE indicated that the acquisition was part of the ongoing "dip your toes" approach into green hydrogen – and that the technology is still several years away from being a "needle mover" from an earnings standpoint – but the momentum continues to build.
- **M&A.** There was a lot of chatter regarding CNP's recent announcement regarding plans to sell LDCs in AR and OK. Nearby utilities BKH and OGS indicated a general openness to giving the assets a look, but not at valuations in the 1.5-2X rate base range – both expressed skepticism that their bids (if they bid) would prevail and appeared content to see a higher valuation from another party, which could lend support for LDC valuations overall. Northern utilities ALE and WEC did not express an interest in the assets and AQN commented that while they haven't ruled LDC acquisitions out, mgmt. prefers electric and water. SR provided broad comments that the company has been out of the M&A space due to frothy takeout multiples and would re-engage at more reasonable valuations along with cultural and regulatory considerations. While not categorically ruling out M&A, NWE noted they like the current electric/gas mix as well as serving areas where gas is not under attack and therefore cannot imagine moving outside of their Midwest region (but did not specify if AR and OK are in their region). Lastly, SWX expressed an openness to acquisitions, which would bolster the utility portion of the earnings mix, but did not comment specific to CNP's assets. More broadly, we think the need to create rate headroom in order to accelerate de-carbonization strategies could drive strategic combinations that offer scale and synergies.
- **Gas LDCs Strike A Positive Tone.** With the LDC utility business model in the spotlight as the electrification theme looms, we sensed greater comfort among gas executives that key stakeholders are acknowledging the role of gas distribution infrastructure in the pursuit of affordable de-carbonization (even in NJ). Companies also highlighted continued strong demand for LDC service including healthy new customer connect trends and opportunities to build-out the gas system into new areas. Consistent with the Q3 calls, most of the companies are actively exploring RNG opportunities and beginning to research the potential of adding hydrogen to the gas mix (early days). When asked whether RNG/hydrogen will detract from natural gas' affordability argument, executives drew a parallel with renewables in their infancy suggesting there's a need and expectation that the cost curves will be driven down over time. The LDCs also touted energy efficiency programs as a much more cost effective avenue toward de-carbonization.

Featured Picks

- **Public Service Enterprise Group (PEG/Overweight)**
  We like the set up for PEG heading into '21 as the company continues to transition to an appealing clean energy, predominantly regulated utility story (85% of earnings). Potential catalysts include (1) completion of the planned sale of the non-regulated fossil fuel and solar generation assets, which will simplify and "clean" up the story, (2) likely additional regulated capex arising out the CEF filings (Cloud & EV) and a new potential accelerated infrastructure investment program and (3) greater clarity on the long-term earnings profile for the nuclear fleet pending the outcome of an ongoing NJ BPU investigation. In the near-term, mgmt. is quite optimistic that the BPU will bless the $721mm CEF-Energy Cloud (AMI) (an all or nothing proposal) but is a little bit more iffy on the $261mm CEF-EV proposal. Evidentiary hearings on both the Energy Cloud and EV filings have been suspended as parties engage in settlement discussions. Separately, we touched on PEG's recent decision to acquire a 25% ownership interest in Ørsted's Ocean Wind project. While not unexpected, the decision frees up mgmt. to discuss the longer-term offshore wind opportunities that will likely sequence after Ocean Wind. Ørsted has 2,400 MW remaining in the Ocean Wind lease area and PEG/Ørsted jointly own the 1,000 MW Garden State Offshore Energy (GSOE) lease area. Now that PEG has opted into Ocean Wind 1, we fully expect Ørsted/PEG to jointly pursue future solicitations in NJ and the Mid-Atlantic (i.e., MD); this could set up for additional growth opportunities post '25 that will supplement PSE&G's strong rate base growth. As for the initial Ocean Wind stake, PEG will generate a substantial amount of cash upfront by taking the ITC & MACRS tax benefits (PEG has a U.S. tax appetite whereas Ørsted does not). We reiterate our Overweight rating and maintain our $69/sh price target.

- **Essential Utilities (WTRG/Overweight)**
  We came away from our WTRG meeting incrementally more bullish on the name and believe there are potential near-term catalysts to build upon the stock's recent strength. First, CEO Chris Franklin expressed confidence in the ability to get the pending DELCORA deal done and believes the judge may rule by Christmas on Delaware County's two legal challenges – the most important of which is the validity of the asset purchase agreement. Mr. Franklin reiterated that the County's concerns seem to be around the price and use of proceeds as opposed to be against actually selling to WTRG. As we have previously opined, a last minute settlement still cannot be ruled out. We believe the DELCORA deal represents material long-term value given meaningful capex needs that fall beyond the current 5-year forecast as well as the likely substantial wastewater tuck-in deals that could transpire in the area. Second, management believes investors will find the 1/11 guidance event constructive both in terms of the updated 3-year EPS and rate base growth outlook as well as environmental commitments at Peoples. Finally, we talked about the water and wastewater M&A pipeline and there continues to be attractive, sizeable opportunities that not too long ago WTRG would have never thought possible. We reiterate our Overweight rating and increase our 12-18 month price target to $52/share (29X our 22E EPS of $1.78) from $47.

- **Atmos Energy Corporation (ATO/Overweight)**
  ATO is our top pick in the Gas LDC space. We see the opportunity for multiple expansion from the current ~10% premium to gas peers. ATO is not a catalyst rich name, but offers consistent 6-8% EPS growth, a relatively low-risk regulated strategy, a strong balance sheet with well above-average credit metrics, supportive regulatory mechanisms and an excellent track record in our view. ATO also operates in gas-friendly states with ~70% of rate base in TX where we expect to see legislation proposed in 2021 that would prohibit the adoption of local bans on new gas hookups. We think continued execution through 2021 along with improving sentiment toward the LDC group will drive outperformance. We reiterate our Overweight rating and maintain our $114/sh price target.

Acronyms:

ALJ – Administrative Law Judge
AMI – Advanced Metering Infrastructure
BPU – Board of Public Utilities
C&I – Commercial & Industrial
DELCORA – Delaware Country Regional Water Quality Control Authority
EPA – Environmental Protection Agency
ESG – Environmental, Social, Governance
EV – Electric Vehicle
IRP – Integrated Resource Plan
ITC – Investment Tax Credit
LDC – Local Distribution Company
MACRS – Modified Accelerated Cost Recovery System
MW - Megawatt
O&M – Operations & Maintenance
RNG – Renewable Natural Gas

Rating Basis Information:

ATO Thesis: We are attracted to ATO's highly visible growth outlook, pure play regulated gas strategy and strong balance sheet. We do not believe these positive features are adequately reflected in the current share price.

PEG Thesis: We believe PEG shares offer investors an attractive risk/reward proposition. Key features include (1) a premier utility with well-above average rate base & EPS growth prospects, (2) a carbon-free nuclear generation fleet that generates significant FCF and (3) a strong balance sheet, which provides the company with financial flexibility.

WTRG Thesis: Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived and near-term regulatory risk is low as both the water and gas utilities completed rate cases in 2019), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

Price Target Information:

PEG Basis and Risks: Our $69/sh price target is based on a sum-of-the-parts analysis consisting of (1) $60.50/sh for PSE&G/Enterprise/Other (~20.5X our 22E EPS of $2.94) and (2) $8.50/sh for PSEG Power based on a DCF analysis. Risks to our valuation include earnings sensitivity to commodity prices, operational risks, unfavorable regulatory/political developments particularly as it relates to PEG's nuclear fleet.

ATO Basis and Risks: Our price target is based on a P/E multiple analysis (apply a 15-20% premium to the Gas LDC peer group multiple of ~18X on our '22E EPS). Key risks include regulatory risk (primarily in TX), potential pushback to rate increases, risk of gas-related incidents, and fluctuations in the Rider Rev mechanism at APT.

WTRG Basis and Risks: Our $52/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.78. For WTRG's water utility multiple, we ascribe a roughly 5% discount to the 21E multiple we use for AWK (34-34.5X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The roughly 5% discount reflects a modestly lower earnings growth rate (we forecast 6-7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 19X (based on ATO, NWN, OGS & SR) and then apply a 5-10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive PA regulatory framework. Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

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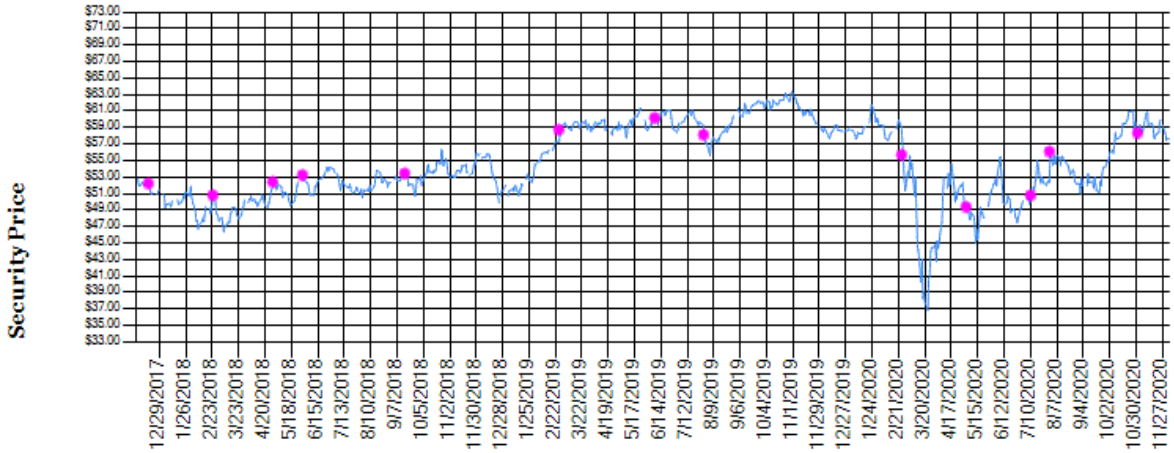
Public Service Enterprise Group Incorporated (PEG) 3-yr. Price Performance



Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
12/4/2017		Kalton				
12/4/2017	NA	1	56	NE	NE	52.89
12/18/2017	52.30	1	59	NE	NE	51.97
2/25/2018	50.53	1	56	NE	NE	50.53
4/30/2018	52.02	1	57	NE	NE	52.15
5/31/2018	52.98	1	63	NE	NE	52.98
9/16/2018	53.27	1	60	NE	NE	53.27
2/27/2019	58.56	1	66	NE	NE	58.56
6/9/2019	60.01	1	72	NE	NE	60.01
7/30/2019	57.87	1	69	NE	NE	57.89
2/26/2020	55.57	1	67	NE	NE	55.57
5/4/2020	49.14	1	57	NE	NE	49.14
7/12/2020	50.59	1	65	NE	NE	50.59
7/31/2020	55.94	1	68	NE	NE	55.94
11/1/2020	58.15	1	69	NE	NE	58.15

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Source: Wells Fargo Securities, LLC estimates and Reuters data

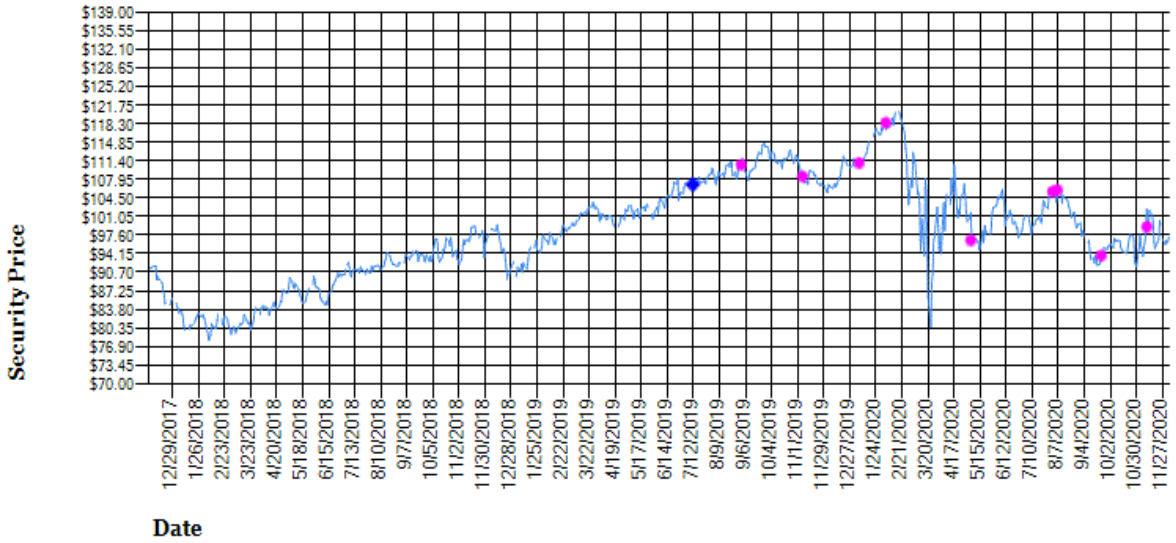
Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

Atmos Energy Corp. (ATO) 3-yr. Price Performance



Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
7/14/2019		Akers				
◆ 7/14/2019	106.46	1	119	NE	NE	106.46
● 9/2/2019	110.23	1	123	NE	NE	110.23
● 11/7/2019	108.40	1	119	NE	NE	108.18
● 1/8/2020	110.74	1	122	NE	NE	110.74
● 2/5/2020	116.82	1	131	NE	NE	118.28
● 5/7/2020	96.55	1	108	NE	NE	96.38
● 8/3/2020	105.31	1	115	NE	NE	105.31
● 8/7/2020	104.70	1	117	NE	NE	105.71
● 9/24/2020	92.87	1	104	NE	NE	93.59
● 11/12/2020	98.72	1	114	NE	NE	98.72

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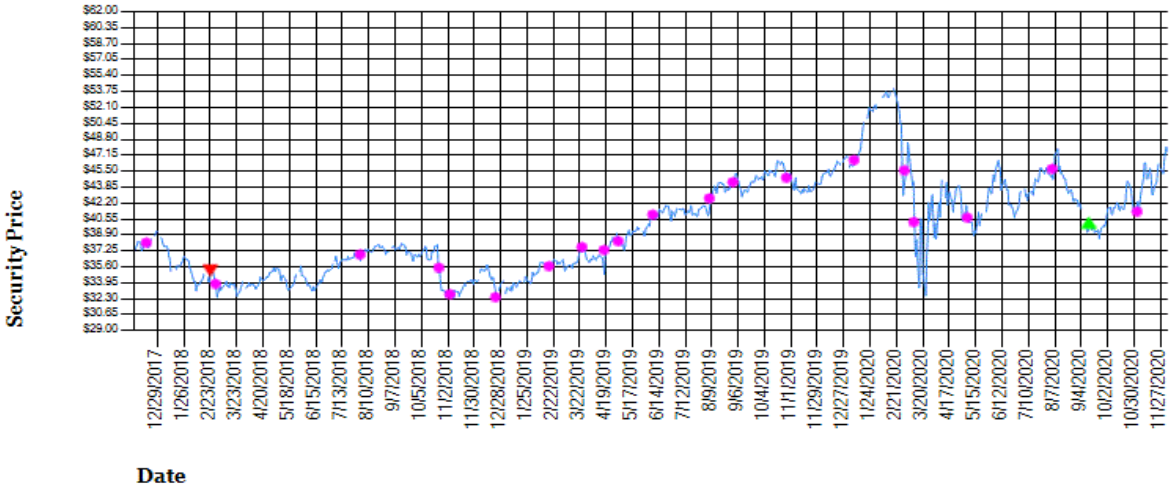
- ◨ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	12/4/2017		Reeder				
	12/4/2017	NA	1	40	NE	NE	37.67
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51
●	3/2/2020	43.01	2	45	NE	NE	45.44
●	3/11/2020	44.41	2	48	NE	NE	40.03
●	5/7/2020	40.49	2	42	NE	NE	40.53
●	8/6/2020	45.56	2	45	NE	NE	45.56
▲	9/14/2020	39.35	1	45	NE	NE	39.82
●	11/4/2020	41.19	1	47	NE	NE	41.19

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- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

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V=A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: December 10, 2020

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Essential Utilities, Inc.

WTRG: Solid Update Provided at 1/11 Guidance Event

WTRG Remains Our Favorite Water Utility Pick

Overweight/$52

Water Utilities

Earnings Estimates Revised Up

- **Key Points.** We viewed WTRG's 1/11 guidance event as supportive of our Overweight thesis. The '21 EPS guidance range of $1.64-1.69 was consistent with investor expectations and management extended the 5-7% EPS CAGR through '23. New items include (1) two new municipal transactions totaling $87M as well as (2) red meat for ESG conscience investors. We nudge up our 2021-24E EPS to/from $1.67/$1.65, $1.80/$1.78, $1.93/$1.91 & $2.07/$2.03. We also introduce our 25E of $2.20. Our forecast results in an EPS CAGR near the upper end of WTRG's targeted 5-7% range which we believe is reasonable given strong underlying rate base growth driven by accelerated pipeline replacement needs supplemented by a municipal M&A strategy that continues to gain momentum.
- **2 New M&A Deals Revealed – Positive Momentum Continues.** WTRG closed four municipal deals in 2020 for total rate base of $63M. In the pending column, the $277M DELCORA deal steals the show however WTRG has four other transactions with a combined value of $144M – includes three separate chunky wastewater deals (East Whiteland, PA $55M; Lower Makefield, PA $53M; Bourbonnais, IL $32M). WTRG has also been announced the winning bidder of two additional systems with a combined value of $30M which will move into the pending column once APA's are finalized. The company's deal development pipeline remains robust and management continues to express optimism that activity will start ramping up in the years ahead in the four states that only somewhat recently adopted FMV legislation (NC & OH in '18; TX in '19; VA in '20). Our model reflects primarily announced deal closures over the 2020-22 period plus a $75M/year placeholder in '23 & beyond.
- **Spotlighting DELCORA (Again!).** As we have previously opined, we believe the DELCORA deal represents material long-term value that is not currently reflected in the share price. Following the favorable court rulings on 12/28, PaPUC approval is the remaining hurdle with next key milestones including a 1/20 anticipated ALJ recommendation and a 3/11 commission approval deadline. Beyond the $277M rate base pick up at closure (expected early Q2'21), we are attracted to (1) the $700M of capital investments – $25-50M/year for typical repair/replace work plus roughly $300M over the 2026-28 period related to DELCORA's treatment plant – as well as (2) the likely substantial wastewater tuck-in deals that could transpire in the area. Simply put, we believe the DELCORA deal should, at a minimum, allow WTRG to continue to target a 5-7% EPS CAGR through the end of the decade if not bump it up to 6-8%.
- We offer some additional highlights from the 1/11 update on p.2 including (1) extension of the rate base growth targets, a brief discussion of the relatively low near-term regulatory risk profile and (3) announcements to hopefully lessen the ESG overhang.

$ EPS	2019A	2020E Curr.	2020E Prior	2021E Curr.	2021E Prior
Q1 (Mar.)	0.28	0.60 A	NC	0.67	NE
Q2 (June)	0.37	0.29 A	NC	0.25	NE
Q3 (Sep.)	0.48	0.23 A	NC	0.25	NE
Q4 (Dec.)	0.34	0.46	NC	0.50	NE
FY	1.47	1.58	NC	**1.67**	**1.65**
CY	1.47	1.58		1.67	
FY P/EPS	32.6x	30.4x		28.7x	
Rev.(MM)	890	1,931		2,055	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile
Adjusted EPS excludes items considered non-recurring.
WTRG expects 2021 adjusted EPS of $1.64-1.69 range and targets a 5-7% EPS CAGR through 2023 off the 2019 adjusted base of $1.47.
WTRG expects 2020 adjusted EPS at the top end of the $1.53-1.58 range.

Ticker	WTRG
Price Target/Prior:	**$52/NC**
Price (01/11/2021)	**$47.98**
52-Week Range:	$30-55
Shares Outstanding: (MM)	245.2
Market Cap.: (MM)	$11,764.7
S&P 500:	3,799.61
Avg. Daily Vol.:	931,178
Dividend/Yield:	$1.00/2.1%
LT Debt: (MM)	$5,277.4
LT Debt/Total Cap.:	53.2%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	7.0%
CY 2021 Est. P/EPS-to-Growth:	4.1x
Last Reporting Date:	11/03/2020 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Other highlights from the 1/11 guidance event and update include:

- **Capex & Rate Base Guidance Largely Upheld.** Management indicated plans to invest $550M on the water/wastewater side (ex. M&A) in '21 and $450M for gas (up from $400M in '20). In total, roughly $3B of spend is expected over the 2021-23 period which will drive underlying 6-7% water/wastewater and 8-10% gas rate base CAGRs through '23. More than 50% of the spend is eligible for rider mechanism recovery

- **WTRG offers investors relatively low near-term regulatory risk.** The next PA water & wastewater rate case filing is expected in late '21. While WTRG's PA rate cases can never be overlooked given the meaningful % of rate base represented (more than 70% on the water/wastewater side), the utility has a long history of reaching constructive outcomes via settlement agreements and the ALJ recommendation in the pending AWK case honors a settlement agreement reached on 10/30.

  Otherwise commission approvals for FMV deals as well as regulatory treatment of the catchup portion of Peoples' repairs tax deduction (RTD) are the main items we are keeping an eye on at the state level. Further on the RTD treatment, a PaPUC order is expected in Q2'20 and we are optimistic that something similar to WTRG's proposal will be adopted. We would not rule out the possibility of a settlement with intervenors and note that evidentiary hearings are scheduled for later this month. Recall, WTRG's proposal would share the benefits 40% with ratepayers (through rate surcredits on bills) with the remaining 60% used as an increasing income tax expense offset over 2023-25 – this would avoid the need for Peoples to file to implement a base rate increase prior to 1/1/2026 while supporting the elevated pace of capex deployment and ensuring a fair opportunity to earn the allowed ROE.

- **Addressing The ESG Overhang.** WTRG committed to reducing annual Scope 1 and 2 GHG emissions by 60% by 2035 (using 2019 baseline) across both the gas and water utility platforms utilizing existing and proven methods and will look to get to net zero once technological advances allow. Other ESG-friendly updates include establishing multi-year plans to increase supplier and employee diversity as well as tying incentive comp to those metrics. Successfully addressing the ESG concerns that arose out of the recent acquisition of the Peoples gas utility and gaining wider spread acceptance by the investment mantra that seems to only be growing in popularity could help close some of the valuation gap between AWK.

Acronyms:

ALJ – Administrative Law Judge
APA – Asset Purchase Agreement
DELCORA – Delaware Country Regional Water Quality Control Authority
ESG – Environmental, Social, Governance
FMV – Fair Market Value
GHG – Greenhouse Gas
PaPUC – Pennsylvania Public Utility Commission

Price Target

Price Target: $52 from NC

Our $52/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.80. For WTRG's water utility multiple, we ascribe a roughly 5% discount to the 21E multiple we use for AWK (34-34.5X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The roughly 5% discount reflects a modestly lower earnings growth rate (we forecast 6-7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 17.0-17.5X (based on ATO, NWN, OGS & SR) and then apply a roughly 10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive PA regulatory framework. Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

Investment Thesis

Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived and near-term regulatory risk is low as both the water and gas utilities completed rate cases in 2019), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

Company Description

Headquartered in Bryn Mawr, PA, Essential Utilities (WTRG) - formerly Aqua America - is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTRG's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total water customer base and nearly 70% of consolidated water rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio.

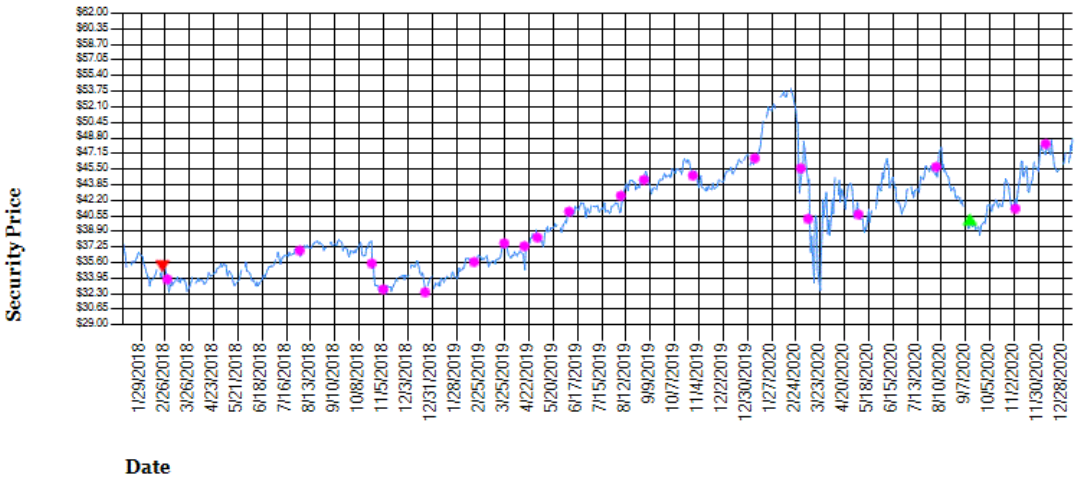
In March 2020, WTRG closed on the acquisition of Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, WTRG paid 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to other gas utility transactions at the time. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

Regulated operations account for more than 99% of consolidated revenues. Consolidated EPS is expected to be driven roughly 70% by water utility operations with the gas utility contributing the remaining 30%.

In February 2020, the new name Essential Utilities, Inc. and new ticker WTRG became effective. Prior, the company was known as Aqua America Inc. and traded under the ticker WTR.

Required Disclosures

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	1/8/2018		Reeder				
	1/8/2018	NA	1	43	NE	NE	37.71
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51
●	3/2/2020	43.01	2	45	NE	NE	45.44
●	3/11/2020	44.41	2	48	NE	NE	40.03
●	5/7/2020	40.49	2	42	NE	NE	40.53
●	8/6/2020	45.56	2	45	NE	NE	45.56
▲	9/14/2020	39.35	1	45	NE	NE	39.82
●	11/4/2020	41.19	1	47	NE	NE	41.19
●	12/10/2020	47.70	1	52	NE	NE	48.02

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Source: Wells Fargo Securities, LLC estimates and Reuters data

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▲ Rating Upgrade
● Price Target/Val Range Change
◆ Initiation, Resumption, Drop or Suspend
■ Analyst Change
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WELLS FARGO SECURITIES

Essential Utilities, Inc.

WTRG: Analyst Day Wrap Up -- Adjusting EPS Outlook

Equal Weight/$45

Water Utilities

Price Target Change

- **Key Points.** WTRG's 2/27 analyst day provided clarity around the company's EPS power for the next few years. After reporting adjusted '19 EPS of $1.47 (reflects the base water business without the impacts from external financings completed in 2019 for the Peoples acquisition), '20 EPS are expected to be $1.53-1.58 (pro forma for a 1/1 Peoples close vs. the anticipated 3/16). In addition, management forecasts a 5-7% EPS CAGR through '22 off the $1.47 base. This trails expected consolidated rate base growth of roughly 8% due to earned ROEs at recent/pending muni deals not yet earning the full keep plus some dilution. However, once another PA water rate case goes into effect (we assume a '21 filing; rates effective '22), then it sounds like EPS growth should track more closely to rate base growth. After flowing '19 actuals and analyst day disclosures through our model, we lower our 20-22E EPS to/from $1.56/$1.57, $1.65/$1.70 & $1.77/$1.80. We project a 6.5% EPS CAGR through '24. No change to our overall thesis or Equal Weight rating despite recent underperformance (down 10% since 2/18 relative to the S&P Utilities) as shares trade in-line with a 70% water/30% gas LDC blended multiple. We lower our 12-18 month price target to $45/share from $48 (26X our 22E) due primarily to lower peer group multiples since our last update.
- **EPS Outlook.** Our 2020-24E EPS are $1.56, $1.65, $1.77, $1.90 & $2.02. The addition of Peoples (3/16 close expected), including the $0.08-0.12 of EPS benefits anticipated by electing and flowing through the current portion of RTD at Peoples Gas, is what allows WTRG to guide to 2020 pro forma EPS of $1.53-1.58 (as if the deal closed 1/1). Our prior outlook did not include the RTD benefits – which we thought offered $0.10-0.15 upside – however we, as well as most investors that we have talked to, did not appreciate the headwinds facing the base water business in '20. This led to the guidance being viewed as somewhat disappointing and shares underperforming. After reporting adjusted '19 EPS of $1.47, management indicated 2020 base water EPS would have been relatively flat, all else equal. This is because (1) '19 benefited from the PA water repair tax deduction flowing to shareholders until new PA rates were effective mid-May, (2) there is roughly $200M of recent municipal system acquisition rate base additions that are not yet earning the allowed ROE in '20 (may actually be closer to break-even) and (3) the absence of any PA DSIC revenues until '21.
- **WTRG's Strategy.** The core growth drivers remain twofold. (1) Reinvest aggressively in existing systems and seek timely regulatory recovery. 2020 capex is $550M for water and $400M for gas with a total of $2.8B budgeted over the 2020-22 period. And we do not expect any falloff in those levels for the foreseeable future. (2) Actively pursue municipal M&A. ***Comment continues on p. 2***

$ EPS	2019A	2020E Curr.	2020E Prior	2021E Curr.	2021E Prior
Q1 (Mar.)	0.28	0.62		NE	
Q2 (June)	0.37	0.23		NE	
Q3 (Sep.)	0.48	0.24		NE	
Q4 (Dec.)	0.34	0.47		NE	
FY	1.47	**1.56**	**1.57**	**1.65**	**1.70**
CY	1.47	1.56		1.65	
FY P/EPS	29.3x	27.6x		26.1x	
Rev.(MM)	890	1,927		2,058	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile
Adjusted EPS excludes items considered non-recurring.
WTR expects 2020 adjusted EPS of $1.53-1.58 and targets a 5-7% EPS CAGR through 2022 off the 2019 adjusted base of $1.47

Ticker	WTRG
Price Target/Prior:	**$45/$48**
Price (02/28/2020)	**$43.01**
52-Week Range:	$34-55
Shares Outstanding: (MM)	220.8
Market Cap.: (MM)	$9,496.6
S&P 500:	2,954.22
Avg. Daily Vol.:	1,204,010
Dividend/Yield:	$0.94/2.2%
LT Debt: (MM)	$3,077.0
LT Debt/Total Cap.:	44.1%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	6.0%
CY 2020 Est. P/EPS-to-Growth:	4.6x
Last Reporting Date:	02/26/2020 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Please see page 3 for rating definitions, important disclosures and required analyst certifications. All estimates/forecasts are as of 03/02/20 unless otherwise stated. 03/02/20 06:51:16 ET

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Together we'll go far

- **WTRG's Strategy *(continued…).*** Deal activity in the industry remains elevated, in large part due to states adopting FMV legislation, and WTRG is in various levels of discussions with systems representing a total of 320,000 customers. Besides PA and IL, WTRG seems to believe OH, TX and KY hold the most promise. Management's compensation is tied to a $60M/yr deal value target and the goal is to achieve 2-3% customer growth through organic and M&A. Management believes the capex budget can be financed without new equity whereas deal flow would require roughly 50% new equity, perhaps through the establishment of an ATM program in front of the DELCORA deal close (expected late '20). Speaking of DELCORA, enthusiasm remains high for the deal from the immediate rate base addition, meaningful future capex needs ($700M by 2028) as well as potential bolt-on wastewater deals perspectives. Other management priorities outlined at the analyst day include completing/integrating the Peoples and DECLORA transactions as well as maintaining ESG appeal (highlighted recent diversity and governance enhancements).

Acronyms:

ATM – At-the-market
DSIC – Distribution System Improvement Charge
ESG – Environmental, Social, and Governance
FMV – Fair Market Value
RTD – Repairs Tax Deduction

Price Target

Price Target: $45 from $48

Our $45/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 2.5% discount to our 70% water/30% gas utility hybrid multiple to our 2022E of $1.77. The 2.5% discount reflects merger execution/integration risk. For WTRG's water utility multiple, we start with AWK's 2021 P/E multiple of 29.4X (AWK represents the closest publicly traded peer) and apply a 5% discount (given AWK's higher growth rate and best-in-class management team). For WTRG's gas utility multiple, we utilize the 2021 pure play gas LDC median of 21.2X. Key risks include regulatory and M&A strategy execution related.

Investment Thesis

We are attracted to WTRG's strong fundamentals - a proven EPS growth strategy, a growing rate base, constructive regulation, efficient operations and a strong balance financial profile. Our Equal Weight rating reflects valuation considerations in light of WTRG's pending agreement to acquire Peoples (a gas utility) and the associated P/E multiple, regulatory and deal execution/integration related risks.

Company Description

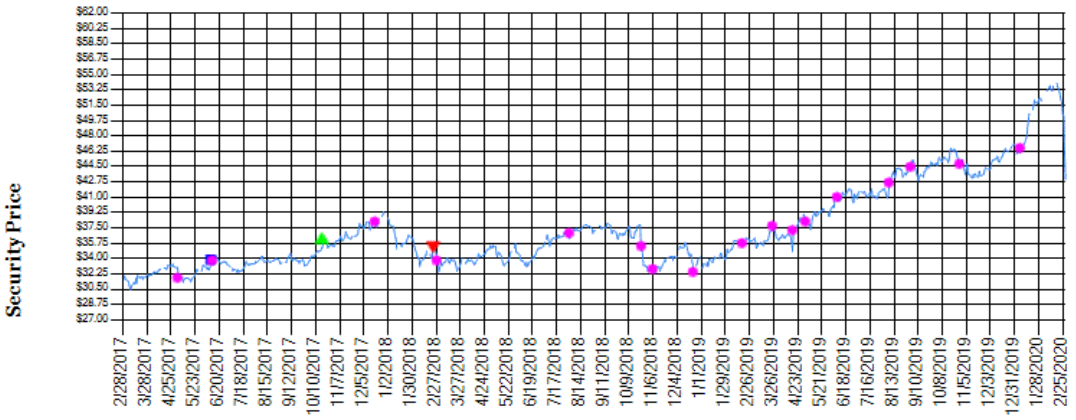
Headquartered in Bryn Mawr, PA, Essential Utilities (WTRG) - formerly Aqua America - is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTRG's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total water customer base and nearly 70% of consolidated water rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio. Regulated operations account for more than 99% of consolidated revenues.

On 10/23/18, WTRG announced a deal to acquire Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, the deal appears to be 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to what we have seen in recent gas utility transactions. WTRG received PA regulatory approval on 1/16 and the deal is expected to close imminently. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

On 2/3, the new name Essential Utilities, Inc. and new ticker WTRG became effective. Prior, the company was known as Aqua America Inc. and traded under the ticker WTR.

Required Disclosures

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	2/28/2017		Kalton				
	2/28/2017	NA	2	NE	31.00	33.00	31.74
●	5/4/2017	31.70	2	NE	32.00	34.00	31.73
■	6/13/2017		Reeder				
●	6/13/2017	33.62	2	35	NE	NE	33.62
▲●	10/19/2017	35.30	1	40	NE	NE	36.03
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51

*Effective December 7, 2019, Wells Fargo Securities' Equity Research modified its ratings definitions. Complete definitions of current ratings can be found below. For information related to prior ratings definitions, please contact equityresearch1@wellsfargo.com.

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

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2=Equal Weight: Total return on stock expected to be 0-10% over the next 12 months. HOLD
3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

VOLATILITY RATING
V = A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: March 2, 2020

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WELLS FARGO SECURITIES

Essential Utilities, Inc.

WTRG: What's In A Name? - Change Ironically A Harbinger Of COVID Resiliency

Equal Weight/$42

Water Utilities

Price Target Change

- **Key Points.** Management affirmed all aspects of guidance provided at the late February analyst day as WTRG's utility businesses are expected to be resilient to the challenges presented by COVID-19. It helps that the bulk of customers and revenues, for both water and gas, are residential and that the gas utility is past the high-demand heating season. In addition, constructive regulatory treatment of any incremental COVID-19 costs is expected. No change to our 2020-24E EPS of $1.56, $1.65, $1.77, $1.90 & $2.02. Our outlook is consistent with management's 2020 pro forma (as if the Peoples deal closed 1/1 and experienced normal weather from 1/1 through the 3/16 close) EPS guidance of $1.53-1.58 and 5-7% CAGR through 2022 off the '19 base. We reiterate our Equal Weight rating but lower our 12-18 month price target to $42/sh (23.5-24.0X our 22E) from $48/sh due to lower peer group multiples since our last update.
- **COVID-19 Impacts – Sales/Expenses.** Although it is early, management mentioned that preliminary April data shows that the increased residential usage is offsetting the decrease in C&I and gov't/public customers on the water side as the month came in right at budget. And with the heavy-use heating season over on the gas side, management does not see a material financial impact from usage but that could depend on how long the stay-at-home orders are in place. WTRG plans to track COVID-19 related expenses with an expectation that regulators will afford constructive recovery, particularly of bad debt expense given the implemented no shutoff policies for non-payment. Bad debt expense rose to 1.1% of revenues in the 2008-09 financial crisis which is about double the 0.5% that has been historically observed and embedded in water rates. That said, there are some costs that are lower which could help defray any increases. Net-net, the overall expense impact is not expected to be material.
- **COVID-19 Impacts – Capex/Liquidity.** In terms of capital deployment, a two week moratorium implemented on water work in PA did set the utility about $30M behind schedule. However, the ground is expected to be made up over the balance of the year and there is no change to WTRG's overall water and gas capex budgets. Access to capital is not an issue. WTRG, like other utilities, have taken precautionary steps to boost near-term liquidity. The capex budget can be financed without equity but M&A deals will require some – we expect about 50% of the purchase price. With that in mind, we think WTRG could be flexible with the exact timing of the $300M of equity needs outlined for later this year to finance DELCORA and other deals in the pipeline.
- Please see p. 2 for discussions of municipal M&A activity (spoiler alert, COVID-19 could increase the deal flow!), regulatory updates and a brief EPS & capex discussion.

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Q1 (Mar.)	0.28	**0.60 A**	**0.62**	NE	
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FY	1.47	1.56	NC	1.65	NC
CY	1.47	1.56		1.65	
FY P/EPS	27.5x	26.0x		24.5x	
Rev.(MM)	890	1,927		2,058	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile
Adjusted EPS excludes items considered non-recurring.
WTR expects 2020 adjusted EPS of $1.53-1.58 and targets a 5-7% EPS CAGR through 2022 off the 2019 adjusted base of $1.47

Ticker	WTRG
Price Target/Prior:	**$42/$48**
Price (05/07/2020)	**$40.49**
52-Week Range:	$30-55
Shares Outstanding: (MM)	220.8
Market Cap.: (MM)	$8,940.2
S&P 500:	2,879.45
Avg. Daily Vol.:	900,670
Dividend/Yield:	$0.94/2.3%
LT Debt: (MM)	$3,077.0
LT Debt/Total Cap.:	44.1%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	6.0%
CY 2020 Est. P/EPS-to-Growth:	4.3x
Last Reporting Date:	05/06/2020 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Please see page 4 for rating definitions, important disclosures and required analyst certifications. All estimates/forecasts are as of 05/07/20 unless otherwise stated. 05/07/20 16:35:45 ET

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Together we'll go far

- **COVID-19 Impacts – Municipal M&A.** Similar to the thoughts expressed by AWK a few hours earlier, WTRG expects the volume of municipal M&A discussions/deals to be positively impacted by COVID-19. Many municipalities were already challenged financially and some even operationally (complying with increasingly stringent EPA standards) before the pandemic. The economic shutdowns have likely only exacerbated those pressures.

  Management remains upbeat about the pipeline of deals, noted how a number of decent-sized opportunities have been advanced that can hopefully be talked about in the not so distant future and highlighted how fair market value (FMV) legislation continues to open doors. VA adopted FMV earlier this year – all 8 of WTRG's water states now have it – and deal momentum continues to build in other recently adopted states like OH & TX. Having closed on the Campbell, OH water deal earlier this year, WTRG has the New Garden, PA ($30M), East Norriton, PA ($21M) and DELCORA ($277M) wastewater deals pending. The goal remains to achieve 2-3% customer growth through organic and M&A efforts.

- **Regulatory Updates.** WTRG's near-term regulatory calendar is fairly light as the PA water and gas utilities completed major base rate cases last year. The two proceedings of greatest investor interest are the DELCORA acquisition approval (filed in Q1; late '20 close expected) and PA regulatory treatment of the catch-up component of Peoples repairs tax deduction benefit (file this summer; clarity perhaps around YE'20; any retention by WTRG should be incremental to current outlook). Despite the challenges presented by stay-at-home orders, WTRG has not experienced any material regulatory timeline delays.

- **EPS Outlook.** Our 2020-24E EPS are $1.56, $1.65, $1.77, $1.90 & $2.02. The core growth drivers remain (1) capex/rate base growth by aggressively reinvesting in existing systems and seeking timely regulatory recovery and (2) municipal M&A. 2020 capex remains $550M for water and $400M for gas with a total of $2.8B budgeted over the 2020-22 period and we do not expect any falloff in those levels for the foreseeable future.

- In fact, an internally ordered report conducted by Black & Veatch to assess the overall safety of the Peoples gas system, including pressure risk, was completed earlier this month. While the conclusions were that the system is safe, WTRG is evaluating the recommendations made and preparing an action plan. There is an opportunity to invest more to further enhance safety and that will be addressed in future plans with an eye towards rate affordability.

Acronyms:

C&I – Commercial & Industrial
DELCORA – Delaware Country Regional Water Quality Control Authority

Price Target

Price Target: $42 from $48

Our $42/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.77. For WTRG's water utility multiple, we ascribe a 5-10% discount to the 21E multiple we use for AWK (27.0-27.5X). The 5-10% discount reflects both a modestly lower EPS growth rate (we forecast 6.5% for WTRG vs. 8% for AWK) as well as lower ESG appeal (in particular, the recent Peoples deal). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of roughly 21X. Key risks include regulatory and M&A strategy execution related.

Investment Thesis

We are attracted to WTRG's strong fundamentals - a proven EPS growth strategy, a growing rate base, constructive regulation, efficient operations and a strong balance financial profile. Our Equal Weight rating reflects valuation considerations in light of WTRG's recently closed acquisition of Peoples (a gas utility) and the associated P/E multiple, regulatory and deal execution/integration related risks.

Company Description

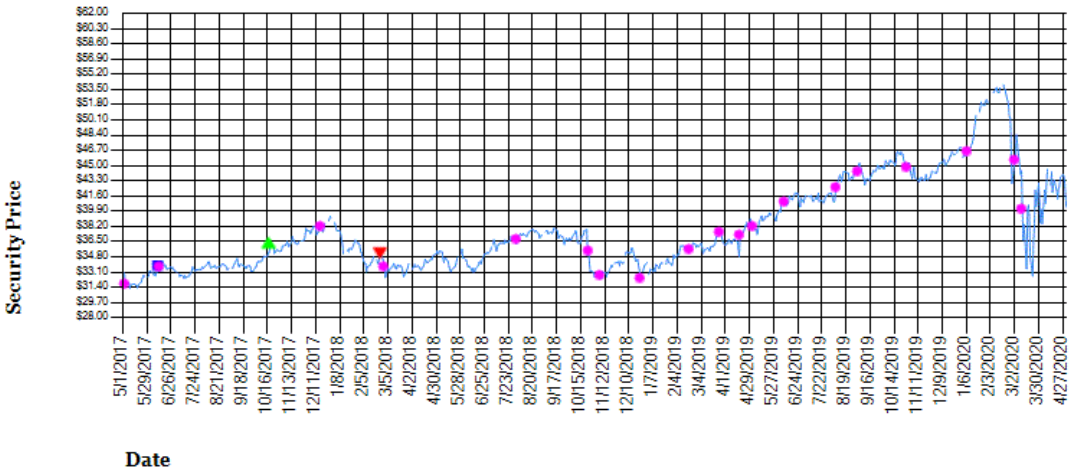
Headquartered in Bryn Mawr, PA, Essential Utilities (WTRG) - formerly Aqua America - is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTRG's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total water customer base and nearly 70% of consolidated water rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio. Regulated operations account for more than 99% of consolidated revenues.

On 10/23/18, WTRG announced a deal to acquire Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, the deal appears to be 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to what we have seen in recent gas utility transactions. WTRG received PA regulatory approval on 1/16/20 and the deal closed two months later on 3/16. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

On 2/3, the new name Essential Utilities, Inc. and new ticker WTRG became effective. Prior, the company was known as Aqua America Inc. and traded under the ticker WTR.

Required Disclosures

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	5/1/2017		Kalton				
	5/1/2017	NA	2	NE	31.00	33.00	32.94
●	5/4/2017	31.70	2	NE	32.00	34.00	31.73
■	6/13/2017		Reeder				
●	6/13/2017	33.62	2	35	NE	NE	33.62
▲●	10/19/2017	35.30	1	40	NE	NE	36.03
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51
●	3/2/2020	43.01	2	45	NE	NE	45.44
●	3/11/2020	44.41	2	48	NE	NE	40.03

*Effective December 7, 2019, Wells Fargo Securities' Equity Research modified its ratings definitions. Complete definitions of current ratings can be found below. For information related to prior ratings definitions, please contact equityresearch1@wellsfargo.com.

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

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WTRG: Key risks include regulatory and M&A strategy execution related.

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2=Equal Weight: Total return on stock expected to be 0-10% over the next 12 months. HOLD
3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

VOLATILITY RATING
V = A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: May 7, 2020

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WELLS FARGO SECURITIES

Essential Utilities, Inc.

WTRG: Recent Pullback Creates Opportunity – Upgrade To Overweight

Overweight/$45

Water Utilities

Rating Change

- **Key Points.** We upgrade our rating on shares of WTRG to Overweight from Equal Weight as we believe the recent underperformance has created an attractive entry point. The cause of the relative pullback is not entirely clear (we offer some potential drivers in this report) but the bottom line is that we do not believe anything that has transpired fundamentally since the Q2'20 report in early August has materially impacted (1) the likelihood of DELCORA closing, (2) our EPS outlook or (3) our investment thesis.

  While the DELCORA deal is highly supportive of WTRG's growth aspirations, we consider the future to be bright without it driven by elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends. We believe relatively low risk, regulated EPS growth of at least 6% is achievable – that rate of growth would simply be enhanced if DELCORA closes given the $700M of required investment needed in the system by 2028 as well as potential further municipal wastewater deals in the region. No change to our 2020-24E EPS of $1.56, $1.65, $1.77, $1.90 & $2.02 (which assumes an end of Q1'21 DELCORA close). Our 12-18 month price target of $45/share (25.4X our 22E) is supported by P/E and DDM analyses.

- **Breaking Down Our P/E Valuation – Water.** Our P/E analysis results in a $45/share value and remains predicated on a 70% water/30% gas utility hybrid P/E multiple applied to our 2022E of $1.77. For WTRG's water utility multiple, we ascribe a 5-10% discount to the 21E multiple we use for AWK (30X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The 5-10% discount reflects a modestly lower earnings growth rate (we forecast 6-7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility).

- **Breaking Down Our P/E Valuation – Gas.** For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 18X (based on ATO, NWN, OGS & SR) and then apply a 5-10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of an accelerated pipeline replacement effort under the PaPUC-approved LTIIP program which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive regulatory framework of the PaPUC which includes fully forecasted test years, infrastructure surcharge mechanism recovery and a history of settled regulatory outcomes. ***(Comments continue on p. 2)***

$ EPS	2019A	2020E Curr.	2020E Prior	2021E Curr.	2021E Prior
Q1 (Mar.)	0.28	0.60 A	NC	NE	
Q2 (June)	0.37	0.29 A	NC	NE	
Q3 (Sep.)	0.48	**0.20**	**0.25**	NE	
Q4 (Dec.)	0.34	**0.47**	**0.43**	NE	
FY	1.47	1.56	NC	1.65	NC
CY	1.47	1.56		1.65	
FY P/EPS	26.8x	25.2x		23.9x	
Rev.(MM)	890	1,926		2,054	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile
Adjusted EPS excludes items considered non-recurring.
WTR expects 2020 adjusted EPS of $1.53-1.58 and targets a 5-7% EPS CAGR through 2022 off the 2019 adjusted base of $1.47

Ticker	WTRG
Price Target/Prior:	**$45/NC**
Price (09/11/2020)	**$39.35**
52-Week Range:	$30-55
Shares Outstanding: (MM)	245.2
Market Cap.: (MM)	$9,648.6
S&P 500:	3,340.97
Avg. Daily Vol.:	1,333,840
Dividend/Yield:	$1.00/2.5%
LT Debt: (MM)	$5,277.4
LT Debt/Total Cap.:	53.2%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	6.0%
CY 2020 Est. P/EPS-to-Growth:	4.2x
Last Reporting Date:	08/05/2020 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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- **Breaking Down Our P/E Valuation – Gas.** For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 18X (based on ATO, NWN, OGS & SR) and then apply a 5-10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort (mainly bare unprotected steel) under the PaPUC-approved LTIIP program which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA (the bulk of Peoples service territory), which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive regulatory framework of the PaPUC which includes fully forecasted test years, infrastructure surcharge mechanism recovery and a history of settled regulatory outcomes. Lastly, with the electrification theme gaining momentum and potentially challenging the long-term outlook for the gas LDC model (existential threat?), we no longer believe the publicly traded LDC multiples really reflect a takeout premium and thus no adjustment is necessary when valuing Peoples.

- **Other P/E Valuation Thoughts.** Shares trade at 23.8X & 22.2X our 21E & 22E EPS or roughly 15% discounts to the "large cap" pure play waters (AWK, AWR, CWT, MSEX & SJW) of 27.9X and 26.1X. That seems a bit steep given a relatively commensurate EPS growth profile, a large concentration of EPS power and growth stemming from the water utility and a similarly large concentration of EPS power stemming from the constructive PA regulatory environment. Perhaps the main differences relate to WTRG's inferior ESG appeal and credit metrics (though S&P assigns WTRG an "A"/Stable credit rating; the same as AWK & MSEX, a notch below AWR & CWT and a notch above SJW). If an in-line water multiple was applied, it would suggest a 12-18 month forward share price of closer to $50/share. It is also interesting to note that shares of WTRG currently trade at P/E multiples similar to high quality electric utilities WEC & XEL despite the water utility group median as a whole trading at roughly 70% premiums to regulated electrics.

- **What If DELCORA Does Not Happen?** At the risk of stating the obvious, we prefer the WTRG story with the DELCORA deal closing than without it. DELCORA is really somewhat of a unique strategic deal in our view given it not only increases WTRG's rate base by $277M out of the gate but offers meaningful future capex needs ($700M by 2028) as well as potential bolt-on wastewater deals in the region, particularly from municipalities that are wholesale wastewater customers of DELCORA's as well as the Tredyffrin Township Municipal Authority's trunk sewer system that WTRG acquired in 2018.

  However, much of the accretion and longer-term benefits of the deal that we love so much do not start impacting WTRG's financials until the back half of our 2020-24 outlook or beyond – in fact, we believe the assumptions embedded in our model could prove conservative if DELCORA closes. On the capex side, we only bump up our '21 & '22 forecast by $25M for DELCORA spend and then modestly grow that in '23 & '24 as it is our understanding that the majority of the $700M of capex actually occurs more in the 2026-28 period as a treatment plant expansion and pipeline is needed to get DELCORA off Philadelphia's wastewater system by 2028. On the M&A side, we do not increase our annual deal value placeholder of $60M for the enhanced opportunity set in the Southeast PA region that DELCORA could provide.

  If we were to completely strip out the DELCORA deal, the aforementioned tick up in capex that we assume in '21-24 and all of the associated external financing (including roughly $150M of equity), it only has a modest $0.03-0.05 impact (less than 3%) on our 2021-24E EPS. Keep in mind that when FMV deals are first consummated, the acquiring utility typically just inherits the existing rates and it therefore takes at least 2-3 years to go through a rate case cycle in order get the acquired system's rate base to earn similar returns as the rest of acquiring utility's water or wastewater operations in the state.

  Put another way, we believe WTRG's future growth would still be attractive even if the DELCORA deal does not come to fruition. There would still be time for management to continue to capitalize on the industry's FMV consolidation momentum – including in OH and TX which recently adopted the legislation and where WTRG is the big fish in the pond – and replace the growth that we believe will transpire in the 2nd half of the decade if the DELCORA deal does close.

- **Dissecting The Underperformance.** Since 8/10, shares of WTRG are -18%. Amongst water peers, SJW is -16% over the same period while the others range from -11% (MSEX) to -5% (AWK). Also worth noting, the gas LDCs are -12% while the S&P Utilities are -5%. So what gives? We have fielded a number of inbound inquiries from investors and have talked to the company but it is honestly hard to pinpoint the reason. We offer three potential contributing factors.

(1) Macro And The Flight To Quality. Utilities as a whole have remained out of favor in the risk-on market and those that investors seemingly want to own have been the highest quality names with generally the strongest credit metrics. This would be AWK & AWR on the water side whereas SJW & WTRG have weaker credit metrics due to recent large scale M&A.

(2) Gas Further Out Of Favor. It also does not help that gas LDCs have fallen further out of favor and again trade essentially in-line with electrics on a P/E basis. Gas LDCs used to trade at a premium to electrics (but below waters) due to higher rate base CAGRs spurred by pipe replacement and relatively lower regulatory risk. However the concern lately seems to be more existential due to natural gas bans being contemplated in cities on both the west and east coasts as well as electrification potential and the rising prospects of renewables plus storage to replace gas-fired generation. Most investors that we talk to use a gas multiple to value the 30% of WTRG's EPS derived from Peoples, which is consistent with our approach.

(3) Management Putting The Cart Before The Horse? Uncertainty exists as to whether the pending $277M DELCORA deal actually closes. We are relatively confident in WTRG's ability to gain PaPUC approval though it remains early days. Recently on 8/31, OCA's request (citing COVID) for a 60-day extension of the statutory deadline to 3/26/21 was granted whereas Delaware County's petition (which was supported by OCA and BI&E) to stay the proceeding in its entirety until the Court of Common Pleas litigation (discussed below) concludes was denied – neither should have caused WTRG shares to underperform in our opinion. Key remaining items under the PaPUC's updated procedural schedule issued 9/4 include standard public input hearings on 9/16, intervenor testimony due on 9/29, evidentiary hearings begin 11/9 and a recommended decision by 1/20. While the PaPUC docket is certainly worth monitoring, we consider the courts to be the critical path to deal closure.

There is a complaint in the Court of Common Pleas of Delaware County filed by Delaware County regarding essentially the County Council's attempt to (1) dissolve DELCORA based on an ordinance the County Council passed on 6/4/20 and/or (2) dispute the legality of the irrevocable trust and therefore gain access to the $210M of net sales proceeds (after DELCORA debt pay down) earmarked for the trust fund. If successful on #1, the County Council may argue that the asset purchase agreement with Aqua Pennsylvania is unenforceable. On #2, the County Council would like to see at least some of the proceeds go for taxpayer benefit (offset forecasted tax increases) versus just ratepayers. DELCORA's plan, as outlined when the deal with WTRG was announced in September 2019, is to create a rate stabilization fund (via the trust) that will keep ratepayers' annual bill increases at 3% or less over the next 8 years despite the massive amount of capital that needs to be invested into the system.

A hearing in the court case was held last Wednesday (9/9). WTRG interpreted the judge's tone as leaning positive based on the strong legal arguments in support of the transaction. However, the timeline for resolution appears like it will (not surprisingly) take longer than management originally thought. It is our understanding that the next scheduled court hearing on 9/23 will predominately focus on the issues around the trust while the final hearings are not slated to conclude until 10/21. As such, the judge's ruling might not come until late October at the earliest unless of course a settlement is reached.

Despite this uncertainty, WTRG pulled the trigger on a roughly $300M forward stock offering in mid-August. WTRG could of course elect cash settlement if all of the equity is not ultimately needed (we estimate roughly half is for non-DELCORA deals). Regardless, it is somewhat reminiscent of the share issuance "jumping of the gun" by WTRG & SJW in the recent Peoples & CTWS mergers where ultimate regulatory approval did not come for another roughly 9 months.

That all being said, it is our understanding that the deal is not necessarily dead if the court rules in Delaware County's favor. According to WTRG management, dialogue from the new all-Democrat County Council members seems to support system privatization efforts. Therefore it could be possible to perhaps re-cut the deal – whether that could be done through exclusive negotiations or if the County Council would put the DELCORA system out for bid is unclear (would open the door for others, like AWK who has previously expressed an interest in acquiring the system, to come in and compete). However, if the court only sides with Delaware County regarding the trust and the County Council is able to get their hands on some/all of the sale proceeds, the deal

could still happen it would just result in higher rates for DELCORA ratepayers as WTRG seeks recovery of the significant capital upgrades needed with lower/no funds set aside to help offset the impact.

- **Quick Repairs Tax Update.** The only other WTRG development since the Q2'20 call worth noting relates to Peoples pending request for treatment of the repairs tax catchup benefit. Initial intervenor statements regarding WTRG's proposal were filed on 8/26. Not surprisingly OCA and BI&E expressed concerns regarding the balance of ratepayer and shareholder interests. That said, WTRG was not surprised by the parties' stated positions.

  Recall, WTRG filed in early August for PaPUC treatment of the catch up portion of the Peoples repairs tax deduction election. The filing outlined a $381M catch up deduction and proposed to share the benefits between customers (40%) and shareholders (60%). For customers it would amount to a $14M/year benefit (in the form of a nearly 2% surcredit on the average monthly bill) over 4 years beginning 1/1/21. The remaining benefit would be deferred and amortized as an offset to income tax expense over the 2023-2025 period – specifically, 5% in 2023, 35% in 2024 and 60% in 2025 – in an effort to offset normal regulatory lag while essentially keeping the earned ROE consistent with allowed levels. This would extend the time between the next base rate case to approximately 6 years (delay the need for a base rate increase effective prior to 1/1/2026 per Peoples' current projections) while supporting the elevated pace of capex deployment needed to replace pipes and drive safety improvements.

  WTRG had communications with regulators and other key parties prior to making this filing which makes us hopeful that the proposal will be positively received and that a constructive outcome will ensue, perhaps via a settlement. Approval of the shareholder benefit aspect of the request would increase our confidence in the gas utilities' ability to achieve our forecast – we assume gas utility earned ROEs of 10-10.3% which we believe is reasonable and consistent with Peoples 2019 rate order. On the flip side, if the PaPUC decides to go a different direction with the catchup benefits, we still believe our 2023 & beyond EPS levels are reasonable within the backdrop of the constructive PA regulatory framework. It could simply necessitate filing for a base rate increase sooner which would bring with it associated regulatory risk.

Acronyms:
BI&E – the PaPUC's Bureau of Investigation and Enforcement
DELCORA – Delaware Country Regional Water Quality Control Authority
ESG – Environmental, Social, Governance
FMV – Fair Market Value
LDC – Local Distribution Company
LTIIP – Long-Term Infrastructure Improvement Plan
OCA – Office of Consumer Advocate
PaPUC – Pennsylvania Public Utility Commission
S&P – Standard & Poor's

Ticker, Rating, Price (9/11/20)

AWK, Equal Weight, $141.1

AWR, Equal Weight, $73.44

SJW, Equal Weight $59.72

Source: Wells Fargo Securities, LLC, FactSet

Price Target

Price Target: $45 from NC

Our $45/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.77. For WTRG's water utility multiple, we ascribe a 5-10% discount to the 21E multiple we use for AWK (30X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The 5-10% discount reflects a modestly lower earnings growth rate (we forecast 6-7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 18X (based on ATO, NWN, OGS & SR) and then apply a 5-10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive PA regulatory framework. Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

Investment Thesis

Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

Company Description

Headquartered in Bryn Mawr, PA, Essential Utilities (WTRG) - formerly Aqua America - is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTRG's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total water customer base and nearly 70% of consolidated water rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio.

In March 2020, WTRG closed on the acquisition of Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, WTRG paid 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to other gas utility transactions. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

Regulated operations account for more than 99% of consolidated revenues. Consolidated EPS is expected to be driven roughly 70% by water utility operations with the gas utility contributing the remaining 30%.

In February 2020, the new name Essential Utilities, Inc. and new ticker WTRG became effective. Prior, the company was known as Aqua America Inc. and traded under the ticker WTR.

Rating Basis Information:

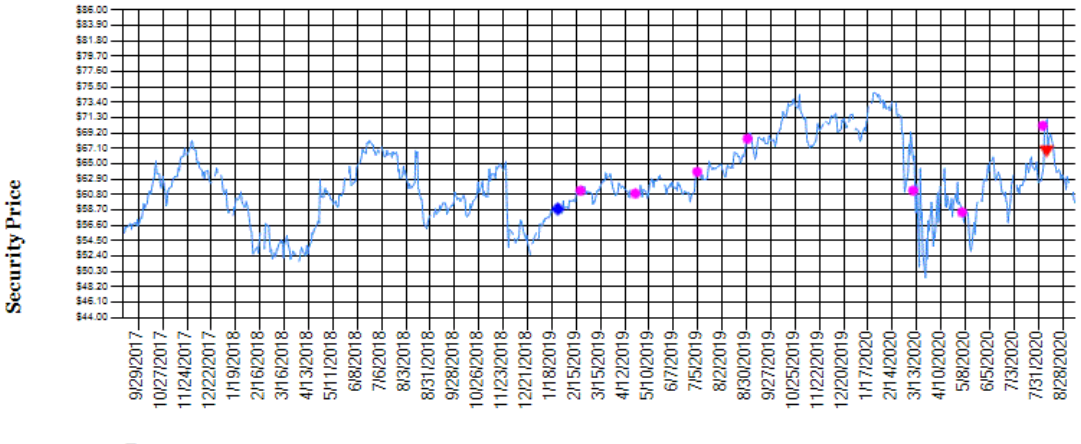
AWK Thesis: We believe AWK is well positioned to capitalize on favorable industry dynamics which should lead to above average rate base, EPS and DPS growth. Our Equal Weight rating reflects the fact that shares trade at roughly 10% premiums to water utility peers on our 21E & 22E EPS which we believe is adequate. While we consider AWK's EPS (8.0-8.5%) and dividend (9%) growth prospects as well as management team best in class for the water industry (as well as top tier for our utility coverage in general), takeout and liquidity/scarcity premiums that are arguably embedded in the water median multiple should not apply to AWK. In addition, we are cognization of the fact that water utilities as a whole trade at roughly 55% premiums to regulated electric and gas peers.

AWR Thesis: We regard AWR as a low risk water utility with a growing dividend that operates under generally constructive CA regulatory principles. That said, the overall constructiveness of CA regulation has been called into question recently and bears monitoring. On the non-regulated side, we believe ASUS could contribute 20-25% to consolidated EPS with upside potential if new military contracts are awarded. Our Equal Weight rating reflects valuation considerations as shares trade at roughly 10% P/E premiums to water utility peers on our 21E & 22E EPS. We consider a 5-10% premium warranted as AWR has the industry's strongest balance sheet and credit metrics (no new equity is needed) as well as a good financial track record (management consistently executes/delivers strong results). However, those positives are partially by offset by an EPS CAGR (6-7%) that is largely commensurate with peers and heightened regulatory risk.

SJW Thesis: We regard SJW as a relatively low-risk water utility with a secure and growing dividend. Despite the CTWS merger which added regulatory diversity, roughly 60% of utility earnings are derived from California. As such, SJW remains highly dependent upon California regulation which offers the state's utilities generally constructive regulatory principles. That said, the constructiveness of CA regulation has been called into question recently and SJW's lack of a full decoupling mechanism exposes earnings to a degree of volatility that other CA water utilities do not currently face. Our Equal Weight rating is premised on the fact that, given recent outperformance, shares of SJW now trade at only 7-8% discounts to "pure play" water utility peers on our 21E & 22E EPS. While we think shares could continue to "re-rate" a little more over time, the pathway and timing combined with the magnitude of upside is less compelling from a risk/reward standpoint today.

Required Disclosures

SJW Group (SJW) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	1/28/2019		Reeder				
◆	1/28/2019	58.50	1	70	NE	NE	58.43
●	2/21/2019	61.24	1	74	NE	NE	61.24
●	4/25/2019	60.66	1	72	NE	NE	60.66
●	7/5/2019	62.79	1	76	NE	NE	63.75
●	9/2/2019	68.33	1	80	NE	NE	68.33
●	3/11/2020	66.10	1	78	NE	NE	61.08
●	5/5/2020	58.80	1	67	NE	NE	58.24
●	8/7/2020	70.04	1	76	NE	NE	70.04
▼	8/11/2020	71.06	2	76	NE	NE	66.43

*Effective December 7, 2019, Wells Fargo Securities' Equity Research modified its ratings definitions. Complete definitions of current ratings can be found below. For information related to prior ratings definitions, please contact equityresearch1@wellsfargo.com.

Source: Wells Fargo Securities, LLC estimates and Reuters data

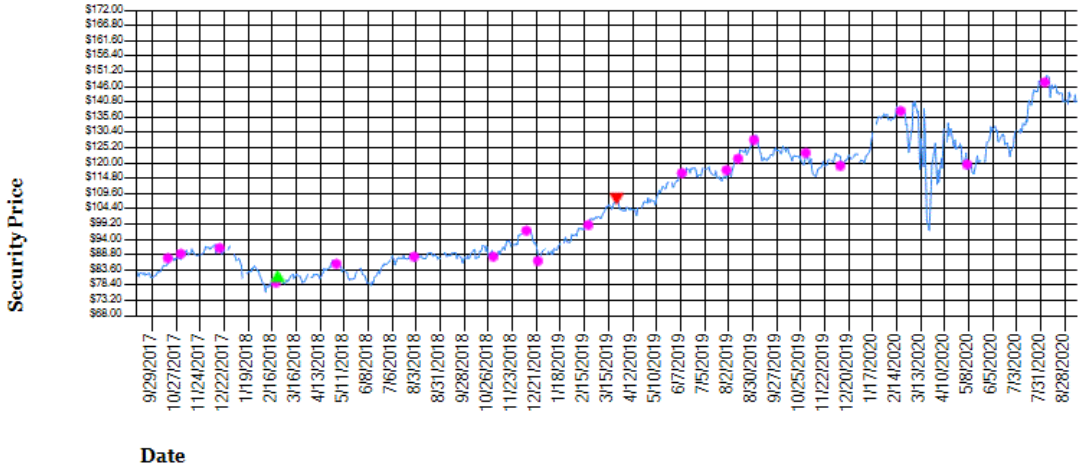
Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

American Water Works Company, Inc. (AWK) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	9/11/2017		Reeder				
	9/11/2017	NA	2	84	NE	NE	82.92
●	10/19/2017	86.22	2	89	NE	NE	87.24
●	11/3/2017	89.45	2	92	NE	NE	88.76
●	12/18/2017	90.82	2	95	NE	NE	90.49
●	2/21/2018	78.85	2	83	NE	NE	78.85
▲●	2/25/2018	80.63	1	88	NE	NE	80.63
●	5/3/2018	85.29	1	95	NE	NE	85.29
●	8/2/2018	87.54	1	100	NE	NE	87.54
●	11/2/2018	88.33	1	97	NE	NE	87.38
●	12/11/2018	96.48	1	104	NE	NE	96.48
●	12/24/2018	91.19	1	101	NE	NE	86.31
●	2/20/2019	98.66	1	109	NE	NE	98.66
▼●	3/26/2019	107.20	2	111	NE	NE	107.20
●	6/9/2019	116.29	2	120	NE	NE	116.29
●	8/1/2019	117.02	2	122	NE	NE	117.02
●	8/14/2019	121.83	2	128	NE	NE	121.20
●	9/2/2019	127.32	2	133	NE	NE	127.32
●	11/1/2019	123.27	2	131	NE	NE	122.78
●	12/12/2019	118.44	2	128	NE	NE	118.43
●	2/20/2020	138.70	2	147	NE	NE	137.30
●	5/7/2020	120.74	2	125	NE	NE	119.08
●	8/6/2020	146.93	2	136	NE	NE	146.97

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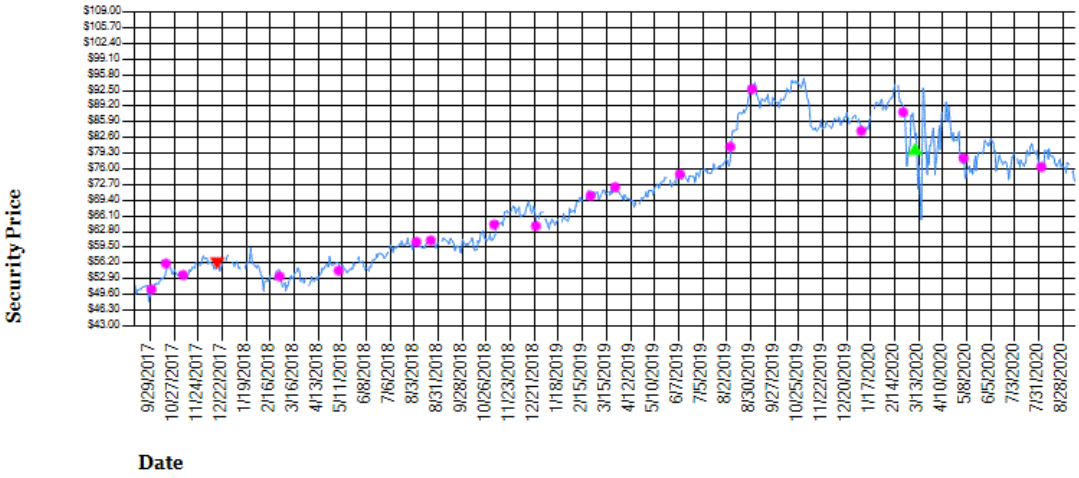
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

American States Water Company (AWR) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	9/11/2017		Reeder				
	9/11/2017	NA	2	46	NE	NE	51.53
●	10/2/2017	49.96	2	48	NE	NE	50.40
●	10/19/2017	55.03	2	51	NE	NE	55.85
●	11/7/2017	53.44	2	50	NE	NE	53.44
▼	12/18/2017	56.68	3	50	NE	NE	55.62
●	2/28/2018	54.29	3	48	NE	NE	53.12
●	5/8/2018	54.42	3	49	NE	NE	54.42
●	8/7/2018	59.98	3	54	NE	NE	60.51
●	8/24/2018	61.06	3	52	NE	NE	60.81
●	11/6/2018	64.05	3	56	NE	NE	64.05
●	12/24/2018	67.38	3	58	NE	NE	63.65
●	2/26/2019	70.12	3	62	NE	NE	70.13
●	3/26/2019	71.94	3	63	NE	NE	71.94
●	6/9/2019	74.72	3	67	NE	NE	74.72
●	8/7/2019	80.41	3	72	NE	NE	80.41
●	9/2/2019	92.53	3	77	NE	NE	92.53
●	1/8/2020	83.59	3	78	NE	NE	83.59
●	2/25/2020	87.67	3	87	NE	NE	87.67
▲●	3/11/2020	83.47	2	84	NE	NE	79.80
●	5/5/2020	77.96	2	76	NE	NE	77.96
●	8/4/2020	76.03	2	79	NE	NE	76.03

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- ❒ Split Adjustment

Rating Code Key

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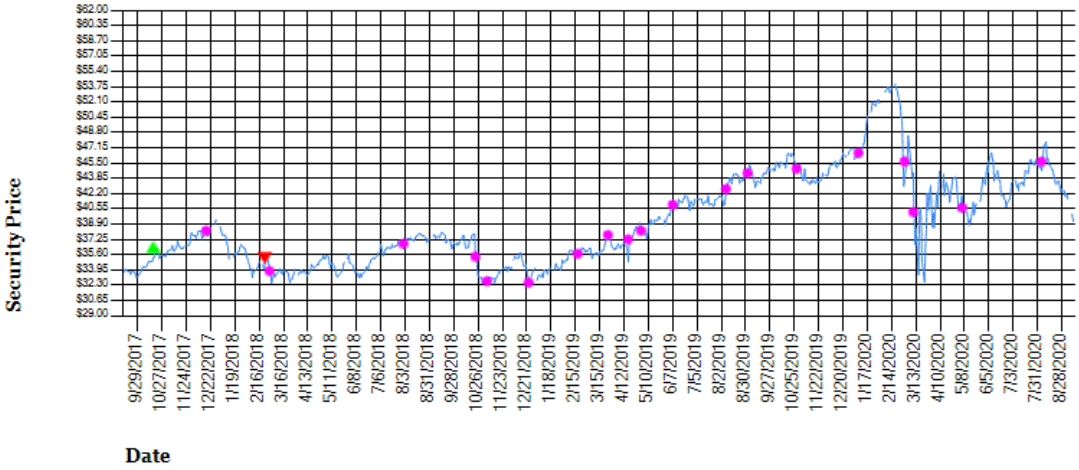
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	9/12/2017		Reeder				
	9/12/2017	NA	2	35	NE	NE	33.88
▲●	10/19/2017	35.30	1	40	NE	NE	36.03
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51
●	3/2/2020	43.01	2	45	NE	NE	45.44
●	3/11/2020	44.41	2	48	NE	NE	40.03
●	5/7/2020	40.49	2	42	NE	NE	40.53
●	8/6/2020	45.56	2	45	NE	NE	45.56

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Additional Information Available Upon Request

I certify that:

1) All views expressed in this research report accurately reflect my personal views about any and all of the subject securities or issuers discussed; and
2) No part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by me in this research report.

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- Wells Fargo Securities, LLC is currently acting as financial advisor to American Water Works Company, Inc. in the announced sale of its regulated New York operations to Liberty Utilities, the regulated utility business of parent company Algonquin Power & Utilities Corp. This transaction is subject to regulatory approval.
- Essential Utilities, Inc. currently is, or during the 12 month period preceding the date of distribution of the research report was, a client of Wells Fargo Securities, LLC. Wells Fargo Securities, LLC provided investment banking services to Essential Utilities, Inc..
- Wells Fargo Securities, LLC or its affiliates received compensation for investment banking services from Essential Utilities, Inc. in the past 12 months.
- Wells Fargo Securities, LLC or its affiliates received compensation for investment banking services from an affiliate of American Water Works Company, Inc. in the past 12 months.
- Wells Fargo Securities, LLC, or any of its affiliates, intends to seek or expects to receive compensation for investment banking services from American Water Works Company, Inc., Essential Utilities, Inc. in the next three months.
- Wells Fargo Securities, LLC or its affiliates intends to seek or expects to receive compensation for investment banking services in the next three months from an affiliate of American Water Works Company, Inc.
- Wells Fargo Securities, LLC, or its affiliates, managed or co-managed a public offering of securities for Essential Utilities, Inc. within the past 12 months.
- Wells Fargo Securities, LLC or its affiliates managed or co managed a public offering of securities for an affiliate of American Water Works Company, Inc. within the past 12 months
- Wells Fargo Securities, LLC maintains a market in the common stock of American States Water Company, American Water Works Company, Inc., Essential Utilities, Inc., SJW Group.
- Wells Fargo Securities, LLC or its affiliates has a significant financial interest in American States Water Company, American Water Works Company, Inc., Essential Utilities, Inc..

AWK: Key risks include regulatory and profitably executing the non-regulated and tuck-in acquisition growth strategies.
AWR: Key risks include California regulatory, lack of geographical diversity and ASUS construction levels.
SJW: Key risks include regulatory, CTWS acquisition related and potential to aggressively pursue additional M&A growth.
WTRG: Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

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STOCK RATING
1=Overweight: Total return on stock expected to be 10%+ over the next 12 months. BUY
2=Equal Weight: Total return on stock expected to be 0-10% over the next 12 months. HOLD
3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

VOLATILITY RATING
V = A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: September 14, 2020

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40% of companies covered by Wells Fargo Securities, LLC Equity Research are rated Equal Weight.	Wells Fargo Securities, LLC has provided investment banking services for 34% of its Equity Research Equal Weight-rated companies.
10% of companies covered by Wells Fargo Securities, LLC Equity Research are rated Underweight.	Wells Fargo Securities, LLC has provided investment banking services for 30% of its Equity Research Underweight-rated companies.

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Essential Utilities Inc. (WTRG): Secular water growth opportunity still under-appreciated; reiterate Buy (on CL)

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We reiterate our Buy rating (on Conviction List) on regulated water/gas utility Essential Utilities (WTRG) following 3Q2020 and a positive guidance revision. As highlighted in our recent upgrade note, we continue to see WTRG as a secular winner to benefit from an estimated $750 billion of water infrastructure investment needs (per the EPA) in a very fragmented market. This represents at least a $7bn opportunity – well above its total current water asset base – excluding any market share gains through municipal and other water utility acquisitions.

We see the market valuing WTRG as a 60% gas utility despite its 70% water earnings composition, given the current 6x (20%) P/E discount for the company's water utility segment versus the only other large-cap water utility American Water (AWK, Buy). With WTRG's normalized EPS growth potential similar to AWK's, one of the highest in our coverage universe, and management's strategy to further increase its water utility exposure over time, we believe WTRG deserves a premium valuation to reflect its high growth, largely ESG-friendly profile.

Below we highlight some key takeaways from the 3Q20 earnings call:

- **WTRG continues to benefit from work-from-home (WFH) demand trends.** The company recorded net positive demand at its utilities in both 2Q20 and 3Q20, given the vast majority of its revenues come from its residential customer base, which more than offset declines in commercial and industrial demand. We see this as a positive indicator of its ability to weather covid-related demand changes, which also allowed WTRG to raise its 2020 guidance to the top end of its range. We raise our 2020 EPS to $1.57 from $1.55 partly to reflect this benefit, while our 2021-2022 estimates remain unchanged.
- **Peoples Gas remains a one-off gas utility acquisition.** Management reiterated that the recent acquisition of PA-based Peoples Gas made sense based on its robust organic growth through decarbonizing gas pipe replacements, as well as its favorable geographic position in the heart of the Marcellus shale that provides low-cost for a region where gas remains a complementary energy source for the long-term. That said, they confirmed that future inorganic growth will only come from municipal water system acquisitions. We see WTRG's 70% water utility earnings exposure that should grow over time as still warranting closer to a water utility premium average.

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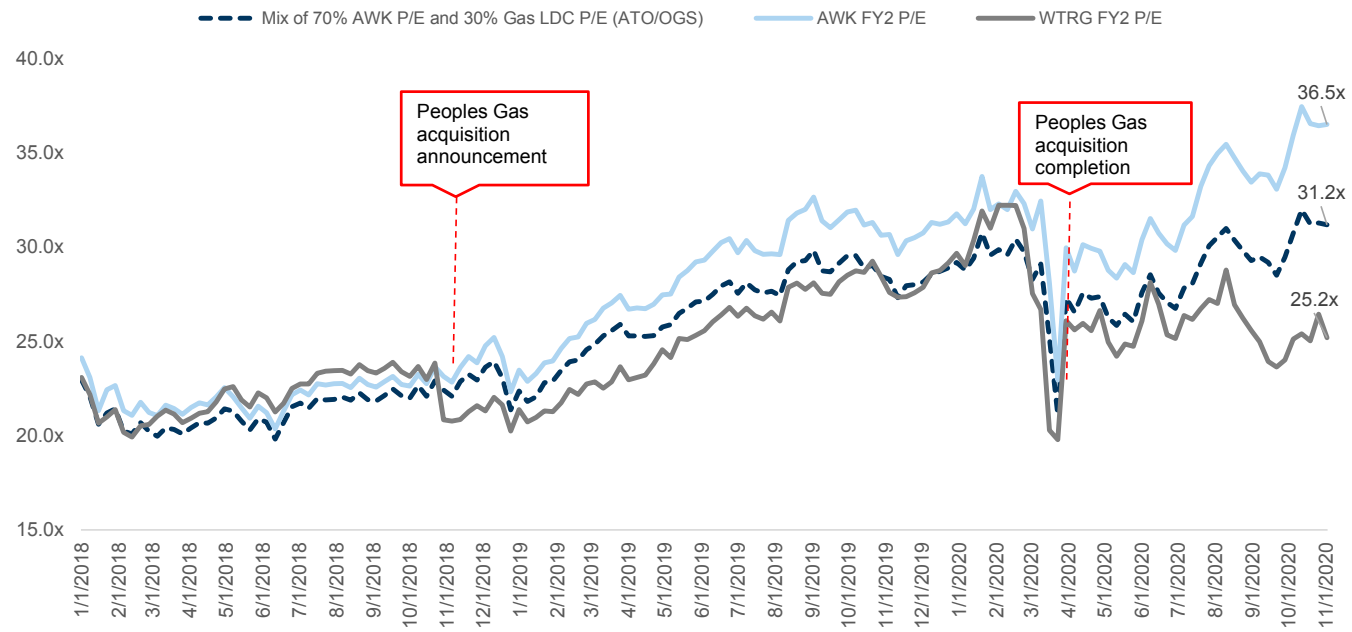
- **Management still expects the DELCORA wastewater acquisition to close in 1H2021.** While awaiting the outcome on the validity of the asset purchase agreement for the proposed acquisition, management remains confident in their ability to close the deal by March or April 2021. We believe WTRG's pipeline of potential acquisitions should still enable the company to sustain its inorganic growth even if the DELCORA deal does not materialize, with ~$300mn in forward equity already priced to help finance the additions. Our model continues to assume 1Q2021 issuance for the equity.

Our $51 12-month price target (unchanged) is based on a SOTP approach, with 35x/22x P/E applied to our 2021 water/gas utility EPS estimates, respectively. **Downside risks to our call include:** 1) PA regulation turns less constructive, which impacts earnings growth potential given the bulk of WTRG's earnings are derived from the state's water/gas operations, 2) the proposed DELCORA municipal water system acquisition fails to receive necessary approvals for completion, which could impact longer-term water rate base growth outlook barring replacement with other municipal acquisitions, and 3) longer-term growth concerns about the gas utility segment further compresses WTRG's valuation, both on an absolute basis and relative to pure-play water utilities.

Exhibit 1: We continue to view WTRG's meaningful relative P/E discount as unwarranted based on its 70%/30% water/gas profile...
FY2 P/E for AWK, WTRG, and an illustrative performance of a 70%/30% water/gas utility



ATO/OGS chosen as illustrative gas utility comps based on company profile, including their status as the two largest gas LDCs by market cap

Source: FactSet, Goldman Sachs Global Investment Research

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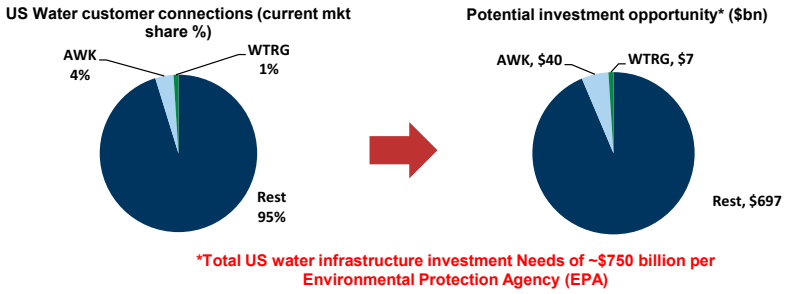
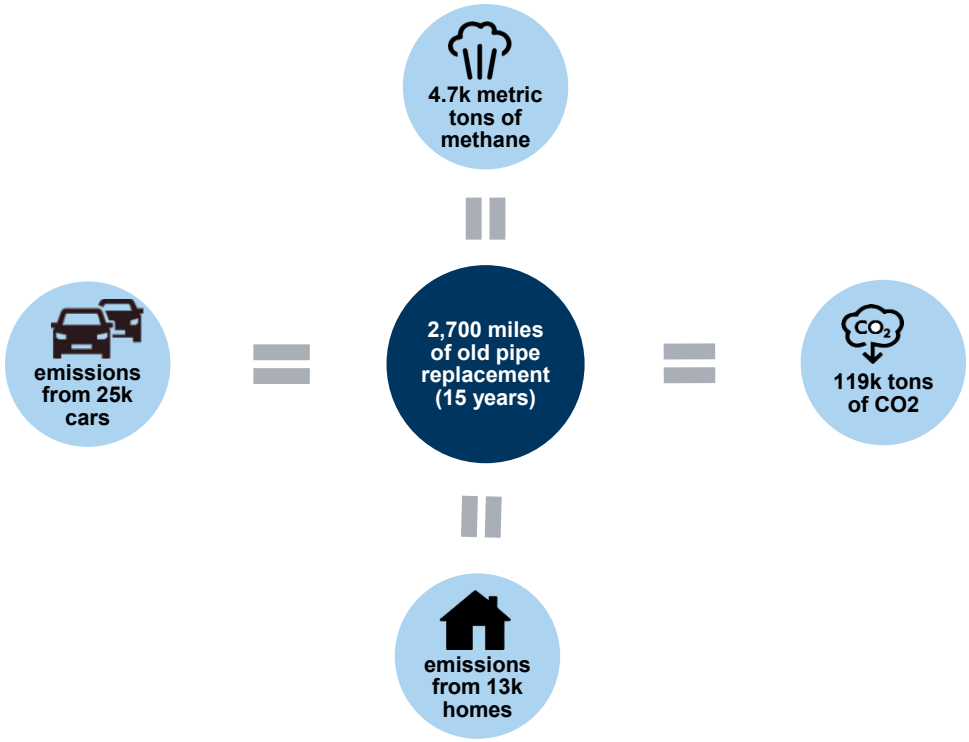
Exhibit 2: ...given a robust long-term visibility of water utility investments that could support at least a $7bn opportunity for WTRG at current market share, well above its total current water asset base...
US water investment needs, potential opportunity for WTRG/AWK



Source: Company data, Goldman Sachs Global Investment Research, EPA

Exhibit 3: ...along with aging gas infrastructure replacement that supports de-carbonization
Potential emission reductions from aging gas pipe replacement



Old pipe replacement refers to bare steel and cast iron pipes

Source: Goldman Sachs Global Investment Research, Company data

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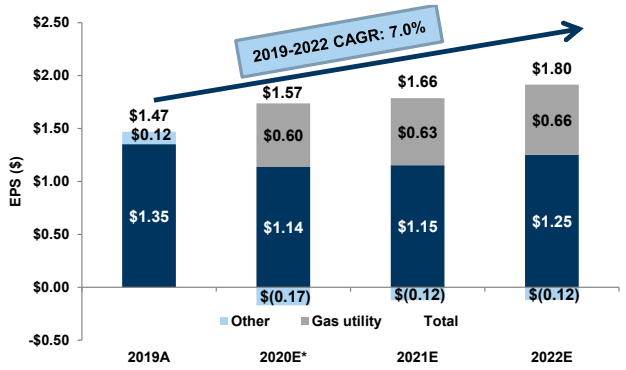
Exhibit 4: We raise our 2020 EPS estimate to reflect better YTD demand, while 2021/2022 estimates remain unchanged...
GSe vs Consensus

	EPS Estimates			% Difference	
	New	Old	Consensus	vs Old	vs Consensus
2019A	$1.47	$1.47	$1.47	0%	0%
2020E	$1.57	$1.55	$1.56	1%	1%
2021E	$1.66	$1.66	$1.66	0%	0%
2022E	$1.80	$1.80	$1.79	0%	0%

Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 5: ...reflecting a robust 7% EPS CAGR through 2022
EPS 2019A-2022E



Source: Goldman Sachs Global Investment Research, Company data

Exhibit 6: Our SOTP-based $51 price target reflects a 23% total return potential versus 10% for Regulated Utilities
WTRG SOTP Valuation

VALUATION	
Water utility EPS 2021	**1.15**
Water utility multiple	30.00x
Assumed premium	5.00x
Adjusted P/E	35.0x
Water utility valuation	**40.36**
Gas utility EPS 2021	**0.63**
Gas utility multiple	20.00x
Assumed premium	2.00x
Adjusted P/E	22.0x
Gas utility valuation	**13.95**
Valuation - Other	**(0.12)**
2020 Blended multiple	30.39x
Other valuation	**(3.73)**
Total valuation	**51.00**
Current price per share	$42.33
Return potential	**20.48%**
Dividend yield	2.21%
Total return potential	**23%**

Share Price as of 11/3/2020 Close

Source: Goldman Sachs Global Investment Research

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WTRG	12m Price Target: **$51.00**	Price: **$41.19**	Upside: **23.8%**

Buy CL

Market cap: $10.5bn
Enterprise value: $16.0bn
3m ADTV: $52.1mn
United States
Americas Utilities
M&A Rank: 3
Americas Conviction List

GS Forecast

	12/19	12/20E	12/21E	12/22E
Revenue ($ mn) New	**889.7**	**1,573.0**	**1,997.2**	**2,114.9**
Revenue ($ mn) Old	889.7	1,571.7	1,995.4	2,113.5
EBITDA ($ mn)	521.4	769.5	1,049.3	1,123.6
EBIT ($ mn)	360.8	514.7	757.0	801.7
EPS ($) New	**1.47**	**1.57**	**1.66**	**1.80**
EPS ($) Old	1.47	1.55	1.66	1.80
P/E (X)	27.6	26.3	24.7	22.9
Dividend yield (%)	2.2	2.4	2.5	2.7
Net debt/EBITDA (X)	2.3	7.2	6.0	6.1

	6/20	9/20E	12/20E	3/21E
EPS ($)	0.29	0.23	0.45	0.69

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 4 Nov 2020 close.

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Reg AC

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Growth is based on a stock's forward-looking sales growth, EBITDA growth and EPS growth (for financial stocks, only EPS and sales growth), with a higher percentile indicating a higher growth company. **Financial Returns** is based on a stock's forward-looking ROE, ROCE and CROCI (for financial stocks, only ROE), with a higher percentile indicating a company with higher financial returns. **Multiple** is based on a stock's forward-looking P/E, P/B, price/dividend (P/D), EV/EBITDA, EV/FCF and EV/Debt Adjusted Cash Flow (DACF) (for financial stocks, only P/E, P/B and P/D), with a higher percentile indicating a stock trading at a higher multiple. The **Integrated** percentile is calculated as the average of the Growth percentile, Financial Returns percentile and (100% - Multiple percentile).

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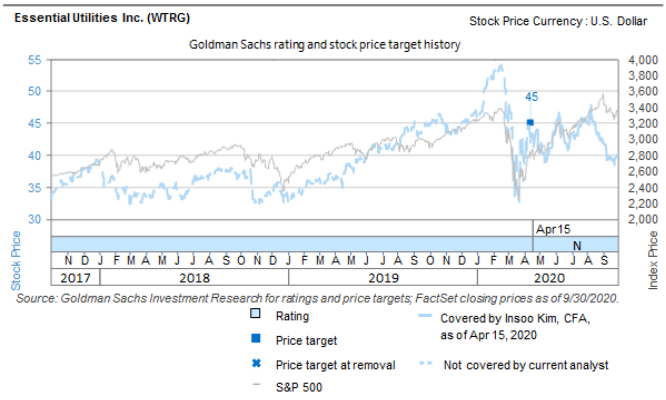

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HSBC Global Research

28 May 2020

Essential Utilities (WTRG US)

Buy: Current challenges a catalyst for integration

Equities
Water Utilities

United States

- Challenges in US water – how Essential is responding
- Guidance intact; bond proxy status unaltered
- Maintain Buy rating and USD50 target price

Growth strategy: Essential Utilities has a 3-pronged growth strategy: A growing core water and wastewater business; opportunistic pursuit of large, regulated utility/infrastructure targets – the company delivered on this with the Peoples gas acquisition (recently completed) and the DELCORA waste water transaction, which is expected to complete regulatory approvals by 2022; and MBAs (Market Based Activities), which are probably going to be less of a priority given the current challenges.

COVID-19 challenges: We analyse the risks to Essential from COVID-19 – many of these are mitigated by its large residential customer base. During its Q1 earnings call, management explained that the Peoples acquisition had been completed on the day that the US went into COVID-19 lockdown. This was a catalyst for harmonising business practices across the two separate businesses, so corporate integration might be quicker than otherwise expected. Its 2020 guidance remains: 2020 EPS of USD1.53 to USD1.58, and 2019-22e earnings CAGR of 5% to 7%.

Bond proxy: Essential's share price has outperformed the S&P 500 by 1% since 1 January 2019. It is trading at a discount to its water peer group's 2020e PE, but in line with some of the US electricity utilities, according to Refinitiv Datastream. This reflects, in our view, its multi-utility status. The US Treasury 10-year yield has fallen sharply. WTRG, as a defensive utility, should be inversely correlated to bond yields.

Maintain Buy rating and target price of USD50: We value Essential Utilities via three methodologies: DCF, dividend yield, and the average of PE multiple and rate-based valuations: We now adopt a lower 2.5% risk-free rate (from 3.0%) set by our equity strategists and used for the other US utilities under our coverage. We maintain our equity risk premium and beta assumptions of 3% and 0.60, respectively. Our DCF valuation increases to USD50.0 (from USD41.1). In our PE multiple-based valuation, we maintain our target multiple in line with market peers, at 30.0x. We use an unchanged water peer group P/B of 2.4x as a proxy for a rate-base valuation. This is consistent with the US utilities under our coverage and a proxy for EV. The average of our PE and rate-based valuations adjusts to USD51.6 (from USD51.9). For our Yield-based valuation, we increase our target yield to 2.13% from 1.75%, in line with Water and Related Utilities peers. This results in a lower Yield-based valuation of USD47.5 (from USD57.8). Overall, these valuations lead to an unchanged TP of USD50.00, which implies 21.0% upside. Consequently, we maintain our Buy rating.

MAINTAIN BUY

TARGET PRICE (USD)	PREVIOUS TARGET (USD)
50.00	**50.00**
SHARE PRICE (USD)	UPSIDE/DOWNSIDE
41.31	**+21.0%**
(as of 26 May 2020)	

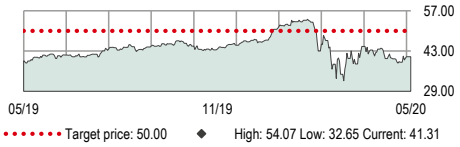
MARKET DATA

Market cap (USDm)	10,123	Free float	100%
Market cap (USDm)	10,123	BBG	WTRG US
3m ADTV (USDm)	59	RIC	WTRG.N

FINANCIALS AND RATIOS (USD)

Year to	12/2019a	12/2020e	12/2021e	12/2022e
HSBC EPS	1.04	1.55	1.67	1.79
HSBC EPS (prev)	1.04	1.56	1.68	1.81
Change (%)	0.0	-0.9	-0.2	-1.2
Consensus EPS	1.48	1.48	1.66	1.80
PE (x)	39.7	26.7	24.7	23.1
Dividend yield (%)	2.3	2.5	2.6	2.9
EV/EBITDA (x)	22.8	17.8	16.5	15.7
ROE (%)	7.6	8.3	7.5	7.6

52-WEEK PRICE (USD)



Source: Refinitiv IBES, HSBC estimates

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Financials & valuation: Essential Utilities

Buy

Financial statements

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Profit & loss summary (USDm)				
Revenue	890	1,884	2,144	2,278
EBITDA	497	817	913	993
Depreciation & amortisation	-157	-239	-267	-292
Operating profit/EBIT	340	578	646	701
Net interest	-131	-150	-170	-192
PBT	212	428	476	509
HSBC PBT	209	428	476	509
Taxation	13	-34	-38	-41
Net profit	225	394	438	469
HSBC net profit	225	394	438	469
Cash flow summary (USDm)				
Cash flow from operations	339	702	723	770
Capex	-550	-950	-1,000	-1,000
Cash flow from investment	-605	-5,225	-1,277	-1,000
Dividends	-189	-257	-286	-309
Change in net debt	-1,352	3,191	540	539
FCF equity	-212	-248	-277	-230
Balance sheet summary (USDm)				
Intangible fixed assets	64	939	939	939
Tangible fixed assets	7,224	11,335	12,345	13,053
Current assets	2,011	2,152	2,189	2,208
Cash & others	1,869	1,869	1,869	1,869
Total assets	9,360	14,488	15,534	16,261
Operating liabilities	1,468	1,678	1,733	1,761
Gross debt	3,077	6,269	6,809	7,347
Net debt	1,208	4,400	4,940	5,478
Shareholders' funds	3,881	5,606	6,058	6,218
Invested capital	5,962	10,879	11,871	12,569

Ratio, growth and per share analysis

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Y-o-y % change				
Revenue	6.2	111.8	13.8	6.3
EBITDA	5.7	64.4	11.8	8.8
Operating profit	5.3	69.9	11.8	8.4
PBT	18.6	102.4	11.2	7.0
HSBC EPS	-3.4	48.9	8.1	7.0
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	6.4	6.3	5.2	5.3
ROE	7.6	8.3	7.5	7.6
ROA	4.1	4.5	4.0	4.1
EBITDA margin	55.9	43.4	42.6	43.6
Operating profit margin	38.2	30.7	30.2	30.8
EBITDA/net interest (x)	3.8	5.4	5.4	5.2
Net debt/equity	31.1	78.5	81.5	88.1
Net debt/EBITDA (x)	2.4	5.4	5.4	5.5
CF from operations/net debt	28.0	16.0	14.6	14.1
Per share data (USD)				
EPS Rep (diluted)	1.04	1.55	1.67	1.79
HSBC EPS (diluted)	1.04	1.55	1.67	1.79
DPS	0.94	1.01	1.09	1.18
Book value	17.97	22.04	23.15	23.76

Valuation data

Year to	12/2019a	12/2020e	12/2021e	12/2022e
EV/sales	12.7	7.7	7.0	6.8
EV/EBITDA	22.8	17.8	16.5	15.7
EV/IC	1.9	1.3	1.3	1.2
PE*	39.7	26.7	24.7	23.1
PB	2.3	1.9	1.8	1.7
FCF yield (%)	-2.1	-2.5	-2.7	-2.3
Dividend yield (%)	2.3	2.5	2.6	2.9

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2019a
GHG emission intensity*	n/a
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social Indicators	**12/2019a**
Employee costs as % of revenues	n/a
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	12/2019a
No. of board members	8
Average board tenure (years)	7.0
Female board members (%)	25
Board members independence (%)	87.5

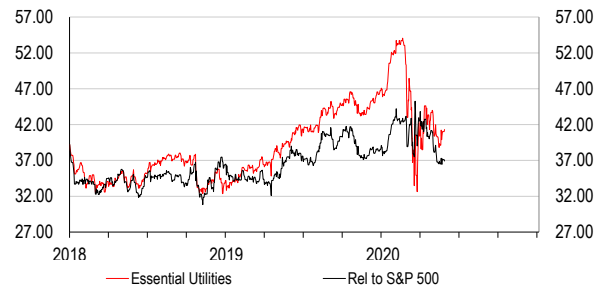
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	41.31	Free float	100%
Target price (USD)	50.00	Sector	Water Utilities
RIC (Equity)	WTRG.N	Country/Region	United States
Bloomberg (Equity)	WTRG US	Analyst	Verity Mitchell
Market cap (USDm)	10,123	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 26 May 2020

Current challenges a catalyst for integration

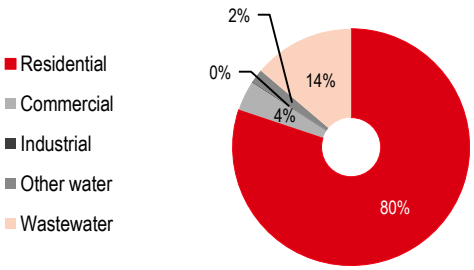
- Challenges in US water – how Essential is responding
- Guidance intact; bond proxy status unaltered
- Maintain Buy rating and USD50 target price

Investment summary: Three-pronged approach

Essential Utilities has core competencies in infrastructure investment (pipes and water production plant), regulatory affairs, and operations. Using these as pillars, Essential has created a 3- pronged growth strategy:

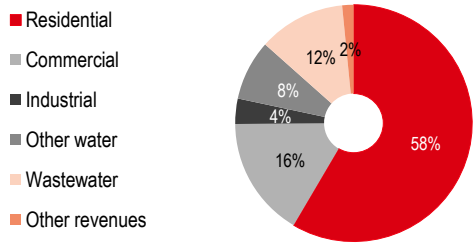
1. Municipal initiative: A growing core water and wastewater business - Aqua. This remains the primary focus for the company;
2. Strategic M&A: Opportunistic pursuit of large, regulated utility/infrastructure targets – the company delivered on this with the Peoples gas acquisition (recently completed) and the DELCORA waste water transaction, which is expected to complete regulatory approvals by 2022.
3. MBAs (Market Based Activities): Complementary to the regulated businesses. Capitalises on broader infrastructure renewals, but are probably going to be less of a priority given the current challenges.

Customer composition at FY2019



Source: Essential Utilities - company presentation data

Revenue composition at FY2019



Source: Essential Utilities - company presentation data

Quick integration

During its Q1 earnings call, management explained that the Peoples acquisition had been completed on the day that the US went into COVID-19 lockdown. This was a catalyst for harmonising business practices across the two separate businesses in order to protect staff, and continue to deliver essential services. This has meant that corporate integration might be quicker than otherwise expected for the two companies.

COVID-19 pandemic related risks for US water and gas utilities

Essential Utilities is a stable company with regulated revenue base. However, it is not completely immune to the impending economic downturn. We highlight some of these risks as follows, how material they are, and discuss how the company is addressing and mitigating them.

- **Customer delinquencies:** Water and gas utilities are expected to experience an increase in customers being delinquent in paying their water bills. However, water utilities will have to continue to provide water to these delinquent customers rather than enact shut-offs. Hence, companies will incur additional costs.
- **Revenue shortfall:** US utilities are likely to experience some revenue shortfall due to declines in commercial, industrial, and institutional water consumption. This revenue shortfall may be offset by an increase in residential user charge revenue due to “stay-at-home” orders. Essential receives only 20% of its revenues from commercial and industrial customers. In April, according to management on the Q1 call, the company saw increased domestic demand from the shutdown offsetting much of the commercial and industrial volume reductions. The same principle applied in the Peoples business.
- **Reduced system development charges:** The COVID-19 crisis may slow the growth in new development and housing starts, which will impact the financial losses of water and gas utilities. A slowing of new customer growth would reduce new system development. Essential however, given its scale, still has growth from infrastructure rehabilitation for its existing customer rate base.
- **Increased personnel expenses:** There may well be some potential for additional costs associated with the pandemic such as for PPE. The company said during the Q1 that these expenses are relatively immaterial.
- **Delayed and reduced capital expenditures:** At Q1, management said only cUSD30m of project work had been delayed compared with its cUSD1bn of capital expenditure run rate.
- **Deferred water and gas rate increases:** Utilities may also experience future revenue losses as a result of deferrals of planned rate increases. These deferrals may exacerbate community economic impacts by further reducing utility capital spending and put the utility sector further behind in addressing its capital infrastructure needs. Essential has pending rate cases in Indiana, New Jersey, North Carolina, and Ohio, with total annualised revenue increase of USD10.1m. Rate cases appear to be proceeding on track and there is no indication of deferrals as yet. Given the rate cases proposed are relatively modest we do not see this as a risk.

Q1 2020 summary

Essential Utilities hosted a conference call for Q1 2020 earnings on 7 May 2020.

- Essential invested USD118.7m in the first three months. This does not include an additional USD53.5m that was invested by Peoples.
- It closed its acquisition of the water system of Campbell, Ohio; a utility with approximately 3,100 customer connections. For the quarter, customer growth for the company's water utilities totalled 0.6%, including organic growth.
- As a preventive measure to address liquidity concerns related to COVID-19 and its potential economic and capital markets impacts, the company secured and borrowed an additional USD500m on a 364-day term loan in early April 2020.

Outlook: FY2020 outlook reiterated

Essential reiterated its FY2020 outlook as follows:

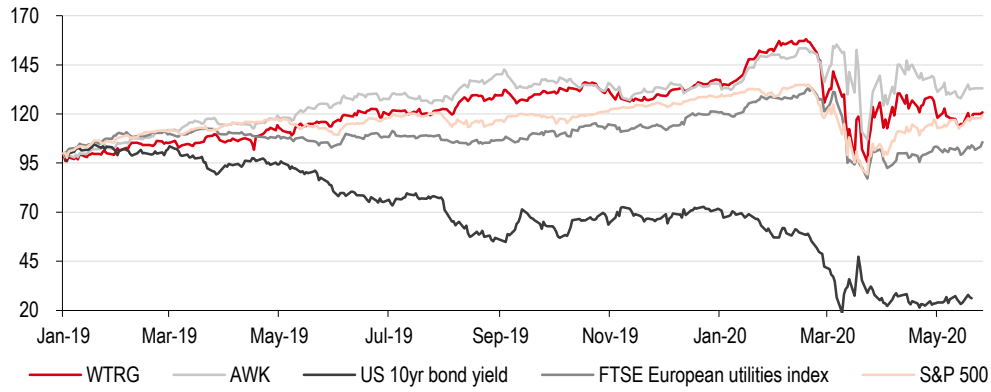
- Essential has signed purchase agreements for other municipal water and wastewater acquisitions that are expected to add the equivalent of over 205,000 water and wastewater retail customers, and approximately USD327m in expected rate base.
- Adjusted income per diluted common share (non-GAAP) of USD1.53 to USD1.58
- 2019-22e earnings CAGR of 5 to 7%
- Regulated water segment infrastructure investments of cUSD550m in 2020
- Regulated natural gas segment infrastructure investments of cUSD400m in 2020 on a full-year basis (adjusted to include capital invested in 2020 prior to Essential's ownership)
- Infrastructure investments of approximately USD2.8bn through 2022 in existing operations to rehabilitate and strengthen water, wastewater, and natural gas systems (including regulated natural gas segment capital invested in 2020 prior to Essential's ownership)
- 2019-22e regulated water segment rate base CAGR of 6% to 7%
- 2019-22e regulated natural gas segment rate base CAGR of 8 to 10%
- Total annual regulated water segment customer growth of between 2% and 3% on average depending upon regulatory approval
- Gas customer count expected to be relatively stable for 2020.

Performance against peers

Essential's share price has outperformed the S&P 500 by 2% since 1 January 2019. It is trading at a discount to its water peer group's 2020e PE, but in line with some of the US electricity utilities according to Refinitiv Datastream. This reflects, in our view, its multi-utility status.

The US Treasury 10-year yield has fallen sharply. WTRG, as a defensive utility, should be inversely correlated to bond yields.

WTRG vs AWK vs UST 10yr bond yield vs FTSE European utilities index vs S&P500



Source: Refinitiv Datastream

Credit metrics analysis

According to Moody's, WTRG needs to maintain its RCF/ net debt ratio in the range of 7%-14% and FFO/ net debt in the range of 11%-18% to maintain its Baa2 credit rating.

During the Q1 2020 conference call, Essential said that as the equity markets recover, the company will look for the appropriate time to issue approximately USD300m of equity in later 2020 or early 2021. That equity, as first mentioned on the Investor Day, is necessary to appropriately capitalise DELCORA and other acquisitions in the pipeline.

We have modelled for this equity issuance as well as completion of this acquisition in 2021. Given the increased equity, the company's credit metrics appear to remain in the target metric range for the current credit rating.

Credit metrics analysis

	2020e	2021e	2022e
RCF/ net debt	8.6%	8.5%	8.3%
FFO/ net debt	14.5%	14.3%	14.0%

Source: HSBC estimates

Change in estimates

We have updated our estimates post the Q1 2020 results posted on 7 May 2020. We have also updated our model for USD300m of equity offering, which has increased our number of shares outstanding and lowered our net debt assumptions for 2021e.

We continue to use pro-forma 2020 assumptions to smooth the effect of the costs and timing of the Peoples deal, excluding transaction costs and assuming the deal was completed to benefit from the gas heating season on a normalised weather basis. This is the basis on which Essential will report its underlying results.

Changes in estimates (USDm)

	2020e	2021e	2022e
EBIT			
Revised	578	646	701
Previous	585	631	689
Change	*-1%*	*2%*	*2%*
Net income			
Revised	394	438	469
Previous	397	426	461
Change	*-1%*	*3%*	*2%*
EPS (USD)			
Revised	1.55	1.67	1.79
Previous	1.56	1.68	1.81
Change	*-1%*	*0%*	*-1%*
DPS (USD)			
Revised	1.01	1.09	1.18
Previous	1.01	1.09	1.18
Change	*0%*	*0%*	*0%*

Source: HSBC estimates

Valuation and risks

We value Essential Utilities via three methodologies: DCF, dividend yield, and the average of PE multiple and rate-based valuations. Taking the average of the three approaches gives us our target price of USD50.00 (unchanged).

- Previously we had used a 3% risk-free rate, in line with the utility methodology set out in our report *European Utilities: The three Rs: Renewables, low rates and low risk* (20 February 2020). We now adopt the lower HSBC 2.5% set by our equity strategists (see *Cost of Equity*, 10 February 2020) and used for other US utilities under our coverage. Our equity risk premium and beta assumptions remain unchanged at 3% and 0.60, respectively. Our DCF valuation increases to USD50.0 (from USD41.1).
- In our PE multiple-based valuation, we maintain our target multiple in line with market peers, at 30.0x. We use a water peer group P/B of 2.4x (unchanged) as a proxy for a rate-based valuation. This is consistent with all US utilities under our coverage and is a proxy for EV. The average of the two declines to USD51.6 (from USD51.9), reflecting our updated estimates.
- For our Yield-based valuation, we increase our target yield to 2.13% from 1.75%, in line with its Water and Related Utilities peers. This results in a decreased Yield valuation of USD47.5 (from USD57.8).

Overall, these changes lead to an unchanged TP of USD50.00, which implies 21.0% upside; we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

Summary of valuation (USD)

Particulars	New	Previous
Current price as on 26-May-20	**41.3**	**NA**
DCF (updated estimates lower risk-free rate	50.0	41.1
Yield 2.13% from 1.75% (sector average)	47.5	57.8
PE and rate-based (updated estimates)	51.6	51.9
Target price (average rounded)	**50.0**	**50.0**
Upside/ downside to target price	21.0%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity Valuation	USDm
Cost of debt		**+ DCF value**	**16,221**
Pre-tax cost of debt	8.5%	+ ST marketable assets	0
Marginal tax rate	8.0%	+ Value of associates	0
Cost of equity		+ Other assets	878
Risk-free rate (previously 3%)	2.5%	**EV (asset side)**	**17,100**
Equity risk premium	3.0%	- Net debt (+ if Net cash)	(4,371)
Additional risk		- Quasi debt (pension)	0
Beta (unchanged)	**0.60**	- Value of minorities	0
Debt - 39%	7.8%	Total non-equity claims	(4,371)
Equity - 61%	4.8%	Value of equity	12,729
Cost of capital	**5.9%**	**Value per share (USD)**	**50.0**

Source: HSBC estimates

Multiples and rate base (EV) valuation

	2020e rate base
Regulated water	
Pennsylvania	3,682
Ohio	368
Illinois	382
Texas	319
New Jersey	214
North Carolina	245
Indiana	90
Virginia	83
Regulated gas	**2,451**
Total rate base	7,834
Rate-based valuation assuming 2.4x multiple, in line with sector average P/B	**18,802**
Non-regulated 2020 PE multiple	9
Net debt 2020e, pensions & Minority	(4,371)
Estimated equity value	14,440
Estimated equity value per share (USD)	**56.8**
PE Multiple valuation	
2020 earnings	1.55
2020 PE sector average	30.0
Value per share	**46.4**
Average of rate base valuation and PE multiple valuation	**51.6**

Source: HSBC estimates

Downside risks include:

Essential Utilities failing to achieve the desired rate case revisions and infrastructure surcharges; lacking organic growth from asset replacement; inability to take advantage of the Fair Market Value legislation opportunity; dividend growth at a lower rate than we assume; inability to gain the Fair Market Value premium required in the systems it wants to acquire in Pennsylvania. Its current acquisitions of systems – New Garden and Limerick – are facing challenges to the premium proposed by Aqua.

Disclosure appendix

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From 23rd March 2015 HSBC has assigned ratings on the following basis:

The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

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Upside/Downside is the percentage difference between the target price and the share price.

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For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

As of 27 May 2020, the distribution of all independent ratings published by HSBC is as follows:

Buy	55%	(31% of these provided with Investment Banking Services)
Hold	37%	(31% of these provided with Investment Banking Services)
Sell	8%	(22% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

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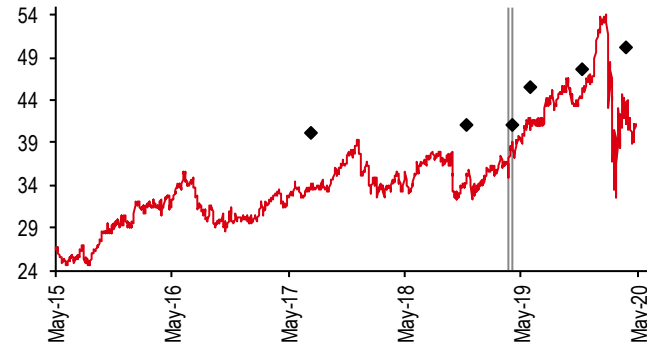
Share price and rating changes for long-term investment opportunities

Essential Utilities (WTRG.N) share price performance USD Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	40.00	08 Aug 2017	Verity Mitchell
Price 2	41.00	06 Dec 2018	Verity Mitchell
Price 3	Restricted	15 Apr 2019	
Price 4	41.00	30 Apr 2019	Verity Mitchell
Price 5	45.50	28 Jun 2019	Verity Mitchell
Price 6	47.50	06 Dec 2019	Verity Mitchell
Price 7	50.00	22 Apr 2020	Verity Mitchell

Source: HSBC

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HSBC & Analyst disclosures

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Company	Ticker	Recent price	Price date	Disclosure
ESSENTIAL UTILITIES	WTRG.N	41.31	26 May 2020	5, 6

Source: HSBC

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[1148009]

First Read

Essential Utilities Inc

Q1'20 EPS $0.60 vs. Consensus $0.60

What happened?

Essential Utilities reported adjusted normalized operating earnings for Q1'20 of $0.60/share. This compares reasonably well with both consensus and UBS estimates of $0.60 and $0.62, respectively. The adjusted and normalized nature of the earnings reflect the closure of the Peoples Gas acquisition on March 16, resulting in 15 days of actual earnings from that subsidiary, and 75 days of estimated assumed normalized earnings. GAAP earnings for the quarter were $0.20. Full year 2020 guidance, which is premised on the same estimated adjusted normalized basis, was affirmed at $1.53-$1.58, as was the long term earnings growth target of 5-7%.

Regulatory & Acquisition Update:

In conjunction with its earnings release, WTRG updated investors on both its ongoing regulatory calendar and water segment acquisitions. With regard to regulatory activities, the company has completed rate case and surcharge proceedings in IL/VA/OH/NC (representing $5.2mm of annualized revenue increases) and has pending cases in IN/NJ/NC/OH (representing $10.1mm of potential annualized increases). The repairs tax benefit in the quarter totalled $5.9mm, the company will be filing for treatment of the 'catch-up' portion over the summer, this 'catch-up' component is not included in current guidance. Year-to-date, WTRG has closed one acquisition (Campbell – rate base $7.5mm) and three acquisitions are pending (New Garden – rate base $29mm/East Norriton – rate base $21mm/DELCORA – rate base $276mm). Management indicated that they continue to see additional, larger, acquisition opportunities.

Operational Update:

Despite a slight pause on some construction projects (PA) management believe they are on track to achieve their capital spending plan for the year of $1.1 billion (water $550mm/gas $400mm). WTRG continues to see potential capital spending opportunities totalling $2.8 billion through 2022.

Valuation:

The unique nature of 2020 guidance and reporting format make interpretation difficult, however, investors should take comfort in the operating performance of the company.

Equities

Americas
Water Utilities

12-month rating	**Neutral**
12m price target	**US$43.00**
Price (06 May 2020)	**US$40.67**

RIC: WTRG.N **BBG:** WTRG US

Trading data and key metrics

52-wk range	US$54.07-32.65
Market cap.	US$7.26bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	455
Avg. daily value (m)	US$19.7
Common s/h equity (12/20E)	US$2.25bn
P/BV (12/20E)	3.2x
Net debt / EBITDA (12/20E)	5.1x

EPS (UBS, diluted) (US$)

	12/20E	
	UBS	Cons.
Q1E	0.62	0.60
Q2E	0.35	0.20
Q3E	0.47	0.27
Q4E	0.13	0.52
12/20E	1.58	1.51
12/21E	1.68	1.65
12/22E	1.79	1.78

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Highlights (US$m)	12/17	12/18	12/19	12/20E	12/21E	12/22E	12/23E	12/24E
Revenues	810	838	881	921	956	995	1,033	1,072
EBIT (UBS)	329	337	370	399	425	454	482	512
Net earnings (UBS)	240	251	265	281	299	319	342	365
EPS (UBS, diluted) (US$)	1.35	1.41	1.48	1.58	1.68	1.79	1.92	2.05
DPS (US$)	0.79	0.88	0.94	1.00	1.07	1.15	1.23	1.32
Net (debt) / cash	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)	(3,378)

Profitability/valuation	12/17	12/18	12/19	12/20E	12/21E	12/22E	12/23E	12/24E
EBIT margin %	40.6	40.3	42.0	43.3	44.5	45.6	46.7	47.7
ROIC (EBIT) %	8.4	7.9	8.0	8.0	8.1	8.3	8.4	8.6
EV/EBITDA (core) x	17.0	17.6	18.7	18.0	17.3	16.6	15.7	15.3
P/E (UBS, diluted) x	24.8	25.0	27.3	25.8	24.3	22.7	21.2	19.9
Equity FCF (UBS) yield %	(1.6)	(1.6)	(1.8)	0.2	0.5	0.9	1.3	1.7
Net dividend yield %	2.4	2.5	2.3	2.5	2.6	2.8	3.0	3.2

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$40.67 on 06 May 2020 19:34 EDT

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Forecast returns

Forecast price appreciation	+5.7%
Forecast dividend yield	2.5%
Forecast stock return	+8.2%
Market return assumption	5.2%
Forecast excess return	+3.0%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 3% discount to the 2021 average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 9% discount to reflect impact of lower P/E associated with gas earnings.

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	48%	32%
Neutral	FSR is between -6% and 6% of the MRA.	40%	28%
Sell	FSR is > 6% below the MRA.	13%	20%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 31 March 2020.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
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UBS Securities LLC: Daniel Ford, CFA; Paul Cole.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Essential Utilities Inc[16]	WTRG.N	Neutral	N/A	US$40.67	06 May 2020

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date
16. UBS Securities LLC makes a market in the securities and/or ADRs of this company.

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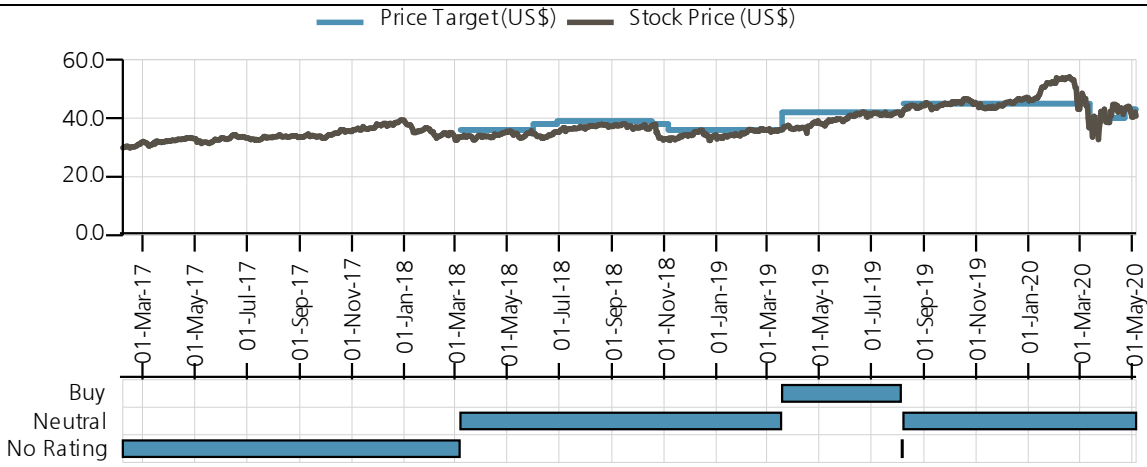
Essential Utilities Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2017-02-06	29.86	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy
2019-08-06	41.15	-	No Rating
2019-08-08	42.47	45.0	Neutral
2020-03-13	38.43	40.0	Neutral
2020-04-23	42.62	43.0	Neutral

Source: UBS; as of 06 May 2020

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WELLS FARGO SECURITIES

Essential Utilities, Inc.

WTRG: M&A In Focus – Close Pending Wastewater Deals w/ New Ones Imminent

Overweight/$47

Water Utilities

Price Target Change

- **Key Points.** WTRG reported solid Q3'20 results aided by higher residential water usage due to favorable weather and COVID has FY2020 EPS trending towards top end of the $1.53-1.58 guidance range. In addition, management indicated roughly $70M of additional tuck-in deals were expected to be announced by YE2020. For our part, we increase our 20E EPS accordingly to $1.58 from $1.56 and bump up our '22 & beyond M&A placeholder to $75M/year of deals rather than $60M given the continued positive momentum on that front. Our 2021-24E EPS of $1.65, $1.78, $1.91 & $2.03 reflects a mid-'21 DELCORA close and results in a 6.6% CAGR off the '19 base of $1.47. If we were to strip out the DELCORA deal, it only has a modest $0.03-0.05 impact (less than 3%) on our '22 & beyond EPS. We reiterate our Overweight rating and increase our 12-18 month price target to $47/share (26.4X our 22E EPS) from $45.
- **Water/Wastewater M&A Update.** In addition to getting the $363M of pending deals closed (represents $0.07 of incremental EPS power), management indicated a handful of new deals are expected to be announced by YE'20 representing $70M of rate base and roughly 10,000 customers. Overall, WTRG is actively pursuing (i.e. having dialogue) municipal acquisition opportunities representing 360,000 customers, the majority of which are wastewater. Management expects the level of discussions/deals to be positively impacted by COVID as municipalities face additional financial and operational challenges and we remain optimistic that efforts could start to bear meaningful fruit in WTRG's states that have more recently adopted fair market value legislation (NC, OH, TX & VA) – we note that WTRG is the deepest-pocketed IOU in NC, OH & TX.
- ***DELCORA – The Latest.*** Much investor attention on the Q3 call was understandably on the pending $277M DELCORA wastewater deal that is potentially at risk due to a court challenge by Delaware County's County Council. Hearings were recently completed on the legality of the trust aspect DELCORA's plan and the more important hearings related to the enforceability of the asset purchase agreement (does WTRG have a valid deal?) are expected in the next few weeks. A ruling from the judge in the Court of Common Pleas of Delaware County is expected within 60 days of the hearing. That said, the judge continues to encourage parties to reach a settlement. ***While WTRG management was unable to confirm whether or not settlement discussions are taking place, the company remains confident in the ability to close the deal perhaps by late March or April.*** This is consistent with the PaPUC approval process were evidentiary hearings are scheduled next week and the statutory deadline for a decision is 3/26/21. ***(comments continue on p. 2.)***

$ EPS	2019A	2020E Curr.	2020E Prior	2021E Curr.	2021E Prior
Q1 (Mar.)	0.28	0.60 A	NC	NE	
Q2 (June)	0.37	0.29 A	NC	NE	
Q3 (Sep.)	0.48	**0.23 A**	**0.20**	NE	
Q4 (Dec.)	0.34	**0.46**	**0.47**	NE	
FY	1.47	**1.58**	**1.56**	1.65	NC
CY	1.47	1.58		1.65	
FY P/EPS	28.0x	26.1x		25.0x	
Rev.(MM)	890	1,931		2,052	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
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V = Volatile
Adjusted EPS excludes items considered non-recurring.
WTR expects 2020 adjusted EPS at the top end of the $1.53-1.58 range and targets a 5-7% EPS CAGR through 2022 off the 2019 adjusted base of $1.47.

Ticker	WTRG
Price Target/Prior:	**$47/$45**
Price (11/04/2020)	**$41.19**
52-Week Range:	$30-55
Shares Outstanding: (MM)	245.2
Market Cap.: (MM)	$10,099.8
S&P 500:	3,443.44
Avg. Daily Vol.:	1,162,150
Dividend/Yield:	$1.00/2.4%
LT Debt: (MM)	$5,277.4
LT Debt/Total Cap.:	53.2%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	6.0%
CY 2020 Est. P/EPS-to-Growth:	4.4x
Last Reporting Date:	11/03/2020 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Please see page 4 for rating definitions, important disclosures and required analyst certifications. All estimates/forecasts are as of 11/04/20 unless otherwise stated. 11/04/20 16:37:17 ET

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Together we'll go far

- ***DELCORA – The Latest (continued…).*** While the DELCORA deal is highly supportive of WTRG's growth aspirations and management continues to express confidence in the ability to close the transaction, we consider the future to be bright without it driven by elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends. We believe relatively low risk, regulated EPS growth of at least 6% is achievable – that rate of growth would simply be enhanced if DELCORA closes, particularly in the later part of our 5-year forecast and beyond, given the $700M of required investment needed in the system by 2028 as well as potential further municipal wastewater deals in the region.

- ***Lower Makefield Township.*** An agreement to acquire the 11,000 connection wastewater system in Bucks County, PA for $53M was announced on 9/24. The deal is subject to PaPUC approval – which we expect will be received – and therefore closure probably is not likely until Q4'21. We view the deal as highly supportive of our EPS outlook as it essentially fills in our full year '21 M&A placeholder of $60M.

Other Q3 Call Nuggets.

- **No Gas M&A** – Management made it clear that all M&A efforts are focused on the water/wastewater platform. No M&A expansion on the gas utility side is being contemplated. That said and despite gas utilities being largely out of favor with investors given anti-gas sentiment (existential threat?) in some parts of the country, management defended the Peoples deal and outlined the why the future is bright for the Western PA utility (and brighter than most other gas LDCs). We largely agree with management's arguments and our positive investment thesis and price target reflect it.

- **ESG** – Appealing to ESG investors/rating agencies is a priority. Management believes the company has made great strides in recent years with plans to further improve and therefore has a good story to tell. WTRG plans to establish credible, meaningful and attainable emissions reduction goals for Peoples within 6 months.

- **Peoples Repairs Tax** – No real updates on this front since WTRG filed in early August for PaPUC treatment of the catch up portion of the Peoples repairs tax deduction election. The filing outlined a $381M catch up deduction and proposed to share the benefits between customers (40%, via a 2% bill surcredit over 2021-24) and shareholders (60%, via an increasing income tax expense offset over 2023-25). If approved, a base rate increase would not be needed prior to 1/1/2026 while supporting the elevated pace of capex deployment.

  WTRG had communications with regulators and other key parties prior to making this filing which makes us hopeful that the proposal will be positively received and that a constructive outcome will ensue. The timing of a potential settlement could be before the evidentiary hearings in late January take place. Whether WTRG settles or the hearings occur and the proceeding is fully litigated, management believes a final decision is likely an early Q2'21 event.

  Approval of the shareholder benefit aspect of the request would increase our confidence in the gas utilities' ability to achieve our forecast – we assume gas utility earned ROEs of 10-10.3% which we believe is reasonable and consistent with Peoples 2019 rate order. On the flip side, if the PaPUC decides to go a different direction with the catchup benefits, we still believe our 2023 & beyond EPS levels are reasonable within the backdrop of the constructive PA regulatory framework. It could simply necessitate filing for a base rate increase sooner which would bring with it associated regulatory risk.

Acronyms:
DELCORA – Delaware Country Regional Water Quality Control Authority
ESG – Environmental, Social, Governance
FMV – Fair Market Value
IOU – Investor Owned Utility
LDC – Local Distribution Company
PaPUC – Pennsylvania Public Utility Commission

Price Target

Price Target: $47 from $45

Our $47/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.78. For WTRG's water utility multiple, we ascribe a 5-10% discount to the 21E multiple we use for AWK (31.5-32X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The 5-10% discount reflects a modestly lower earnings growth rate (we forecast 6-7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 18X (based on ATO, NWN, OGS & SR) and then apply a 5-10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive PA regulatory framework. Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

Investment Thesis

Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived and near-term regulatory risk is low as both the water and gas utilities completed rate cases in 2019), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

Company Description

Headquartered in Bryn Mawr, PA, Essential Utilities (WTRG) - formerly Aqua America - is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTRG's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total water customer base and nearly 70% of consolidated water rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio.

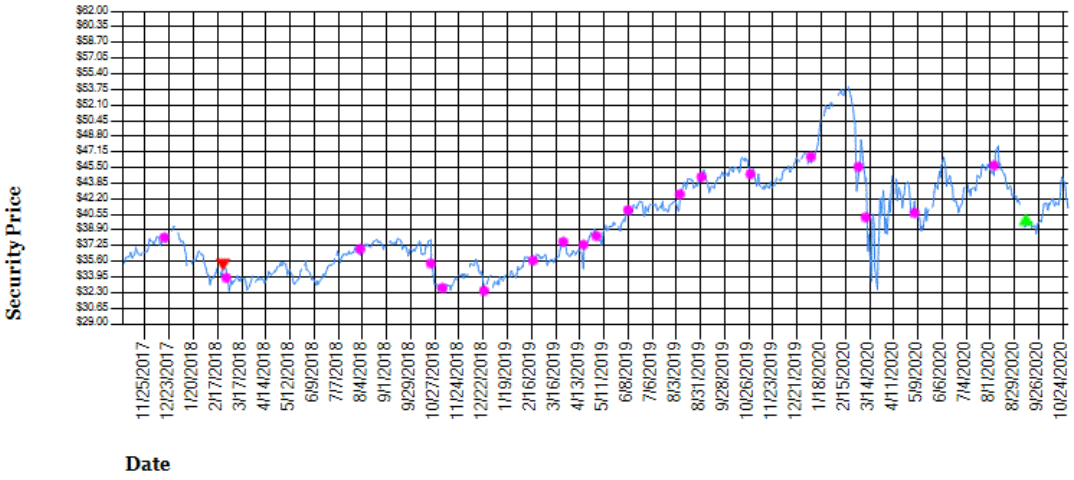
In March 2020, WTRG closed on the acquisition of Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, WTRG paid 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to other gas utility transactions at the time. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

Regulated operations account for more than 99% of consolidated revenues. Consolidated EPS is expected to be driven roughly 70% by water utility operations with the gas utility contributing the remaining 30%.

In February 2020, the new name Essential Utilities, Inc. and new ticker WTRG became effective. Prior, the company was known as Aqua America Inc. and traded under the ticker WTR.

Required Disclosures

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	10/30/2017		Reeder				
	10/30/2017	NA	1	40	NE	NE	35.42
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51
●	3/2/2020	43.01	2	45	NE	NE	45.44
●	3/11/2020	44.41	2	48	NE	NE	40.03
●	5/7/2020	40.49	2	42	NE	NE	40.53
●	8/6/2020	45.56	2	45	NE	NE	45.56
▲	9/14/2020	39.35	1	45	NE	NE	39.82

*Effective December 7, 2019, Wells Fargo Securities' Equity Research modified its ratings definitions. Complete definitions of current ratings can be found below. For information related to prior ratings definitions, please contact equityresearch1@wellsfargo.com.

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

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WTRG: Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

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2=Equal Weight: Total return on stock expected to be 0-10% over the next 12 months. HOLD
3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

VOLATILITY RATING
V = A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: November 4, 2020

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Essential Utilities Inc WTRG (NYSE) | ★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Capital Allocation	Industry Group	ESG Risk Rating Assessment[1]
48.86 USD	39.00 USD	Low	Narrow	Stable	Standard	Utilities - Regulated	

Essential Utilities Combines Growing Water Business With Stable Gas Utility

Travis Miller
Strategist
Morningstar

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Research as of 11 Jun 2021
Estimates as of 11 Jun 2021
Pricing data through 11 Jun 2021 00:00
Rating updated as of 11 Jun 2021 00:00

[1]The ESG Risk Rating Assessment is a representation of Sustainalytics' ESG Risk Rating.
Rating as of 02 Jun 2021 00:00

Currency amounts expressed with "$" are in U.S. dollars (USD) unless otherwise denoted.

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Business Strategy and Outlook 11 Jun 2021

For more than 50 years, Essential Utilities--formerly Aqua America--was one of the few pure-play water utilities in the United States. But its $4.3 billion acquisition of Peoples Gas in March 2020 made the company nearly 50% larger and diversified its earnings mix.

The acquisition hasn't changed Essential's core investment proposition. Essential's gas and water utility earnings remain mostly rate regulated, and we expect management to run it like most other regulated U.S. utilities, prioritizing infrastructure investment growth and a robust dividend. Our outlook for 8% earnings growth during the next five years is a little higher than our growth outlook for most other U.S. utilities.

Although core retail water use has been falling steadily as a result of efficiency savings for several decades, Essential has been able to grow earnings and the dividend for many years. Like many utilities, Essential is replacing and upgrading infrastructure that is decades old across its system, resulting in organic rate base growth. We also expect Essential to grow by acquiring small, typically municipal-owned water systems. In the U.S., 85% of the population is served by a municipal water utility, offering a long runway of acquisition growth opportunities.

Similarly, we expect little natural gas usage growth at Peoples Gas, which had been owned by a private equity group. But the gas business still should produce steady earnings growth as Essential replaces and upgrades the system infrastructure.

Fair market value laws in several states support Essential's water business acquisition strategy. These laws require Essential to pay municipalities at least the assessed value of the system it acquires and allow Essential to add these assets to rate base at the assessed value rather than historical cost. The municipalities benefit by ensuring they get fair prices, and Essential shareholders benefit by ensuring the company doesn't overpay for growth. In many cases, these deals are immediately value-accretive. Recent FMV legislation in Kentucky and West Virginia opens acquisition opportunities near areas Essential already serves.

Vital Statistics

Market Cap (USD Mil)	12,002
52-Week High (USD)	48.93
52-Week Low (USD)	38.28
52-Week Total Return %	14.5
YTD Total Return %	4.4
Last Fiscal Year End	31 Dec 2020
5-Yr Forward Revenue CAGR %	11.2
5-Yr Forward EPS CAGR %	8.6
Price/Fair Value	1.25

Valuation Summary and Forecasts

Fiscal Year:	2019	2020	*2021(E)*	*2022(E)*
Price/Earnings	31.9	29.9	*28.9*	*27.3*
EV/EBITDA	23.0	24.7	*20.4*	*17.4*
EV/EBIT	33.6	39.3	*30.5*	*25.3*
Free Cash Flow Yield %	-2.0	-2.8	*-6.2*	*-2.2*
Dividend Yield %	—	—	*2.1*	*2.3*

Financial Summary and Forecasts (USD Mil)

Fiscal Year:	2019	2020	*2021(E)*	*2022(E)*
Revenue	890	1,463	*1,800*	*1,962*
Revenue YoY %	6.2	64.4	*23.0*	*9.0*
EBIT	340	435	*581*	*702*
EBIT YoY %	5.3	27.8	*33.7*	*20.8*
Net Income, Adjusted	317	402	*435*	*469*
Net Income YoY %	65.3	26.8	*8.1*	*7.9*
Diluted EPS	1.47	1.58	*1.69*	*1.79*
Diluted EPS YoY %	36.6	7.5	*7.0*	*6.1*
Free Cash Flow	-73	-143	*-525*	*-13*
Free Cash Flow YoY %	-345.3	97.3	*266.0*	*-97.5*

Historical/forecast data sources are Morningstar Estimates and may reflect adjustments.

Profile

Essential Utilities is a Pennsylvania-based holding company for U.S. water, wastewater, and natural gas distribution utilities. The company's water business serves 3 million people in eight states. Nearly three fourths of its water earnings come from Pennsylvania, primarily suburban Philadelphia. It also has a small market-based water business that provides water and water services to third parties, notably natural gas producers. Its $4.3 billion Peoples Gas acquisition that closed in March 2020 adds 750,000 gas distribution customers in Pennsylvania, West Virginia, and Kentucky.

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Essential Utilities Inc WTRG (NYSE) | ★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Capital Allocation	Industry Group	ESG Risk Rating Assessment[1]
48.86 USD	39.00 USD	Low	Narrow	Stable	Standard	Utilities - Regulated	

Morningstar Analysis

Initiating Coverage of Essential Utilities With Narrow Moat, $39 Fair Value 11 Jun 2021

We are initiating coverage of Essential Utilities with a $39 per share fair value estimate, narrow moat rating, and stable moat trend.

We consider the stock 23% overvalued based on the $48 stock price as of June 11. The stock trades at 28 times our 2021 earnings estimate, a 30% premium to the current median U.S. utilities P/E. Although we think Essential deserves a premium valuation relative to electric and gas utilities because of its higher returns on capital and growth potential in the water business, we think investors should wait for a pullback. Its closest peer, American Water Works, trades at a 30% premium to our fair value estimate and 38 P/E.

Essential, formerly Aqua America, was one of the few pure-play U.S. water distribution and wastewater utilities before acquiring Pennsylvania-based Peoples Gas in 2020. The company now gets two thirds of its earnings from its water business and one third of earnings from gas distribution.

The $4.3 billion Peoples Gas acquisition doesn't change Essential's core regulated utility business model, but we think it was a setback for investors. Essential paid more than double book value for the business, which has good near-term growth potential but long-term uncertainty as the U.S. moves away from fossil fuels. We think that capital would have been better spent growing its water businesses.

Our five-year, 8% annual earnings growth outlook tops most other U.S. utilities' outlooks. We think the water business has long, attractive runway of growth mostly through acquisitions of municipal utilities. Fair market value laws in some states allow Essential to mark up book value on its water acquisitions, eliminating the risk of overpaying.

We expect Essential to continue its impressive dividend growth track record. The company has paid a dividend every year since 1945 and has raised the dividend by 5% or more every year for the last 25 years. We consider management's 65% payout target more attractive than its peers.

Fair Value & Profit Drivers 11 Jun 2021

We are initiating coverage of Essential Utilities with a $39 per share fair value estimate.

We expect earnings to grow 8% annually during the next four years, which is above management's 5%-7% annual earnings growth target. Our growth rate is based on $1 billion of annual capital investment and $150 million of water utility acquisitions per year, on average. Our growth rate is higher than management's target range primarily due to our assumption that Essential will find more acquisition opportunities than it has in the past. We think the spread of fair market value legislation and increasing need for system investments will lead more municipal utilities to consider selling their systems.

Apart from acquisitions, the combination of surcharges and base rate increases support our earnings growth outlook. This includes favorable outcomes for likely base rate reviews in Pennsylvania, its largest service territory, in 2022-23.

In our discounted cash flow valuation, we use a 6.0% cost of capital based on a 7.5% cost of equity. This is lower than the 9% rate of return we expect investors will demand of a diversified equity portfolio, reflecting Essential's lesser sensitivity to the economic cycle and lower degree of operating leverage. We incorporate $5 per share of incremental value to better recognize the benefits accruing to shareholders from Essential having issued debt at coupon rates far below our long-term cost of debt assumption.

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Essential Utilities Inc WTRG (NYSE) | ★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Capital Allocation	Industry Group	ESG Risk Rating Assessment[1]
48.86 USD	39.00 USD	Low	Narrow	Stable	Standard	Utilities - Regulated	

Scenario Analysis

In our bear case, a 20% annual reduction in our 2021-24 capital expenditure forecast would lower our fair value estimate by $2 per share. A 50-basis-point cut in our long-term allowed regulatory return on equity assumption would reduce our fair value an additional $3 per share.

In our bull case, a 20% increase in our capital spending assumption would raise our fair value estimate by $2 per share, assuming full regulatory support at current allowed returns. A 50 basis-point increase in our long-term allowed regulatory return on equity assumption would add another $3 per share.

A 50-basis-point change in our cost of equity assumption would lead to a $2 per share change in our fair value estimate.

Economic Moat

We have greater than 50% confidence that Essential can generate economic profits on a consolidated basis for at least the next 10 years based on its efficient scale competitive advantage for its water, wastewater, and natural gas distribution businesses. Essential Utilities' consolidated returns are the foundation for our narrow moat rating.

We have strong confidence that Essential's returns on invested capital will remain at a healthy spread over its weighted average cost of capital for the foreseeable future, leading us to assign the company a narrow moat rating. Essential owns a difficult-to-replicate network of water, wastewater, and natural gas distribution infrastructure that provides essential energy sources to customers. In exchange for a service territory monopoly, state and federal regulators set rates for Essential's water distribution, wastewater, and natural gas distribution utilities at levels that aim to keep customer costs low while providing adequate returns for capital providers. This implicit contract between regulators and the utilities should, in the long run, allow Essential to earn a consistent spread over its cost of capital. Rate-setting mechanisms in the states that Essential serves are mostly constructive, leading to ROICs modestly above its WACC.

In the water distribution and wastewater businesses, Essential enjoys fair market value legislation in seven of the eight states where it has operations. This allows Essential to ensure its growth acquisitions are value-accretive by allowing it to adjust its regulated earning asset base to reflect the deal value based on a third-party valuation. This effectively eliminates the drag on returns created by goodwill and the risk of cost overruns for organic growth investment. Essential made 57 water system acquisitions between 2015 and 2019, and goodwill represented only 1% of Essential's net asset base. Thus, Essential's earned ROICs tend to track very closely its regulatory allowed ROICs, the foundation of an economic moat for regulated utilities.

As with all regulated utilities, we think regulatory caps on revenue and returns preclude Essential from establishing a wide economic moat.

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Essential derives about 1% of earnings from businesses that have few competitive advantages, particularly its water and wastewater services. Essential exited some of these businesses in 2017, and we expect these businesses' share of earnings will continue to shrink as management focuses on growth at the regulated distribution utilities.

Moat Trend

We think Essential's moat trend is stable. We do not expect the regulatory rate structures that support earnings and ROICs for Essential's water or gas utilities to change substantially, given state laws that demonstrate the political and regulatory support for maintaining Essential's financial health, stability, and investments. We believe regulators will rely on state legislation and constructive rate plans to uphold the implicit contract with capital providers that allows Essential to earn above its cost of capital on balance, in the long run. Fair market value legislation ensures Essential's growth-by-acquisition strategy is value-accretive for shareholders.

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Bulls Say/Bears Say

Bulls Say

- Constructive regulation allows Essential to raise rates through surcharges or rate cases to reduce regulatory lag and enhance cash flow available to pay the dividend and invest in growth projects.
- Fair market valuation state laws allow Essential to make municipal water utility acquisitions immediately value-accretive for shareholders.
- Essential has raised its dividend 30 times in the last 29 years, including 29 consecutive increases of more than 5%.

Bears Say

- Essential Utilities paid a peak market price for Peoples Gas, which will probably drag on consolidated returns for many years.
- Essential's capital investment plan likely means annual rate increases for most of its customers, which could cause regulatory pushback that would slow earnings growth.
- Rising interest rates could raise financing costs for Essential to fund its investments and make its dividend yield less attractive for income investors.

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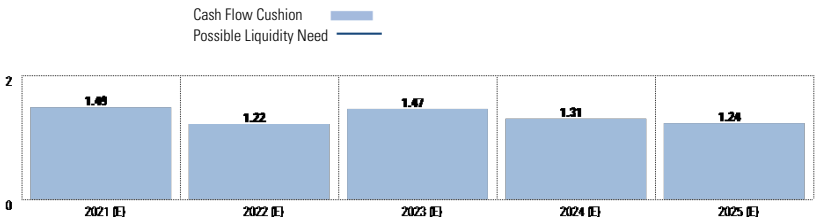
Five Year Adjusted Cash Flow Forecast (USD Mil)

	2021(E)	2022(E)	2023(E)	2024(E)	2025(E)
Cash and Equivalents (beginning of period)	5	277	339	351	425
Adjusted Available Cash Flow	893	1,528	638	1,171	716
Total Cash Available before Debt Service	898	1,805	977	1,523	1,141
Principal Payments	-406	-1,257	-425	-902	-653
Interest Payments	-197	-220	-242	-261	-266
Other Cash Obligations and Commitments	—	—	—	—	—
Total Cash Obligations and Commitments	-603	-1,477	-667	-1,163	-919

Cumulative Annual Cash Flow Cushion



Adjusted Cash Flow Summary

	USD Millions	% of Commitments
Beginning Cash Balance	5	0.1
Sum of 5-Year Adjusted Free Cash Flow	4,946	102.4
Sum of Cash and 5-Year Cash Generation	4,951	102.5
Revolver Availability	—	—
Asset Adjusted Borrowings (Repayment)	—	—
Sum of Cash, 5-Year Cash Generation, Revolver and Adjustments	4,951	102.5
Sum of 5-Year Cash Commitments	-4,828	—

Financial Strength

Essential maintains a capital structure in line with its regulatory allowed capital structure for ratemaking purposes and leverage metrics in line with high investment-grade credit ratings. We don't expect that to change.We expect Essential to issue new debt to fund growth investments and acquisitions in the coming years. We don't expect any material new equity needs once it completes its $300 million equity forward sale in August. With constructive regulation, we expect Essential will be able to use its cash flow to fund most of its equity investment needs during the next five years.Essential has paid an annual dividend since 1945 and increased it at least 5% for each of the last 25 years. We think Essential will be able to continue growing the dividend at this rate or higher while staying below management's 65% maximum payout ratio threshold, which is in line with Essential's peer utilities.

Risk & Uncertainty

The biggest uncertainty for Essential is rate regulation in the states it serves. Although Essential has a long history of constructive rate regulation, customers and regulators remain sensitive to rate increases that drive Essential's earnings growth. Deterioration of regulatory relations and policies could jeopardize Essential's growth potential.Customer growth and value-accretive water acquisitions have kept earnings growing even while water use has fallen steadily for several decades. Unlike many utilities that have lobbied to decouple rates from usage trends, Essential has maintained usage-based rates to avoid potential pushback from regulators. Customer growth, tax benefits, and constructive rate regulation have more than offset unfavorable usage trends.Essential's ability to make annual rate adjustments in states it serves offsets some of the regulatory ratemaking uncertainty. These surcharges effectively eliminate regulatory lag and improve cash flow to support capital investment and dividends.Essential's large capital investment plan will require good execution to

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keep projects on time and on budget. Delays or cost overruns could reduce shareholder returns.Essential also faces environmental, social, and governance risk, given its water and natural gas distribution businesses. At the water business, Essential must meet strict quality measures. It faces the risk of supplying contaminated drinking water for its customers if it has an operational failure, although we think this risk is low. Essential has invested in monitoring technology that allows it to supply water that is far cleaner than government requirements and reduces per- and polyfluoroalkyl substances, or PFAS.At the natural gas business, there is a long-term risk that policymakers will move retail customers away from gas heating, but we think that's unlikely in the near future, given the technical and economic hurdles in the colder climate where Essential operates.

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Management & Ownership

Management Activity

Name	Position	Shares Held	Report Date*	InsiderActivity
CHRISTOPHER H. FRANKLIN	Chief Executive Officer	175,702	27 Feb 2021	—
ROBERT A. RUBIN	Chief Accounting Officer	74,025	27 May 2021	—
MR. CHRISTOPHER P. LUNING	Sr. VP, General Counsel & Sec	49,911	16 Mar 2021	—
MR. DANIEL J. SCHULLER	Executive Vice President	40,634	16 Mar 2021	—
MS. ELLEN T. RUFF	Director,Director	32,198	31 Mar 2021	—
MR. RICHARD S. FOX	Chief Operating Officer	29,566	16 Mar 2021	—
MR. MATTHEW R. RHODES	EVP, Strategy & Corp Dev	23,069	16 Mar 2021	—
MR. DANIEL J. HILFERTY	Director,Director	20,678	31 Mar 2021	—

*Represents the date on which the owner's name, position, and common shares held were reported by the holder or issuer.

Fund Ownership

Top Owners	% of Shares Held	% of Fund Assets	Change (k)	Portfolio Date
Liberty One CAPSTONE	21.83	2.49	53,581	31 May 2021
Vanguard Total Stock Market Index Fund	2.80	0.03	-4	31 May 2021
Vanguard US Total Market Shares ETF	2.80	0.03	-4	31 May 2021
iShares Core S&P Mid-Cap ETF	2.48	0.45	1	31 May 2021
Vanguard Small Cap Index	2.45	0.21	17	31 May 2021
Concentrated Holders				
Ecofin Global Water Composite	0.01	8.39	4	31 May 2021
AAM UBS Lgr Tm Inv Ser Envir Trd 19-2	0.00	5.12	—	31 May 2021
Lyxor World Water (DR) ETF	0.48	4.73	—	31 May 2021
Pramerica Sicav Clean Water	0.11	4.59	25	31 May 2021
Invesco S&P Global Water ETF	0.36	4.54	4	31 May 2021

Institutional Transactions

Top 5 Buyers	% of Shares Held	% of Fund Assets	Shares Bought/ Sold (k)	Portfolio Date
Royal Bank of Canada	2.82	0.09	4,992	31 May 2021
NORGES BANK	1.77	0.05	4,357	31 May 2021
NORGES BANK	1.77	0.05	4,357	31 May 2021
BlackRock Inc	9.55	0.04	935	31 May 2021
Mariner Value Strategies, LLC	1.17	2.41	865	31 May 2021
Top 5 Sellers				
Pictet Asset Management SA (Junked)	—	—	-7,080	31 May 2021
Washington Crossing Advisors, LLC	—	—	-1,685	31 May 2021
Invesco Capital Management LLC	1.29	20.66	-1,427	31 May 2021
BMO Capital Markets Corp.	0.51	0.18	-1,120	31 May 2021
Bank of Montreal	0.56	0.04	-1,103	31 May 2021

Capital Allocation 11 Jun 2021

We give Essential Utilities a Standard capital allocation rating, balancing the company's long history of shareholder-friendly capital allocation in the water business with what we think was an ill-advised move into the gas business.

Essential has an impressive record of paying a dividend every year since 1945 and raising it 30 times in the last 29 years. While returning this cash to shareholders, Essential still found ways to invest in organic growth and acquisitions.

We think Essential overpaid for Peoples Gas. The equity dilution from the $4.3 billion cash price will be difficult to overcome even if everything goes perfectly. The $2.3 billion of goodwill on its balance sheet following the acquisition will remain a drag on returns. Goodwill was nearly equal to the book value of the assets.

Essential also gave up its premium market valuation with the Peoples acquisition. As one of the few pure-play water utilities, Essential was a staple in portfolios focused on environmental, social, and governance issues, especially water. Adding fossil-fuel exposure with the gas business could turn off some ESG investors. We think this would be an overreaction based on natural gas' low-carbon profile, but that's not likely to persuade strict environmentally focused investors to continue holding Essential.

CEO and chairman Chris Franklin has been in his role since 2015 and with the company for 28 years. CFO Dan Schuller joined the company in 2015.

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Analyst Notes

Initiating Coverage of Essential Utilities With Narrow Moat, $39 Fair Value 11 Jun 2021

We are initiating coverage of Essential Utilities with a $39 per share fair value estimate, narrow moat rating, and stable moat trend.

We consider the stock 23% overvalued based on the $48 stock price as of June 11. The stock trades at 28 times our 2021 earnings estimate, a 30% premium to the current median U.S. utilities P/E. Although we think Essential deserves a premium valuation relative to electric and gas utilities because of its higher returns on capital and growth potential in the water business, we think investors should wait for a pullback. Its closest peer, American Water Works, trades at a 30% premium to our fair value estimate and 38 P/E.

Essential, formerly Aqua America, was one of the few pure-play U.S. water distribution and wastewater utilities before acquiring Pennsylvania-based Peoples Gas in 2020. The company now gets two thirds of its earnings from its water business and one third of earnings from gas distribution.

The $4.3 billion Peoples Gas acquisition doesn't change Essential's core regulated utility business model, but we think it was a setback for investors. Essential paid more than double book value for the business, which has good near-term growth potential but long-term uncertainty as the U.S. moves away from fossil fuels. We think that capital would have been better spent growing its water businesses.

Our five-year, 8% annual earnings growth outlook tops most other U.S. utilities' outlooks. We think the water business has long, attractive runway of growth mostly through acquisitions of municipal utilities. Fair market value laws in some states allow Essential to mark up book value on its water acquisitions, eliminating the risk of overpaying.

We expect Essential to continue its impressive dividend growth track record. The company has paid a dividend every year since 1945 and has raised the dividend by 5% or more every year for the last 25 years. We consider management's 65% payout target more attractive than its peers.

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Morningstar Analyst Forecasts

Financial Summary and Forecasts

Fiscal Year Ends in December

Growth (% YoY)	3-Year Hist. CAGR	2018	2019	2020	Forecast 2021	Forecast 2022	5-Year Proj. CAGR
Revenue	*21.8*	3.5	6.2	64.4	*23.0*	*9.0*	*11.2*
EBIT	*9.2*	-3.2	5.3	27.8	*33.7*	*20.8*	*20.4*
EBITDA	*13.7*	-0.2	5.7	39.3	*25.9*	*17.4*	*16.9*
Net Income	*18.8*	-19.9	65.3	26.8	*8.1*	*7.9*	*9.5*
Diluted EPS	*5.5*	-20.0	36.6	7.5	*7.0*	*6.1*	*8.6*
Earnings Before Interest, after Tax	*13.2*	20.1	-20.8	52.6	*48.4*	*-1.0*	*14.1*
Free Cash Flow	—	-232.5	-345.3	97.3	*266.0*	*-97.5*	—

Profitability	3-Year Hist. Avg	2018	2019	2020	Forecast 2021	Forecast 2022	5-Year Proj. Avg
Operating Margin %	*35.5*	38.6	38.2	29.7	*32.3*	*35.8*	*38.9*
EBITDA Margin %	*53.1*	56.1	55.8	47.3	*48.4*	*52.1*	*55.3*
Net Margin %	*28.7*	22.9	35.7	27.5	*24.2*	*23.9*	*24.3*
Free Cash Flow Margin %	*-4.8*	3.5	-8.2	-9.8	*-29.2*	*-0.7*	*-0.8*
ROIC %	*6.3*	9.8	5.0	4.2	*5.1*	*4.9*	*5.4*
Adjusted ROIC %	*6.6*	9.9	5.1	4.8	*6.3*	*5.9*	*6.4*
Return on Assets %	*3.6*	5.5	2.8	2.5	*3.0*	*3.0*	*3.2*
Return on Equity %	*11.1*	19.1	7.6	6.7	*8.8*	*8.8*	*9.3*

Leverage	3-Year Hist. Avg	2018	2019	2020	Forecast 2021	Forecast 2022	5-Year Proj. Avg
Debt/Capital	*0.52*	0.56	0.44	0.55	*0.56*	*0.56*	*0.56*
Total Debt/EBITDA	*6.61*	5.45	6.19	8.20	*7.54*	*6.92*	*6.27*
EBITDA/Interest Expense	*4.13*	4.74	3.96	3.67	*4.43*	*4.65*	*5.02*

Valuation Summary and Forecasts

	2019	2020	2021(E)	2022(E)
Price/Fair Value	—	—	—	—
Price/Earnings	31.9	29.9	*28.9*	*27.3*
EV/EBITDA	23.0	24.7	*20.4*	*17.4*
EV/EBIT	33.6	39.3	*30.5*	*25.3*
Free Cash Flow Yield %	-2.0	-2.8	*-6.2*	*-2.2*
Dividend Yield %	—	—	*2.1*	*2.3*

Key Valuation Drivers

Cost of Equity %	7.5
Pre-Tax Cost of Debt %	5.3
Weighted Average Cost of Capital %	6.0
Long-Run Tax Rate %	27.0
Stage II EBI Growth Rate %	5.0
Stage II Investment Rate %	55.6
Perpetuity Year	15

Additional estimates and scenarios available for download at http://select.morningstar.com.

Discounted Cash Flow Valuation

	USD Mil	Firm Value (%)	Per Share Value
Present Value Stage I	-26	-0.2	-0.10
Present Value Stage II	2,970	21.1	11.38
Present Value Stage III	11,125	79.1	42.62
Total Firm Value	**14,069**	**100.0**	**53.90**
Cash and Equivalents	5	—	0.02
Debt	-5,670	—	-21.72
Preferred Stock	—	—	—
Other Adjustments	1,548	—	5.93
Equity Value	**9,952**	**—**	**38.12**
Projected Diluted Shares	261		
Fair Value per Share (USD)	**39.00**		

The data in the table above represent base-case forecasts in the company's reporting currency as of the beginning of the current year. Our fair value estimate may differ from the equity value per share shown above due to our time value of money adjustment and in cases where probability-weighted scenario analysis is performed.

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Essential Utilities Inc WTRG (NYSE) | ★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Capital Allocation	Industry Group	ESG Risk Rating Assessment[1]
48.86 USD	39.00 USD	Low	Narrow	Stable	Standard	Utilities - Regulated	

Morningstar Analyst Forecasts

Income Statement (USD Mil)

Fiscal Year Ends in December	2018	2019	2020	*Forecast* 2021	*Forecast* 2022
Revenue	**838**	**890**	**1,463**	***1,800***	***1,962***
Cost of Goods Sold	—	—	166	*300*	*303*
Gross Profit	**838**	**890**	**1,297**	***1,500***	***1,659***
Selling, General & Administrative Expenses	308	333	529	*550*	*555*
Other Operating Expense (Income)	60	60	77	*79*	*81*
Other Operating Expense (Income)	—	—	—	—	—
Depreciation & Amortization (if reported separately)	147	156	257	*290*	*320*
Operating Income (ex charges)	**323**	**340**	**435**	***581***	***702***
Restructuring & Other Cash Charges	—	—	—	—	—
Impairment Charges (if reported separately)	—	—	—	—	—
Other Non-Cash (Income)/Charges	—	—	—	—	—
Operating Income (incl charges)	**323**	**340**	**435**	***581***	***702***
Interest Expense	99	125	188	*197*	*220*
Interest Income	-46	-3	19	*14*	*10*
Pre-Tax Income	**178**	**212**	**265**	***398***	***493***
Income Tax Expense	-14	-13	-20	*-36*	*23*
Other After-Tax Cash Gains (Losses)	—	—	—	—	—
Other After-Tax Non-Cash Gains (Losses)	—	—	—	—	—
(Minority Interest)	—	—	—	—	—
(Preferred Dividends)	—	—	—	—	—
Net Income	**192**	**225**	**285**	***435***	***469***
Weighted Average Diluted Shares Outstanding	178	216	255	*257*	*262*
Diluted Earnings Per Share	**1.08**	**1.04**	**1.12**	***1.69***	***1.79***
Adjusted Net Income	192	317	402	*435*	*469*
Diluted Earnings Per Share (Adjusted)	**1.08**	**1.47**	**1.58**	***1.69***	***1.79***
Dividends Per Common Share	—	—	—	*1.04*	*1.11*
EBITDA	**470**	**497**	**692**	***871***	***1,022***
Adjusted EBITDA	**470**	**497**	**692**	***871***	***1,022***

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Morningstar Analyst Forecasts

Balance Sheet (USD Mil)

Fiscal Year Ends in December	2018	2019	2020	Forecast 2021	Forecast 2022
Cash and Equivalents	4	1,869	5	*277*	*339*
Investments	—	—	—	—	—
Accounts Receivable	66	67	155	*138*	*145*
Inventory	16	18	58	*38*	*38*
Deferred Tax Assets (Current)	—	—	—	—	—
Other Short Term Assets	62	61	162	*160*	*160*
Current Assets	**147**	**2,015**	**380**	***613***	***682***
Net Property Plant, and Equipment	5,930	6,346	9,513	*10,673*	*11,448*
Goodwill	53	64	2,325	*2,325*	*2,325*
Other Intangibles	—	—	—	—	—
Deferred Tax Assets (Long-Term)	—	—	—	—	—
Other Long-Term Operating Assets	788	876	1,363	*1,350*	*1,300*
Long-Term Non-Operating Assets	46	62	125	*125*	*125*
Total Assets	**6,964**	**9,362**	**13,705**	***15,086***	***15,880***
Accounts Payable	77	75	177	*25*	*26*
Short-Term Debt	160	131	163	*163*	*163*
Deferred Tax Liabilities (Current)	—	—	—	—	—
Other Short-Term Liabilities	162	118	264	*270*	*270*
Current Liabilities	**399**	**323**	**604**	***458***	***458***
Long-Term Debt	2,398	2,943	5,508	*6,408*	*6,908*
Deferred Tax Liabilities (Long-Term)	845	936	1,258	*1,350*	*1,400*
Other Long-Term Operating Liabilities	1,122	1,069	1,347	*1,350*	*1,350*
Long-Term Non-Operating Liabilities	191	210	305	*305*	*305*
Total Liabilities	**4,955**	**5,481**	**9,021**	***9,870***	***10,421***
Preferred Stock	—	—	—	—	—
Common Stock	91	112	124	*124*	*124*
Additional Paid-in Capital	820	2,637	3,379	*3,729*	*3,779*
Retained Earnings (Deficit)	1,174	1,210	1,262	*1,444*	*1,637*
(Treasury Stock)	-76	-78	-81	*-81*	*-81*
Other Equity	—	—	—	—	—
Shareholder's Equity	**2,009**	**3,881**	**4,684**	***5,216***	***5,459***
Minority Interest	—	—	—	—	—
Total Equity	**2,009**	**3,881**	**4,684**	***5,216***	***5,459***

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Morningstar Analyst Forecasts

Cash Flow (USD Mil)

Fiscal Year Ends in December	2018	2019	2020	*Forecast* 2021	*Forecast* 2022
Net Income	192	225	285	*435*	*469*
Depreciation	147	156	257	*290*	*320*
Amortization	—	—	—	—	—
Stock-Based Compensation	—	—	—	—	—
Impairment of Goodwill	—	—	—	—	—
Impairment of Other Intangibles	—	—	—	—	—
Deferred Taxes	-15	-10	-18	*92*	*50*
Other Non-Cash Adjustments	72	-30	40	—	—
(Increase) Decrease in Accounts Receivable	-18	-4	-35	*17*	*-7*
(Increase) Decrease in Inventory	—	—	—	*21*	*0*
Change in Other Short-Term Assets	—	—	—	*2*	—
Increase (Decrease) in Accounts Payable	1	5	-2	*-152*	*0*
Change in Other Short-Term Liabilities	-10	-3	-19	*6*	—
Cash From Operations	**369**	**339**	**508**	***710***	***832***
(Capital Expenditures)	-496	-550	-836	*-1,451*	*-1,095*
Net (Acquisitions), Asset Sales, and Disposals	—	—	—	—	—
Net Sales (Purchases) of Investments	-145	-57	-3,500	—	—
Other Investing Cash Flows	1	2	2	*16*	*50*
Cash From Investing	**-640**	**-605**	**-4,334**	***-1,435***	***-1,045***
Common Stock Issuance (or Repurchase)	4	1,946	743	*350*	*50*
Common Stock (Dividends)	-151	-189	-233	*-253*	*-276*
Short-Term Debt Issuance (or Retirement)	12	10	-129	—	—
Long-Term Debt Issuance (or Retirement)	418	361	1,546	*900*	*500*
Other Financing Cash Flows	-12	3	34	—	—
Cash From Financing	**271**	**2,131**	**1,962**	***997***	***274***
Exchange Rates, Discontinued Ops, etc. (net)	—	—	—	—	—
Net Change in Cash	**-1**	**1,865**	**-1,864**	***273***	***62***

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48.86 USD	39.00 USD	Low	Narrow	Stable	Standard	Utilities - Regulated	

Comparable Company Analysis

These companies are chosen by the analyst and the data are shown by nearest calendar year in descending market capitalization order.

Valuation Analysis

		Price/Earnings			EV/EBITDA			Price/Free Cash Flow			Price/Book			Price/Sales		
Company/Ticker	Price/Fair Value	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)
American Water Works Co Inc AWK	1.31	39.3	37.6	34.1	20.5	19.3	17.9	NM	462.3	NM	—	—	—	7.4	7.1	6.7
Eversource Energy ES USA	1.22	23.8	21.6	20.9	15.3	14.0	12.9	—	NM	NM	—	—	—	3.3	3.1	3.0
NiSource Inc NI USA	0.91	17.4	19.4	18.7	12.1	11.4	10.5	NM	NM	NM	—	—	—	1.9	2.0	1.9
Average		26.8	26.2	24.6	16.0	14.9	13.8	—	462.3	—	—	—	—	4.2	4.1	3.9
Essential Utilities Inc WTRG US	**1.25**	**29.9**	***28.9***	***27.3***	**24.7**	***20.4***	***17.4***	**NM**	***NM***	***NM***	**—**	**—**	**—**	**7.9**	***6.7***	***6.1***

Returns Analysis

		ROIC %			Adjusted ROIC %			Return on Equity %			Return on Assets %			Dividend Yield %		
Company/Ticker	Last Historical Year Total Assets (Mil)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)
American Water Works Co Inc AWK	24,766 USD	6.0	6.5	6.8	6.5	7.0	7.3	11.3	11.7	12.1	3.0	3.1	3.3	1.4	1.5	1.6
Eversource Energy ES USA	46,100 USD	4.8	4.9	4.9	5.5	5.5	5.4	9.0	9.2	9.1	2.8	2.8	2.8	2.6	2.9	3.1
NiSource Inc NI USA	22,041 USD	3.9	5.8	6.3	4.2	6.3	6.9	-1.5	10.0	9.4	-0.3	2.4	2.5	3.7	3.4	3.5
Average		4.9	5.7	6.0	5.4	6.3	6.5	6.3	10.3	10.2	1.8	2.8	2.9	2.6	2.6	2.7
Essential Utilities Inc WTRG US	**13,705** USD	**4.2**	***5.1***	***4.9***	**4.8**	***6.3***	***5.9***	**6.7**	***8.8***	***8.8***	**2.5**	***3.0***	***3.0***	**—**	***2.1***	***2.3***

Growth Analysis

		Revenue Growth %			EBIT Growth %			EPS Growth %			Free Cash Flow Growth %			Dividend/Share Growth %		
Company/Ticker	Last Historical Year Revenue (Mil)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)
American Water Works Co Inc AWK	3,777 USD	4.6	8.7	6.3	3.7	15.4	7.9	8.1	9.2	10.2	24.3	-271.2	-96.0	10.0	9.7	10.0
Eversource Energy ES USA	8,904 USD	4.4	3.1	4.7	25.0	15.8	5.8	5.5	5.2	3.5	—	—	NM	6.1	6.2	5.8
NiSource Inc NI USA	4,682 USD	-10.1	11.2	5.5	-26.3	16.8	8.3	0.4	1.3	3.5	-728.1	-67.2	-435.9	5.0	4.8	4.5
Average		-0.4	7.7	5.5	0.8	16.0	7.3	4.7	5.2	5.7	-351.9	-169.2	-266.0	7.0	6.9	6.8
Essential Utilities Inc WTRG US	**1,463** USD	**64.4**	***23.0***	***9.0***	**27.8**	***33.7***	***20.8***	**7.5**	***7.0***	***6.1***	**97.3**	***266.0***	***-97.5***	**7.0**	***7.2***	***6.7***

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Comparable Company Analysis

These companies are chosen by the analyst and the data are shown by nearest calendar year in descending market capitalization order.

Profitability Analysis

Company/Ticker	Last Historical Year Net Income (Mil)	Gross Margin %			EBITDA Margin %			Operating Margin %			Net Margin %			Free Cash Flow Margin %		
		2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)
American Water Works Co Inc AWK	709 USD	100.0	100.0	100.0	49.0	50.3	50.9	33.0	35.1	35.6	18.8	18.9	19.7	-10.5	1.5	0.5
Eversource Energy ES USA	1,237 USD	66.5	66.5	67.0	33.4	36.5	37.8	22.3	25.1	25.3	13.9	14.4	14.3	—	-6.3	-10.0
NiSource Inc NI USA	508 USD	76.3	70.0	70.0	36.0	35.0	36.1	20.5	21.6	22.1	10.8	10.7	11.2	-14.0	-10.9	-14.4
Average		80.9	78.8	79.0	39.5	40.6	41.6	25.3	27.3	27.7	14.5	14.7	15.1	-12.3	-5.2	-8.0
Essential Utilities Inc WTRG US	**402** USD	**88.7**	***83.3***	***84.6***	**47.3**	***48.4***	***52.1***	**29.7**	***32.3***	***35.8***	**27.5**	***24.2***	***23.9***	**-22.4**	***-41.1***	***-13.4***

Leverage Analysis

Company/Ticker	Last Historical Year Total Debt (Mil)	Debt/Equity %			Debt/Total Cap %			EBITDA/Interest Exp.			Total Debt/EBITDA			Assets/Equity		
		2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)
American Water Works Co Inc AWK	10,940 USD	169.4	154.3	147.8	62.9	60.7	59.6	4.7	4.8	5.2	5.9	5.1	5.0	3.8	3.7	3.6
Eversource Energy ES USA	17,428 USD	122.6	125.8	127.6	55.1	55.7	56.1	5.5	5.3	5.2	5.9	5.6	5.5	3.2	3.2	3.2
NiSource Inc NI USA	9,746 USD	169.4	128.3	133.1	62.9	56.2	57.1	4.6	4.9	5.1	5.8	5.1	5.2	3.8	3.3	3.4
Average		153.8	136.1	136.2	60.3	57.5	57.6	4.9	5.0	5.2	5.9	5.3	5.2	3.6	3.4	3.4
Essential Utilities Inc WTRG US	**5,670** USD	**121.1**	***126.0***	***129.5***	**54.8**	***55.8***	***56.4***	**3.7**	***4.4***	***4.7***	**8.2**	***7.5***	***6.9***	**2.9**	***2.9***	***2.9***

Liquidity Analysis

Company/Ticker	Market Cap (Mil)	Cash per Share			Current Ratio			Quick Ratio			Cash/Short-Term Debt			Payout Ratio %		
		2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)
American Water Works Co Inc AWK	29,100 USD	3.01	0.20	0.19	0.66	0.58	0.59	0.65	0.58	0.59	0.34	0.04	0.03	55.0	55.3	55.2
Eversource Energy ES USA	28,442 USD	0.31	0.34	0.38	0.64	0.56	0.54	0.58	0.50	0.49	0.05	0.05	0.06	64.0	63.0	64.4
NiSource Inc NI USA	10,202 USD	0.33	0.82	0.75	0.73	0.88	0.87	0.55	0.68	0.67	0.24	0.68	0.67	-444.0	65.8	66.4
Average		1.22	0.45	0.44	0.68	0.67	0.67	0.59	0.59	0.58	0.21	0.26	0.25	-108.3	61.4	62.0
Essential Utilities Inc WTRG US	**12,002** USD	**0.02**	***1.08***	***1.30***	**0.63**	***1.34***	***1.49***	**0.53**	***1.26***	***1.41***	**0.03**	***1.71***	***2.09***	**—**	***61.5***	***61.9***

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Research Methodology for Valuing Companies

Qualitative Equity Research Overview

At the heart of our valuation system is a detailed projection of a company's future cash flows, resulting from our analysts' research. Analysts create custom industry and company assumptions to feed income statement, balance sheet, and capital investment assumptions into our globally standardized, proprietary discounted cash flow, or DCF, modeling templates. We use scenario analysis, in-depth competitive advantage analysis, and a variety of other analytical tools to augment this process. We believe this bottom-up, long-term, fundamentally based approach allows our analysts to focus on long-term business drivers, which have the greatest valuation impact, rather than short-term market noise.

Morningstar's equity research group ("we," "our") believes that a company's intrinsic worth results from the future cash flows it can generate. The Morningstar Rating for stocks identifies stocks trading at an uncertainty-adjusted discount or premium to their intrinsic worth—or fair value estimate, in Morningstar terminology. Five-star stocks sell for the biggest risk-adjusted discount to their fair values whereas 1-star stocks trade at premiums to their intrinsic worth.

Four key components drive the Morningstar rating: (1) our assessment of the firm's economic moat, (2) our estimate of the stock's fair value, (3) our uncertainty around that fair value estimate and (4) the current market price. This process ultimately culminates in our single-point star rating.

1. Economic Moat

The concept of an economic moat plays a vital role not only in our qualitative assessment of a firm's long-term investment potential, but also in the actual calculation of our fair value estimates. An economic moat is a structural feature that allows a firm to sustain excess profits over a long period of time. We define economic profits as returns on invested capital (or ROIC) over and above our estimate of a firm's cost of capital, or weighted average cost of capital (or WACC). Without a moat, profits are more susceptible to competition. We have identified five sources of economic moats: intangible assets, switching costs, network effect, cost advantage, and efficient scale.

Companies with a narrow moat are those we believe are more likely than not to achieve normalized excess returns for at least the next 10 years. Wide-moat companies are those in which we have very high confidence that excess returns will remain for 10 years, with excess returns more likely than not to remain for at least 20 years. The longer a firm generates economic profits, the higher its intrinsic value. We believe low-quality, no-moat companies will see their normalized returns gravitate toward the firm's cost of capital more quickly than companies with moats.

When considering a company's moat, we also assess whether there is a substantial threat of value destruction, stemming from risks related to ESG, industry disruption, financial health, or other idiosyncratic issues. In this context, a risk is considered potentially value destructive if its occurrence would eliminate a firm's economic profit on a cumulative or midcycle basis. If we deem the probability of occurrence sufficiently high, we would not characterize the company as possessing an economic moat.

To assess the sustainability of excess profits, analysts perform ongoing assessments of the moat trend. A firm's moat trend is positive in cases where we think its sources of competitive advantage are growing stronger; stable where we don't anticipate changes to competitive advantages over the next several years; or negative when we see signs of deterioration.

Morningstar Research Methodology for Valuing Companies

2. Estimated Fair Value

Combining our analysts' financial forecasts with the firm's economic moat helps us assess how long returns on invested capital are likely to exceed the firm's cost of capital. Returns of firms with a wide economic moat rating are assumed to fade to the perpetuity period over a longer period of time than the returns of narrow-moat firms, and both will fade slower than no-moat firms, increasing our estimate of their intrinsic value.
Our model is divided into three distinct stages:

Stage I: Explicit Forecast

In this stage, which can last five to 10 years, analysts make full financial statement forecasts, including items such as revenue, profit margins, tax rates, changes in working-capital accounts, and capital spending. Based on these projections, we calculate earnings before interest, after taxes, or EBI, and the net new investment, or NNI, to derive our annual free cash flow forecast.

Stage II: Fade

The second stage of our model is the period it will take the company's return on new invested capital—the return on capital of the next dollar invested ("RONIC")—to decline (or rise) to its cost of capital. During the Stage II period, we use a formula to approximate cash flows in lieu of explicitly modeling the income statement, balance sheet, and cash flow statement as we do in Stage I. The length of the second stage depends on the strength of the company's economic moat. We forecast this period to last anywhere from one year (for companies with no economic moat) to 10–15 years or more (for wide-moat companies). During this period, cash flows are forecast using four assumptions: an average growth rate for EBI over the period, a normalized investment rate, average return on new invested capital, or RONIC, and the number of years until perpetuity, when excess returns cease. The investment rate and return on new invested capital decline until the perpetuity stage is reached. In the case of firms that do not earn their cost of capital, we assume marginal ROICs rise to the firm's cost of capital (usually attributable to less reinvestment), and we may truncate the second stage.

Stage III: Perpetuity

Once a company's marginal ROIC hits its cost of capital, we calculate a continuing value, using a standard perpetuity formula. At perpetuity, we assume that any growth or decline or investment in the business neither creates nor destroys value and that any new investment provides a return in line with estimated WACC.

Because a dollar earned today is worth more than a dollar earned tomorrow, we discount our projections of cash flows in stages I, II, and III to arrive at a total present value of expected future cash flows. Because we are modeling free cash flow to the firm—representing cash available to provide a return to all capital providers—we discount future cash flows using the WACC, which is a weighted average of the costs of equity, debt, and preferred stock (and any other funding sources), using expected future proportionate long-term market-value weights.

3. Uncertainty Around That Fair Value Estimate

Morningstar's Uncertainty Rating captures a range of likely potential intrinsic values for a company and uses it to

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Research Methodology for Valuing Companies

assign the margin of safety required before investing, which in turn explicitly drives our stock star rating system. The Uncertainty Rating represents the analysts' ability to bound the estimated value of the shares in a company around the Fair Value Estimate, based on the characteristics of the business underlying the stock, including operating and financial leverage, sales sensitivity to the overall economy, product concentration, pricing power, exposure to material ESG risks, and other company-specific factors.

Analysts consider at least two scenarios in addition to their base case: a bull case and a bear case. Assumptions are chosen such that the analyst believes there is a 25% probability that the company will perform better than the bull case, and a 25% probability that the company will perform worse than the bear case. The distance between the bull and bear cases is an important indicator of the uncertainty underlying the fair value estimate. In cases where there is less than a 25% probability of an event, but where the event could result in a material decline in value, analysts may adjust the uncertainty rating to reflect the increased risk. Analysts may also make a fair value adjustment to reflect the impact of this event.

Our recommended margin of safety widens as our uncertainty of the estimated value of the equity increases. The more uncertain we are about the estimated value of the equity, the greater the discount we require relative to our estimate of the value of the firm before we would recommend the purchase of the shares. In addition, the uncertainty rating provides guidance in portfolio construction based on risk tolerance.

Our uncertainty ratings for our qualitative analysis are low, medium, high, very high, and extreme.

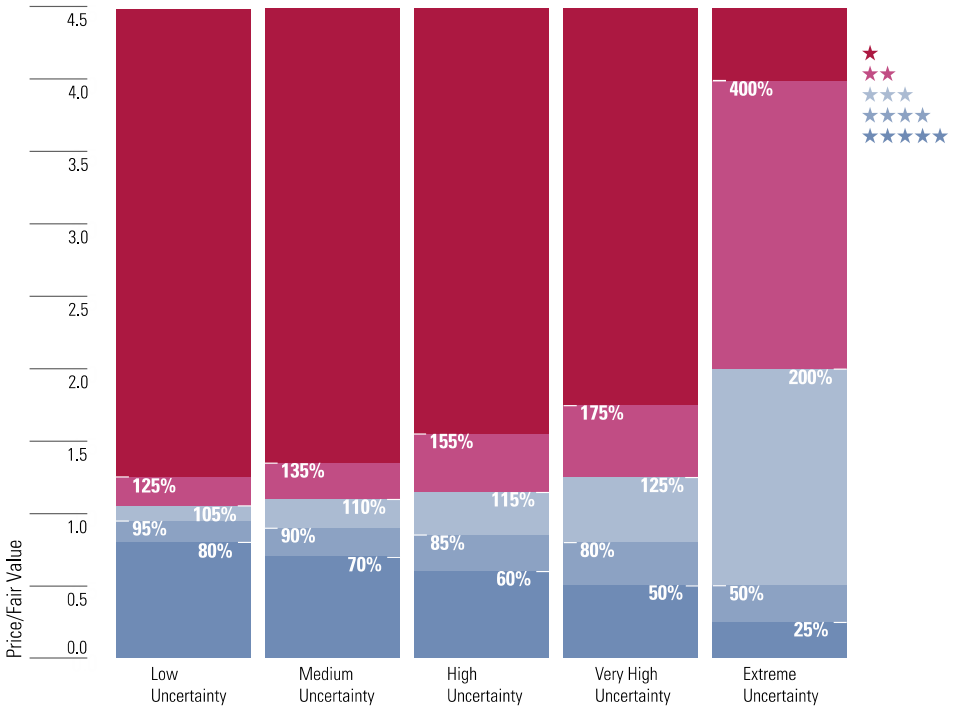
- Low–margin of safety for 5-star rating is a 20% discount and for 1-star rating is 25% premium.
- Medium–margin of safety for 5-star rating is a 30% discount and for 1-star rating is 35% premium.
- High–margin of safety for 5-star rating is a 40% discount and for 1-star rating is 55% premium.
- Very High–margin of safety for 5-star rating is a 50% discount and for 1-star rating is 75% premium.
- Extreme–margin of safety for 5-star rating is a 75% discount and for 1-star rating is 300% premium.

4. Market Price

The market prices used in this analysis and noted in the report come from exchange on which the stock is listed, which we believe is a reliable source.

For more details about our methodology, please go to https://shareholders.morningstar.com.

Morningstar Equity Research Star Rating Methodology



Morningstar Star Rating for Stocks

Once we determine the fair value estimate of a stock, we compare it with the stock's current market price on a daily basis, and the star rating is automatically re-calculated at the market close on every day the market on which the stock is listed is open.

Please note, there is no predefined distribution of stars. That is, the percentage of stocks that earn 5 stars can fluctuate daily, so the star ratings, in the aggregate, can serve as a gauge of the broader market's valuation. When there are many 5-star stocks, the stock market as a whole is more undervalued, in our opinion, than when very few companies garner our highest rating.

We expect that if our base-case assumptions are true the market price will converge on our fair value estimate over time, generally within three years (although it is impossible to predict the exact time frame in which market prices may adjust).

Our star ratings are guideposts to a broad audience and individuals must consider their own specific investment goals, risk tolerance, tax situation, time horizon, income needs, and complete investment portfolio, among other factors.

The Morningstar Star Ratings for stocks are defined below:

★★★★★ We believe appreciation beyond a fair risk-adjusted return is highly likely over a multiyear time frame. The current market price represents an excessively pessimistic outlook, limiting downside risk and maximizing upside potential.

★★★★ We believe appreciation beyond a fair risk-adjusted return is likely.

★★★ Indicates our belief that investors are likely to receive a fair risk-adjusted return (approximately cost of equity).

★★ We believe investors are likely to receive a less than fair risk-adjusted return.

★ Indicates a high probability of undesirable risk-adjusted returns from the current market price over a multiyear time frame, based on our analysis. The market is pricing in an excessively optimistic outlook, limiting upside potential and leaving the investor exposed to Capital loss.

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Research Methodology for Valuing Companies

Other Definitions

Last Price: Price of the stock as of the close of the market of the last trading day before date of the report.

Capital Allocation Rating: Our Capital Allocation (or Stewardship) Rating represents our assessment of the quality of management's capital allocation, with particular emphasis on the firm's balance sheet, investments, and shareholder distributions. Analysts consider companies' investment strategy and valuation, balance sheet management, and dividend and share buyback policies. Corporate governance factors are only considered if they are likely to materially impact shareholder value, though either the balance sheet, investment, or shareholder distributions. Analysts assign one of three ratings: "Exemplary", "Standard", or "Poor". Analysts judge Capital Allocation from an equity holder's perspective. Ratings are determined on a forward looking and absolute basis. The Standard rating is most common as most managers will exhibit neither exceptionally strong nor poor capital allocation.

Capital Allocation (or Stewardship) analysis published prior to Dec. 9, 2020, was determined using a different process. Beyond investment strategy, financial leverage, and dividend and share buyback policies, analysts also considered execution, compensation, related party transactions, and accounting practices in the rating.

Sustainalytics ESG Risk Rating Assessment: The ESG Risk Rating Assessment is provided by Sustainalytics; a Morningstar company.

Sustainalytics' ESG Risk Ratings measure the degree to which company's economic value at risk is driven by environmental, social and governance (ESG) factors.

Sustainalytics analyzes over 1,300 data points to assess a company's exposure to and management of ESG risks. In other words, ESG Risk Ratings measures a company's unmanaged ESG Risks represented as a quantitative score. Unmanaged Risk is measured on an open-ended scale starting at zero (no risk) with lower scores representing less unmanaged risk and, for 95% of cases, the unmanaged ESG Risk score is below 50.

Based on their quantitative scores, companies are grouped into one of five Risk Categories (negligible, low, medium, high, severe). These risk categories are absolute, meaning that a 'high risk' assessment reflects a comparable degree of unmanaged ESG risk across all subindustries covered.

The ESG Risk Rating Assessment is a visual representation of Sustainalytics ESG Risk Categories on a 1 to 5 scale. Companies with Negligible Risk = 5 Globes, Low Risk = 4, Medium Risk = 3 Globes, High Risk = 2 Globes, Severe Risk = 1 Globe. For more information, please visit sustainalytics.com/esg-ratings/.

Ratings should not be used as the sole basis in evaluating a company or security. Ratings involve unknown risks and uncertainties which may cause our expectations not to occur or to differ significantly from what was expected and should not be considered an offer or solicitation to buy or sell a security.

Quantitative Valuation: Using the below terms, intended to denote the relationship between the security's Last Price and Morningstar's quantitative fair value estimate for that security.

- Undervalued: Last Price is below Morningstar's quantitative fair value estimate.
- Fairly Valued: Last Price is in line with Morningstar's quantitative fair value estimate.
- Overvalued: Last Price is above Morningstar's quantitative fair value estimate.

Risk Warning

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Essential Utilities Inc WTRG (NYSE) | ★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Capital Allocation	Industry Group	ESG Risk Rating Assessment[1]
48.86 USD	39.00 USD	Low	Narrow	Stable	Standard	Utilities - Regulated	

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Americas Utilities: Water - infrastructure spend, completed system acquisitions provide LT growth visibility; Buy on AWK, WTRG (on CL)

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Following 4Q2020 earnings, we remain Buy-rated on regulated water utilities American Water (AWK) and Essential Utilities (WTRG, on CL) as we see continued visibility into long-term investment growth from both organic infrastructure modernization and completed municipal system acquisitions, supported by an increasing state/federal focus on water quality and reliability.

Thus far in 2021, in a backdrop where the XLU has underperformed the S&P 500 by 8% driven by rising 10yr bond yields (albeit still at a relatively low ~1.5%), AWK/WTRG shares have declined around 6%/9% on an absolute basis while underperforming the XLU by 1%/4%, respectively. We believe this is driven somewhat by rotation into more value-oriented stocks within our sector, versus anything fundamental to the companies' growth propositions. We view the recent underperformance for both stocks providing a more compelling entry opportunity to gain exposure to these secular winners with a positive ESG footprint, with our $179/$55 price target for AWK/WTRG implying 28%/33% total return, respectively, versus 23% for Regulated Utilities.

WTRG: Water utility expansion, methane reduction strategy fuel growth; remain Buy (on CL)

We stay Buy-rated (on Conviction List) following 4Q2020 earnings on regulated water/gas utility Essential Utilities (WTRG), as we continue to see valuations not fully reflecting the company's primarily water utility exposure, and our expectation for the company to achieve the upper end of its 5-7% EPS CAGR. We believe WTRG's organic/inorganic water growth plans and de-carbonization strategy at its gas utility - as laid out in its January 2021 investor update call - should continue to bolster the case for WTRG as still one of the ESG-friendly stories in our coverage universe. In the near term, we note the pending $276mn DELCORA wastewater system acquisition - with the PA commission decision expected in March - and if completed we expect the Aqua PA utility to file a base rate case later this year. Finally, while WTRG mentioned moderate 1Q21 costs related to their Texas water utilities during the February winter weather event, we note the state represents roughly 6% of total rate base, with management not expecting a net impact to their

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2021 guidance forecast.

We maintain our 2021/2022 estimates while introducing 2023/2024 EPS estimates of $1.93/$2.05, respectively, reflecting a 6.7% CAGR from 2020A-2024E and a 7.1% CAGR from the weather-normal 2020 result of $1.56. We continue to embed issuance of the ~$300mn forward equity in 1Q2021 along with the close of the pending DELCORA municipal acquisition; we also assume $200mn of annual equity to finance future organic/acquisition investments while improving WTRG's FFO/debt from 12% in 2021 to 13% by 2024. Our model reflects the water utilities earning moderately below authorized, along with Peoples Gas ROEs trending down to authorized levels by 2024 (given wind-down of tax repairs and an assumed base rate increase in 2024).

Our $55, 12-month price target (unchanged) is based on a SOTP approach, with 35x/21x P/E applied to our 2022 water/gas utility EPS estimates, and 30x blended P/E on 2022 Other EPS, respectively. Downside risks to our call include: 1) PA regulation turns less constructive, which impacts earnings growth potential given the bulk of WTRG's earnings are derived from the state's water/gas operations, 2) water system acquisitions do not receive necessary approvals for completion, which could impact longer-term water rate base growth outlook barring replacement with other municipal acquisitions, and 3) longer-term growth concerns about the gas utility segment further compresses WTRG's valuation, both on an absolute basis and relative to pure-play water utilities.

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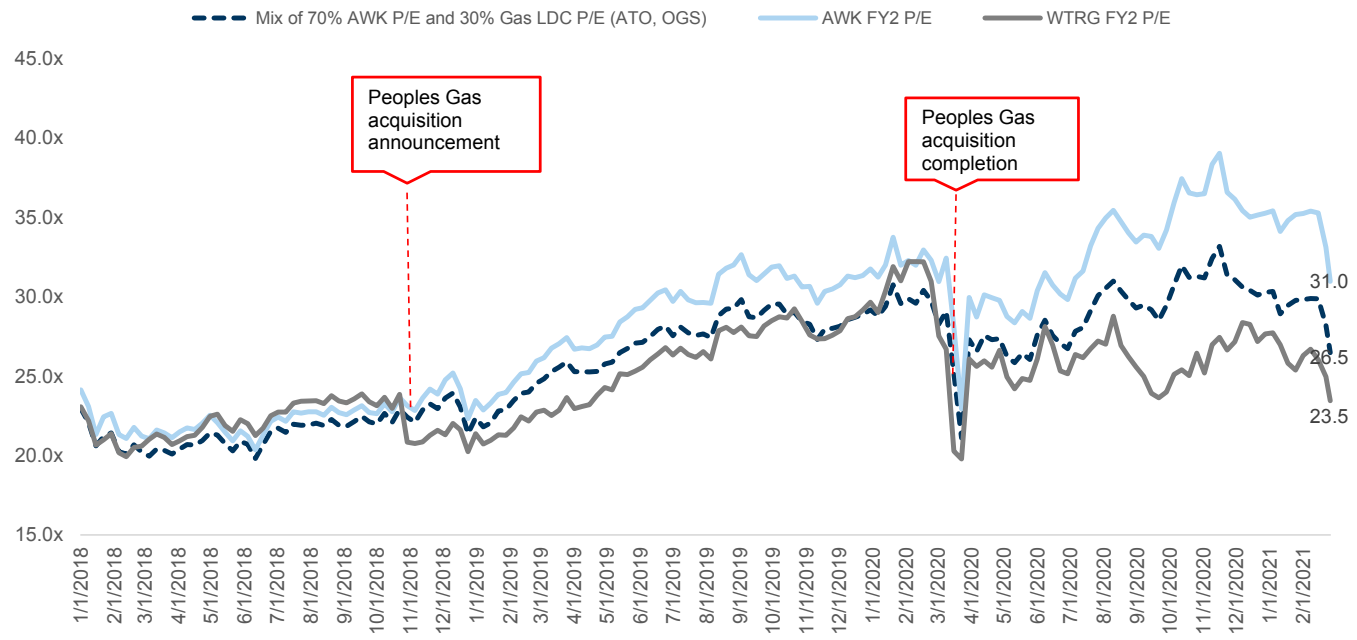
WTRG in Exhibits

Exhibit 1: We continue to see WTRG's valuations not fully reflecting its 70%/30% water/gas profile
FY2 P/E for AWK, WTRG, and an illustrative performance of a 70%/30% water/gas utility



ATO/OGS chosen as illustrative gas utility comps based on company profile, including their status as the two largest gas LDCs by market cap; forward P/Es based on Factset consensus

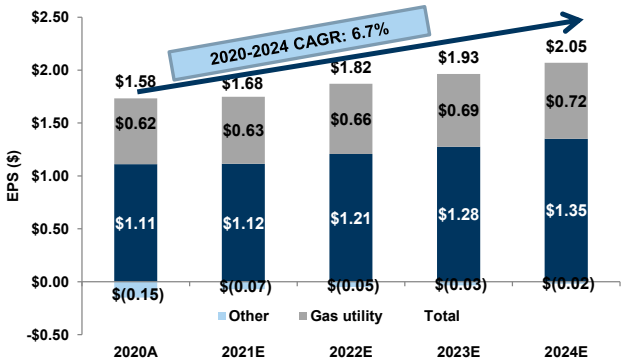
Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 2: We maintain our 2021/2022 estimates, while introducing 2023/2024...
EPS New vs Old vs Consensus

	EPS Estimates			% Difference	
	New	Old	Cons	vs Old	vs Cons
2021E	$1.68	$1.68	$1.67	0%	1%
2022E	$1.82	$1.82	$1.79	0%	2%
2023E	$1.93		$1.89		2%
2024E	$2.05		$2.05		0%

Source: Goldman Sachs Global Investment Research, Thomson Reuters

Exhibit 3: ...implying near-7% EPS CAGR through 2024
EPS CAGR, 2020A-2024E



Source: Company data, Goldman Sachs Global Investment Research

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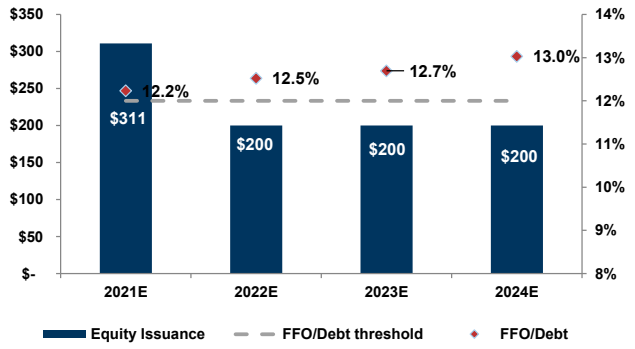
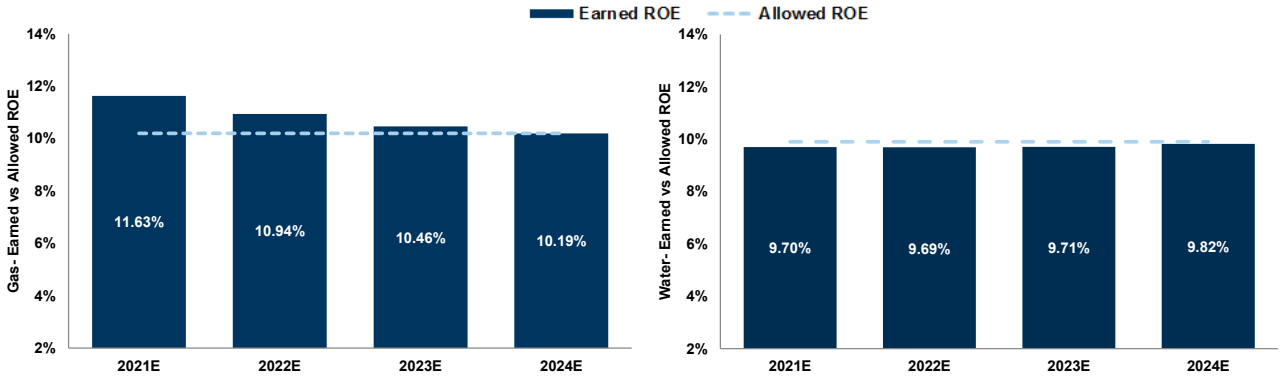
Exhibit 4: We assume annual equity issuances to support organic/inorganic growth while improving the balance sheet
Equity issuance and FFO/debt



Source: Goldman Sachs Global Investment Research

Exhibit 5: We assume the water utilities earn close to their allowed ROEs, while incorporating more robust (but moderating) ROEs for gas utilities given election of repairs tax in PA
Earned vs Allowed ROEs



Source: Company data, Goldman Sachs Global Investment Research

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Exhibit 6: Our SOTP-based $55 price target reflects a 33% total return potential versus 22% on average for our Regulated Utilities
WTRG SOTP Valuation

VALUATION	
Water utility EPS 2022	**1.21**
Water utility multiple	30.00x
Assumed premium	5.00x
Adjusted P/E	35.0x
Water utility valuation	**42.30**
Gas utility EPS 2022	**0.66**
Gas utility multiple	19.00x
Assumed premium	2.00x
Adjusted P/E	21.0x
Gas utility valuation	**13.93**
Valuation - Other	**(0.05)**
2020 Blended multiple	30.04x
Other valuation	**(1.50)**
Total valuation	**55.00**

Source: Goldman Sachs Global Investment Research

AWK: Best-in-class EPS/DPS growth with ESG tailwind; Buy

We stay Buy-rated on AWK post 4Q2020 earnings and Analyst Day given best-in-class EPS and dividend growth. We remain positive on AWK given its status as the only large cap, pure play, publicly traded water utility in the US, as well as its best-in-class ~8.5%+ EPS growth through 2024 driven by robust organic and inorganic water investment opportunities. In addition, we look favorably on the company's increased forecast for water/wastewater municipal system acquisitions that should further support AWK's predominantly regulated utility profile. Finally, we expect the stock to continue to benefit from a scarcity premium and ESG friendly profile that should continue to drive its premium valuation.

We tweak our 2021/2022 EPS estimates while introducing 2023/2024 estimates of $4.98/$5.40, respectively, implying an 8.4% CAGR from 2021A-2024E. Our model assumes $300mn/$200mn/$200mn of equity from 2022-2024, resulting in a 59% net debt/cap ratio and ~17% FFO/debt by 2024, along with earned ROEs of 9.2-9.3% at the Regulated segment versus 9.8% authorized.

Our $179, 12-month price target (unchanged) embeds our water base P/E multiple of 30.0x, as well as a 9x (30%) premium to account for AWK's above-average growth and favorable ESG profile, on our 2022 EPS. Key risks include water quality issues, cost management, regulatory environment, growth at non-regulated segments and reduced

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ESG fund flows.

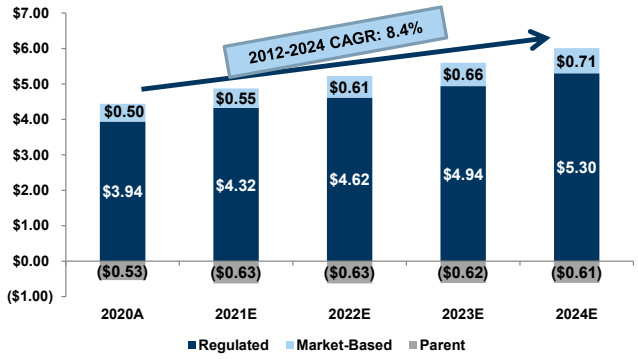
AWK in Exhibits

Exhibit 7: We tweak our 2021/2022 estimates while introducing 2023/2024...
EPS New vs Old vs Consensus

EPS Estimates				% Difference	
	New	Old	Consensus	vs Old	vs Consensus
2021E	$4.24	$4.25	$4.23	0%	0%
2022E	$4.60	$4.59	$4.58	0%	0%
2023E	$4.98		$4.98		0%
2024E	$5.40		$5.46		-1%

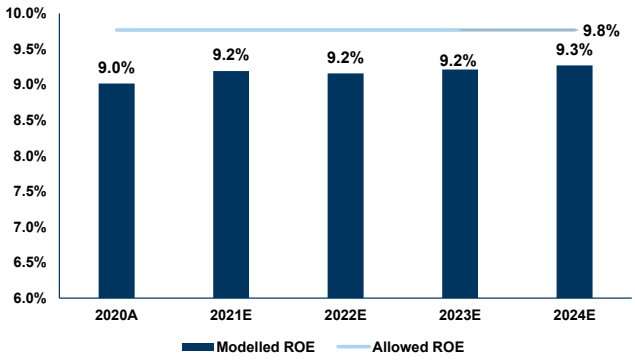
Source: Goldman Sachs Global Investment Research, Thomson Reuters

Exhibit 8: ...which reflect a best-in-class 8.4% EPS CAGR from 2020A-2024E
EPS CAGR, 2020-2024



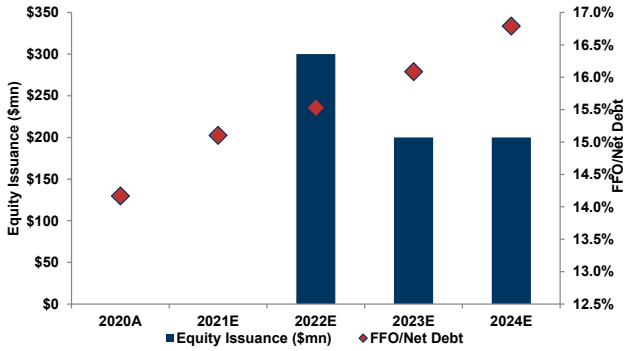
Source: Company data, Goldman Sachs Global Investment Research

Exhibit 9: Our estimates reflect moderate regulatory lag versus authorized ROEs
Authorized versus earned ROEs



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 10: We do assume annual equity issuances from 2022-2024, supporting regulated growth while improving the balance sheet
Equity issuance vs FFO/Net Debt



Source: Company data, Goldman Sachs Global Investment Research

Exhibit 11: Our price target embeds our water base P/E multiple of 30x and a premium to account for AWK's above-average growth and ESG profile
AWK valuation

AWK Valuation	
AWK 2022 EPS	**$4.60**
GS Water Utility Base Multiple	30.0x
Premium / (Discount)	9.0x
Adjusted P/E	**39.0x**
Utility Valuation	**$179**
AWK Valuation	**$179**

Source: Goldman Sachs Global Investment Research

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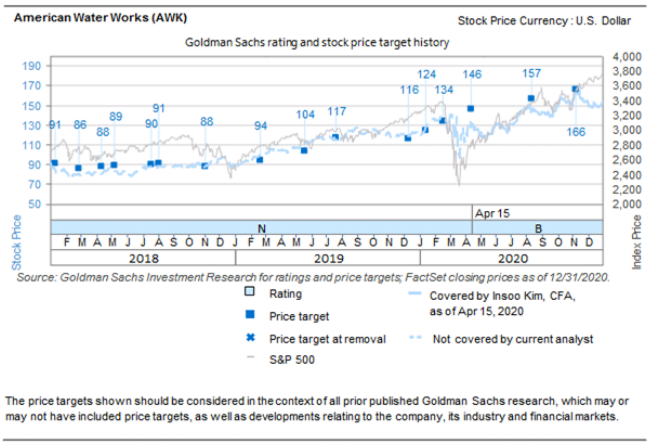

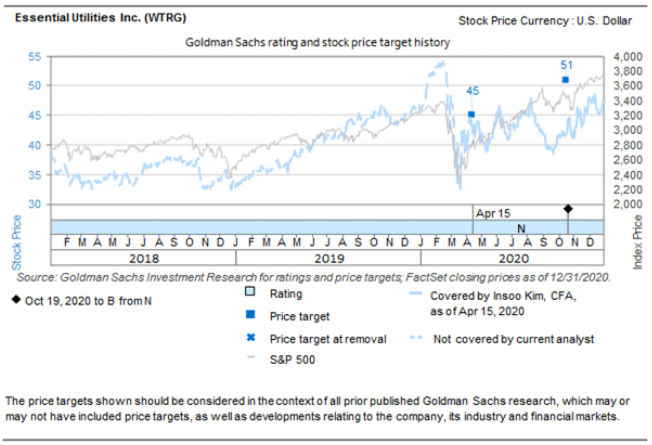

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Americas Energy: GS PUMP Conference: Top ten takeaways from the PUMP Conference panels and dinners

(https://research.gs.com/content/research/themes/power-utilities-mlps-and-pipelines-conference-2019.html)

After hosting this year's GS Power, Utilities, Midstream & Pipeline (PUMP) Conference here in NYC on August 13th, including dinners with FE (Buy), DTE (Buy) and NEE (Buy), we reiterate our top picks, including CL-Buy utilities CNP and SRE, along with NRG within the IPP sector and LNG among midstream stocks.

GS Top Ten Takeaways from Key Panels or Dinners with Company Executives:

1. **FE expects growth to slow after 2021, but from a current elevated rate versus peers of 6%-8%,** as capital spending flattens out and equity financing needs emerge...
2. **...but FE continues to highlight the separation from FES as largely complete.** We note the Nuclear Regulatory Commission's approval of plant ownership licenses - along with bankruptcy court approvals - remain the last steps, expected by 4Q2019.

3. **Substantial regulated renewable development at DTE Electric should support a net income CAGR toward at least the high end of the 7%-8%** operating earnings growth guidance range over the next few years as both the Renewable Energy Plan (REP) and Voluntary Green Program (VGP) spend drives a substantial ramp in renewable capex to meet RPS (renewable portfolio standards) and VGP targets by 2021/2022 - along with the new natural gas power plant in 2022.
4. **Representatives from the credit ratings agencies highlighted** (1) potential does exist, but more time may be needed to prove out the business model, for IPPs to reach investment grade status; (2) changes in oil or especially natural gas production levels could weaken credit metrics for gathering/processing focused midstream companies, but this is not a major 2019 concern yet for the agencies; and (3) offshore wind construction risk emerges now as a credit concern for utility holding companies
5. **NEE views its cost position still as a primary advantage for its FP&L subsidiary** - with costs (per kWh served) at its newly acquired Gulf Power subsidiary almost 2.5x greater than the level at its larger FP&L business, implying ample room for cost management ahead.
6. **More private investment into merchant power likely will occur going forward.** Multiple PE firms highlighted that many conventional merchant generation portfolios deliver double-digit free cash yields - albeit with sizable quarterly volatility - and even after facing new challenges such as subsidized generation (nuclear) in key states like IL, OH, NJ and NY. Funds participating in our conference expect more private capital to come into the space.
7. **WTR highlighted what remains a very attractive M&A landscape for water utilities** as (1) the U.S. has ~40,000+ municipally-owned water systems, and (2) fair market value regulation allows utilities to add goodwill in municipal water utility transactions to rate base.

8. **Capital spending by regulated utilities - as discussed at the conference - will migrate more and more towards distribution** versus spend on other items including large scale transmission.
9. **The Bakken should maintain enough oil/NGL takeaway as new or potential assets come online - more long haul gas pipeline capacity** needs may emerge. In the Bakken, the expansion of the Bakken Pipeline system (DAPL/ETCOP) and startup of OKE's Elk Creek pipeline should provide producers with sufficient long-haul takeaway for both crude oil and natural gas liquids (NGLs). However, there could be additional need for Bakken long-haul natural gas takeaway in the next few years given a reduction in flaring limits and continued growth in gas production.
10. **Along with demand-pull from traditional LNG buyers (including integrated and global utilities), there is growing supply-push from Permian producers** looking to secure flow assurance and end markets for their associated gas production. These producers see new LNG facilities as a way to get their gas to market - and to also reduce flaring levels, assuming pipeline capacity exists to get the gas to the new LNG terminals.

We also highlight a few key insights from panels at the GS PUMP Conference...

Key Trends and Challenges in Midstream Infrastructure in America (Jonathan Stein, CFO, Hess Midstream Partners. Ben Atkins, CFO, NextDecade Corp.)

- NEXT's (Not Covered) Rio Grande LNG project in Brownsville, TX has key competitive advantages over other LNG sites, including proximity to the Permian Basin, and better construction economics given access to labor and an underutilized ship channel.

- A self-funding strategy with minimal leverage remains key to HESM's financing strategy. The partnership is also mitigating its counterparty risk via third-parties - which currently comprise 15% and 30% of HESM's crude oil and natural gas volumes, respectively.

CEO Fireside Chat: The Outlook for Regulated Investment and Growth (Christopher Franklin, Chairman, CEO and President, Aqua America. Charles Jones, President and CEO, FirstEnergy Corp.)

- FE highlighted key types of investment opportunities in a handful of states, including incremental grid modernization in Ohio (i.e., the deployment of ~700,000 smart meters in the state), reliability improvement in Pennsylvania, and renewables as well as energy efficiency in New Jersey (partly driven by the governor's Energy Master Plan).
- WTR noted regulatory encouragement for consolidation across water utilities, as municipalities continue to own the majority of systems in the U.S. Fair market value regulation, allowing acquirers to add goodwill related to water utility M&A in to rate base, has helped make the economics of acquisitions work for IOUs (investor-owned utility).

Merchant and Contracted Power Business Models (Francisco Martinez-Davis, CFO, Atlantica Yield. Brian Vaasjo, President and CEO, Capital Power Corp. Matthew J. O'Connor, Managing Director, Carlyle Power Partners. Darren Olagues, Executive Vice President and CFO, GenOn Energy. Himanshu Saxena, CEO, Starwood Energy Group.)

- The recent delay in the PJM auction was viewed constructively as the correct rules and processes were not in place for a two-step auction. Panelists believe that subsidized assets should not bid in to the same auction as non-subsidized assets, and this will help investors acknowledge/realize the value of competitive assets.

- California's merchant power market structure may create reliability concerns. Current market structure doesn't provide proper compensation for reliability in CA, decreasing interest in incremental baseload generation in the state. In contrast, state policy goals drive significant investment in renewable generation assets. Some panelists believe misaligned incentives and difficulty in forecasting (particularly reliability payments) could create headwinds for CA power investors, but near-term, is supporting elevated RA payments. The GenOn (Not Covered) CFO noted that the NY power market could see a similar uptick in capacity payments as large nuclear assets retire and ambitious renewable goals impact the grid.
- Merchant power (as opposed to contracted power) likely continues to expand globally, with Atlantica Yield's (AY, Not Covered) CFO noting growing levels of comfort with merchant power in other countries -- although not AY's growth strategy. Additionally, panelists highlighted foreign capital searching for yield has driven down financing costs in the U.S., but increased the need for discipline among project developers.

Renewables Ahead, The Role of Natural Gas and The Impact Across the Energy Infrastructure Industries (Peter Oleksiak, Senior Vice President and CFO, DTE Energy. Eric Silagy, President and CEO of FP&L, NextEra Energy)

- NEE highlighted that a combination of customer count and load growth help control the costs of renewables to rate payers, but replacing aging infrastructure continues to provide tailwinds as well. The company noted every $1 of O&M saved creates room for ~$7 of incremental capital spending without impacting customer bills.
- Both NEE and DTE highlighted the cost savings of fleet transformation, with NEE noting $10bn of customer savings since 2001 driven by the heat rate differential between oil and other types of generation. DTE also highlighted the LT savings driven by

fleet rationalization, such as building gas plants near distribution and storage facilities, lower fuel costs, and lower operating and maintenance expenses.

- Within DTE's generation transformation, wind remains the primary source of renewable generation, but DTE expects solar to make headway by the mid-2020s. The company noted (1) it sees significant natural demand from corporates looking to meet internal sustainability goals and (2) its desire to remain in the regulated generation business as it proceeds through fleet transformation - given the value for customers from owning vs PPA'ing a renewable asset as it depreciates.

Generation and Grid Transformation - The Path Ahead (Martin Lyons, Executive Vice President and CFO, Ameren Corporation. Antonio Smyth, Senior Vice President of Transmission, American Electric Power. Rod West, President of Utility Operations, Entergy Corporation.)

- While MO remains a relatively coal-heavy state, AEE expects wind generation capital spending to precede coal plant retirements likely to occur in the next 10-15 years driven by MO's 2035 IRP goals.

The Evolution of State Policies and The Impact on Investment and Opportunity Sets (Stephen Wemple, Director, Consolidated Edison. Maria Pope, President and CEO, Portland General Electric. Steven Rasche, Executive Vice President and CFO, Spire Inc.)

- Panelists highlighted a handful of items on their regulatory wishlists, particularly we flag (1) ED looking for more earnings opportunities from regulatory assets related to renewable projects - as the company cannot own large-scale or customer sited renewables and (2) SR (Not Covered) is looking to replicate Alabama's real-time rate making process in another states.

- POR noted the preference for onshore wind over offshore wind on the West coast continues, driven partly by geographic factors (i.e., wavier waters making the use of buoys to support turbines difficult or the relatively steep nature of the ocean floor) as well as by grid restraints due to the lack of major transmission lines along the coast.

Insights on Power, Utilities and Midstream from the Credit Ratings Agencies (Shalini Mahajan, Managing Director of US Utilities, Fitch Ratings. Peter Molica, Senior Director of US Midstream, Fitch Ratings. James Hempstead, Managing Director of US Utilities, Moody's Investors Service. Elena Nadtotchi, Senior Credit Officer on Oil & Gas, Moody's Investors Service. Michael Grande, Senior Director of Midstream Energy and Refining, S&P Global Ratings. Aneesh Prabhu, Senior Director of Midstream Energy and Refining, S&P Global Ratings.)

- Merchant power can feasibly achieve investment grade credit ratings, but the ratings agencies noted that a limited track record may require more time. The integrated model should in theory work to limit volatility and provide a counter-cyclical business strategy by pairing retail with generation, yet the lack of data around a recession provides little evidence of how it truly holds up under significant stress. Longer-term, the agencies highlighted that there is no fundamental reason why merchant power cannot become IG, given that there is a certain level of debt to EBITDA that would be acceptable and that cash flow volatility has been 17%, lower than some investment grade refiners and with higher cash flow conversion rates.
- Ratings at the holdco level continue to converge to levels around BBB+. With limited benefit to an A credit rating - given tighter spreads - the agencies noted that over the past handful of years, an increasing amount of utility holdcos moved closer to BBB+ and the cash flow to debt metrics for large holding companies declined to about 15% compared to 16% in 2018 and a 2010-2015 average of

about 20%. The agencies highlighted that as utility holdcos give themselves less of a cushion on the credit side, execution risk can become an increasingly large concern over time.

...as well as highlights from our dinners with managements

We hosted a dinner with FE on Tuesday night (8/13) with no new major takeaways, but flag...

- Incremental equity financing will occur to help fund rate base growth and pension requirements - but not likely until 2022+.
- The company views its customer rates as a competitive advantage and does not want to risk losing this edge. FE highlighted its customer bills in key states (NJ, OH, PA, etc.) remain well below peers in those states.
- FE sees limited rate case or regulatory risk - while many investors question earnings levels in OH or PA, the company highlighted that PA earnings levels remain at or below required levels - needing the state's tracker implementation to improve earnings closer to authorized levels.

...while takeaways from our dinner with DTE include...

- Substantial regulated renewable development at DTE Electric should support a net income CAGR toward at least the high end of the 7%-8% operating earnings growth guidance range over the next few years
- Management continues to bake in significant contingencies into DTE's base case guidance. Across the subsidiaries, a level of conservatism makes the 5-7% EPS growth achievable, per management, and DTE highlighted that they often assume mild weather at the regulated segments to determine a starting guidance midpoint, emphasizing the resulting flexibility in their planning.

- Commissioner turnover has continued (with two new commissioners in MI), but DTE believes the key remains providing reliable performance and an open dialogue, understanding the commissioners' goals. Clean energy investments already continue to support significant growth, and the Utility welcomes more opportunities to transform its fleet. In general, following the 2016 energy deal, energy/utility reform does not appear top of mind for state legislators, and they feel comfortable with the current state of regulation.

...and we note a handful of highlights from our dinner with NEE

- The company believes battery storage remains in the very early stages and highlighted expectations to build batteries as part of a wind+solar+battery all-in-one development as well as building batteries in to the distribution and transmission system.
- FP&L highlighted a meaningful difference between its O&M profile relative to the recently acquired Gulf Power. The company noted non-fuel O&M of ~$12/MWh vs Gulf Power's near $30/MWh (near the national average).
- The company remains skeptical of the first wave of offshore wind, highlighting: (1) expectations for massive cost overruns leading to abandoned projects; (2) maintaining and repairing the plants will likely prove more expensive than expected; and (3) believes offshore wind in Europe has advanced largely due to saturation in European power markets.

GS Power & Utilities ratings grid

Exhibit 1: We continue to favor Diversified Utilities over pure-play Regulated Utilities
GS Power & Utilities ratings distribution

	Regulated Utilities	Diversified Utilities	IPPs
Buy	EIX, ES NI	CNP*, DTE ETR, EXC, FE NEE, SRE*	NRG*, NEP
Neutral	AEE, AEP AWK, CMS ED, PNW PPL	AGR, D PEG	CWEN
Sell	DUK, EVRG POR, SO WEC	OGE	

*Part of the Americas Conviction List

Source: Goldman Sachs Global Investment Research

GS Pipelines & MLPs ratings grid

Exhibit 2: LNG remains our top pick, followed by other large caps including ET, EPD and KMI

Pipelines and MLPs rating distribution

	C-Corps	MLPs
Buy	KMI, LNG*	ET, EPD, RTLR
Neutral	TGE, OKE, WMB, ENB, ENB.TO	CQP
Sell	TRP.TO, TRP	TCP

* Denotes Stock is on the Americas Conviction List

Source: Goldman Sachs Global Investment Research

Ratings and PT information

We reiterate our $47, 12-month target price for FE, derived using a SOTP, and remain Buy rated. Key risks for FE include utility regulation, power demand, cost management, and financing.

We remain Neutral rated AEE with a $76, 12-month price target, derived from a 19.75x P/E multiple on 2021E EPS. Key risks for AEE include regulation, project awards, and financing.

We reiterate our $88, 12-month price target for AEP, derived using a sum-of-the-parts, and remain Neutral rated. Key upside/downside risks for AEP include utility regulation, power demand, cost management, and financing.

We remain Buy rated ETR and derive our 12-month target price of $110 using a sum-of-the-parts valuation. Key risks for ETR include utility regulation, demand, and power pricing.

We reiterate our $86, 12-month price target for ED, derived from an 18x P/E multiple on 2021E EPS, and remain Neutral rated. Key risks for ED include CECONY earned RoEs, the ongoing CECONY rate case, CEB contracts, project awards, and financing.

We remain Sell rated with a $50, 12-month target price for POR, derived 85% using a fundamental 18x P/E multiple on 2021E EPS and 15% using a theoretical M&A 21.0x P/E multiple on 2021E EPS. Key risks include utility regulation and demand.

We remain Buy rated on NEE with our $221, 12-month target price, derived using an SOTP. Key risks include utility regulation, renewable development, and cost management.

We remain Buy rated on DTE with our 12 month $136 target price, derived using an SOTP. Key risks include regulatory, legislative, natural gas production, counterparty, transaction, and financing risk.

We remain Buy rated (on the CL) LNG with an $89, 12-month price target, derived with a 12x EV/EBITDA multiple on 2023E EBITDA. Key risks for LNG include construction costs, project financing, operational risk, and global natural gas prices.

We reiterate our $158, 12-month target price for SRE - derived using a sum-of-the-parts - and remain Buy rated (on the CL). Key risks for SRE include construction, utility regulation, and financing.

We remain Buy rated (on the CL) CNP with a $35, 12-month target price, derived using a sum-of-the-parts. Key risks include oil prices, merger synergies, utility regulation, and demand growth.

We remain Buy rated (on the CL) NRG with a $52, 12-month target price. We base our NRG price target 85% on a sum-of-the-parts implying $52/share and 15% on a 9.25x EV/EBITDA M&A multiple implying $54/share. Key risks include power prices, retail margins, cost management, and customer growth.

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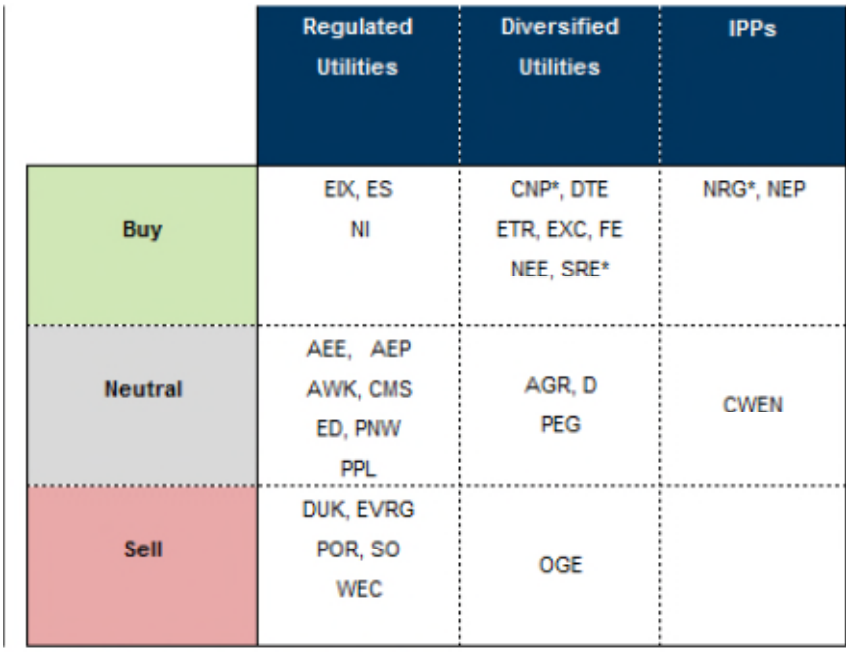

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Essential Utilities Inc. (WTRG): 2021 guidance in-line, 5-7% EPS growth extended to 2023

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Regulated water/gas utility Essential Utilities (WTRG, Buy-CL) today introduced 2021 EPS guidance range of $1.64-$1.69 ($1.67 mid-point), relatively in-line with GS/consensus of $1.68/$1.66. The company also extended its 5-7% EPS CAGR forecast through 2023 (versus 2022 prior), using 2020 as the base while reiterating expectations to achieve the upper end of the 2020 guidance range of $1.53-$1.58. In short, we view today's release as largely in-line with our expectations and reaffirming WTRG's focus on water utility expansion and system de-carbonization. We reiterate our Buy rating (on CL), as we continue to see WTRG as a secular winner to benefit from material water infrastructure investment needs in a fragmented market, with valuations not fully reflecting the company's primarily water utility exposure.

We also highlight some key additional disclosures:

- **Extension of 6-7%/8-10% rate base CAGR through 2023 for water/gas utilities,** respectively, using 2019 as the base. We note the water rate base growth excludes rate base additions from municipal acquisitions; inclusive of acquisitions, we calculate the growth rate at between 8-9%. Management also reaffirmed its strategy to maintain at least a 70%/30% water/gas mix by rate base.
- **Expect DELCORA acquisition close by 2Q2021.** With the recently favorable district court decision supporting the asset purchase agreement (APA) between Aqua and DELCORA, management expects the PA commission to provide its decision in March, with the deal close shortly after. We note this wastewater deal represents the largest municipal acquisition done by WTRG, with the ~$310mn forward equity offering already priced in August 2020.
- **WTRG plans to reduce CO2 emissions 60% by 2035** from 2019 levels, both at the gas and water/wastewater segments, via gas infrastructure replacement as well as using renewable electricity for its water operations.

Our $51, 12-month price target (unchanged) is based on a SOTP approach, with 35x/22x P/E applied to our 2021 water/gas utility EPS estimates, respectively. Downside risks to our call include: 1) PA regulation turns less constructive, which impacts earnings growth potential given the bulk of WTRG's earnings are derived from the state's water/gas operations, 2) the proposed DELCORA municipal water

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system acquisition does not receive necessary approvals for completion, which could impact longer-term water rate base growth outlook barring replacement with other municipal acquisitions, and 3) longer-term growth concerns about the gas utility segment further compresses WTRG's valuation, both on an absolute basis and relative to pure-play water utilities.

WTRG	12m Price Target: **$51.00**	Price: **$48.72**	Upside: **4.7%**

Buy CL

Market cap: $12.4bn
Enterprise value: $17.9bn
3m ADTV: $47.4mn
United States
Americas Utilities
M&A Rank: 3
Americas Conviction List

GS Forecast

	12/19	12/20E	12/21E	12/22E
Revenue ($ mn)	889.7	1,571.5	1,998.9	2,125.8
EBITDA ($ mn)	521.4	748.4	1,008.8	1,102.5
EBIT ($ mn)	360.8	492.1	704.9	767.7
EPS ($)	1.47	1.57	1.68	1.82
P/E (X)	27.6	31.0	29.0	26.7
EV/EBITDA (X)	19.1	23.7	18.8	17.7
FCF yield (%)	(2.4)	(1.5)	(1.7)	(0.1)
Dividend yield (%)	2.2	2.0	2.1	2.3
Net debt/EBITDA (X)	2.3	7.4	6.2	6.2

	9/20	12/20E	3/21E	6/21E
EPS ($)	0.23	0.45	0.69	0.31

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 8 Jan 2021 close.

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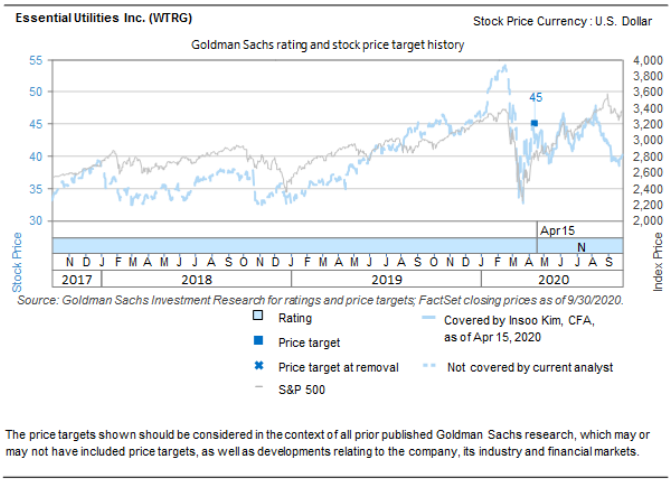

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Americas Utilities: Updating estimates for a few Neutral-rated regulated utilities

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Essential Utilities (WTRG, Neutral)

We tweak down our 2020-2022 EPS estimates to $1.55/$1.63/$1.78 from $1.56/$1.65/$1.78, respectively, to reflect 1) 10-Q update, 2) increased equity dilution in 4Q20 from lower assumed share price, and 3) moderately higher interest expense. We note our 2020 estimate incorporates 1Q20 adjusted EPS of $0.60 as reported by the company, which does not include the mild weather impact on the Peoples Gas segment. We assume relatively flattish gas load growth from 2019A-2022E, while embedding +2%/-1% water customer/usage growth during the same period. We continue to view favorably Essential's heavily residential customer mix for both water/gas businesses that could mitigate the negative COVID-19 related demand impact from commercial/industrial customers. While we estimate a robust 6.4% EPS CAGR from 2019A-2022E, we view WTRG's current valuation as fairly representing the company's water/gas utility mix.

Our $45 12-month price target (unchanged) reflects a 12% total return is based on an SOTP valuation methodology. We apply our 30x base water target P/E multiple to 2021E EPS for the water utility segment, along with a 22x P/E multiple to 2021E EPS for the gas utility segment. Our gas multiple reflects a 10% (or 2x) premium to our 20x base gas target P/E, given our view of the segment's above-average rate base and EPS growth. **Key upside risks** include: 1) Peoples Gas acquisition synergies exceed our expectations, elevating EPS growth profile, 2) tax repairs election for the PA gas utility elevates earned ROEs even above our estimate, and 3) WTRG continues to benefit from ESG fund flows, despite its water/gas utility mix profile on a pro-forma basis. **Key downside risks** include: 1) PA regulation turns less constructive, 2) growth from municipal acquisitions slows, and 3) WTRG credit rating is downgraded.

Eversource Energy (ES, Neutral)

We adjust down our 2020 EPS estimate to $3.63 from $3.66 while our 2021/2022 estimates remain unchanged at $3.89/$4.12, respectively. The lower 2020 estimate stems from a combination of lower expected demand at the New Hampshire electric utility (with no decoupling unlike most of the other ES utility jurisdictions), modestly lower estimates for corporate/other, and partially offset by lower O&M expense (assume -1% CAGR from 2019-2022E). Our model does not incorporate the

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pending $1.1bn acquisition of Nisource's Columbia Gas of Massachusetts (CMA) utility. We view ES with its largely demand decoupled utility portfolio as well positioned to mitigate the current COVID-19 environment while continuing to grow at a robust ~6% EPS CAGR; however, we remain Neutral rated largely on valuation despite acknowledging potential longer-term earnings upside from its investments in offshore wind (mostly in 2024 and beyond).

Our $88 12-month price target (unchanged) implies a 15% total return and is based on a 22.5x P/E applied to our 2021 EPS. **Key upside risks** include improved offshore wind return forecasts, reduced permitting/construction hurdles, indications of additional rate base investments. **Key downside risks** include ineffective cost management, slowing rate base growth, dilutive acquisitions, and delays/cost overruns in ES's offshore wind investments.

Xcel Energy (XEL, Neutral)

We lower our 2020/2021 EPS estimates to $2.75/$2.95 from $2.79/$2.97, while our 2022 estimate remains unchanged at $3.17, implying a 6.3% EPS CAGR from 2019A-2022E. Our adjustments reflect 1) 10-Q update, 2) lower electric demand in 2020/2021 per our GSe forecast, 3) lower O&M expense, and 4) updates related to the recent Texas and New Mexico rate case settlements. Our estimates reflect an 8.6%/8.8%/8.9% earned ROE in 2020-2022, respectively, versus the 9.4% weighted average authorized ROE across the various jurisdictions. We continue to view favorably XEL's revenue decoupling mechanism at its Minnesota and Colorado (residential and small commercial) utilities, which comprise the majority of its consolidated earnings. However, we see the company's ability to implement strong cost controls (-4% to -5% YoY guided by company), especially sustainable cost cuts, as key to achieving its original 2020 EPS guidance range and its 5-7% growth rate. Finally, we view XEL's 7.5% rate base growth as intact, supported by new renewable investments, potential to take ownership of existing PPAs, and ongoing grid modernization efforts.

Our $66 12-month price target (unchanged) reflects a 12% total return and is based on a 2.25x (13%) premium to our baseline 2021E P/E multiple of 20x. Despite our view that XEL could sustain its current ~6.5% EPS growth over the next 10 years given long-term visibility of regulated investment growth, the stock's YTD outperformance - now reflecting a ~3x (15%) premium - makes us incrementally more negative. **Key upside risks** include: 1) Further upward revisions to rate base/EPS growth through increased capital support incremental multiple expansion, 2) XEL realizes higher EPS growth through sustained O&M savings initiatives, and 3) the U.S. government extends federal renewable tax credits, lowering renewable costs and accelerating XEL's capital growth. **Key downside risks** include: 1) negative rate case outcomes impact the utilities' earnings power, 2) XEL realizes less generation into rate base vs. PPA, impacting rate base growth, 3) PPA buyouts do not materialize, stemming incremental rate base growth opportunities, and 4) COVID-19 meaningfully impacts non-decoupled demand in addition to increased cash drag from customer bill non-payment.

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Growth is based on a stock's forward-looking sales growth, EBITDA growth and EPS growth (for financial stocks, only EPS and sales growth), with a higher percentile indicating a higher growth company. **Financial Returns** is based on a stock's forward-looking ROE, ROCE and CROCI (for financial stocks, only ROE), with a higher percentile indicating a company with higher financial returns. **Multiple** is based on a stock's forward-looking P/E, P/B, price/dividend (P/D), EV/EBITDA, EV/FCF and EV/Debt Adjusted Cash Flow (DACF) (for financial stocks, only P/E, P/B and P/D), with a higher percentile indicating a stock trading at a higher multiple. The **Integrated** percentile is calculated as the average of the Growth percentile, Financial Returns percentile and (100% - Multiple percentile).

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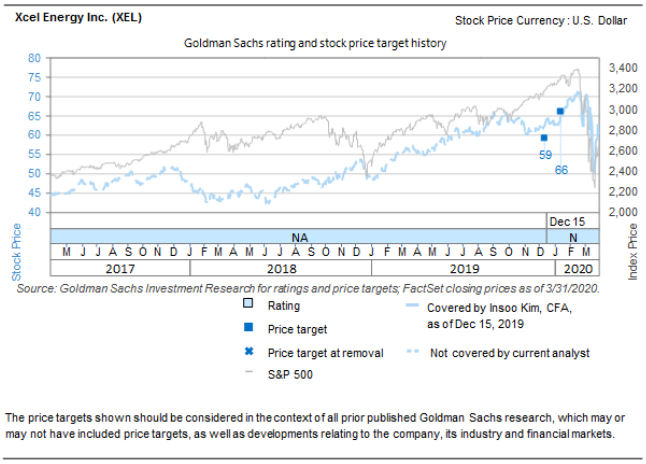

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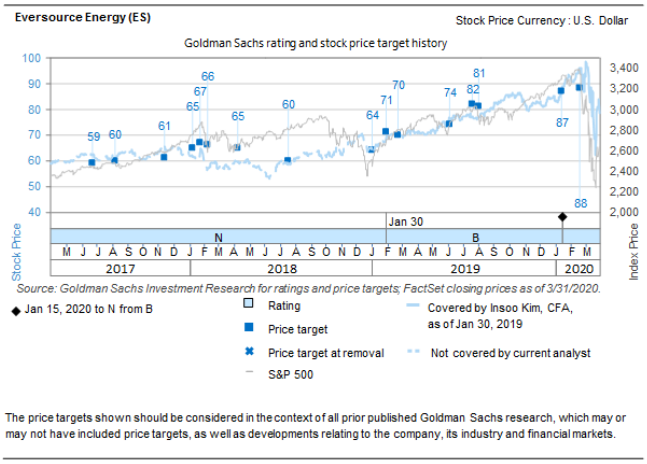

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Americas Utilities: Water: First Takes: AWK, WTRG report solid 2Q20, reiterate guidance

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American Water (**AWK**, Buy) and Essential Utilities (**WTRG**, Neutral) reported quarterly earnings this afternoon. **In short, both companies met or exceeded consensus expectations while reaffirming 2020 guidance, EPS growth, and capital forecasts. We also note that both companies' water demand/margins showed relative resiliency in the current COVID-19 environment, given heavy residential customer exposure**; case in point, WTRG recorded an increase in water usage and margins YoY, as robust residential usage more than offset declines in the other customer classes. We expect shares of both companies to react favorably tomorrow.

American Water Works (AWK, Buy): 2Q2020 results relatively inline, 2020 guidance and EPS growth reiterated

AWK reported 2Q2020 adjusted operating EPS of $0.97, inline with GS and above FactSet estimates of $0.97/$0.96 and versus 2Q2019 of $0.94. The company maintained its 2020 EPS guidance range of $3.79-$3.89 ($3.84 midpoint) versus GS/consensus of $3.85/$3.83, while reiterating the long-term EPS growth CAGR of 7-10%.

Regarding COVID-19, AWK pointed to a -$0.05 EPS for the quarter, driven by a -18%/-12% YoY demand impact for its commercial/industrial segment, partially offset by an 8% increase for residential. We note C&I usage constitutes around 30% of total volumes. At the Homeowner Service segment, AWK noted a -$0.01 of impact due to delayed partner relationships. Total COVID-related impact is expected at between -$0.05 to -$0.08 for the year, while consolidated capital spend expectations remain unchanged at $1.9bn.

Key topics to monitor on AWK's earnings call (8/6 @ 9am ET) include (1) updated thoughts on water/wastewater usage trends for the balance of the year, (2) potential for Homeowner Service revenues could be impacted further given COVID-19, (3) thoughts on potential for increased muni acquisition opportunities over the next 1-2 years above forecast, and (4) potential opportunities/challenges for AWK from potential changes to tax reform and or clean energy/water plans.

Essential Utilities (WTRG, Neutral): 2Q2020 beat GS/consensus, 2020 guidance

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WTRG reported 2Q2020 pro-forma EPS of $0.29, vs GS/consensus of $0.17/$0.23, with the beat largely due to quarterly timing of O&M and other expenses, in our view, but also helped by **positive YoY water usage/margins from positive residential demand more than offseting lower C&I usage**. WTRG maintained its 2020 guidance of $1.53 to $1.58, versus GS/consensus of $1.55/$1.56, as well as its 5-7% EPS forecast from 2019A-2022E; we note the 2020 EPS guidance assumes full quarter contribution from the Peoples acquisition. Management also reiterated their 2020 water/gas capex guidance of $550mn/$400mn, as well as $2.8bn of total capex from 2020-2022.

Key topics to monitor on WTRG's earnings call (8/6 @ 11am ET) include (1) assumptions on gas usage trends in 2H2020, (2) latest update on potential revenue/cost synergy levels from integration of Peoples Gas, 3) thoughts on potential for increased muni acquisition opportunities over the next 1-2 years above forecast, and (4) potential opportunities/challenges for WTRG from potential changes to tax reform and or clean energy/water plans.

Price Targets and Key Risks

AWK, Buy: Our $146, 12-month price target is based on a 34.5x P/E multiple on our 2021E EPS. Key risks include water quality issues, cost management, regulatory environment, growth at non-regulated segments, and reduced ESG fund flows.

WTRG, Neutral: Our $45, 12-month price target is based on an SOTP. Key risks include Peoples Gas acquisition synergies, tax repair election in PA, ESG fund flows, PA regulation, growth from municipal acquisitions, and credit rating downgrade.

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Growth is based on a stock's forward-looking sales growth, EBITDA growth and EPS growth (for financial stocks, only EPS and sales growth), with a higher percentile indicating a higher growth company. **Financial Returns** is based on a stock's forward-looking ROE, ROCE and CROCI (for financial stocks, only ROE), with a higher percentile indicating a company with higher financial returns. **Multiple** is based on a stock's forward-looking P/E, P/B, price/dividend (P/D), EV/EBITDA, EV/FCF and EV/Debt Adjusted Cash Flow (DACF) (for financial stocks, only P/E, P/B and P/D), with a higher percentile indicating a stock trading at a higher multiple. The **Integrated** percentile is calculated as the average of the Growth percentile, Financial Returns percentile and (100% - Multiple percentile).

Financial Returns and Multiple use the Goldman Sachs analyst forecasts at the fiscal year-end at least three quarters in the future. Growth uses inputs for the fiscal year at least seven quarters in the future compared with the year at least three quarters in the future (on a per-share basis for all metrics).

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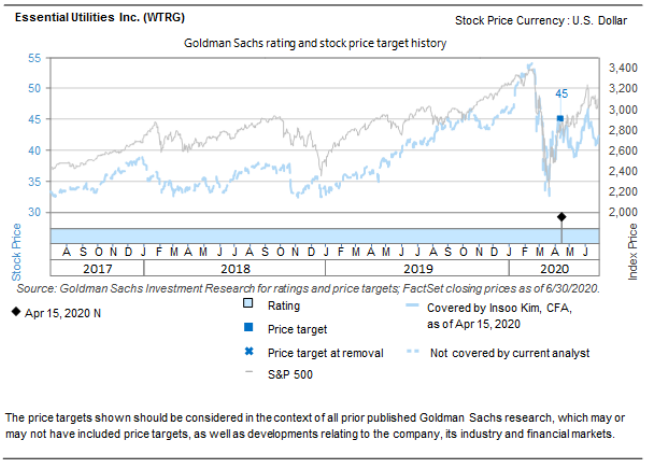

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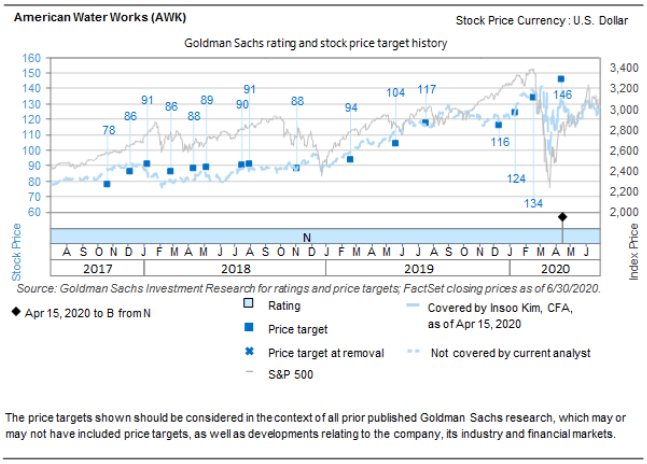

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Buy CL

Essential Utilities Inc. (WTRG)

The under-appreciated water growth opportunity; Upgrade to Buy (add to CL)

WTRG	12m Price Target: **$51.00**	Price: **$41.55**	Upside: **22.7%**

We upgrade regulated water/gas utility Essential Utilities (WTRG) to Buy from Neutral and add to the Conviction List. As one of two large-cap, publicly traded regulated water utilities in the US, we see WTRG as a secular winner to benefit from an estimated $750 billion of water infrastructure investment needs (per the EPA) in a very fragmented market. This represents at least a $7bn opportunity – well above its total current water asset base – excluding any market share gains through municipal and other water utility acquisitions.

After YTD underperformance of 10% versus the XLU, we see current prices reflecting a 7x (20%) P/E discount for the company's water utility segment (comprising ~70% of total earnings) versus the only other large-cap water utility American Water (AWK, Buy); we view this as unwarranted while undervaluing WTRG's normalized EPS growth potential similar to AWK's, representing one of the highest in our coverage universe.

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Key Data

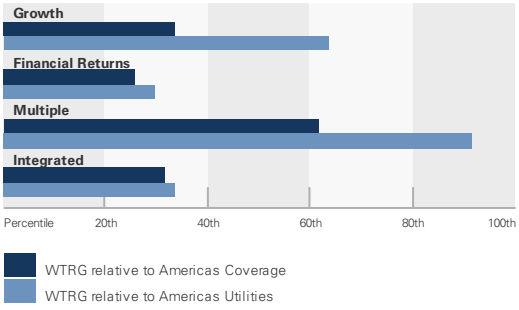
Market cap: $10.6bn
Enterprise value: $16.1bn
3m ADTV: $48.7mn
United States
Americas Utilities
M&A Rank: 3
Americas Conviction List

GS Forecast

	12/19	12/20E	12/21E	12/22E
Revenue ($ mn) New	**889.7**	**1,571.7**	**1,995.4**	**2,113.5**
Revenue ($ mn) Old	889.7	1,571.7	2,032.7	2,165.6
EBITDA ($ mn)	521.4	777.5	1,047.8	1,122.3
EBIT ($ mn)	360.8	525.4	755.5	800.4
EPS ($) New	**1.47**	**1.55**	**1.66**	**1.80**
EPS ($) Old	1.47	1.55	1.65	1.80
P/E (X)	27.6	26.8	25.0	23.1
Dividend yield (%)	2.2	2.3	2.5	2.7
Net debt/EBITDA (X)	2.3	7.2	6.0	6.1

	6/20	9/20E	12/20E	3/21E
EPS ($)	0.29	0.22	0.44	0.69

GS Factor Profile



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Buy CL

Essential Utilities Inc. (WTRG)

Rating since Oct 19, 2020

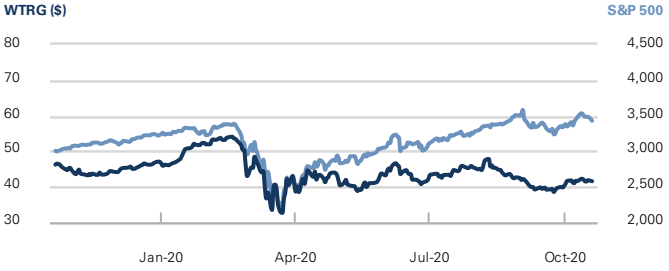
Ratios & Valuation

	12/19	12/20E	12/21E	12/22E
P/E (X)	27.6	26.8	25.0	23.1
EV/EBITDA (X)	19.1	20.5	16.3	15.8
EV/sales (X)	11.2	10.1	8.6	8.4
FCF yield (%)	(2.4)	(1.8)	(1.9)	(0.3)
EV/DACF (X)	19.1	21.0	17.1	16.3
CROCI (%)	6.6	6.9	6.8	6.8
ROE (%)	10.8	9.2	8.8	9.0
Net debt/EBITDA (X)	2.3	7.2	6.0	6.1
Net debt/equity (%)	31.1	118.9	121.6	128.4
Interest cover (X)	–	2.6	3.0	2.9
Inventory days	NM	32.2	25.3	25.3
Receivable days	42.8	30.3	28.0	26.4
Days payable outstanding	NM	156.0	138.3	138.3

Growth & Margins (%)

	12/19	12/20E	12/21E	12/22E
Total revenue growth	6.2	76.7	27.0	5.9
EBITDA growth	23.0	49.1	34.8	7.1
EPS growth	4.2	5.4	7.5	7.9
DPS growth	7.0	7.0	7.0	7.0
Gross margin	100.0	85.2	83.6	84.5
EBIT margin	40.6	33.4	37.9	37.9

Price Performance



	3m	6m	12m
Absolute	(7.1)%	(4.2)%	(10.8)%
Rel. to the S&P 500	(12.6)%	(19.6)%	(22.3)%

Source: FactSet. Price as of 19 Oct 2020 close.

Income Statement ($ mn)

	12/19	12/20E	12/21E	12/22E
Total revenue	889.7	1,571.7	1,995.4	2,113.5
Cost of goods sold	0.0	(232.9)	(327.5)	(327.5)
SG&A	(391.1)	(600.5)	(659.3)	(699.7)
R&D	–	–	–	–
Other operating inc./(exp.)	22.7	39.3	39.2	35.9
EBITDA	**521.4**	**777.5**	**1,047.8**	**1,122.3**
Depreciation & amortization	(160.6)	(252.1)	(292.3)	(321.9)
EBIT	**360.8**	**525.4**	**755.5**	**800.4**
Net interest inc./(exp.)	(125.3)	(201.5)	(249.6)	(274.7)
Income/(loss) from associates	–	–	–	–
Pre-tax profit	**327.9**	**424.5**	**505.9**	**525.7**
Provision for taxes	(10.5)	(30.1)	(71.2)	(56.5)
Minority interest	–	–	–	–
Preferred dividends	–	–	–	–
Net inc. (pre-exceptionals)	**317.4**	**394.4**	**434.7**	**469.1**
Net inc. (post-exceptionals)	**317.4**	**394.4**	**434.7**	**469.1**
EPS (basic, pre-except) ($)	**1.47**	**1.58**	**1.67**	**1.80**
EPS (diluted, pre-except) ($)	**1.47**	**1.55**	**1.66**	**1.80**
EPS (ex-ESO exp., dil.) ($)	**--**	**--**	**--**	**--**
DPS ($)	0.91	0.97	1.04	1.11
Div. payout ratio (%)	61.6	61.4	62.3	61.8
Wtd avg shares out. (basic) (mn)	215.6	249.7	260.9	260.9
Wtd avg shares out. (diluted) (mn)	215.9	254.6	261.1	261.1

Balance Sheet ($ mn)

	12/19	12/20E	12/21E	12/22E
Cash & cash equivalents	1,868.4	110.7	43.4	46.0
Accounts receivable	107.6	152.9	152.9	152.9
Inventory	18.4	22.7	22.7	22.7
Other current assets	18.3	129.7	129.7	129.7
Total current assets	**2,012.7**	**416.0**	**348.6**	**351.2**
Net PP&E	6,345.8	9,389.8	10,625.6	11,427.3
Net intangibles	63.8	2,342.4	2,342.4	2,342.4
Total investments	6.0	5.9	5.9	5.9
Other long-term assets	933.7	1,316.9	1,316.9	1,316.9
Total assets	**9,362.0**	**13,470.9**	**14,639.4**	**15,443.7**
Accounts payable	74.9	124.1	124.1	124.1
Short-term debt	130.8	122.4	147.4	177.4
Current lease liabilities	–	–	–	–
Other current liabilities	113.3	201.7	201.7	201.7
Total current liabilities	**319.0**	**448.2**	**473.2**	**503.2**
Long-term debt	2,943.3	5,548.1	6,160.0	6,710.0
Non-current lease liabilities	–	–	–	–
Other long-term liabilities	2,218.8	2,799.5	2,856.5	2,901.7
Total long-term liabilities	**5,162.2**	**8,347.6**	**9,016.5**	**9,611.8**
Total liabilities	**5,481.1**	**8,795.8**	**9,489.7**	**10,114.9**
Preferred shares	–	–	–	–
Total common equity	**3,880.9**	**4,675.2**	**5,149.7**	**5,328.8**
Minority interest	–	–	–	–
Total liabilities & equity	**9,362.0**	**13,470.9**	**14,639.4**	**15,443.7**
BVPS ($)	18.00	18.73	19.74	20.43

Cash Flow ($ mn)

	12/19	12/20E	12/21E	12/22E
Net income	224.5	293.6	434.7	469.1
D&A add-back	156.5	252.1	292.3	321.9
Minority interest add-back	–	–	–	–
Net (inc)/dec working capital	(62.3)	6.3	–	–
Others	19.3	25.7	57.0	45.2
Cash flow from operations	**338.0**	**577.8**	**784.0**	**836.3**
Capital expenditures	(550.3)	(768.1)	(992.4)	(864.4)
Acquisitions	(59.7)	(3,466.8)	(535.7)	(259.2)
Divestitures	–	–	–	–
Others	5.4	0.0	–	–
Cash flow from investing	**(604.6)**	**(4,234.9)**	**(1,528.2)**	**(1,123.7)**
Dividends paid	(188.5)	(237.2)	(271.0)	(290.0)
Share issuance/(repurchase)	1,947.6	734.1	310.9	–
Inc/(dec) in debt	371.1	1,390.4	636.9	580.0
Others	1.2	11.6	–	–
Cash flow from financing	**2,131.4**	**1,899.0**	**676.8**	**290.0**
Total cash flow	**1,864.8**	**(1,758.1)**	**(67.3)**	**2.6**
Free cash flow	(212.3)	(190.3)	(208.4)	(28.2)
Free cash flow per share (basic) ($)	(0.98)	(0.76)	(0.80)	(0.11)

Source: Company data, Goldman Sachs Research estimates.

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PM Summary

We upgrade regulated water/gas utility Essential Utilities (WTRG) to Buy from Neutral and add to the Conviction List given the following key points:

1. **We see WTRG as a secular winner to benefit from the EPA's estimated $750 billion of water infrastructure investment needs in a very fragmented market.** With the estimates from the Environmental Protection Agency (EPA), and based on WTRG's current 1% market share of US customer connections, this implies at least a $7bn investment opportunity, translating into 15 years of 6-7% organic earnings growth, or ~8% including municipal acquisitions.
2. **WTRG's recent acquisition of PA-based gas utility diluted its pure-play water profile but supports robust growth through de-carbonization.** We view this acquisition as a one-off investment in gas – from a recent conversation with management – given its geographic proximity to water headquarters, along with a robust growth opportunity via aging pipe replacement investments that should reduce 119k tons of CO2 over the next 15 years, equivalent to emissions from 25k cars or 13k homes.
3. **WTRG should benefit from a scarcity premium** as one of two large-cap, publicly traded water utilities in the US that comprise 80% of the sector's total market capitalization, as well as a **renewed ESG focus** given water utilities still comprise 70% of total earnings and management's focus on increasing the exposure.
4. **We view WTRG's multiple compression versus water utilities as overdone,** with current prices reflecting a 7x (20%) discount for the company's water utility segment versus the only other large-cap water utility American Water (AWK, Buy), which we view as unwarranted (Exhibit 4) given comparable long-term growth potential (Exhibit 5). From another angle, we see the market valuing WTRG as a 60% gas utility despite its 70% water earnings composition. Given management's strategy to further increase its water utility exposure over time, we believe WTRG deserves a premium valuation to reflect its high growth, largely ESG-friendly profile.

Our 12-month price target $51 (from $45 prior) reflects a 24% total return versus 13% for Regulated Utilities, with our estimates reflecting a robust 7% EPS/DPS CAGR from 2019A-2022E versus a 5% average for Regulated Utilities.

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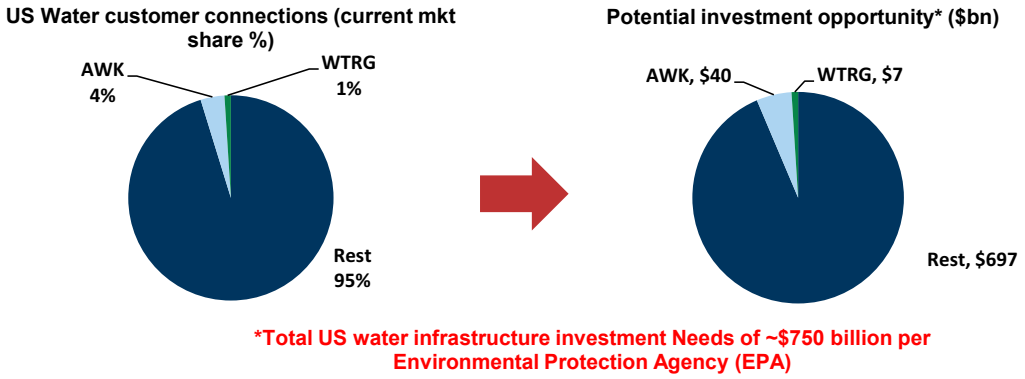
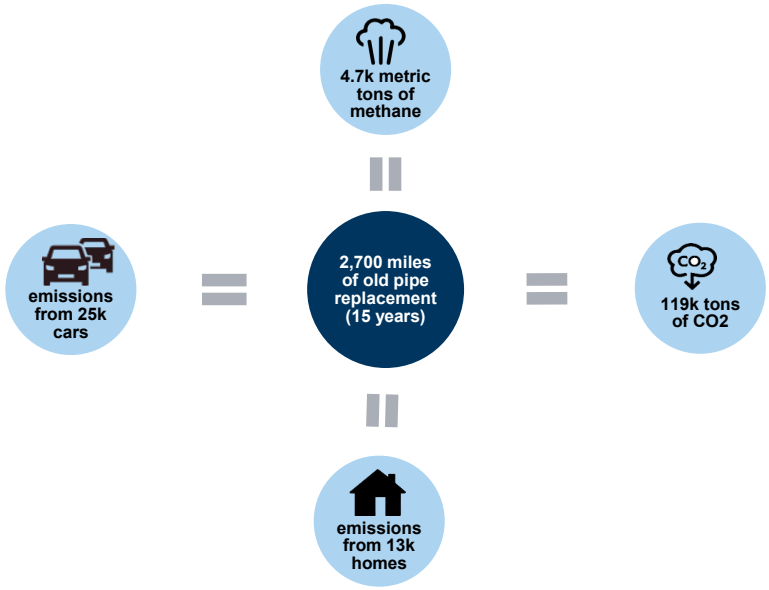
Exhibit 1: With an estimated $750 billion in US water investment needed, WTRG could see at least a $7bn opportunity at current market share, well above its total current water asset base...
US water investment needs, potential opportunity for WTRG/AWK



Source: Company data, Goldman Sachs Global Investment Research, Environmental Protection Agency

Exhibit 2: ...along with aging gas infrastructure replacement that supports de-carbonization
Potential emission reductions from aging gas pipe replacement



Old pipe replacement refers to bare steel and cast iron pipes

Source: Company data, Goldman Sachs Global Investment Research

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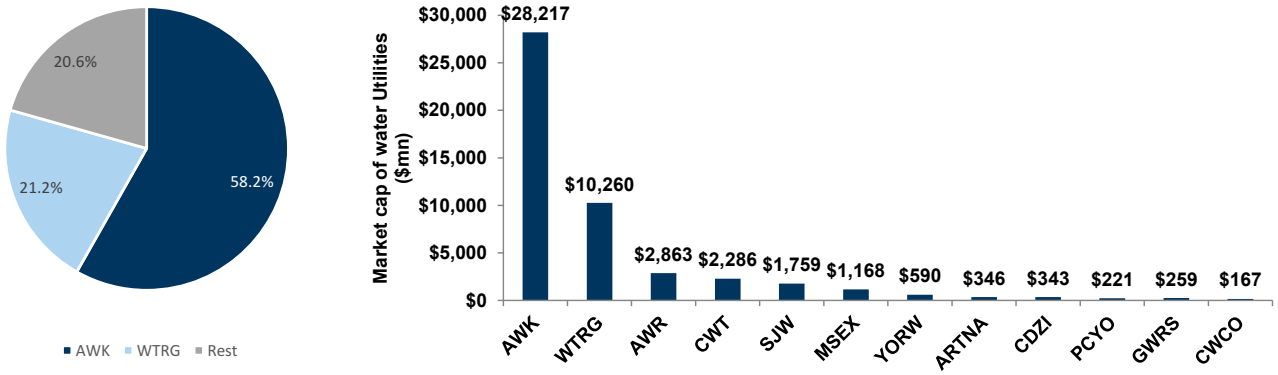
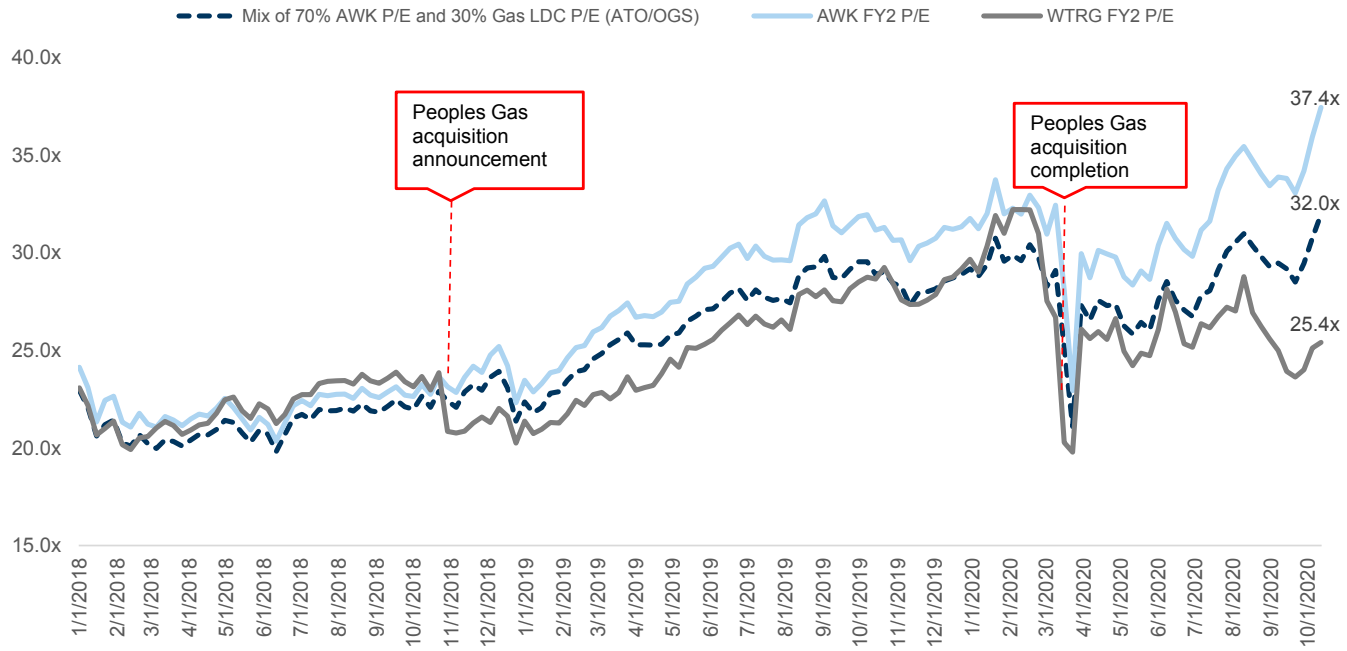
Exhibit 3: WTRG represents one of only two large-cap, publicly traded water utilities in the US, which should support a scarcity premium
Investor-owned water utilities by market cap and by % of total



as of 10/16/20

Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 4: We view WTRG's meaningful relative P/E discount as unwarranted based on its 70%/30% water/gas profile...
FY2 P/E for AWK, WTRG, and an illustrative performance of a 70%/30% water/gas utility



ATO/OGS chosen as illustrative gas utility comps based on company profile, including their status as the two largest gas LDCs by market cap

Source: FactSet, Goldman Sachs Global Investment Research

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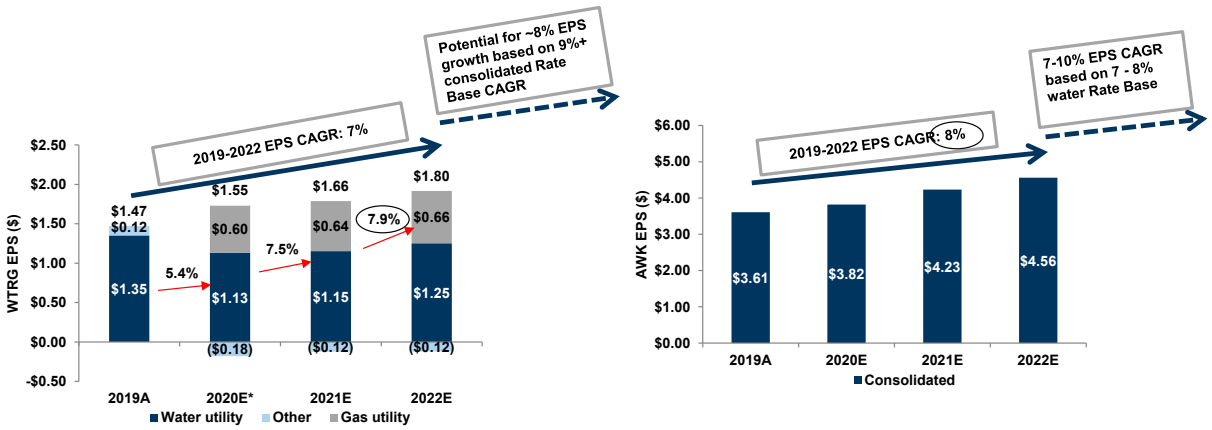
Exhibit 5: ...given we see WTRG's normalized EPS growth potential relatively in-line with that for AWK
WTRG/AWK EPS CAGR, 2019A-2022E; longer-term EPS/rate base growth potential



*Represents AWK's guidance through 2024, with another 1-2% EPS growth contribution expected from its market-based segment. WTRG rate base growth CAGR based on GS estimates.

Source: Company data, Goldman Sachs Global Investment Research

Thesis #1: Material investment needs for US water infrastructure provide secular growth opportunity for WTRG

The $750 billion water proposition. Aging infrastructure and increased regulation in the sector are primary drivers for the need to modernize the country's water and wastewater infrastructure related to water quality and the management of water and wastewater residual discharges. Because pipe assets last a long time, water systems that were built in the latter part of the 19th century and throughout much of the 20th century have not, for the most part, experienced the need for pipe replacement on a large scale. To put this aging infrastructure into context, the Environmental Protection Agency (EPA) estimates almost $750 billion of investment needed to upgrade the country's water systems, both public and private, to meet environmental standards. Based on WTRG's current 1% market share of US customer connections, this implies at least a $7bn investment opportunity, more than the company's current ~$5bn water rate base, supporting visibility to grow rate base at the current 6-7% rate for almost the next 15 years (excluding municipal acquisitions).

The water utility sector is highly fragmented... Of the 50,000/15,000 water/wastewater systems nationwide, only 16%/2% are run by investor-owned utilities (IOUs) and privately held water utilities, making the water industry the most fragmented of the major utility industries (electric, natural gas, water/wastewater). With local municipalities owning and operating the majority of the community water systems, many face challenges associated with their aging, deteriorating water and wastewater assets, do not have the expertise or technical capabilities to continue to comply with ever-increasing environmental regulations or simply want to focus on other community priorities.

...and Fair Market Value (FMV) legislation offers acquisition opportunities for

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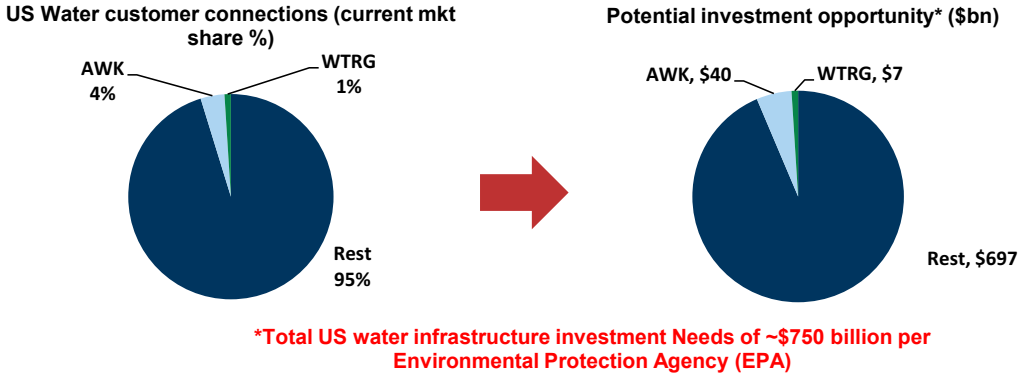
WTRG. The sector has been ripe for consolidation for decades and the largest water utilities have recently altered their strategic growth efforts to focus on buying mid-sized municipal water and wastewater systems fueled by fair market value (or FMV); legislation allows the water utilities to include into rate base the fair market value of the acquired municipal water assets instead of the depreciated original cost of water/wastewater assets. FMV is on the books in all of WTRG's 8 operating jurisdictions, which should allow WTRG to aggressively increase its water utility footprint, per the company's current opportunity set that could increase its customers served by 30% if fully successful. For illustrative purposes, a 1% increase in WTRG's market share by people served could add ~100% of WTRG's 2019A water utility rate base (Exhibit 10), all else equal.

Exhibit 6: We see meaningful water infrastructure replacement opportunities for WTRG that near its current market cap...
US water investment needs, potential opportunity for WTRG/AWK



Source: Company data, Goldman Sachs Global Investment Research, Environmental Protection Agency

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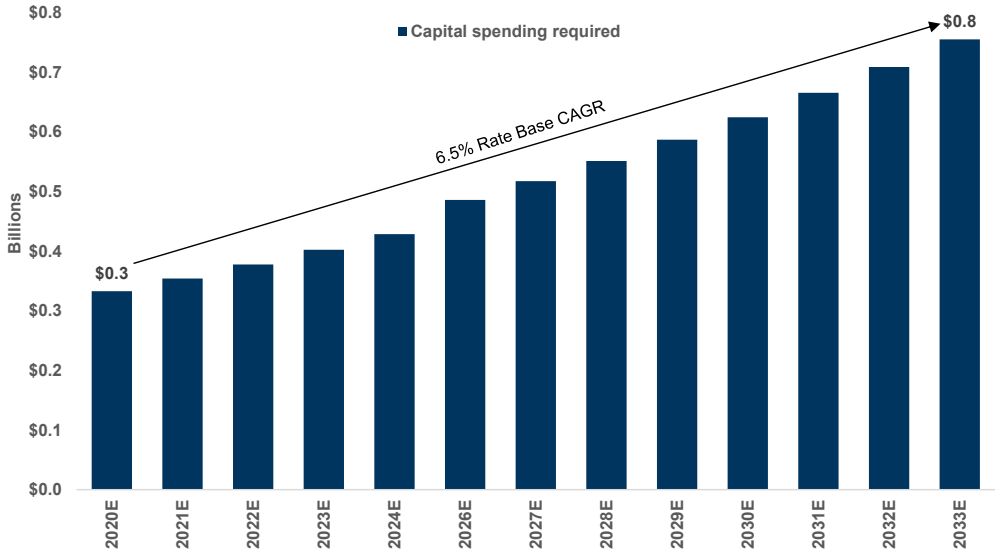
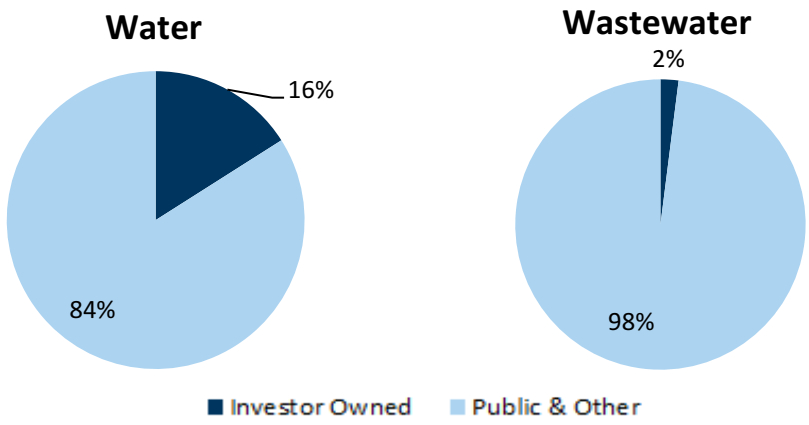
Exhibit 7: ...which could allow WTRG to grow its water rate base at the current 6-7% rate for nearly 15 years (excluding municipal acquisitions that could add an incremental 1-2% growth)
Number of years of 6.5% rate base growth achievable with $7bn of capital spending



Excludes potential rate base additions from municipal system acquisitions

Source: Company data, Goldman Sachs Global Investment Research

Exhibit 8: ...along with consolidation opportunities given IOUs and privately held water utilities operate only a small portion of the US water/wastewater systems
Water Industry- Investor Owned vs Public & Other market share, as of 2019



Source: Company data, Goldman Sachs Global Investment Research

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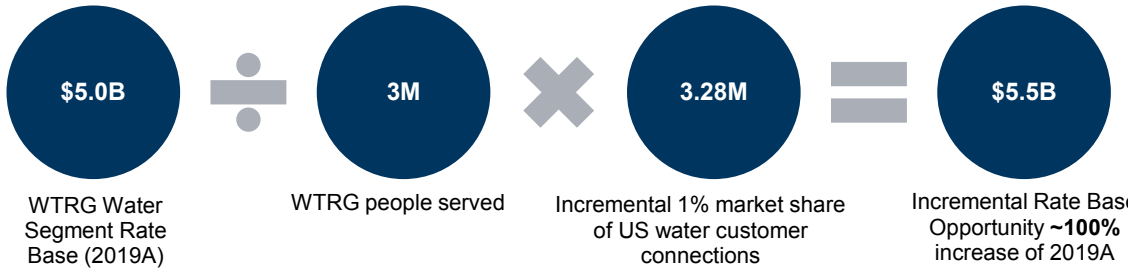
Exhibit 9: FMV legislation provides further impetus for consolidation, with all 8 of WTRG's water utility states passing the law
States with Fair Market Value Legislation for Water Utilities, WTRG states of operations

Source: Company presentation

Exhibit 10: For illustrative purposes, a 1% increase in WTRG's market share by people served could add ~100% of 2019A rate base, all else equal.
Illustrative calculation of incremental rate base from a 1% increase in WTRG's water market share



Source: Company data, AWWA, Goldman Sachs Global Investment Research

Thesis #2: Gas utility infrastructure investments supports robust growth through de-carbonization

We view the recent Peoples Gas acquisition as a one-off investment into gas utilities. WTRG's October 2018 decision to acquire privately held PA-based gas utility Peoples Gas, and the March 2020 completion, created a new asset mix for the company that now comprises 70%/30% water/gas utility by rate base and earnings. While this diluted the company's pure-play water profile supported by ESG-focused investors, in our view, we believe the investment did offer geographic synergy opportunities given WTRG's PA-based headquarters, while adding an under-invested gas system with robust growth opportunities. We note WTRG does not intend to grow its gas utility footprint through other acquisitions, per our recent conversation with management.

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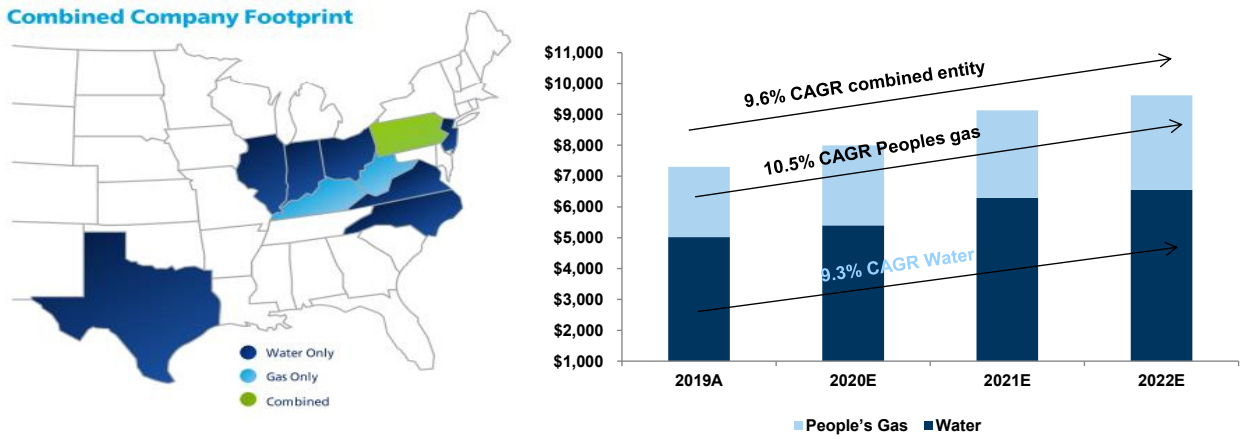
Peoples Gas offers robust growth through aging pipe replacement... We see ~10% rate base growth at Peoples Gas from 2019A-2022E primarily driven by long-term visibility of pipeline replacement projects. We note that Peoples has identified more than 2,700 miles of bare steel and cast iron pipe to be replaced under its Long-term Infrastructure Improvement Plan (LTIIP) by 2034 in its PA service territory, which at ~180-200 miles/year of pipe replacement, implies more than 15 years of increased capital spending to help support visibility of 9% rate base CAGR beyond 2022. We note this growth does not depend on new gas customer connections.

...while achieving de-carbonization. In addition to reliability and safety benefits from aging infrastructure replacement, we highlight that these investments also reduce meaningful methane emissions in the process. Per the company's data, the ~200 miles per year of pipe replacement reduces 9,000 tons of CO2, equivalent to emissions from 1,900 cars or 1,000 homes. Based on the 2,700 miles of identified cast iron/bare steel in the Peoples Gas system, this would equate to 25k cars or 13k homes.

Exhibit 11: We view WTRG's acquisition of Peoples Gas as a one-off gas investment that offers geographic synergies and robust growth...
WTRG operational footpring; rate base ($mn) 2019A-2022E



Water rate base growth includes municipal acquisitions

Source: Company data, Goldman Sachs Global Investment Research

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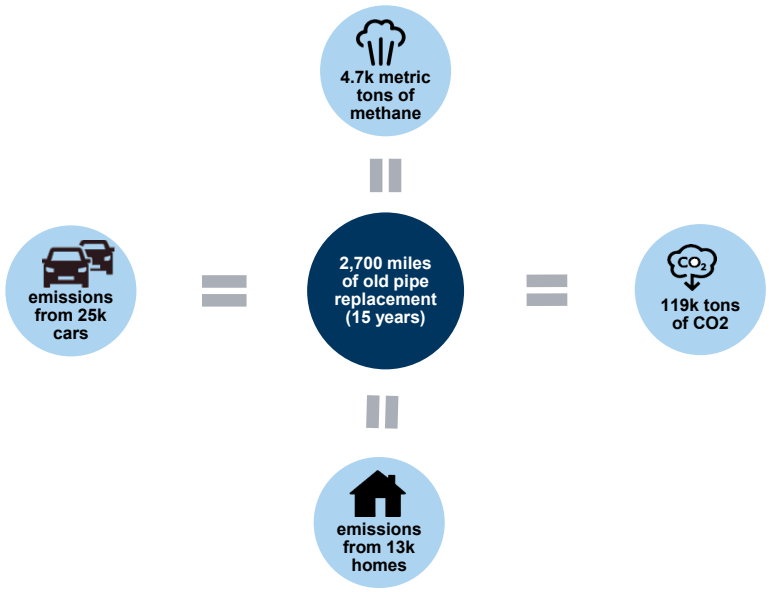
Exhibit 12: ..with aging gas infrastructure replacement that supports de-carbonization
Potential emission reductions from aging gas pipe replacement



Old pipe replacement refers to bare steel and cast iron pipes

Source: Company data, Goldman Sachs Global Investment Research

Thesis #3: WTRG should benefit from a scarcity premium, renewed ESG focus

WTRG is one of only two large-cap, publicly traded water utility in the US. Given the very light trading volumes for the majority of the water IOUs, we believe investors have limited options to invest in water utilities, which should benefit WTRG longer-term. In addition, while the company's recent acquisition of Peoples Gas diluted its status as a pure-play water utility, we see WTRG's 70% earnings mix to water utilities and management's strategy to grow the exposure over time should regain the attention of more ESG-focused investors, given their large overweight position to Water Utilities including WTRG per the recent data and publication from our GS SUSTAIN team (Exhibit 14, Exhibit 16).

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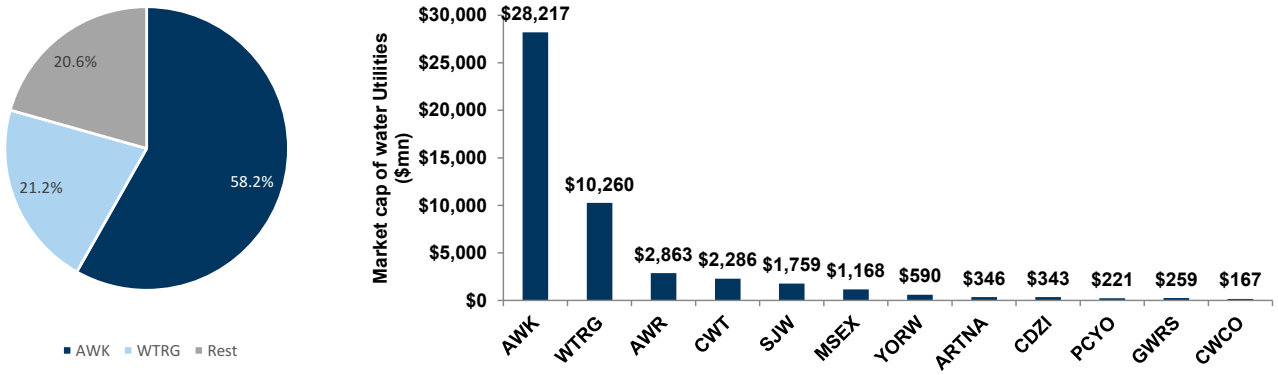
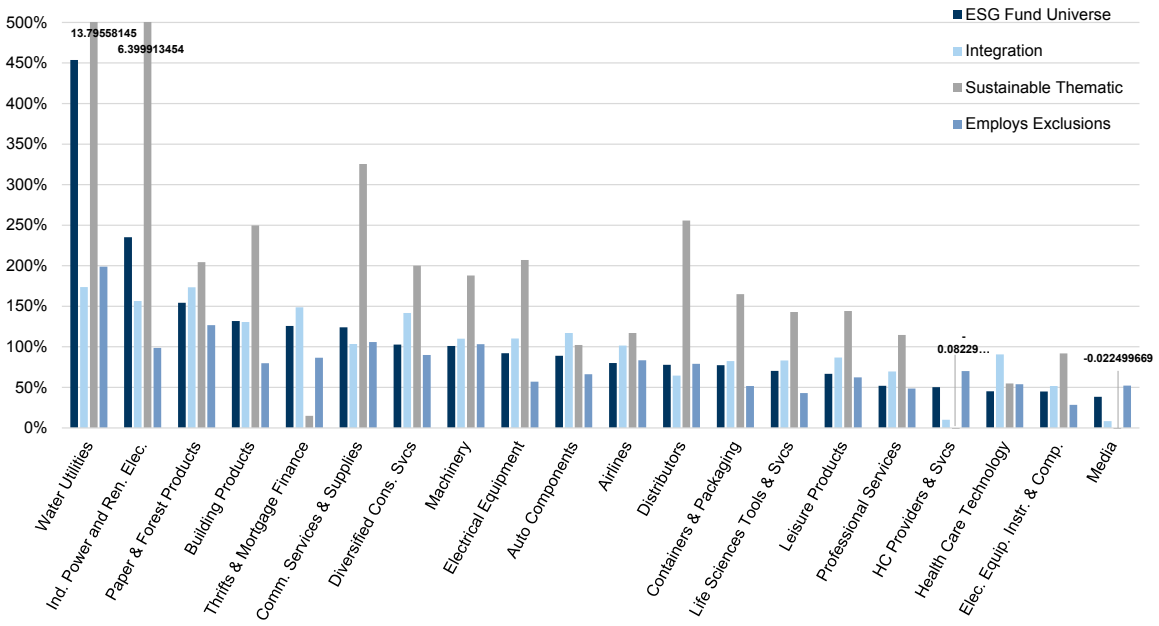
Exhibit 13: WTRG and AWK comprise around 80% of total water IOUs in the US
Investor-owned water utilities by market cap and by % of total



as of 10/16/20

Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 14: Water Utilities are the most overweighted industry by ESG owners
20 most overweighted industries (GICS 3) by ESG-linked equity funds



Source: Morningstar, Thomson Reuters, Goldman Sachs Global Investment Research, GS SUSTAIN

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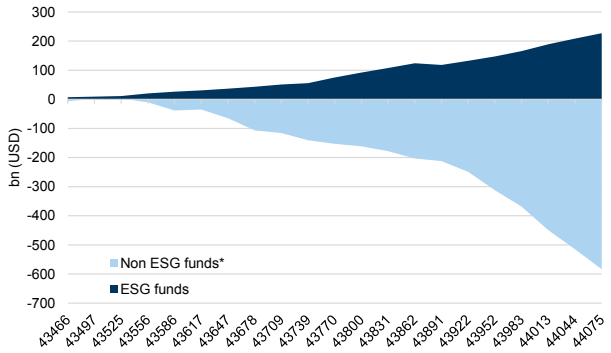
Exhibit 15: ESG fund flows have stood in stark contrast to non-ESG counterparts
Cumulative monthly fund fulows for ESG and non-ESG equity funds (1/2019-9/2020)



Source: Morningstar, Goldman Sachs Global Investment Research, GS SUSTAIN

Exhibit 16: WTRG still ranks as one of the most overweight US companies by ESG funds
Top 10 most relatively overweighted US companies by ESG funds (August 2020)

	Company	Sector
1	First Solar Inc	Info Tech
2	Xylem Inc	Industrials
3	Tetra Tech Inc	Industrials
4	American Water Works	Utilities
5	Sunrun Inc	Industrials
6	Essential Utilities Inc	Utilities
7	IDEX Corp	Industrials
8	Trimble Inc	Info Tech
9	PTC Inc	Info Tech
10	Nuance Communications	Info Tech

Source: Morningstar, Thomson Reuters, Goldman Sachs Global Investment Research, GS SUSTAIN

Thesis #4: WTRG's valuation under-appreciates secular water growth outlook

We view WTRG's multiple compression versus water utilities as overdone, despite its acquisition of privately held PA gas utility Peoples Gas in early 2020 (30% of consolidated earnings) that removed its pure-play water profile and contributed to the underperformance, in our view. Per Exhibit 17, the stock started experiencing P/E multiple compression in October 2018 with the acquisition announcement, with continued pressure following its deal completion in March 2020. The valuation spread versus the other large-cap water utility – American Water (AWK, Buy) – now stands at ~12x P/E on 2021E, versus relatively in-line as of the Peoples Gas acquisition announcement.

We see WTRG's normalized LT EPS growth rate as relatively in-line with that for AWK at around 8% – representing one of the highest growth rates in our coverage universe – given the potential for a 9%+ combined rate base CAGR assuming continued robust municipal acquisitions. We note our estimated 7% EPS CAGR through 2022 reflects certain items including: 1) earnings and financing lag associated with the proposed DELCORA acquisition and timing of inclusion into rate base (1Q2021 equity issuance assumed, rate base inclusion in 2022), 2) the expiration of tax-advantaged rate-making - repairs tax - at the PA water segment and a return to normal rate-making, and 3) the recent election of repairs tax for Peoples Gas and timing of associated earnings benefit.

While we continue to view a discount versus AWK as warranted for WTRG, given our sum-of-the-parts (SOTP) valuation approach for the water/gas businesses versus AWK's pure-play water profile, we see current multiples meaningfully under-valuing the water business (Exhibit 18), based on WTRG's P/E discount versus an illustrative

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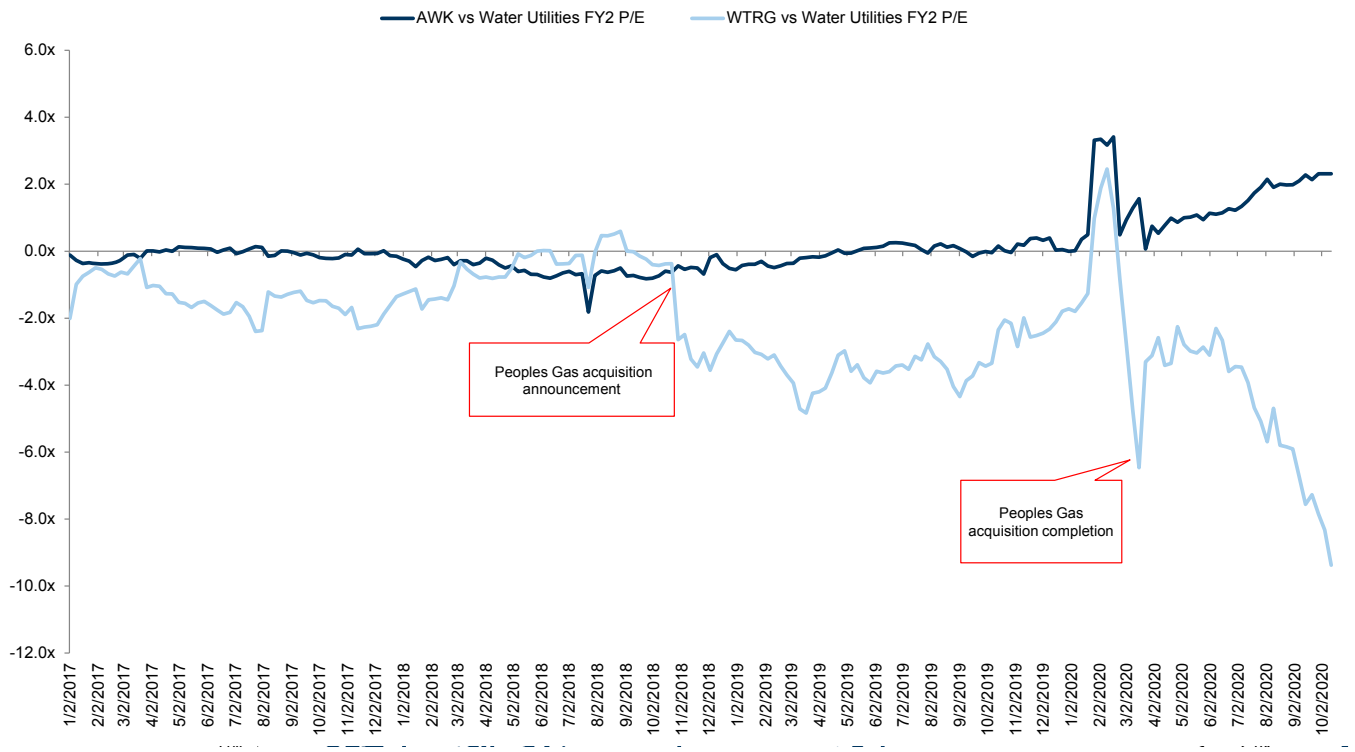
70%/30% water/gas utility mix. In addition, we view management's strategy to increase its water exposure over time as supporting an ESG-friendly profile, which should warrant a premium valuation.

Exhibit 17: WTRG has experienced meaningful relative multiple compression since its announced acquisition of privately held gas utility Peoples Gas

AWK & WTRG vs Water Utilities FY2 P/E (market-cap weighted)



Source: FactSet, Goldman Sachs Global Investment Research

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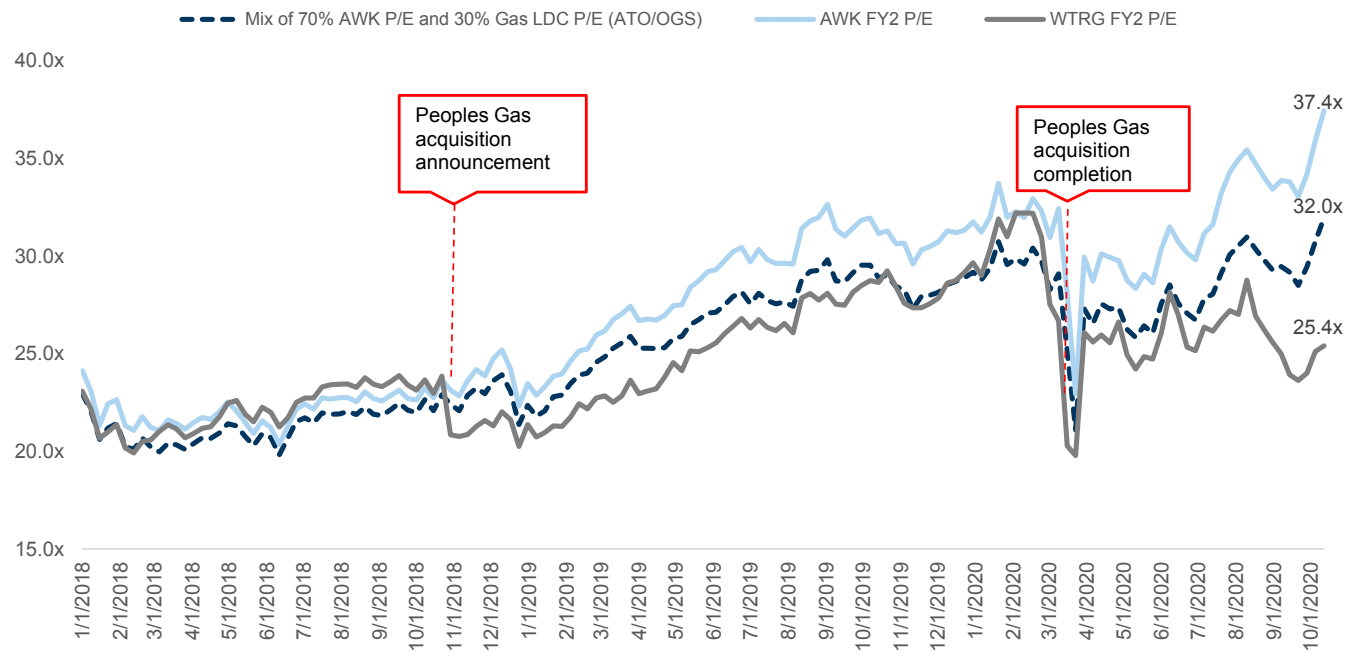
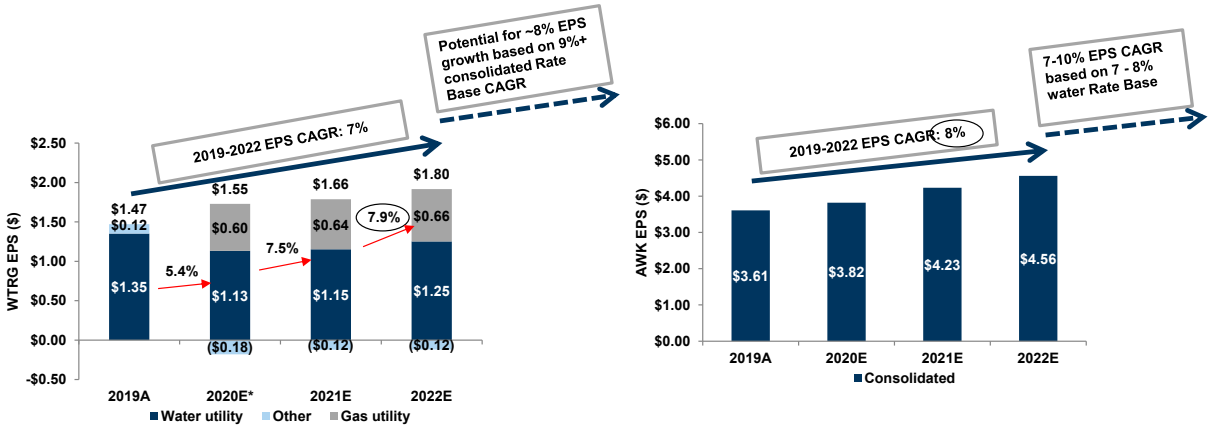
Exhibit 18: We view WTRG's meaningful relative P/E discount as unwarranted based on its 70%/30% water/gas profile...
FY2 P/E for AWK, WTRG, and an illustrative performance of a 70%/30% water/gas utility



ATO/OGS chosen as illustrative gas utility comps based on company profile, including their status as the two largest gas LDCs by market cap

Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 19: ...given we see WTRG's long-term EPS growth potential relatively in-line with that for AWK
WTRG/AWK EPS CAGR, 2019A-2022E; longer-term EPS/rate base growth potential



*Represents AWK's guidance through 2024, with another 1-2% EPS growth contribution expected from its market-based segment. WTRG rate base growth CAGR based on GS estimates.

Source: Company data, Goldman Sachs Global Investment Research

Applying a premium to water segment; upgrade to Buy (add to Conviction List)

Our 2020-2022 EPS estimates remain largely unchanged at $1.55/$1.66/$1.80 – with timing of equity/debt financing the driver of the 2021 estimate from $1.65

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prior - implying a 7% CAGR from 2019A-2022E, along with similar dividend growth during the period. Our 2021 EPS adjustmentWe believe WTRG could achieve a higher growth rate beyond 2022 and closer to its ~9% blended rate base growth, given the more near-term lag from equity financing for the pending DELCORA municipal acquisition, as well as earning on the added rate base.

We raise our 12-month price target to $51 (from $45 prior) based on a SOTP approach, with 35x/22x P/E applied to our 2021 water/gas utility EPS estimates, respectively. We now apply a 5x premium to our base water P/E multiple of 30x to highlight the company's focus on further increasing its water utility exposure that should elevate its ESG-friendly profile, as well as its scarcity premium as one of two large-cap, publicly traded water utilities. Our valuation reflects a 30.6x blended P/E, below our AWK target multiple of 37x, with the relative discount still warranted given WTRG's water/gas business mix. Our new target reflects a 24% total return versus 13% for Regulated Utilities.

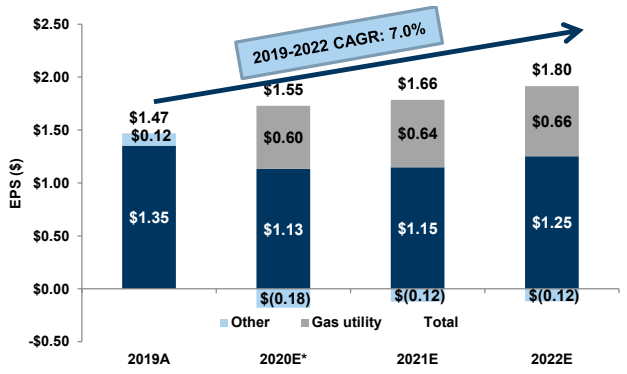
Downside risks to our call include: 1) PA regulation turns less constructive, which impacts earnings growth potential given the bulk of WTRG's earnings are derived from the state's water/gas operations, 2) the proposed DELCORA municipal water system acquisition fails to receive necessary approvals for completion, which could impact longer-term water rate base growth outlook barring replacement with other municipal acquisitions, and 3) longer-term growth concerns about the gas utility segment further compresses WTRG's valuation, both on an absolute basis and relative to pure-play water utilities.

Exhibit 20: Our EPS estimates remain largely in line with consensus through 2022...
GSe vs Consensus

EPS Estimates			% Difference
	GSe	Consensus	vs Consensus
2019A	$1.47	$1.47	0%
2020E	$1.55	$1.56	-1%
2021E	$1.66	$1.66	0%
2022E	$1.80	$1.80	0%

Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 21: ...reflecting a robust 7% EPS CAGR through 2022
EPS 2019A-2022E



*2020 incorporates full-year of Peoples Gas earnings, comparable versus adjusted proforma company guidance. Segment EPS may not add up to consolidated EPS due to rounding.

Source: Company data, Goldman Sachs Global Investment Research

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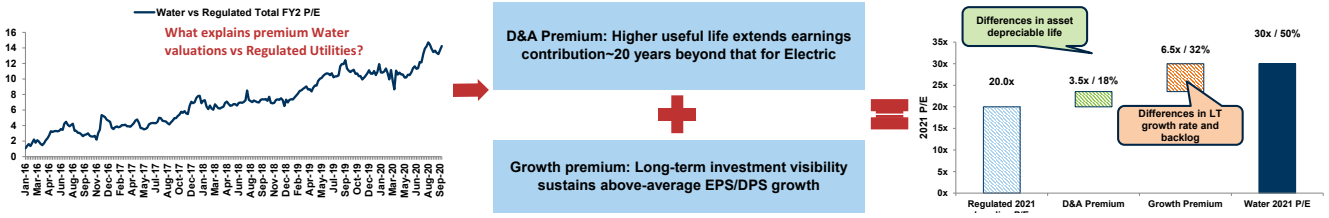
Exhibit 22: Our SOTP-based $51 price target reflects a 25% total return potential
WTRG SOTP Valuation

VALUATION	
Water utility EPS 2021	**1.15**
Water utility multiple	30.00x
Assumed premium	5.00x
Adjusted P/E	35.0x
Water utility valuation	**40.31**
Gas utility EPS 2021	**0.64**
Gas utility multiple	20.00x
Assumed premium	2.00x
Adjusted P/E	22.0x
Gas utility valuation	**13.99**
Valuation - Other	**(0.12)**
2020 Blended multiple	30.37x
Other valuation	**(3.74)**
Total valuation	**51.00**
Current price per share	$41.85
Return potential	**21.86%**
Dividend yield	2.24%
Total return potential	**24%**

Source: Goldman Sachs Global Investment Research

Exhibit 23: Longer useful life and long-term investment visibility largely justify premium water base P/E multiple vs. electric/gas



Source: Goldman Sachs Global Investment Research

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Reg AC

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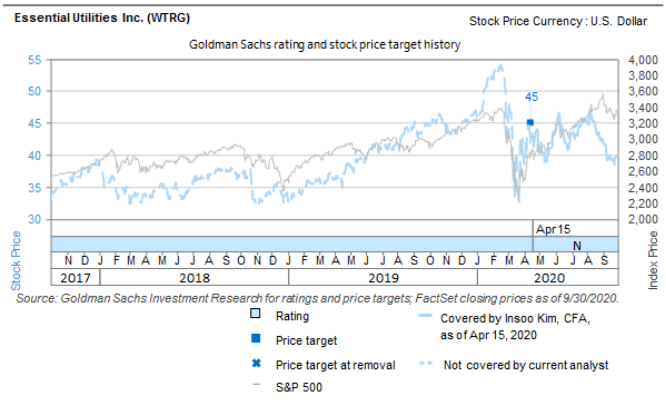

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Essential Utilities Inc. (WTRG): Relative optimism to concerns on asset mix - investor feedback from our upgrade to Buy (add to CL)

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After our October 19 note upgrading regulated water utility WTRG to Buy (on CL), we received a wide range of investor feedback on both sides of the aisle, with some in agreement with the attractive relative valuation and robust long-term growth potential, while others remain concerned about the company's water/gas utility profile from an ESG perspective, along with the market's increasingly negative view on the terminal growth rate for gas demand due to electrification.

We highlight below the main discussion points from our investor conversations on the WTRG upgrade:

1. **Some investors see WTRG as a "show me" story,** despite attractive relative valuations, per their view that the PA-based Peoples Gas utility acquisition diluted its status as a pure-play water utility and did not represent the best strategy for value accretion. That said, they are encouraged by management's commitment to increase its 70% water profile (by earnings) through continued water system acquisitions, which investors view as a higher multiple business that they agree is undervalued at current valuations.
2. **What could improve gas utility valuation multiples?** While investors agreed that WTRG should trade at a discount to pure-play water peers given its exposure to a gas utility, they believe a portion of the company's multiple compression is attributed to the increasingly negative view on gas utilities' terminal growth rate from the electrification theme. They acknowledge that Peoples Gas' majority exposure to gas-friendly Pennsylvania and 10+ year of growth through infrastructure replacement investments (without reliance on new customer connections) should support a premium valuation versus gas LDC peers; however, they remain concerned that continued market pressure on this segment could weigh on WTRG's overall valuation longer than expected.
3. **Investors wonder whether WTRG could continue to maintain its overweight position among ESG funds,** with the stock still ranking as a top 20 relative overweight per our GS SUSTAIN team data. With ESG fund flow continuing to increase, the funds' perception of WTRG's 30% gas exposure remain key to closing the valuation gap versus American Water (AWK, Buy), the only other large-cap water utility that still maintains its pure-play water profile. Some thematic investors did acknowledge the de-carbonization benefit of

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Peoples' gas pipe replacements as a qualifying factor for potential investment; however, others view the elimination of the gas exposure via a spin or sale as the quickest solution to re-capture its clean energy status.

4. **More bearish investors see WTRG un-deserving of a premium P/E multiple,** given their view of the Peoples Gas acquisition as a strategic misstep that may require time to recover. Despite the discount to AWK, they view WTRG's 23-24x P/E on 2022E as not fully capturing the execution and strategic risks, especially versus high-growth, premium electric utilities like Wisconsin Energy (WEC, Sell) or Xcel Energy (XEL, Neutral).

Our $51, 12-month price target (unchanged) is based on a SOTP approach, with 35x/22x P/E applied to our 2021 water/gas utility EPS estimates, respectively. Our valuation reflects a 30.6x blended P/E, below our AWK target multiple of 37x, with the relative discount still warranted given WTRG's water/gas business mix.

Downside risks to our call include: 1) PA regulation turns less constructive, which impacts earnings growth potential given the bulk of WTRG's earnings are derived from the state's water/gas operations, 2) the proposed DELCORA municipal water system acquisition fails to receive necessary approvals for completion, which could impact the longer-term water rate base growth outlook barring replacement with other municipal acquisitions, and 3) longer-term growth concerns about the gas utility segment further compresses WTRG's valuation, both on an absolute basis and relative to pure-play water utilities.

WTRG	12m Price Target: **$51.00**	Price: **$44.50**	Upside: **14.6%**

Buy CL

Market cap: $11.3bn
Enterprise value: $16.9bn
3m ADTV: $53.4mn
United States
Americas Utilities
M&A Rank: 3
Americas Conviction List

GS Forecast

	12/19	12/20E	12/21E	12/22E
Revenue ($ mn)	889.7	1,571.7	1,995.4	2,113.5
EBITDA ($ mn)	521.4	777.5	1,047.8	1,122.3
EBIT ($ mn)	360.8	525.4	755.5	800.4
EPS ($)	1.47	1.55	1.66	1.80
P/E (X)	27.6	28.7	26.7	24.8
EV/EBITDA (X)	19.1	21.4	17.1	16.4
FCF yield (%)	(2.4)	(1.7)	(1.8)	(0.2)
Dividend yield (%)	2.2	2.2	2.3	2.5
Net debt/EBITDA (X)	2.3	7.2	6.0	6.1

	6/20	9/20E	12/20E	3/21E
EPS ($)	0.29	0.22	0.44	0.69

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 23 Oct 2020 close.

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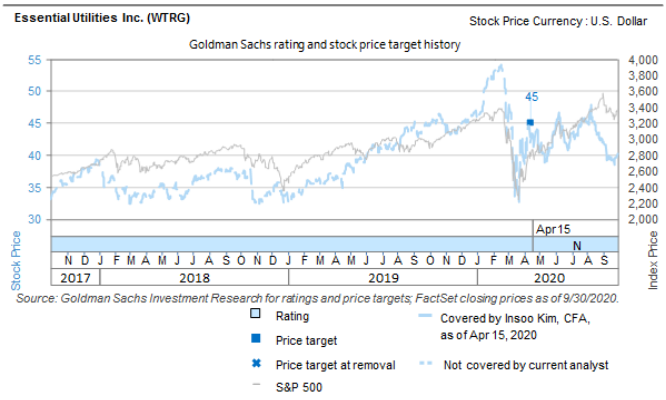

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Utilities: Tidbits and takeaways from EEI

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PM Summary

We come away from our 2020 Edison Electric Institute (EEI) meetings with management with two major themes:

1. **Clean energy transition and lowering emissions:** Companies remain focused on transitioning their generation fleet towards renewables, reducing emissions while supporting increased investments. Both state policy (Renewable Portfolio Standards) and federal tax credits (ITCs/PTCs) along with declining renewable costs are driving the transition.
2. **Shrink to grow opportunities:** Corporate simplification - either announced or in consideration - are driving many of the Diversified Utilities (CNP, DTE, EXC, PPL) as management teams seek to simplify the story and close valuation discounts.

We remain positive on utilities despite recent upticks in share prices and valuations as the sector still trades at a discount to the S&P500 versus a historical 20%-25% premium in a similar low-rate environment. Additionally, utility yields continue to screen favorably in comparison to IG bonds and the UST 10-year. Our top picks include renewable/green names such as NEP and WTRG (both Buy-rated and on the CL), while attractive generation fleet transformation plays include AEE, DUK, and PNW. For more value opportunities, we also see compelling upside in Buy-rated value names FE and PCG, along with Diversified Utilities with SOTP discounts like Buy-rated DTE, EXC and SRE (on CL).

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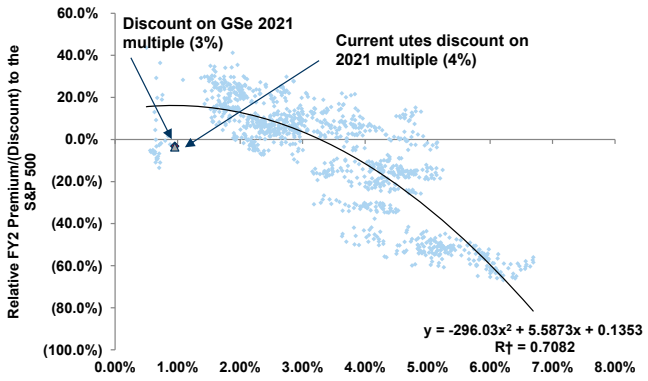
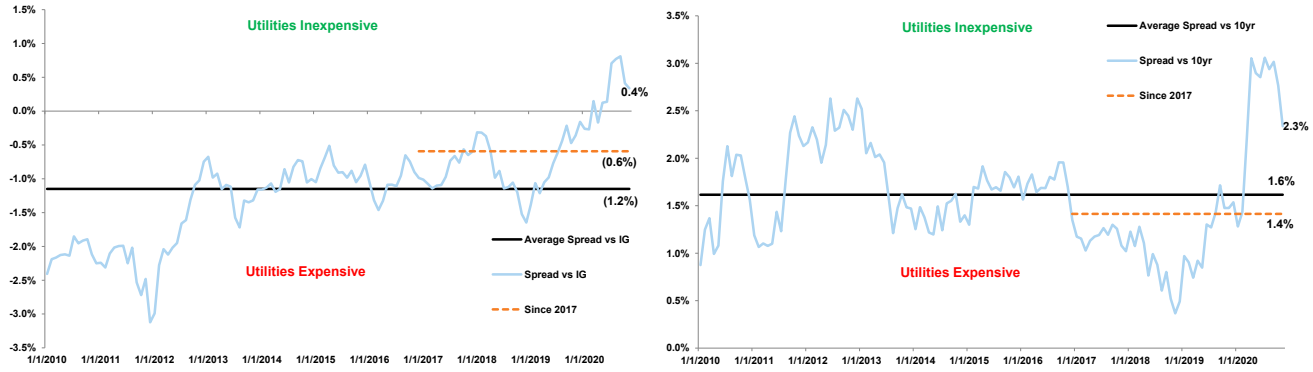
Exhibit 1: Utilities currently trade at a discount to the S&P 500, at a 20%-25% discount to what history would imply in a low rate environment
Utilities FY2 P/E premium/(discount) to the S&P vs UST 10-year yields



Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 2: Utilities continue to trade above average yield spreads in relation to IG bonds and US 10-year treasuries
Utilities yield vs IG bonds vs UST 10 year



Source: FactSet

Top 10 Takeaways from EEI

1. **WTRG expects increased municipal water system acquisition opportunities,** driven by potential increased focus on water quality at both the federal and state levels.
2. **SRE appears still super bullish LNG growth** and financing options for developing new LNG without needing sizable contributions from SRE to fund construction.
3. **Securitization and the wildfire certificate process could drive relief rallies in PCG** – as PCG does not seem significantly concerned on receiving the wildfire safety certificate in the near term and securitizing debt in the longer term.
4. **EVRG maintains high conviction in its Sustainable Transformation Plan (STP)** — recognizing though that new state legislation in KS/MO is the key driver to this, with no clarity coming before early 2021.
5. **D highlights its sizable clean energy related growth at its core regulated VA**

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electric utility - but recognizes permitting hurdles and rate making in VA (longer term) and SC (near term) present risks.

6. **EXC remains a sum of the parts story - and the company does not embed a "carbon value"** in its assessment of its ExGen subsidiary's potential value.
7. **CNP continues to see upside to its regulated growth plan,** at both the electric and gas utilities, while continuing to assess options to reduce its midstream exposure as expeditiously as possible.
8. **PNW remains confident in its robust renewable/storage investment plans,** which should achieve both de-carbonization and long-term customer rate benefit, while looking for a constructive clean energy recovery mechanism.
9. **DTE's 2021 guidance includes more contingency than normal.** Management indicated that given the ongoing pandemic and the uncertainty related to load and margin mix, they believe that they incorporated more than the typical level of conservatism in their initial guidance.
10. **More settlements in Michigan?** With both DTE/CMS announcing rate case settlements this year, the management teams indicated that the new MPSC composition coupled with significant multi-year filings approving large chunks of capex ahead of time could bode well for more settled rate cases in the future.

Company Takeaways

We hosted meetings at the fall EEI (Edison Electric Institute) conference - an industry conference for US utilities. We highlight the following company updates:

- **PPL expects to compare all options against simply reducing debt and buying back shares with potential UK sale proceeds**, but debt reduction remains key post sale to elevate FFO/debt target ~15%-16% from current ~12%-13% level - as detailed in our prior note on this topic. The company hopes, once becoming a pure play US utility, to trade more in line with peer levels post the sale. Likely a federal cash tax payer soon, diversifying into renewables may allow PPL to utilize tax credits and we note management prefers solar over wind from a competitive perspective. Upside may exist to rate base growth in Kentucky — but not till 2022 or later - as they plan to file an Integrated Resource Plan (IRP) in the state to outline gradual generation fleet changes in this coal heavy state.
- **With AZ commission elections complete, PNW remains confident in medium-term renewables/storage investment plans with conviction in ability to demonstrate cost competitiveness.** The company continues to target procurement of utility scale solar coupled with storage aggressively and believes higher clean energy in resource mix creates significant fuel savings despite initial bill impacts. In the ongoing APS rate case, PNW proposed in the recent rebuttal testimony the Advanced Energy Mechanism (AEM), which would provide rider recovery of renewable/storage investments. If not approved in the rate case, the company looks to push the proposal separately, reducing rate case filings while

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aligning clean energy investment goals. On the financing side, while the outcome of the rate case would give additional clarity on the timing/magnitude of equity issuance (current forecast at around $300-$400mn), management expects issuance timing as prior to the next rate case filing, while noting that an approval of a clean energy rider could help push back such a filing and/or mitigate the amount.

- **CMS remains well positioned to continue executing with supportive regulation and a constant eye on operational improvements.** Management reiterated the low hanging fruit of fuel (Palisades; MCV) and O&M (Karn 1&2 and defined contribution vs benefit) tailwinds benefiting the customer over the current 5 year plan. However, CMS emphasized that the real value continues to come from operational cost improvements that heighten the quality of experience for both customers and employees as ways to benefit all stakeholders in MI. The state remains focused on decarbonizing and CMS believes that their current targets and plans already remain on track or exceed those goals while offering significant growth. However, management did note that energy storage remains an area where the next IRP could see more investment sooner and the coal Campbell Units 1 &2 could potentially retire earlier. Management sees multi-year filings as providing support for potentially settling rate cases given more known and already agreed upon factors during future rate cases, but noted the ongoing electric rate case is already far along given the PFD. CMs does not view longer-term trackers as likely, preferring the flexibility with annual or near annual filings, indicating that performance based ratemaking has come up and is already evident in energy efficiency and RPS spend.
- **ETR sees, as part of its multi year guidance, modest under earning levels continuing — and sizable rate base growth as well - but regulatory risk remains.** The company anticipates earning 9%-9.5% RoE levels - below authorized - given rate increase caps or regulatory lag in a few jurisdictions like AR, MS and LA. The FERC docket for its SERI segment could present downside - they've highlighted $0.15+ of EPS at risk, largely to finance refunds, but believe they could potentially mitigate this. Recent 2020 storms likely cost roughly $2bn - they hope to securitize these, based on precedents in Louisiana and Texas - otherwise financing this could weigh on earnings slightly. Low utility rates relative to other utilities remains a tailwind for rate base growth - they seek to add $1.4bn of renewables to the system over the next few years and could add emerging technologies (a new CCGT that is hydrogen capable) as well - RFP processes, especially for its Texas utility, remain key for investors to monitor. Finally, the company - while not a large coal fired generator - still owns the sizable White Bluffs facility in Arkansas with plans to retire in the late 2020s - an earlier expected retirement, being evaluated now, could add to rate base and earnings growth.
- **AGR remains confident in its offshore wind timeline, in addition to its growth through PNM and NECEC.** On Vineyard Wind, the company is expecting final environmental impact statement (EIS) this week and final approval by end of year, but notes an approval delayed until 1Q2021 would not alter their 2024 COD target. Given this timeline, AGR would still qualify for 18% ITCs, while looking to take advantage of any extensions/changes to offshore wind ITC rules if appropriate. The

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company also reiterated its interest in onshore transmission for future offshore wind projects, which is not embedded in the current capital plan. On the New England Clean Energy Connect (NECEC) transmission project, AGR continues to monitor the Maine citizens' initiative as the group plans for a 2nd referendum in opposition, but management believes the project's clean energy and economic benefits to the state will outweigh the opposition arguments. Despite the hurdles to overcome with a project of this magnitude, management expressed interest in considering other future large-scale transmission projects to route clean energy to the NY/NE area to meet clean energy targets. Regarding the company's balance sheet forecast, while AGR looks for Moody's to relax the downgrade threshold for post the PNM acquisition, the guided 14.5%+ FFO/debt from 2022-2025 embeds a potential one-notch downgrade at Moody's.

- **The Florida utilities remain a growth engine for NEE while seeing only modest rate case risk - the renewable segment benefits from massive tailwinds and advantages.** NEE anticipates filling a joint rate case for FP&L and Gulf Power in Florida, where 4 of the current 5 PSC commissioners will oversee the 2021 rate case process. While they likely will seek a rate increase, they recognize RoE risks exist - but they also see potential for continued lower costs going forward that would create headroom for higher rate base growth. The company still sees buyer power, financing advantages, lower O&M costs, site selection skills and economies of scale as their biggest advantages in renewables given their status as the biggest US operator - and an extension of renewable tax credits would not change this, if the new administration in Washington pushes for this. Hydrogen grabs a lot of mind share today - they do not see this as a major near term (2021-25) contributor to earnings, but like energy storage 8-10 years ago, see this as worth monitoring as cost curves improve.
- **CNP sees incremental capital spend spread across its electric/gas jurisdictions,** with 2/3 of the $3bn incremental plan expected at the electric utilities (TX/IN). Electric items include transmission connections for increasing solar build in TX, investments to support customer growth (2-2.5% in TX, 1% in Indiana), while gas investments primarily consist of accelerated gas pipe replacements. Management expects the guided 1-2% annual O&M reductions through 2025 driven by unearthing sustainable O&M savings, conversion from coal to natural gas/renewables, and utilizing technology to improve efficiencies. CNP looks to shift to a majority electric utility profile - partly driving its plan to divest one or two of its regulated gas utilities - while continuing to assess options to reduce its midstream exposure as expeditiously as possible.
- **WEC benefits from a favorable service territory - especially for gas utility service - and believes the current state administration will back its recently announced fleet transformation plan**. With Governor Evers' climate task force still underway, WEC does not fully know the impact of any proposals that will emerge - but they believe retiring older coal/gas units and replacing with solar and storage, along with new gas capacity, will fit in well with broader policy objectives. Cost management could continue in the coming years — while 2020 benefited from greater than originally anticipated levels, more integration could drive even lower

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costs. As a utility in a cash tax paying status, WEC could continue buying renewable projects and keeping the tax benefits - a competitive advantage versus others who need tax equity.

- **DTE maintains outsized regulated growth and contingency in its initial 2021 guidance, noting more cost headroom over time translates to more investment from their substantial backlog of opportunities.** The current 5-year plan assumes regulated net income growth in excess of 7-8%/9% at DTE Electric/Gas, offsetting REF roll-offs and equity conversion headwinds during 2022-2023. While the current capital expenditure forecast implies slower levels during the back half of the 5-year plan, if management can find more cost savings they can pull forward more distribution and potentially renewable capex into the plan. DTE noted that given the uncertainty related to the ongoing pandemic, their initial 2021 guidance implies more than their typical 1 standard deviation below normal load in cushion. Other topics included an expectation to assess retiring the Belle River (2030) and Monroe (2040) coal plants earlier in the next IRP, which could require more capex in 2024/2025 to replace the Belle River capacity but would also require accelerated depreciation of the rate base. Management believes that providing more granularity on a standalone GSP/DTE Midstream company will create value for shareholders, highlighting the strength of their platform and opportunities for growth – especially in the Haynesville as well as the Nexus/Link platforms.
- **Potential corporate structure changes - as initially outlined by EXC in its 3Q2020 release - drove a sizable portion of our discussion with EXC,** as the company evaluates a possible separation of ExGen from the regulated businesses. Realizing higher valuation levels remains a key aspect of the decision making process - but regulatory approvals at state/federal levels remain key as well to whether they move forward or not with any changes. They do not "price in" or assume a value for carbon or a carbon tax when assessing the company's largely nuclear ExGen fleet — as they do not seem overly optimistic of a national carbon regime emerging soon - but see this as a "call option" not embedded in their base case. The company reiterated plans to meet its regulated utility EPS growth guidance given out previously - despite the impact of weak demand driven partially by COVID 19.
- **For AEP, while earned RoE's may decline, higher equity layers could offset this partially.** In our chat with management, they discussed that guidance assumes a low 9% range for earned RoE's - driven by regulatory lag in jurisdictions like Oklahoma and Louisiana - but hope to offset this with increased investment in projects with trackers and with higher equity layers in rates. The new 5-year capital spending plan incorporates not just the North Central wind project, but other smaller scale renewable spend as well as incremental transmission investment.
- **Dominion faces limited regulatory risk in the near term, but acknowledges longer term risk still exists.** The 2021 triennial earnings review in Virginia creates limited risk given the $50mn cap on revenue reductions, but the company did recognize that (1) risk in Virginia exists in the 2024 review, where no revenue reduction caps exist and (2) the ongoing South Carolina rate case may see

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intervenor testimony that seeks a far lower rate increase than sought by Dominion. Potential changes at the state utility regulatory commission remain worth monitoring in Virginia. D stays positive on gas utilities given trackers that exist in markets like Ohio, paired with opportunities to grow renewable natural gas and even do its first small scale hydrogen pilot test in Utah. D also iterated that it does not expect change in the company's views on its remaining contracted assets like Cove Point LNG or Millstone nuclear in CT.

- **SRE remains very bullish its mix of US utilities and infrastructure businesses - and expects positive LNG related news in the coming months.** With SRE having sold its Latin American utilities and its US renewable business in the last year, the company's new simplified structure should prove easier for investors to understand going forward. Rate base growth remains material in California given the transition to clean energy - and even with a potential risk to authorized RoE's for 2022 there, authorized levels remain above national averages. Texas remains a growth opportunity - they just raised rate base growth projections by $300mn and could see another $775m+ upside in the coming years - and do not expect an overly contentious rate case proceeding in 2021. On the LNG front, Sempra expects to FID the Costa Azul LNG project - and assume limited construction risk — with only $250m of Sempra's equity capital used to finance this project - and still see Port Arthur LNG as one of the few US facilities potentially moving forward in the coming years.
- **WTRG highlights increasing water quality focus as a potential catalyst to support municipal water acquisitions.** While increased federal funding for water infrastructure, if implemented, could deter certain acquisition opportunities, management expects smaller systems to continue to face funding shortages, especially when combined with potential increase in water quality standards. On its recently acquired Peoples Gas system, WTRG expects pipeline replacement to fuel robust rate base growth at Peoples, while its low pressure systems and above-ground checkpoints enhancing its operational safety.
- **ED continues to face uncertainty related to COVID-related costs and storm response,** while reiterating its equity issuance plan (up to $600mn in 2020, $1.1bn total from 2021-2022) with an update expected with 4Q2020 earnings. At CECONY, ED sees potential investment opportunities to improve grid reliability, including potential for additional undergrounding of its distribution system. ED also looks to continue growing its renewable footprint, although offshore wind remains above its risk tolerance level except for associated onshore transmission investments. Finally, management reiterated its view that its midstream equity stakes in Mountain Valley Pipeline (MVP) and Stagecoach are non-core while looking to mitigate the exposure.
- **DUK anticipates trying to put together a coalition to seek electricity related state legislation in N Carolina** – seeking (1) revised rate making – including multi-year plans, decoupling and/or trackers, (2) policy support for a timeline around coal plant retirements, (3) detailed emission reduction targets and (4) policy support for offshore wind. Cognizant of managing the rate impact, which remains key to get industrial customers on board, the company may need to agree to annual or multi-year rate caps. However, we note their IRP (Integrated Resource Plan) base

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case assumes ~1% annual rate change and the more aggressive no carbon plan assumes ~2.5% annual increases - so none that appear overly material or that would drive rate concerns for customers. Increased spend at the gas utilities will help drive overall rate base growth - they still see these businesses as attractive growth opportunities - as would higher solar related spend at the Florida electric utility. Florida remains worth monitoring given (1) a proposal to add 750 MWs of community solar, which will go before the PSC in late 2020 and (2) next year's rate case, where DUK will likely seek small rate increase levels.

- **The regulatory front and wildfire recovery will drive EIX from here**. EIX remains bullish regarding changes in California utility regulation — they see faster regulatory decisions as showing the state utility commission wants to work in a more expedited approval process. Recent approvals on securitization, insurance cost recovery, COVID 19 cost deferral and recovery, and wildfire spend recovery (2018-2020), show the state continues to see utilities as necessary "partners" in moving to a cleaner energy economy. They view the cost estimates for 2020 wildfires as likely falling within insurance recovery levels and continue to work to resolve claims related to the 2017/2018 wildfires, after reaching settlements with public entities and the subrogation claims holders. EIX still plans to issue $1bn in common equity - more likely doing so after wildfire season ends in late 2020 and as they get closer to reaching settlements with claimants from prior wildfires — and can utilize $800mn of insurance to pay out claims for now on the 2018 wildfires.
- **XEL looks to continue its robust renewable investment pipeline,** while ITC/PTC extensions - if realized - could support incremental renewable PPA buyout opportunities. Along with the renewable theme, XEL highlighted its commitment to support EV infrastructure and increased EV adoption, with $500mn of planned investments across its various jurisdictions. Finally, XEL expects to be able to grow at the upper half of 5-7% EPS growth guidance with just its base capital plan, while the proposed $1.4bn in incremental wind/solar investments could pad the growth toward the upper end of the guidance range, supported by a flattish base O&M CAGR through the mid-2020's.
- **In our discussion with PG&E Corp's (PCG) interim president and other officers, the company highlighted skills sought in incoming CEO/CFO** level personnel - with announcements likely in the months ahead on who will fill these seats. Operational experience, political and regulatory expertise remain key to the skillset needed for PCG's incoming CEO — while the CFO search focuses on individuals with strong investor relations skill sets as well as in balancing capital spend goals with the impact on customer rate levels. The company did not seem overly concerned regarding the Wildfire Safety Certificate process - they view the delay as more of a technical issue - and hope to get resolution soon. The 2019 certificate remains in place unless the state regulator outright rejects their 2020 application. PCG still anticipates $625m of costs related to the 2019 wildfire - but upside to this may exist and certainty may not emerge for another 1-2 years. They remain optimistic about cost savings opportunities as well as on securitization - they hope to finalize the regulatory docket by late spring 2021 and utilize securitization proceeds to pay down temporarily issued debt in the near term (up to $6bn), with

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plans to pay down $3bn of outstanding holding company debt over the next 2-3 years. Upside may exist to rate base forecast levels - but risks to the authorized RoE for 2022 remains given the state's cost of capital mechanism.

- **Grid infrastructure investment remains top of mind for AEE, while continuing its fleet transition initiatives.** In Illinois, while management continues to pursue passage of the proposed legislation to extend formula rate-making (expiring in 2022) while opening the doors for renewable investments, they view traditional rate-making as relatively constructive as well given a future test year and de-coupling. In Missouri, the utility noted positive feedback and reception from all stakeholders on the recently filed Integrated Resource Plan (IRP) which, combined with ongoing grid investments in the state, should provide robust long-term rate base growth. Management noted that an extension of renewable tax credits - if implemented, could warrant further acceleration of its renewable growth plan.
- **EVRG remains focused on the state legislative front in Kansas and Missouri - outcomes next year likely will significantly impact earnings growth** and realizing EPS targets. The company still believes, as outlined at 2Q2020 earnings, that retiring up to 500 MWs of coal generation earlier than planned - and securitizing these costs - and redeploying the proceeds into new renewables remains, along with raising transmission/distribution investment, the best growth strategy available. They believe strong support exists for energy transition planning in Kansas — and will seek consensus backing on this in Missouri next year - but risks exist that other low cost alternatives, besides simply company owned generation in rate base, could emerge and present a modest risk to their goals of adding more renewables to rate base. Higher transmission spend comes with limited lag — they anticipated higher levels for multiple years to help Kansas integrate wind capacity, but actually see a bit of an uptick in its smaller segment in Missouri (Missouri West). EVRG does not see asset sales as likely needed or leading to lower costs - early retirements remain the core driver.
- **AWK spoke on opportunities to address water contaminants even in the absence of a federal water quality mandate,** which could drive both organic and inorganic growth via continued acquisitions of small municipal water and wastewater systems. While private capital is present in larger systems, AWK is best positioned to do tuck-in deals with 20,000 customers or less, as they can provide investment and improved service while spreading costs across the entire AWK business. The company still expects the NY utility sale to close in early 2021, with NY commission approval the only outstanding condition. AWK continues to replace water pipes within its system, and is targeting a 100-year replacement cycle versus 120-130 years currently compared to many municipal systems at 200 years. AWK's military business continues to see good traction, with numerous opportunities and proposals currently in the works while the Homeowner Services Business has seen some headwind from COVID-19 in 2020 but margins should be stable moving forward ex-COVID.
- **NI continues to see both electric and gas utilities as integral components of the US energy mix.** Management sees an attractive growth trajectory for both types of Utilities, noting that the recent pressure on regulated natural gas valuations

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in the public markets does not appear to reflect the fundamental value they deliver for customers that is not easily replaced. The company does see opportunities to decarbonize on the natural gas side through infrastructure replacement as well as RNG, especially given Ohio and Indiana offer attractive RNG resource – noting this will represent a small amount of volume. On the electric side, management highlighted that potential renewable tax credit extensions could potentially support further acceleration of coal retirements, pulling Michigan City earlier than 2028. Separately, NI reiterated that management remains comfortable with current guidance, incorporating ~$0.05 of impact related to COVID.

- **POR continues to see state-driven clean energy goals supporting on-going renewable/storage investments in Oregon,** as well a growing focus on EV infrastructure opportunities, especially for industrial customer base. With the recent state wildfires mostly contained, POR continues to assess the overall cost from an expense/capital standpoint, although they see the levels as largely manageable and supported by the approved cost deferrals from the state commission. POR in 4Q2020 earnings looks to provide an update on both the wildfire cost estimate as well as thoughts on timing of the next base rate case; for 2021, the company looks to grow earnings (using 2019 as the base and 4-6% long-term growth forecast) driven by cost management, benefit from the completion of the Wheatridge renewable facility, and lower costs associated with the retired Boardman coal plant.
- **OGE focuses on maintaining and growing its regulated electric utility profile, primarily through continued transmission & distribution investments at its Oklahoma/Arkansas jurisdictions, supported by improving regulatory frameworks through certain investment recovery mechanisms.** While fleet de-carbonization is not a primary investment driver near-term, OGE does see select solar opportunities that could combine with gas-fired generation in replacing retiring coal plants. Finally, management views the growth of its regulated utilities as the primary use of any capital allocation opportunities.

Valuation and Key risks

PPL Corp. (PPL, Neutral): $31/sh 12 month target price is based on a sum of the parts analysis. Key risks include regulatory risk, power demand and financing.

Pinnacle West Capital Corp. (PNW, Buy): $94, 12-month price target based on 19.5x P/E multiple on 2021 EPS. Key downside risks include 1) APS rate case outcome corresponding to our bear-case scenario that could pressure valuation multiples in the near-to-medium term, 2) realized electric demand is worse than expected, impacting earnings and cash flows, 3) the November 2020 election results in a non-constructive commission, and 4) PNW is unable to secure much ownership in future renewable generation build-out, limiting rate base growth.

CMS Energy Corp. (CMS, Buy): $69, 12-month price target based on 24x 2021 P/E multiple. Key risks include regulation, legislation, cost management, and financing.

Entergy Corp. (ETR, Buy): $119, 12 month target price based on a sum of the parts analysis. Primary risks include regulatory risks, power demand and financing.

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Avangrid Inc. (AGR, Sell): $45, 12-month price target based on a sum-of-the-parts analysis. Key upside risks for AGR include 1) AGR receives approvals to defer all COVID-19 related costs, mitigating the earnings impact, 2) incremental O&M savings help offset other EPS headwinds, and 3) U.S. government extends federal renewable tax credits, which improve future renewable investment return profiles for AGR's renewable business.

NextEra Energy Inc. (NEE, Neutral): $74, 12-month price target based on a sum-of-the-parts analysis. Key risks include Florida utility regulation, renewable development, tax credit legislation, and operating cost management levels.

Centerpoint Energy Inc. (CNP, Neutral): $22, 12-month price target is based on a sum-of-the-parts valuation. Key risks include customer demand/growth, COVID-related costs, and financing.

WEC Energy Group (WEC, Sell): $88, 12-month target price based a 22x P/E multiple on our 2021 EPS. Key risks to our view include higher than expected capital spend and rate base growth for 2021+, lower than expected operating costs and improved demand.

DTE Energy Co. (DTE, Buy): $142, 12 month price target derived from a sum-of-the-parts valuation. Multiple risks exist to our current view of DTE: (1) Unlike a sale, spinoff valuation remains an unknown for shareholders, if midstream valuations change due to adjustments in legislation, taxes, or supply and demand balances in a negative way, this could impact DTE's valuation. (2) The regulated asset base – representing ~70% of earnings today and theoretically 90% post spin-off – maintains a single state regulatory environment. If MI sees significant changes in regulatory quality – especially the ability to earn timely recovery on investment as well as authorized returns — this could impact our view. (3) Similarly, demand, cost, and investment trends in the state remain critical. (4) DTE currently offers a substantial regulated growth profile, in order to finance this DTE may require equity beyond our forecasts or debt financing costs ahead of our expectations.

Exelon Corp. (EXC, Buy): $53, 12-month price target based off a SOTP analysis. Key risks include retail MWh sales, power prices, generation output, and utility regulation.

American Electric Power (AEP, Neutral): $90, 12-month target price based on SOTP. Key risks include power demand, rate case and regulatory risks, as well as financing.

Dominion Energy Inc. (D, Neutral): $84, 12-month target price based on SOTP. Key risks include regulation, project execution, power demand and financing.

Sempra Energy (SRE, Buy on CL): $150, 12-month price target derived using SOTP. Key risks include project awards, regulatory approvals, construction, and financing.

Essential Utilities (WTRG, Buy on CL): $51, 12-month price target based on SOTP. Key risks include regulation, municipal water system acquisition approvals, and longer-term growth concerns about the gas utility weighing on valuation.

ConEdison (ED, Sell): $78, 12-month price target based on 18x P/E on 2021 EPS. Risks

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include NY utility commission authorization of COVID-19 related costs and bad debt expense, NY economic conditions, renewable segment growth.

Duke Energy (DUK, Buy): $99, 12-month price target based on 19x P/E on 2021 EPS. Key risks include utility regulation, power demand and coal ash related issues.

Edison International (EIX, Buy): $74, 12-month price target based on 17x P/E on 2022 earnings discounted back to 2021. Key risks include wildfire related costs, litigation claims, utility regulation and financing.

Xcel Energy (XEL, Neutral): $71, 12-month price target based on 20x P/E on 2021 EPS. Key risks include upward revisions to rate base/EPS growth, O&M savings, renewable tax credit extension, negative rate case outcomes, less generation in rate base, materialization of PPA buyouts, COVID-19 related cash drag.

PG&E Corp. (PCG, Buy): $15, 12-month price target based on 14x P/E on 2022 EPS discounted back to 2021, and DDM. Key risks include wildfire risk, continued underearning due to legacy holding costs, financing risk and trading risk.

Ameren Corp. (AEE, Buy): $93, 12-month price target based on 24.5x P/E on 2021 EPS. Key risks include regulation, project awards, and financing.

Evergy, Inc. (EVRG, Neutral): $58, 12-month price target based on 18x P/E on 2021 EPS. Key risks include utility regulation, power demand and cost management.

American Water Works (AWK, Buy): $166, 12-month price target based on 39x P/E on 2021 EPS. Key risks include water quality issues, cost management, regulatory environment, growth at non-regulated segments, reduced ESG fund flows.

NiSource (NI, Buy): $27, 12-month price target based on 20x P/E on 2021 EPS. Key risks include Indiana regulatory approvals for renewables, earnings/cash impacts due to COVID-19, higher than expected O&M, electricity demand and customer growth, and financing.

Portland General Electric (POR, Sell): $39, 12-month price target based on 16x P/E on 2021 EPS. Key risks include COVID-19 impacts on earnings/cash, level of COVID/wildfire related cash drag, renewable ownership, and M&A target risk.

OGE Energy (OGE, Neutral): $35, 12-month price target based on 18.5x P/E on 2021 EPS. Key risks include upsized rate base growth, the company could be a target of a take-out, customer and demand growth, further distribution cuts at ENBL, COVID-19 headwinds.

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Disclosure Appendix

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We, Michael Lapides, Insoo Kim, CFA, David Fishman, CFA, Rebecca Yuan and Adam Williams, hereby certify that all of the views expressed in this report accurately reflect our personal views about the subject company or companies and its or their securities. We also certify that no part of our compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

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Growth is based on a stock's forward-looking sales growth, EBITDA growth and EPS growth (for financial stocks, only EPS and sales growth), with a higher percentile indicating a higher growth company. **Financial Returns** is based on a stock's forward-looking ROE, ROCE and CROCI (for financial stocks, only ROE), with a higher percentile indicating a company with higher financial returns. **Multiple** is based on a stock's forward-looking P/E, P/B, price/dividend (P/D), EV/EBITDA, EV/FCF and EV/Debt Adjusted Cash Flow (DACF) (for financial stocks, only P/E, P/B and P/D), with a higher percentile indicating a stock trading at a higher multiple. The **Integrated** percentile is calculated as the average of the Growth percentile, Financial Returns percentile and (100% - Multiple percentile).

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Essential Utilities Inc. (WTRG): Virtual management meetings address water/gas growth opportunities; Neutral

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We hosted virtual meetings with Chris Franklin, President and CEO of water/gas utility Essential Utilities (WTRG, Neutral). Key discussion topics included 1) latest demand and financial updates around COVID-19, 2) update on the pending DELCORA municipal water system acquisition as well as the pace of other acquisition opportunities, and 3) strategic thoughts on Essential's water/gas business mix. We remain Neutral-rated WTRG, although we turn incrementally more positive given recent share underperformance versus water utilities and broader regulated utility peers.

Below are our key takeaways from the virtual NDRS:

- **WTRG continues to see COVID-19 impact as manageable,** with increased demand from its predominantly residential customer base (at both water/gas) offsetting the negative impact from lower commercial/industrial load, along with positive weather benefit in 3Q also supporting demand for the year. Regarding bad debt, deferral treatment authorized in Pennsylvania, its largest jurisdiction, should allow WTRG to execute within its guidance range for the year even when accounting for some cash drag. They look for lifting of shutoff moratoriums in the near-term, especially in PA, given the upcoming winter heating season for the gas segment.
- **Despite some opposition, WTRG expects to complete its proposed acquisition of the PA-based municipal wastewater system DELCORA.** Management noted that the dispute with the Delaware County Council stems from plans to utilize a portion of the proceeds to help manage customer bill increases through a trust. Regardless of the outcome on this matter, the company's commitment remains unchanged regarding the proposed acquisition. They now expect a final approval from the Pennsylvania commission by 1Q2021, a moderate delay from the original YE2020 forecast given an extension to the PA regulatory docket. However, given the capital spend for this business isn't slated to begin until beyond 2021, management sees the delay as immaterial to the 2021 earnings potential.
- **The company noted a rapid increase in municipal acquisition interest and activity since the start of COVID-19,** which management partly attributes to the economic pressures facing many municipalities in the current environment.

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WTRG remains active in the various bidding processes, both within its largest territory in PA but also its other jurisdictions, all which allow Fair Market Value treatment - the ability for the private utility to rate base the acquired system at FMV. However, in the next 12-18 months, **they do not anticipate a need to issue common equity** given the relative smaller size of each opportunity relative to the pending DELCORA proposal, and also given the company accounted for certain future transactions in the recent $311mn equity issuance.

- **Water quality remains a key focus, with potential investment opportunities ahead.** The company's water quality standard - 13 parts per trillion (ppt) - remains well below the EPA's 70 ppt advisory level and the CDC's 35 ppt guidance, and management sees increased federal/state focus on this issue creating potential to increase certainty on cost recovery as well capital for rate base, although not a significant portion of the overall planned investments.
- **WTRG looks to assess clean options for gas business,** although they admitted it's still very early in the process given the recent completion of the Peoples Gas system. Management believes there is a long-term need for gas, whether natural gas or other cleaner forms, while seeing old pipe replacement as a more immediate need at its newly acquired Peoples Gas to both improve reliability and reduce methane emissions.
- **WTRG plans to remain predominantly a water utility,** with organic/inorganic growth that could increase its current 70% exposure from its water segment. Management does not have any intention of expanding its gas utility footprint through other acquisitions.

We increase our 2021-2022 EPS estimates to $1.65/$1.80 from $1.63/$1.78 prior with our 2020 EPS of $1.55 unchanged, primarily to reflect 1) 2Q20 actuals and 10-Q update, 2) $311m equity issuance in 3Q20 (moderately higher than our estimate), 3) reduction in debt issuances in 2021, and 3) moderately higher earned ROE expectations at Peoples Gas to account for incremental tax repairs benefit. Our estimates reflect a 6.9% EPS CAGR from 2019-2022E, at the upper end of management's 5-7% forecast.

Our $45 (unchanged), 12-month price target is based on an SOTP approach, with 30x/22x P/E applied to the our 2021 water/gas utility EPS estimate. Upside risks to our call include: 1) Peoples Gas acquisition synergies exceed our expectations, elevating EPS growth profile, 2) tax repairs election for the PA gas utility elevates earned ROEs even above our estimate, and 3) WTRG continues to benefit from ESG fund flows, despite its water/gas utility mix profile on a pro-forma basis. Downside risks to our call include: 1) PA regulation turns less constructive, 2) the proposed DELCORA acquisition fails to receive necessary approvals, and 3) additional longer-term concerns about the gas segment further compresses multiples.

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WTRG	12m Price Target: **$45.00**	Price: **$39.60**	Upside: **13.6%**

Neutral

Market cap: $8.5bn
Enterprise value: $14.1bn
3m ADTV: $50.1mn
United States
Americas Utilities
M&A Rank: 3

GS Forecast

	12/19	12/20E	12/21E	12/22E
Revenue ($ mn) New	**889.7**	**1,571.7**	**2,032.7**	**2,165.6**
Revenue ($ mn) Old	889.7	1,593.3	2,062.8	2,180.9
EBITDA ($ mn)	521.4	784.7	1,083.1	1,179.3
EBIT ($ mn)	360.8	532.5	787.8	858.4
EPS ($) New	**1.47**	**1.55**	**1.65**	**1.80**
EPS ($) Old	1.47	1.55	1.63	1.78
P/E (X)	27.6	25.5	24.0	22.0
Dividend yield (%)	2.2	2.4	2.6	2.8
Net debt/EBITDA (X)	2.3	7.0	5.7	5.7

	6/20	9/20E	12/20E	3/21E
EPS ($)	0.29	0.22	0.43	0.61

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 16 Sep 2020 close.

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Disclosure Appendix

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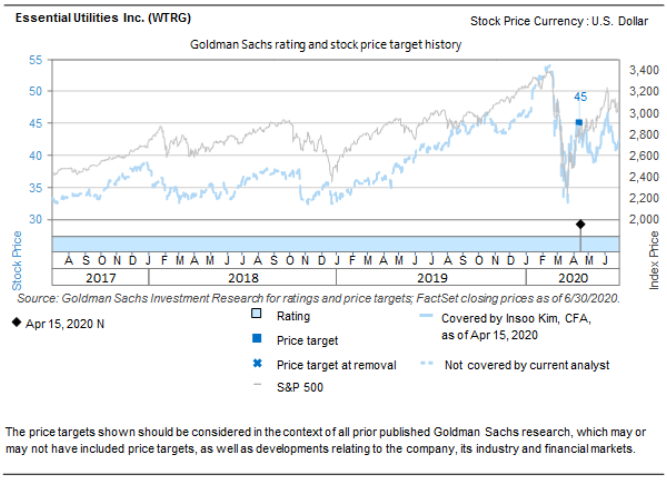

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HSBC Global Research

28 June 2019

Aqua America (WTR US)

Buy: Multi-utility creation – work-in-progress

Equities
Water Utilities

United States

- Peoples acquisition: completion now likely later in 2019 given regulatory progress; financing has been secured
- Texas: fair market value continues to drive water growth
- Maintain Buy rating; TP increased from USD41 to USD45.5

Peoples Natural Gas update (work in progress). On 11 June, 2019, Aqua America (Aqua), participated in a hearing of the Pennsylvania Public Utility Commission and filed a settlement agreement for the acquisition of Peoples Gas. Two of the parties (intervenors) to the case opposed the settlement because of a disagreement on the treatment of a small gas system. This means the acquisition is now anticipated to occur in the fall of 2019, later than Q2 as originally anticipated by Aqua. Aqua has already started to raise the cUSD2.5bn of equity to buy Peoples. It wants a sufficient equity cushion to maintain a 12-13% FFO/adjusted net debt ratio. Merger approval has already been received in W Virginia and Kentucky.

Texas adopts Fair Market Value legislation

On 12 June Aqua management commented that Texas had become the seventh state to adopt Fair Market Value legislation. This continues to be a key driver for the sales of regulated water systems (at an 'appraised value' at a premium to book value). In 2017 the American Society of Civil Engineers gave Texas a D+ rating for water and D rating for waste water. We think the combination of underinvested public health infrastructure with a mechanism for small cities to sell their systems at a premium to dedicated water companies underpins the strong attraction of US water stocks.

Maintain Buy rating with increased target price of USD45.5 from USD41: We value Aqua America via three methodologies: DCF, dividend yield and the average of a PE multiples and a SOP (rate-based) valuation. Taking the average of the three approaches gives us our target price of USD45.5 (previously USD41). In our DCF valuation, we have updated our assumption of beta from 0.60 to 0.58 which is in line with its market peers. In our multiples-based valuation, we have updated the multiples in line with the market peers. This results in an increase in PE multiple from 26.1x to 27.8x. Finally, in yield valuation, we reduce our yield from 2.25% to 2% which is in line with its peers. Overall, these changes lead to an increased TP of USD45.5 from USD41. Our TP implies 12.5% upside; we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

MAINTAIN BUY

TARGET PRICE (USD)	PREVIOUS TARGET (USD)
45.50	**41.00**
SHARE PRICE (USD)	UPSIDE/DOWNSIDE
40.45	**+12.5%**
(as of 26 Jun 2019)	

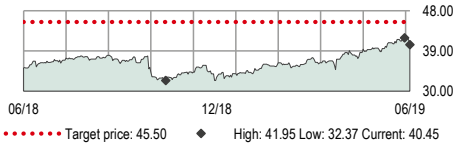
MARKET DATA

Market cap (USDm)	8,727	Free float	100%
Market cap (USDm)	8,727	BBG	WTR US
3m ADTV (USDm)	131	RIC	WTR.N

FINANCIALS AND RATIOS (USD)

Year to	12/2018a	12/2019e	12/2020e	12/2021e
HSBC EPS	1.08	1.50	1.59	1.65
HSBC EPS (prev)	-	-	1.58	1.66
Change (%)	-	-	0.6	-0.6
Consensus EPS	1.41	1.46	1.56	1.66
PE (x)	37.6	27.0	25.4	24.6
Dividend yield (%)	2.1	2.3	2.4	2.6
EV/EBITDA (x)	24.0	22.1	16.8	16.3
ROE (%)	9.7	12.9	11.6	8.5

52-WEEK PRICE (USD)



Source: Refinitiv IBES, HSBC estimates

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Financials & valuation: Aqua America

Buy

Financial statements

Year to	12/2018a	12/2019e	12/2020e	12/2021e
Profit & loss summary (USDm)				
Revenue	838	905	1,906	2,003
EBITDA	470	525	815	864
Depreciation & amortisation	-147	-160	-237	-260
Operating profit/EBIT	323	365	578	604
Net interest	-147	-84	-158	-170
PBT	178	281	420	434
HSBC PBT	176	281	420	434
Taxation	14	-14	-21	-22
Net profit	192	267	399	412
HSBC net profit	192	267	399	412
Cash flow summary (USDm)				
Cash flow from operations	369	340	675	676
Capex	-496	-500	-770	-770
Cash flow from investment	-640	-500	-5,045	-770
Dividends	-151	-162	-247	-267
Change in net debt	439	322	2,118	361
FCF equity	-176	-160	-95	-94
Balance sheet summary (USDm)				
Intangible fixed assets	53	53	928	928
Tangible fixed assets	6,718	7,058	10,991	11,501
Current assets	144	105	191	199
Cash & others	4	4	4	4
Total assets	6,961	7,262	12,156	12,674
Operating liabilities	1,546	1,420	1,545	1,558
Gross debt	2,564	2,886	5,003	5,364
Net debt	2,560	2,882	5,000	5,361
Shareholders' funds	2,009	2,114	4,765	4,910
Invested capital	5,365	5,792	10,561	11,067

Ratio, growth and per share analysis

Year to	12/2018a	12/2019e	12/2020e	12/2021e
Y-o-y % change				
Revenue	3.5	8.0	110.6	5.1
EBITDA	1.0	11.7	55.2	6.0
Operating profit	-1.8	12.9	58.4	4.5
PBT	-30.5	57.5	49.5	3.3
HSBC EPS	-20.0	39.4	6.3	3.3
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	6.8	6.2	6.7	5.3
ROE	9.7	12.9	11.6	8.5
ROA	4.5	5.1	5.8	4.7
EBITDA margin	56.1	58.0	42.8	43.1
Operating profit margin	38.6	40.3	30.3	30.1
EBITDA/net interest (x)	3.2	6.2	5.2	5.1
Net debt/equity	127.4	136.4	104.9	109.2
Net debt/EBITDA (x)	5.4	5.5	6.1	6.2
CF from operations/net debt	14.4	11.8	13.5	12.6
Per share data (USD)				
EPS Rep (diluted)	1.08	1.50	1.59	1.65
HSBC EPS (diluted)	1.08	1.50	1.59	1.65
DPS	0.85	0.91	0.99	1.07
Book value	11.29	11.88	19.04	19.62

Valuation data

Year to	12/2018a	12/2019e	12/2020e	12/2021e
EV/sales	13.5	12.8	7.2	7.0
EV/EBITDA	24.0	22.1	16.8	16.3
EV/IC	2.1	2.0	1.3	1.3
PE*	37.6	27.0	25.4	24.6
PB	3.6	3.4	2.1	2.1
FCF yield (%)	-2.0	-1.8	-1.1	-1.1
Dividend yield (%)	2.1	2.3	2.4	2.6

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2018a
GHG emission intensity*	[n/a]
Energy intensity*	[n/a]
CO_2 reduction policy	Yes
Social Indicators	**12/2018a**
Employee costs as % of revenues	[n/a]
Employee turnover (%)	[n/a]
Diversity policy	Yes

Governance Indicators	12/2018a
No. of board members	9
Average board tenure (years)	8.2
Female board members (%)	33.3
Board members independence (%)	88.9

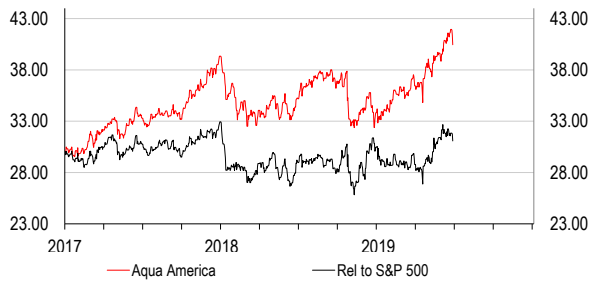
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	40.45	Free float	100%
Target price (USD)	45.50	Sector	Water Utilities
RIC (Equity)	WTR.N	Country	United States
Bloomberg (Equity)	WTR US	Analyst	Verity Mitchell
Market cap (USDm)	8,727	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 26 Jun 2019

Multi-utility creation: work-in-progress

- Peoples Natural Gas acquisition: completion now likely later in 2019 given regulatory progress; financing has been secured
- Fair market value continues to drive water growth: Texas now added to the states adopting the legislation
- Maintain Buy rating; TP increased from USD41 to USD45.5

Investment summary

Aqua America (Aqua) targets regulated asset growth of c7% through to 2021 in its water and wastewater business, supplemented by a strong pipeline of acquisitions of municipal water and wastewater systems. The majority of the states in which Aqua operates are either moving or have already moved to Fair Market Value (FMV), which allows municipalities to sell assets at an appraised value which is generally higher than book value. This 'fair' valuation offers attractive proceeds to a municipality and the ability for Aqua to earn returns on a fairly revalued rate base.

Other regulatory mechanisms, such as infrastructure surcharges allowing annual increases in rates for pipe replacement and the use of future test years in rate cases, are positive steps in removing the regulatory lag and smoothing out the time between rate cases. These changes are helping Aqua to improve the stability of revenues and allow it to accelerate investment.

The recent acquisition of Peoples Natural Gas Company, which is intended to diversify earnings into faster growing gas distribution, has increased the certainty of short-term growth. The high rate base growth (8-10%), once fully integrated, should drive short-term growth.

From a larger base and with organic growth planned in gas, accelerating water acquisitions of a larger size should maintain the 70:30 water to gas mix, which investors believe is an attractive balance of businesses.

Because of these factors we maintain our Buy rating on the stock with a target price of USD45.5.

Latest regulatory developments

On 11 June, 2019, Aqua participated in a hearing of the Pennsylvania Public Utility Commission and filed a settlement agreement for the acquisition of Peoples Gas. Two of the parties (intervenors) to the case opposed the settlement because of a disagreement on the treatment of a small gas system. This means the acquisition is now anticipated to occur in the fall of 2019, later than Q2 as originally anticipated by Aqua. Aqua has already started to raise the cUSD2.5bn of equity to buy Peoples. It wants a sufficient equity cushion to maintain a 12-13% FFO/adjusted net debt ratio. Merger approval has already been received in W Virginia and Kentucky.

PA rate case updates: Aqua's water and gas businesses have both filed for rate increases in their 'home' state of Pennsylvania (PA). It is the first time the company is using the fully projected future test year ending October 2020 for these. New rates are expected to go into effect in the fall 2019. Fair Market Value legislation continues to be a driver for the sales of regulated water systems (at an 'appraised value' at a premium to book value).

Texas adopts Fair Market Value legislation

On 12 June Aqua management commented that Texas had become the seventh state to adopt Fair Market Value legislation. This continues to be a key driver for the sales of regulated water systems (at an 'appraised value' at a premium to book value). In 2017 the American Society of Civil Engineers gave Texas a D+ rating for water and D rating for waste water. The combination of underinvested public health infrastructure with a mechanism for small cities to sell their systems at a premium to dedicated water companies underpins the strong attraction that US water stocks hold for us.

Growth

The company remains on track to grow customers at between 2% and 3% in 2019. Aqua invested USD133.8m in Q1 2019 to improve its infrastructure systems. To replace and expand its water utility infrastructure, the company expects to invest more than USD550m in 2019 and approximately USD1.4bn through 2021.

To date in 2019, the company's state subsidiaries in Ohio, Illinois and Pennsylvania have received rate awards or infrastructure surcharges totalling an estimated increase in annualized revenues of USD4.9m. Aqua currently has rate or surcharge proceedings pending in New Jersey, North Carolina and Ohio collectively totalling for USD6.3m. The timing and extent to which rate increases may be granted by the regulatory agencies will vary by state.

For Q1 2019 Aqua declared a quarterly cash dividend of USD0.2190 per share of common stock which represented 7% y-o-y growth.

Peoples transaction: break-up of the funds

Aqua has secured funding for the Peoples acquisition. Canada Pension Plan Investment Board (CPPIB) has acquired 21.3m newly issued shares of Aqua's common stock. CPPIB's investment is contingent upon the Peoples acquisition going ahead and getting final approval from the regulators. General corporate purposes include working capital and capital needs or repayment of certain revolving credit facility borrowings. During the Q1 2019 conference call Aqua management said, 'Our permanent financing plan targets a strong balance sheet and strong investment grade credit ratings for a fully regulated company.' We believe that Aqua will be able to maintain its credit ratings. Aqua America is rated Baa2 with stable outlook by Moody's. We set out our credit analysis below.

Sources and uses of funds

Sources of funds	USDm	Uses of funds	USDm
Common stock	1294	Peoples equity purchase price	2905
CPPIB Equity Investment	750	Assumption of Peoples debt	1370
Tangible equity units (mandatory convertible)	690	Private placement note refinancing	314
Debt	900	Transaction costs/ expenses	265
Assumption of Peoples debt	1370	General corporate purposes	150
Total Sources of funds	**5004**	**Total uses of funds**	**5004**

Source: Company presentation

Aqua has issued USD900m of senior notes at a weighted average yield of 3.96% with a weighted average maturity of 21 years. In addition to this, on 24 April, Aqua settled interest rate swaps (concurrent with the pricing of senior notes) that resulted in a payment by Aqua of USD83.5m compared with fair value of USD94.6m. Thus in the second quarter a beneficial charge in fair value of USD11.1m should be recorded.

Peoples transaction timeline visualised

Time line	Status
23-Oct-18	Aqua announced acquisition of peoples
13-Nov-18	Aqua files merger application with PA and WV PUCs
20-Nov-18	Aqua files merger application with KY PSC
28-Jan-19	Peoples filed a rate case for PA
8-Feb-19	Aqua filed a rate case settlement for PA
13-Mar-19	KY PSC approved merger application
27-Mar-19	Proposed merger settlement filed with WV PSC
29-Mar-19	Aqua announced USD750m equity investment from CPPIB
Apr-19	Aqua equity and debt offerings
Apr-19	WV PSC approved merger application
May-19	Aqua PA rate case expected to be in effect
4Q 2019	Targeted final resolution of PA merger proceedings
End 2019	Transaction expected to close

Source: Company presentation

Rate cases and surcharges

We can see from the table below that Aqua completed cUSD5m of rates and surcharges by Q1 2019 and has cUSD78m of rate cases and surcharges pending.

On 12 June 2019, Texas announced the adoption of Fair Market Value legislation for the purchase of the water and wastewater systems. Before these changes system values were determined by their depreciation cost, which generally did not reflect a reasonable market value for those assets and became a barrier to a sale.

Aqua's Chairman and CEO Christopher Franklin has said the new law encourages consolidation in the fragmented water and wastewater industry, enabling resources to be shared among a larger service area, which ultimately benefits customers.

Aqua 2019 rates and surcharges for water (W) and wastewater (WW)

State	Type	Annualised revenue increase (USD000)
Completed as at Q1 2019		
Illinois	Surcharge (W)	1394
Illinois	Surcharge (WW)	268
Ohio	Rate case (W)	974
Ohio	Surcharge (W)	2267
Pennsylvania	Surcharges (W/WW)	2
Total completed at Q1 2019		**4905**
Pending as at Q1 2019		
New Jersey	Rate case (W)	7202
North Carolina	Surcharge (W)	602
North Carolina	Surcharges (W/WW)	62
Ohio	Tax compliance surcharge	-3917
Ohio	Surcharge (W)	2335
Pennsylvania	Rate case (W)	58299
Pennsylvania	Rate case (WW)	13470
Total pending at Q1 2019		**78053**

Source: Company presentation

From the table below we believe that signed municipal contracts will help Aqua to reach its target of 2-3% customer growth for FY2019.

Signed municipal agreements at 1Q2019

Acquisitions	State	Type	Total customers	Rate base
New Garden	PA	WW	2106	29500
Schuykill	PA	WW	600	3600
Grant Park	IL	WW	540	2300
Cheltenham	PA	WW	10450	50250
Skyline	IL	W/WW	752	3550
East Norriton	PA	WW	4952	21000
Total			**19400**	**110200**

Source: Company presentation

2019 outlook

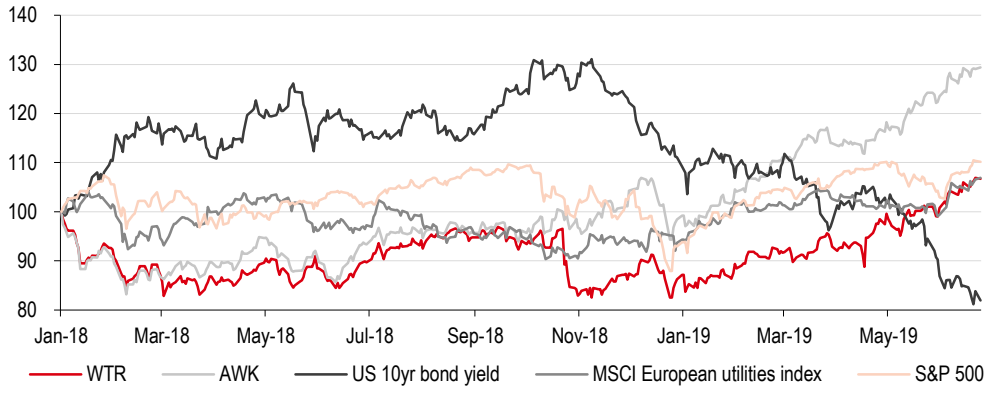
Aqua has guided for adjusted income of USD1.45 to USD1.50 per share (excluding Peoples) for 2019. Infrastructure investments of USD550m in 2019 for communities served by Aqua and investments of USD1.4bn to 2021 were confirmed at the Q1 to rehabilitate and strengthen systems. Aqua is targeting rate base growth of 7% in the water business through to 2021 and 8-10% in the gas business through to 2021. Aqua is targeting total customer growth of between 2-3% for FY2019. It will announce Q2 results on Wednesday, 7 August 2019.

Performance against peers

Aqua's share price has underperformed the S&P 500 by 3% since 1 January 2018, but it has outperformed by c5% YTD and c1.5% over 1 month. It appears that much of the scepticism about creating a multi-utility with the acquisition of Peoples has already been priced in. On our numbers, the deal is accretive in the first full year of the merged group and credit metrics remain on-track, see Credit metrics analysis below. On 2019e PE, it now trades at a discount to its water peer group and is in line with some of the US electricity utilities according to Refinitiv Datastream.

One more point to note is that the US Treasury 10 year yield is falling sharply. Aqua share price, as a defensive utility, is likely to be inversely correlated to bond yields.

Performance of Aqua America vs American Water Works vs UST 10yr vs MSCI European utilities index vs S&P 500 index



Source: Refinitiv DataStream

Change in estimates

We have updated the estimates based on the Q1 2019 results and to take account of the Pennsylvania rate case. This has impacted our estimates slightly. We had already assumed that the Peoples deal would not contribute to earnings until Q1 2020.

Change in estimates (USDm)

	2019e	2020e	2021e
EBIT			
Revised	365	578	604
Previous	365	578	604
Change	*0%*	*0%*	*0%*
Net income			
Revised	267	399	412
Previous	267	392	412
Change	*0%*	*2%*	*0%*
EPS (USD)			
Revised	1.50	1.59	1.65
Previous	1.50	1.58	1.66
Change	*0%*	*1%*	*-1%*
DPS (USD)			
Revised	0.91	0.99	1.07
Previous	0.91	0.99	1.07
Change	*0%*	*0%*	*0%*

Source: HSBC estimates

Credit metrics analysis

Aqua America is rated Baa2 with stable outlook by Moody's. To maintain this rating, Aqua will need to maintain RCF/Net debt in the range of 7-14% and FFO/Net debt in the range of 11-18%. From the calculated estimates below we can see that Aqua should be able to maintain the rating in the short term, but at the lower end of Moody's range of metrics.

Credit metrics analysis

	2019e	2020e	2021e
RCF/ Net debt	9.2%	7.8%	7.6%
FFO/ Net debt	14.8%	12.7%	12.5%

Source: HSBC estimates

Valuation and risks

We value Aqua America via three methodologies: DCF, dividend yield and the average of PE multiples and SOP (rate-based) valuation. Taking the average of the three approaches gives us our target price of USD45.5 (previously USD41).

In our DCF valuation, we have updated our assumption of beta from 0.60 to 0.58 to be in line with its market peers and have incorporated our updated estimates post Q1 2019 results. In our multiples-based valuation, we have updated the multiples in line with the market peers. This results in increase in PE multiple from 26.1x to 27.8x. Finally, in yield valuation, we have reduced our yield from 2.25% to 2% which is in line with its peers. Overall, these changes lead to an increased TP of USD45.5 from USD41. Our TP implies 12.5% upside; we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

Summary of valuation (USD)

Particulars	New	Previous
Current price as on 26-June-19	**40.5**	**NA**
DCF (updated estimates, lower beta)	46.0	39.5
Yield 2% (previously 2.25%)	49.4	43.9
SOP & Peer multiple (updated multiples)	41.0	39.6
Target price (average rounded)	**45.5**	**41.0**
Upside/ downside to target price	12.5%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity Valuation	USDm
Cost of debt		**+ DCF value**	**15,725**
Pre-tax cost of debt	3.9%	+ ST marketable assets	-
Marginal tax rate	11.0%	+ Value of associates	-
Cost of equity		+ Other assets	788
Risk-free rate	3.0%	**EV (asset side)**	**16,513**
Equity risk premium	3.0%	- Net debt (+ if Net cash)	(5,000)
Additional risk		- Quasi debt (pension)	-
Beta (previously 0.60)	**0.58**	- Value of minorities	0
Debt - 34%	3.5%	Total non-equity claims	(5,000)
Equity - 66%	4.7%	**Value of equity**	**11,513**
Cost of capital	**4.3%**	**Value per share (USD)**	**46.0**

Source: HSBC estimates

Sum-of-the-parts (SOP) and Multiples valuation

	2020e Rate base
Regulated water	
Pennsylvania	3,673
Ohio	363
Illinois	366
Texas	269
New Jersey	196
North Carolina	233
Indiana	95
Virginia	86
Regulated gas	2,733
Total	**8,014**
Price to rate base	14,424
Non-regulated 2020 PE multiple	13
Net debt 2020e, pensions & Minority	(5,000)
Estimated equity value	**9,437**
Estimated equity value per share (USD)	**37.7**
PE Multiple valuation	
2020 earnings	1.59
2020 PE sector average	27.8
Value per share	**44.3**
Average of rate base valuation and PE multiple valuation	**41.0**

Source: HSBC estimates

Downside risks

Aqua America fails to achieve the desired rate case revisions and infrastructure surcharges; it lacks organic growth from asset replacement; it cannot take advantage of the FV market legislation opportunity; its dividend grows at a lower rate than we assume.

It is not able to gain the Fair Market Value premium required in the systems it wants to acquire in Pennsylvania. Its current acquisitions of systems – New Garden and Limerick – are facing challenges to the premium proposed by Aqua.

Disclosure appendix

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Upside/Downside is the percentage difference between the target price and the share price.

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For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

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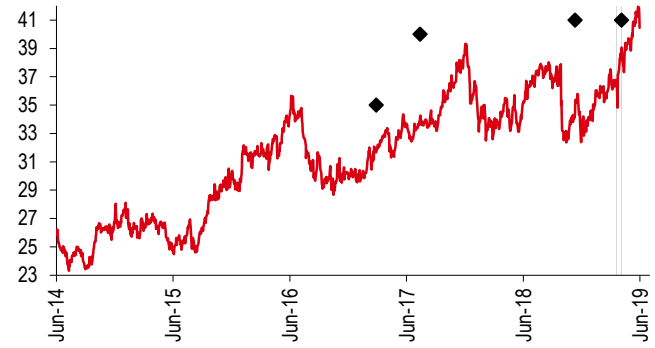
Share price and rating changes for long-term investment opportunities

Aqua America (WTR.N) share price performance USD Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	35.00	24 Mar 2017	Verity Mitchell
Price 2	40.00	08 Aug 2017	Verity Mitchell
Price 3	41.00	06 Dec 2018	Verity Mitchell
Price 4	Restricted	15 Apr 2019	
Price 5	41.00	30 Apr 2019	Verity Mitchell

Source: HSBC

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Company	Ticker	Recent price	Price date	Disclosure
AQUA AMERICA	WTR.N	40.45	26 Jun 2019	1, 2, 5, 6

Source: HSBC

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[1123548]

HSBC Global Research

27 August 2020

Essential Utilities (WTRG US)

Buy: Capital raise to underpin growth

Equities
Water Utilities

United States

- H1 results and 3% (USD311m) capital increase should underpin growth
- Fair Value legislation and infrastructure rehabilitation key drivers for growth
- Maintain Buy rating and target price of USD50

H1 2020 results and 3% capital raise: On 5 August 2020, Essential reported its H1 results. EPS was USD0.5, up 28%, and affirmed its full-year guidance of USD1.53-USD1.58. On 10 August 2020, it successfully raised an additional USD311m through issuing 6.7m new shares (c3%) of equity. The need for this to fund regulated growth was previously flagged.

Growth: Essential's equity raise will be used to underpin a stable capital structure in its growing regulated water and gas businesses. US regulators generally assume a capital structure of 50:50 debt and equity so the equilibrium on a growing rate base needs to be maintained. In addition, Essential sees opportunities for further acquisitions using the Fair Value principles. Acquisitions are mostly going to be focused on water rather than gas. Its gas expansion is at present focused on mains replacement at Peoples Gas. Essential is focusing on repair tax principles here, which it has utilised in water in Pennsylvania. The use of capital allowances to reduce taxes delays the need to file for rate cases, smoothing customer rates in times of accelerated investment.

Maintain Buy and target price of USD50: We value Essential Utilities via three methodologies: DCF, dividend yield and the average of our PE multiple and rate-based valuations. Taking the average of the three approaches gives us our target price of USD50.00 (unchanged). In our DCF, we maintain our beta at 0.6, in line with its peers. We update our estimates as explained above, which decreases our DCF valuation to USD48.1 from USD50.0. For our PE-multiple-based valuation, we update our target multiple to 31.0x from 30.0x to keep it in line with peers. We use a water peer group P/B of 2.4x (unchanged) as a proxy for a rate-based valuation, which is consistent with all US utilities under our coverage and is a proxy for EV. The average of the two increases to USD52.1 from USD51.6, reflecting our updated estimates. For our yield-based valuation, we reduce our target yield to 2.0% from 2.13%, in line with its Water and Related Utilities peers. This results in an increase in our yield valuation to USD50.1 from USD47.5. Overall, these changes lead to an unchanged target price of USD50.00, which implies 15.5% upside. We reiterate our Buy rating as we believe the combination of regulated investment growth and earnings growth is attractive.

MAINTAIN BUY

TARGET PRICE (USD)	PREVIOUS TARGET (USD)
50.00	**50.00**
SHARE PRICE (USD)	UPSIDE/DOWNSIDE
43.28	**+15.5%**
(as of 25 Aug 2020)	

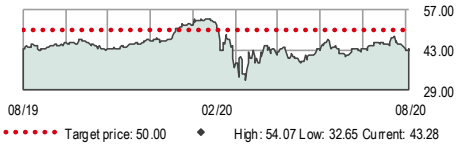
MARKET DATA

Market cap (USDm)	10,610	Free float	100%
Market cap (USDm)	10,610	BBG	WTRG US
3m ADTV (USDm)	52	RIC	WTRG.N

FINANCIALS AND RATIOS (USD)

Year to	12/2019a	12/2020e	12/2021e	12/2022e
HSBC EPS	1.04	1.53	1.66	1.79
HSBC EPS (prev)	1.04	1.55	1.67	1.79
Change (%)	0.0	-1.0	-0.8	0.0
Consensus EPS	1.48	1.48	1.66	1.80
PE (x)	41.6	28.2	26.1	24.2
Dividend yield (%)	2.2	2.3	2.5	2.7
EV/EBITDA (x)	23.8	17.5	16.7	15.9
ROE (%)	7.6	8.1	7.2	7.3

52-WEEK PRICE (USD)



Source: Refinitiv IBES, HSBC estimates

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Disclosures & Disclaimer
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Issuer of report: HSBC Bank plc

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Financials & valuation: Essential Utilities

Buy

Financial statements

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Profit & loss summary (USDm)				
Revenue	890	1,882	2,141	2,276
EBITDA	497	834	906	989
Depreciation & amortisation	-157	-249	-266	-292
Operating profit/EBIT	340	585	639	697
Net interest	-131	-150	-156	-177
PBT	212	435	484	520
HSBC PBT	209	435	484	520
Taxation	13	-35	-39	-42
Net profit	225	400	445	479
HSBC net profit	225	400	445	479
Cash flow summary (USDm)				
Cash flow from operations	339	718	729	780
Capex	-550	-950	-1,000	-1,000
Cash flow from investment	-605	-5,225	-1,277	-1,000
Dividends	-189	-262	-288	-308
Change in net debt	-1,352	2,814	535	528
FCF equity	-212	-232	-271	-220
Balance sheet summary (USDm)				
Intangible fixed assets	64	939	939	939
Tangible fixed assets	7,224	11,325	12,335	13,043
Current assets	2,011	2,152	2,188	2,207
Cash & others	1,869	1,869	1,869	1,869
Total assets	9,360	14,477	15,524	16,251
Operating liabilities	1,468	1,677	1,732	1,761
Gross debt	3,077	5,891	6,426	6,954
Net debt	1,208	4,022	4,557	5,085
Shareholders' funds	3,881	5,974	6,432	6,602
Invested capital	5,962	10,870	11,862	12,560

Ratio, growth and per share analysis

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Y-o-y % change				
Revenue	6.2	111.6	13.8	6.3
EBITDA	5.7	67.7	8.7	9.2
Operating profit	5.3	72.0	9.3	9.0
PBT	18.6	105.7	11.2	7.6
HSBC EPS	-3.4	47.4	8.3	7.6
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	6.4	6.4	5.2	5.2
ROE	7.6	8.1	7.2	7.3
ROA	4.1	4.5	3.9	4.0
EBITDA margin	55.9	44.3	42.3	43.5
Operating profit margin	38.2	31.1	29.9	30.6
EBITDA/net interest (x)	3.8	5.6	5.8	5.6
Net debt/equity	31.1	67.3	70.9	77.0
Net debt/EBITDA (x)	2.4	4.8	5.0	5.1
CF from operations/net debt	28.0	17.8	16.0	15.3
Per share data (USD)				
EPS Rep (diluted)	1.04	1.53	1.66	1.79
HSBC EPS (diluted)	1.04	1.53	1.66	1.79
DPS	0.94	1.00	1.07	1.15
Book value	17.97	22.88	24.00	24.63

Valuation data

Year to	12/2019a	12/2020e	12/2021e	12/2022e
EV/sales	13.3	7.8	7.1	6.9
EV/EBITDA	23.8	17.5	16.7	15.9
EV/IC	2.0	1.3	1.3	1.2
PE*	41.6	28.2	26.1	24.2
PB	2.4	1.9	1.8	1.8
FCF yield (%)	-2.0	-2.2	-2.5	-2.1
Dividend yield (%)	2.2	2.3	2.5	2.7

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2019a
GHG emission intensity*	n/a
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social Indicators	**12/2019a**
Employee costs as % of revenues	n/a
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	12/2019a
No. of board members	8
Average board tenure (years)	7.0
Female board members (%)	25
Board members independence (%)	87.5

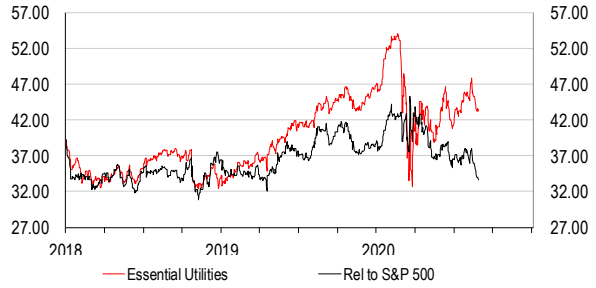
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	43.28	Free float	100%
Target price (USD)	50.00	Sector	Water Utilities
RIC (Equity)	WTRG.N	Country/Region	United States
Bloomberg (Equity)	WTRG US	Analyst	Verity Mitchell
Market cap (USDm)	10,610	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 25 Aug 2020

Capital raise underpins growth

- H1 results and USD311m (3%) capital increase to underpin growth
- Fair Value legislation and infrastructure rehabilitation key drivers for growth
- Maintain Buy rating and target price of USD50

H1 results and funding for growth

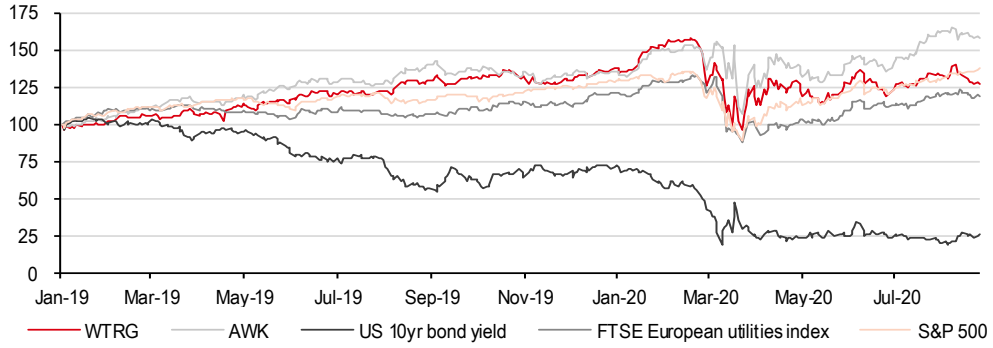
H1 results and 3%capital raise: Essential reported H1 results EPS of USD0.5 +28%. The company affirmed FY guidance of USD1.53 – USD1.58. On 10 August 2020 it successfully raised an additional USD311m 6.7m new shares (c3%) of equity (c3%) of equity. The need for this to fund regulated growth had been previously flagged.

Growth: Essential's equity raise will underpin a stable capital structure in its growing regulated water and gas businesses. US regulated assets assume a capital structure of 50:50 debt and equity so the equilibrium on a growing rate base needs to be maintained. In addition, it sees opportunities for further acquisitions using the Fair Value principles (FV). Acquisitions are mostly going to be focused on water rather than gas. Its gas expansion is at present focused on mains replacement at Peoples Gas. Essential is focusing on repair tax principles here which it has utilised in water in Pennsylvania. Use of capital allowances to reduce tax delays the need to file for rate cases smoothing customer rates in times of accelerated investment.

Performance against peers

Essential's share price has underperformed the S&P 500 by 10% since 1 January 2019. It is trading at a discount to its water peer group's 2020e PE, but in line with some of the US electricity utilities according to Refinitiv Datastream. This reflects, in our view, its multi-utility status. The US Treasury 10-year yield has fallen sharply. WTRG, as a defensive utility, should be inversely correlated to bond yields.

WTRG vs AWK vs UST 10yr vs FTSE European utilities index vs S&P500



Source: Refinitiv DataStream

Credit metrics analysis

Moody's requires RCF/net debt in the range of 7-14% and FFO/net debt in the range of 11-18% to maintain a Baa credit rating. Essential's credit metrics for 2020, shown below, meet the requirements – it currently has a Baa2 credit rating from Moody's with stable outlook. This is mainly due to the liquidity created by the company by issuing equity as mentioned above.

Credit metrics analysis

	2020e	2021e	2022e
RCF/Net Debt	9.7%	9.4%	9.2%
FFO/Net Debt	16.2%	15.7%	15.2%

Source: HSBC estimates

Estimate changes

We update our model post the H1 2020 results, which included updated guidance due to the COVID-19 pandemic and post the issuance of equity. Essential mentioned at its H1 results that growth for its municipal water segment has been more than offset by the reduction in its industrial and commercial water segments, which reflects the resilience of the municipal segment. Given that we expect increased commercial activities in H2, we increase our estimates for 2020e only slightly as shown in the table below (However, 2020e EPS is lower down due to the slight dilution from equity issuance). For 2021, we assume that Essential begins to utilise the repair tax, which lowers current taxes so increases net income, but the equity issuance dilutes EPS and DPS).

Estimate changes

	2020e	2021e	2022e
EBIT (USDm)			
Revised	585	639	697
Previous	578	646	701
Change	*1%*	*-1%*	*-1%*
Net income (USDm)			
Revised	400	445	479
Previous	394	438	469
Change	*2%*	*2%*	*2%*
EPS (USD)			
Revised	1.53	1.66	1.79
Previous	1.55	1.67	1.79
Change	*-1%*	*-1%*	*0%*
DPS (USD)			
Revised	1.00	1.07	1.15
Previous	1.01	1.09	1.18
Change	*-1%*	*-2%*	*-3%*

Source: HSBC estimates

Valuation and risks

We value Essential Utilities using the average of three approaches: 1) DCF; 2) dividend yield; and 3) the average of our PE multiple and rate-based valuations, which renders our unchanged target price of USD50.

- In our DCF, we maintain our beta at 0.6 in line with its peers. We slightly increase our estimates for 2020 but the dilution from the capital increase decreases our DCF valuation marginally from USD50.0 to USD48.1.
- For our yield-based valuation, we reduce our target yield to 2.0% from 2.13% to keep it in line with the water and related utilities peers. This increases our yield valuation to USD50.1 from USD47.5.

- For our PE multiple-based valuation in the average of a PE multiple and rate-based valuation approach, we update our target multiple to 31.0x from 30.0x to keep it in line with that of peers. We continue to use a water peer group P/B of 2.4x as a proxy for a rates-based valuation. This is consistent with all US utilities under our coverage and is a proxy for EV. The average of the two increases to USD52.1 from USD51.6, reflecting our updated estimates. We continue to use regulated water peers not gas utility peers because water utilities have higher implicit growth. Peoples was acquired because it too has an accelerated mains replacement cycle.

Overall, these changes lead to no unchanged in our target price of USD50, which implies 15.5% upside. We reiterate our Buy rating as we believe the combination of regulated investment growth and earnings growth is attractive.

Valuation summary (USD)

Particulars	New	Previous
Current price as on 25-Aug-20	**43.3**	**NA**
DCF (updated estimates)	48.1	50.0
Yield 2% (previously 2.13%)	50.1	47.5
SOTP and peer multiple (updated multiples)	52.1	51.6
Target price (average rounded)	**50.0**	**50.0**
Implied upside/downside to target price	15.5%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity Valuation	USDm
Cost of debt		**+ DCF value**	**15,681**
Pre-tax cost of debt	3.9%	+ ST marketable assets	0
Marginal tax rate	8.0%	+ Value of associates	0
Cost of equity		+ Other assets	878
Risk-free rate	2.5%	**EV (asset side)**	**16,560**
Equity risk premium	3.0%	- Net debt (+ if Net cash)	(3,993)
Additional risk		- Quasi debt (pension)	0
Beta	**0.60**	- Value of minorities	0
Debt - 34%	3.6%	Total non-equity claims	(3,993)
Equity - 66%	4.3%	Value of equity	12,566
Cost of capital	**4.1%**	**Value per share (USD)**	**48.1**

Source: HSBC estimates

Sum-of-the-parts (SOTP) using rate bases and multiple valuation

USDm	2020e Rate Base
Regulated water	
Pennsylvania	3,682
Ohio	368
Illinois	382
Texas	319
New Jersey	214
North Carolina	245
Indiana	90
Virginia	83
Regulated gas	2,451
Total	**7,834**
Price to rate base (USDm)	18,802
Non-regulated 2020 PE multiple (20x)	7
Net debt 2020e, pensions and minorities	(3,993)
Estimated equity value	14,815
Estimated equity value per share (USD)	**56.7**
PE multiple valuation	
2020 earnings per share (USD)	1.53
2020 PE sector average (x)	31.0
Value per share	**47.5**
Average of rate-based valuation and PE multiple valuation	**52.1**

Source: HSBC estimates

Downside risks: Essential Utilities failing to achieve the desired rate case revisions and infrastructure surcharges; lacking organic growth from asset replacement; inability to take advantage of the Fair Market Value legislation opportunity; dividend growth at a lower rate than we assume; inability to gain the Fair Market Value premium required in the systems it wants to acquire in Pennsylvania. Its current acquisitions of systems – New Garden and Limerick – are facing challenges to the premium proposed by Aqua.

Disclosure appendix

Analyst Certification

The following analyst(s), economist(s), or strategist(s) who is(are) primarily responsible for this report, including any analyst(s) whose name(s) appear(s) as author of an individual section or sections of the report and any analyst(s) named as the covering analyst(s) of a subsidiary company in a sum-of-the-parts valuation certifies(y) that the opinion(s) on the subject security(ies) or issuer(s), any views or forecasts expressed in the section(s) of which such individual(s) is(are) named as author(s), and any other views or forecasts expressed herein, including any views expressed on the back page of the research report, accurately reflect their personal view(s) and that no part of their compensation was, is or will be directly or indirectly related to the specific recommendation(s) or views contained in this research report: Verity Mitchell and Adam Dickens

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From 23rd March 2015 HSBC has assigned ratings on the following basis:

The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

Prior to this date, HSBC's rating structure was applied on the following basis:

For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

As of 26 August 2020, the distribution of all independent ratings published by HSBC is as follows:

Buy	55%	(31% of these provided with Investment Banking Services)
Hold	36%	(33% of these provided with Investment Banking Services)
Sell	9%	(25% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

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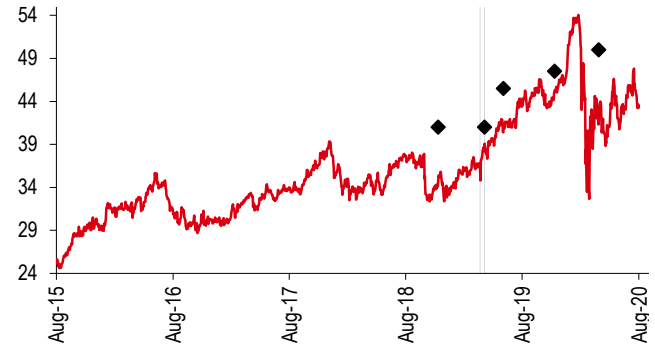
Share price and rating changes for long-term investment opportunities

Essential Utilities (WTRG.N) share price performance USD Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	41.00	06 Dec 2018	Verity Mitchell
Price 2	Restricted	15 Apr 2019	
Price 3	41.00	30 Apr 2019	Verity Mitchell
Price 4	45.50	28 Jun 2019	Verity Mitchell
Price 5	47.50	06 Dec 2019	Verity Mitchell
Price 6	50.00	22 Apr 2020	Verity Mitchell

Source: HSBC

To view a list of all the independent fundamental ratings disseminated by HSBC during the preceding 12-month period, please use the following links to access the disclosure page:

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HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price date	Disclosure
ESSENTIAL UTILITIES	WTRG.N	43.28	25 Aug 2020	1, 5, 6

Source: HSBC

1 HSBC has managed or co-managed a public offering of securities for this company within the past 12 months.

2 HSBC expects to receive or intends to seek compensation for investment banking services from this company in the next 3 months.

3 At the time of publication of this report, HSBC Securities (USA) Inc. is a Market Maker in securities issued by this company.

4 As of 31 July 2020, HSBC beneficially owned 1% or more of a class of common equity securities of this company.

5 As of 30 June 2020, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of investment banking services.

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7 As of 30 June 2020, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of non-securities services.

8 A covering analyst/s has received compensation from this company in the past 12 months.

9 A covering analyst/s or a member of his/her household has a financial interest in the securities of this company, as detailed below.

10 A covering analyst/s or a member of his/her household is an officer, director or supervisory board member of this company, as detailed below.

11 At the time of publication of this report, HSBC is a non-US Market Maker in securities issued by this company and/or in securities in respect of this company

12 As of 21 Aug 2020, HSBC beneficially held a net long position of more than 0.5% of this company's total issued share capital, calculated according to the SSR methodology1

13 As of 21 Aug 2020, HSBC beneficially held a net short position of more than 0.5% of this company's total issued share capital, calculated according to the SSR methodology.

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Additional disclosures

1 This report is dated as at 27 August 2020.

2 All market data included in this report are dated as at close 25 August 2020, unless a different date and/or a specific time of day is indicated in the report.

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1. This report was produced and signed off by the author on 26 Aug 2020 17:02 GMT.

2. In order to see when this report was first disseminated please see the disclosure page available at https://www.research.hsbc.com/R/34/7TBb6VF

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[1154243]

HSBC Global Research

16 November 2020

Essential Utilities (WTRG US)

Buy: Q3 progress through regulatory complexity

Equities
Water Utilities

United States

- Q3 results – top end of annual EPS targets
- Strong acquisitions pipeline – Delcora complexity the exception to the rule; regulatory settlements for infrastructure continuing
- Maintain Buy rating, increase TP to USD55 (from USD50)

Q3 results summary. For the first nine months of 2020, customer growth for the company's water utilities totalled 1.5%. Essential invested USD554.1m in the first nine months of the year to improve its regulated water and natural gas infrastructure systems. Management expects adjusted EPS at the top end of the USD1.53-1.58 range for 2020e, with an earnings CAGR target of 5-7% for 2019 through to 2022e.

Strong pipeline of acquisitions, regulatory settlements continuing. The company has signed purchase agreements for municipal water and wastewater acquisitions that are expected to add the equivalent of more than 212,000 water and wastewater retail customers and approximately USD363m in expected rate base. Its most significant acquisition, Delcora, is mired in regulatory and legal complexity. Essential hopes that all issues will be resolved by March-April 2021. This complexity, in our view, should be regarded as the exception to what is normally a smooth process. To date in 2020, the regulated water segment has received rate awards or infrastructure surcharges in Illinois, Indiana, North Carolina, Ohio, Virginia and Pennsylvania totalling an estimated annualised revenue increase of USD21.0m.

Maintain Buy rating; increase target price from USD50 to USD55. We value Essential Utilities using the average of three approaches: (1) DCF, (2) dividend yield, and (3) the average of our PE multiple and rate-based valuations, which renders our increased target price of USD55 (previously USD50). In our DCF, we increase our estimates for 2020e slightly and roll forward our base to 2021e, which increases our valuation to USD50.80 (from USD48.10). For our yield-based approach, we maintain our target yield at 2.0%. We have rolled forward the dividend, which increases our yield valuation to USD53.70 from USD50.10. For our approach using the average of PE and rate-based valuations, we update our target multiple to 33.0x from 31.0x. We use a water peer group PB of 2.6x as a proxy for our rate-based valuation. The average of the two increases to USD61.80 (from USD52.10), reflecting our updated estimates. Peoples Natural Gas was acquired because it, too, has an accelerated mains replacement cycle. Overall, these changes lead to an increased target price of USD55 (previously USD50), which implies c23% upside from current levels. We reiterate our Buy rating as we believe the combination of regulated investment growth and earnings growth remains attractive.

MAINTAIN BUY

TARGET PRICE (USD)	PREVIOUS TARGET (USD)
55.00	**50.00**
SHARE PRICE (USD)	UPSIDE/DOWNSIDE
44.80	**+22.8%**
(as of 12 November 2020)	

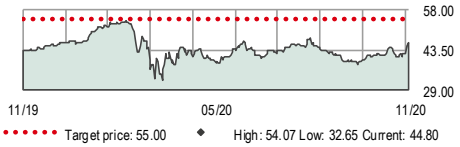
MARKET DATA

Market cap (USDm)	10,983	Free float	100%
Market cap (USDm)	10,983	BBG	WTRG US
3M ADTV (USDm)	51	RIC	WTRG.N

FINANCIALS AND RATIOS (USD)

Year to	12/2019a	12/2020e	12/2021e	12/2022e
HSBC EPS	1.04	1.61	1.67	1.81
HSBC EPS (prev)	1.04	1.53	1.66	1.79
Change (%)	0.0	5.2	0.5	1.3
Consensus EPS	1.48	1.53	1.66	1.79
PE (x)	43.1	27.8	26.9	24.8
Dividend yield (%)	2.1	2.2	2.4	2.6
EV/EBITDA (x)	24.5	18.7	17.7	16.9
ROE (%)	7.6	8.6	7.5	7.8

52-WEEK PRICE (USD)



Source: Refinitiv IBES, HSBC estimates

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Financials & valuation: Essential Utilities

Buy

Financial statements

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Profit & loss summary (USDm)				
Revenue	890	1,882	2,141	2,276
EBITDA	497	834	916	989
Depreciation & amortisation	-157	-249	-266	-292
Operating profit/EBIT	340	585	649	697
Net interest	-131	-155	-192	-201
PBT	212	430	457	495
HSBC PBT	209	430	457	495
Taxation	13	-34	-37	-40
Net profit	225	396	420	456
HSBC net profit	225	396	420	456
Cash flow summary (USDm)				
Cash flow from operations	339	713	705	757
Capex	-550	-950	-1,000	-1,000
Cash flow from investment	-605	-5,225	-1,277	-1,000
Dividends	-189	-246	-270	-289
Change in net debt	-1,352	3,443	542	532
FCF equity	-212	-237	-295	-243
Balance sheet summary (USDm)				
Intangible fixed assets	64	939	939	939
Tangible fixed assets	7,224	11,325	12,335	13,043
Current assets	2,011	2,152	2,188	2,207
Cash & others	1,869	1,869	1,869	1,869
Total assets	9,360	14,477	15,524	16,251
Operating liabilities	1,468	1,677	1,732	1,761
Gross debt	3,077	6,521	7,063	7,595
Net debt	1,208	4,652	5,194	5,726
Shareholders' funds	3,881	5,345	5,795	5,961
Invested capital	5,962	10,870	11,862	12,560

Ratio, growth and per share analysis

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Y-o-y % change				
Revenue	6.2	111.6	13.8	6.3
EBITDA	5.7	67.7	9.8	8.0
Operating profit	5.3	72.0	11.0	7.3
PBT	18.6	103.3	6.3	8.4
HSBC EPS	-3.4	55.1	3.4	8.4
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	6.4	6.4	5.3	5.2
ROE	7.6	8.6	7.5	7.8
ROA	4.1	4.5	4.0	4.0
EBITDA margin	55.9	44.3	42.8	43.5
Operating profit margin	38.2	31.1	30.3	30.6
EBITDA/net interest (x)	3.8	5.4	4.8	4.9
Net debt/equity	31.1	87.0	89.6	96.0
Net debt/EBITDA (x)	2.4	5.6	5.7	5.8
CF from operations/net debt	28.0	15.3	13.6	13.2
Per share data (USD)				
EPS Rep (diluted)	1.04	1.61	1.67	1.81
HSBC EPS (diluted)	1.04	1.61	1.67	1.81
DPS	0.94	1.00	1.07	1.15
Book value	17.97	21.79	23.00	23.66

Source: Company data, HSBC estimates

Valuation data

Year to	12/2019a	12/2020e	12/2021e	12/2022e
EV/sales	13.7	8.3	7.6	7.3
EV/EBITDA	24.5	18.7	17.7	16.9
EV/IC	2.0	1.4	1.4	1.3
PE*	43.1	27.8	26.9	24.8
PB	2.5	2.1	1.9	1.9
FCF yield (%)	-1.9	-2.2	-2.7	-2.2
Dividend yield (%)	2.1	2.2	2.4	2.6

*Based on HSBC EPS (diluted)

Source: Company data, HSBC estimates

ESG metrics

Environmental indicators	12/2019a
GHG emission intensity*	n/a
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social indicators	**12/2019a**
Employee costs as % of revenue	n/a
Employee turnover (%)	n/a
Diversity policy	Yes

Governance indicators	12/2019a
Number of board members	8
Average board tenure (years)	7.0
Female board members (%)	25
Board member independence (%)	87.5

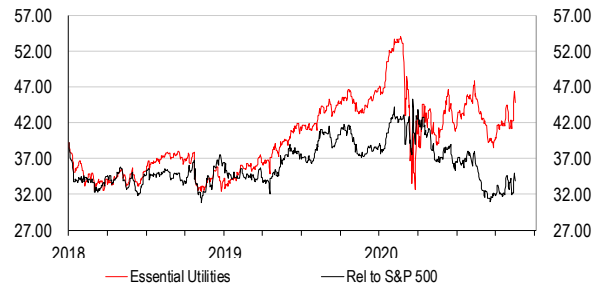
* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Source: Company data, HSBC

Issuer information

Share price (USD)	44.80	Free float	100%
Target price (USD)	55.00	Sector	Water Utilities
RIC (Equity)	WTRG.N	Country/Region	United States
Bloomberg (Equity)	WTRG US	Analyst	Verity Mitchell
Market cap (USDm)	10,983	Contact	+44 20 7991 6840

Price relative



Note: Priced at close of 12 November 2020

Source: HSBC

Q3 Progress, some regulatory complexity remains

- Q3 results – top end annual EPS targets indicated
- Strong pipeline of acquisitions – Delcora complexity the exception to the rule; regulatory settlements for infrastructure continuing
- Maintain Buy rating; increase TP to USD55 (from USD50)

Q3 2020 results summary

Essential Utilities reported Q3 results on 3 November 2020. The regulated water segment reported revenues for the quarter of USD255.7m, an increase of 5.3%. Increased volume and rates and surcharges were the largest contributors to the increase in revenues for the period, in addition to customer growth from both organic growth and acquisitions. Operations and maintenance expenses for the regulated water segment decreased by 2.2% to USD79.3m for the third quarter of 2020. The regulated natural gas segment reported revenues for the third quarter of 2020 of USD88.9m. Operations and maintenance for the same period for the regulated natural gas segment were USD59.6m and purchased gas costs were USD14.8m. The first nine months of 2020, customer growth for the company's water utilities has totalled 1.5%.

The company has signed purchase agreements for other municipal water and wastewater acquisitions that are expected to add the equivalent of over 212,000 water and wastewater retail customers and approximately USD363m in expected rate base.

Essential invested USD554.1m in the first nine months of the year to improve its regulated water and natural gas infrastructure systems and to enhance its customer service across its operations. This does not include an additional USD53.5m that was invested by Peoples, pre-closing, during the period from 1 January to 15 March 2020.

To date in 2020, the regulated water segment has received rate awards or infrastructure surcharges in Illinois, Indiana, North Carolina, Ohio, Virginia and Pennsylvania totalling an estimated increase in annualized revenues of USD21.0m.

Essential declared a quarterly cash dividend of $0.2507 +7%.

The outlook:

- Expects adjusted income per diluted common share (non-GAAP) at the top end of the USD1.53 to USD1.58 range
- Earnings growth CAGR of 5 to 7% for 2019 through to 2022
- Regulated water segment infrastructure investments of approximately USD550m in 2020
- Regulated natural gas segment infrastructure investments of approximately USD400m in 2020 on full-year basis (adjusted to include capital invested in 2020 prior to Essential's ownership)

- Infrastructure investments of approximately USD2.8bn through to 2022 in existing operations to rehabilitate and strengthen water, wastewater, and natural gas systems (including regulated natural gas segment capital invested in 2020 prior to Essential's ownership)
- Regulated water segment rate base compound annual growth rate of 6 to 7% through to 2022
- Regulated natural gas segment rate base compound annual growth rate of 8 to 10% through to 2022
- Total annual regulated water segment customer growth of between 2 and 3% on average depending upon regulatory approval

Delcora the exception that proves the rule on regulatory complexity – expect closure by March-April 2021

Management provided an update to its proposed Delcora acquisition which is currently mired in regulatory and legal complexity. There is an imminent court proceeding to decide whether there is a valid and enforceable contract in place between Essential and Delcora. In addition, there are separate issues about the Delcora trust. In addition to these legal complexities the PUC will then become involved in assessing the acquisition. Essential hopes that all issues – legal and regulatory – will be resolved by March-April 2021. This complexity, in our view, should be regarded as the exception to what is normally a smooth process.

Use of equity raise proceeds

The CEO also mentioned in the earnings call Q&A that the USD300m August equity offering wold be deployed even if there were continuing delays in the Delcora acquisition. Management is seeing a number of medium to large acquisition opportunities. Equity currently deferred would be deployed as and when needed in order to finance these acquisitions.

Acquisitions will remain focused on water and waste water. The Peoples gas rate base growth is targeted to be 8% to 10% annually without acquisitions given the need for pipe replacement.

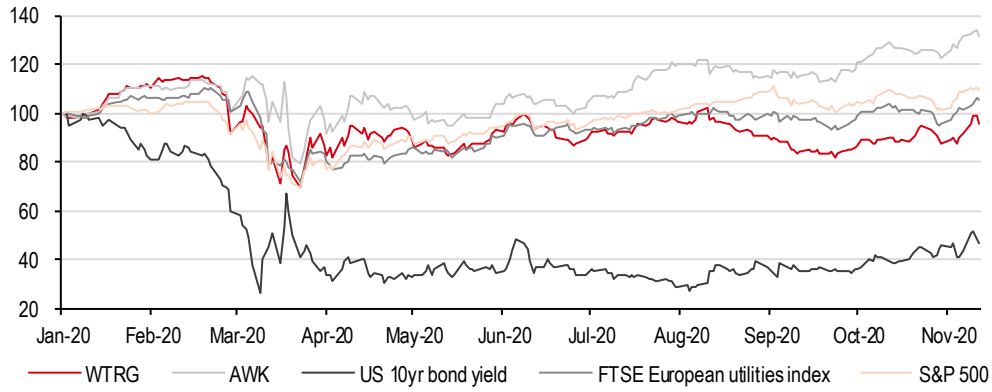
Peoples rate case use tax repair – resolution expected Q2 2021

Essential is focusing on repair tax principles which it has utilised in water in Pennsylvania. It filed a request for USD380 of repair tax in July from the Pennsylvania PUC. This is a catch-up deduction for the tax repair eligible capital invested prior to Essential's ownership of Peoples. Regulatory evidentiary hearings area expected at the end of January. The company expects a final order sometime early in the second quarter of 2021.

Performance against peers

YTD, Essential's share price has underperformed the S&P 500 by 14%. It is trading at a discount to its water peer group's 2020e PE, but in line with some of the US electricity utilities according to Refinitiv Datastream. This reflects, in our view, its multi-utility status. The US Treasury 10-year yield has fallen sharply. WTRG, as a defensive utility, should be inversely correlated to bond yields.

YTD performance of WTRG vs AWK vs UST 10yr vs FTSE European utilities index vs S&P500



Source: Refinitiv Datastream

Credit metrics analysis

Moody's requires RCF/net debt in the range of 7-14% and FFO/net debt in the range of 11-18% to maintain a 'Baa' credit rating. Essential's credit metrics for 2020, shown below, meet the requirements – it currently has a Baa2 credit rating from Moody's with stable outlook.

Credit metrics analysis

	2020e	2021e	2022e	2023e	2024e	2025e
RCF / net debt	8.6%	8.1%	8.1%	8.0%	8.1%	8.3%
FFO / net debt	13.9%	13.3%	13.1%	13.1%	13.4%	13.8%

Source: HSBC estimates

Change in estimates

We have updated our estimates post Q3 2020 results to reflect improved performance at the P&L bottom line. We continue to assume the USD300m of equity issuance, which was done on a forward basis.

Change in estimates (USDm)

	2020e	2021e	2022e
EBIT (USDm)			
Revised	585	649	697
Previous	585	639	697
Change	*0%*	*2%*	*0%*
Net income (USDm)			
Revised	396	420	456
Previous	400	445	479
Change	*-1%*	*-6%*	*-5%*
EPS (USD)			
Revised	1.61	1.67	1.81
Previous	1.53	1.66	1.79
Change	*5%*	*1%*	*1%*
DPS (USD)			
Revised	1.00	1.07	1.15
Previous	1.00	1.07	1.15
Change	*0%*	*0%*	*0%*

Source: HSBC estimates

Valuation and risks

We value Essential Utilities using the average of three approaches: (1) DCF, (2) dividend yield, and (3) the average of our PE multiple and rate-based valuations, which renders our increased target price of USD55 (previously USD50).

- In our DCF, we maintain our beta at 0.6 in line with its peers. We updated our estimates as above, moved equity issuance to for Delcora to 2021 and rolled forward our DCF valuation to 2021e which increases our valuation from USD48.10 to USD50.80.
- For our yield-based valuation, we maintain our target yield at 2.0% to keep it in line with the water and related utilities peers. We have rolled forward the dividend which increases our yield valuation to USD53.70 from USD50.10.
- For our approach using the average of PE multiple and rate-based valuations, we update our target multiple to 33.0x from 31.0x to keep it in line with that of peers. We use a water peer group PB of 2.6x as a proxy for a rate-based valuation. This is consistent with all US utilities under our coverage and is a proxy for EV. The average of the two increases to USD61.80 (from USD52.10), reflecting our updated estimates. We continue to use regulated water peers, not gas utility peers, because water utilities have higher implicit growth. Peoples was acquired because it, too, has an accelerated mains replacement cycle.

Overall, these changes lead to an increased target price of USD55 (previously USD50), which implies c23% upside from current levels. We reiterate our Buy rating as we believe the combination of regulated investment growth and earnings growth remains attractive.

Summary of valuation (USD)

Particulars	New	Previous
Current price at close of 12-Nov-2020	**44.8**	**NA**
DCF (updated estimates, rolled forward valuation)	50.8	48.1
Yield 2% (yield unchanged, dividend rolled forward)	53.7	50.1
SOP & Peer multiple (updated estimates and multiples)	61.8	52.1
Target price (average rounded)	**55.0**	**50.0**
Upside/ downside to target price	22.8%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity valuation	USDm
Cost of debt		**+ DCF value**	**16,555**
Pre-tax cost of debt	3.9%	+ ST marketable assets	0
Marginal tax rate	8.0%	+ Value of associates	0
Cost of equity		+ Other assets	878
Risk-free rate	2.5%	**EV (asset side)**	**17,433**
Equity risk premium	3.0%	- Net debt (+ if Net cash)	(4,623)
Additional risk		- Quasi debt (pension)	0
Beta (unchanged)	**0.60**	- Value of minorities	0
Debt - 32%	3.6%	Total non-equity claims	(4,623)
Equity - 68%	4.3%	Value of equity	12,811
Cost of capital	**4.0%**	**Value per share (USD)**	**50.8**

Source: HSBC estimates

Sum-of-the-parts (SOP) and multiples valuation

	2021e Rate base
Regulated water	
Pennsylvania	3,954
Ohio	393
Illinois	409
Texas	342
New Jersey	229
North Carolina	263
Indiana	96
Virginia	89
Regulated gas	2,634
Total	**8,409**
Price to rate base	21,864
Non-regulated 2020 PE multiple	9
Net debt 2020e, pensions & Minority	(4,623)
Estimated equity value	17,251
Estimated equity value per share (USD)	**68.5**
PE Multiple valuation	
2020 earnings	1.67
2020 PE sector average	33.0
Value per share	**55.1**
Average of rate base valuation and PE multiple valuation	**61.8**

Source: HSBC estimates

Downside risks: Essential Utilities failing to achieve the desired rate case revisions and infrastructure surcharges; lacking organic growth from asset replacement; inability to take advantage of the Fair Market Value legislation opportunity; dividend growth at a lower rate than we assume; inability to gain the Fair Market Value premium required in the systems it wants to acquire in Pennsylvania. Its current acquisitions of systems – New Garden and Limerick – are facing challenges to the premium proposed by Aqua.

Disclosure appendix

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The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

Prior to this date, HSBC's rating structure was applied on the following basis:

For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

As of 16 November 2020, the distribution of all independent ratings published by HSBC is as follows:

Buy	57%	(33% of these provided with Investment Banking Services)
Hold	34%	(30% of these provided with Investment Banking Services)
Sell	9%	(27% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

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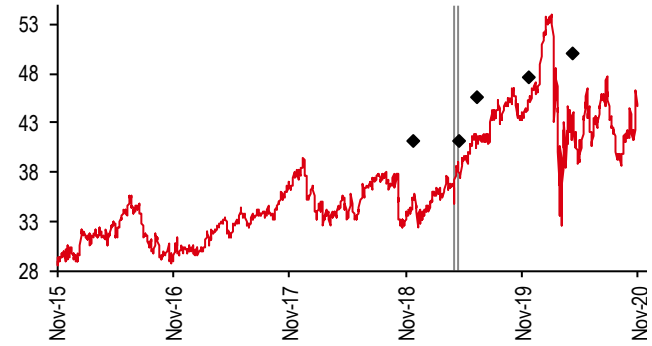
Share price and rating changes for long-term investment opportunities

Essential Utilities (WTRG.N) share price performance
USD Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	41.00	06 Dec 2018	Verity Mitchell
Price 2	Restricted	15 Apr 2019	
Price 3	41.00	30 Apr 2019	Verity Mitchell
Price 4	45.50	28 Jun 2019	Verity Mitchell
Price 5	47.50	06 Dec 2019	Verity Mitchell
Price 6	50.00	22 Apr 2020	Verity Mitchell

Source: HSBC

To view a list of all the independent fundamental ratings disseminated by HSBC during the preceding 12-month period, please use the following links to access the disclosure page:

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Disclosure checklist

Company	Ticker	Recent price	Price date	Disclosure
ESSENTIAL UTILITIES	WTRG.N	44.71	13 Nov 2020	5, 6

Source: HSBC

1 HSBC has managed or co-managed a public offering of securities for this company within the past 12 months.

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3 At the time of publication of this report, HSBC Securities (USA) Inc. is a Market Maker in securities issued by this company.

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5 As of 30 September 2020, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of investment banking services.

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9 A covering analyst/s or a member of his/her household has a financial interest in the securities of this company, as detailed below.

10 A covering analyst/s or a member of his/her household is an officer, director or supervisory board member of this company, as detailed below.

11 At the time of publication of this report, HSBC is a non-US Market Maker in securities issued by this company and/or in securities in respect of this company

12 As of 10 Nov 2020, HSBC beneficially held a net long position of more than 0.5% of this company's total issued share capital, calculated according to the SSR methodology

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[1159925]

HSBC Global Research

6 December 2019

Aqua America (WTR US)

Buy: Expansion in progress

Equities
Water Utilities

United States

- 9M2019 net income up 13%; Peoples transaction to be completed in early 2020, Delcora next
- Further expansion in PA through acquisition of DELCORA
- Maintain Buy rating; increase TP from USD45.5 to USD47.5

Still growing: Aqua America (WTR) posted growth of 7.7% and 13.1% in revenue and net income respectively at its 9m results on 5 November. To date in 2019, the company's state subsidiaries in Illinois, New Jersey, North Carolina, Ohio, and Pennsylvania have received rate awards or infrastructure surcharges totalling an estimated increase to annualized revenues of USD59.8m. WTR currently has two rate case proceedings pending in Indiana totalling USD63,000. A dividend of USD0.2343 was announced and its 2019 outlook for EPS is reaffirmed of USD1.45-USD1.50.

DELCORA acquisition: a larger, deeper footprint in Pennsylvania: The September agreement with the Delaware County Regional Water Quality Control Authority (DELCORA), to acquire the municipal authority's wastewater assets for cUSD276.5m, will intensify its activities in the state. The transaction is subject to Pennsylvania Public Utility Commission (PUC) approval.

Peoples transaction to be completed in early 2020: All but two of the interveners to the case have entered into or chosen not to oppose the settlement agreement. On October 28 2019, the administrative law judge rendered a recommended decision concluding that Aqua is technically, legally and financially fit to assume control of Peoples; that the acquisition of Peoples will affirmatively promote the service, accommodation, convenience or safety of the public in some substantial way; and recommended that the Pennsylvania Public Utility Commission issue all approvals necessary for Aqua to carry out the acquisition of Peoples.

Maintain Buy rating with increased target price from USD45.5 to USD47.5: We value Aqua America via three methodologies: DCF, dividend yield and the average of PE multiples and SOP (rate-based) valuation. Taking the average of the three approaches gives us our target price of USD47.5 (previously USD45.5). We have rolled forward our estimates in all valuations detailed below. In our DCF valuation, we maintained our assumption of beta at 0.58 to be in line with its market peers and have rolled forward our valuation to FY2020e. In our multiples based valuation, we have updated the multiples in line with the market peers. This results in an increase in PE multiple from 27.8x to 29.8x. Finally, in our yield valuation, we maintain our yield at 2% which is in line with its peers. Overall, these changes lead to an increased TP of USD47.5 from USD45.5. Our TP implies 5.2% upside; we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

MAINTAIN BUY

TARGET PRICE (USD)	PREVIOUS TARGET (USD)
47.50	**45.50**
SHARE PRICE (USD)	UPSIDE/DOWNSIDE
45.14	**+5.2%**
(as of 05 Dec 2019)	

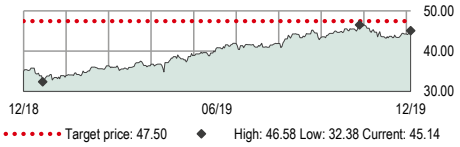
MARKET DATA

Market cap (USDm)	9,743	Free float	100%
Market cap (USDm)	9,743	BBG	WTR US
3m ADTV (USDm)	73	RIC	WTR.N

FINANCIALS AND RATIOS (USD)

Year to	12/2018a	12/2019e	12/2020e	12/2021e
HSBC EPS	1.08	1.50	1.59	1.65
HSBC EPS (prev)	1.08	1.50	1.59	1.65
Change (%)	0.0	0.0	0.0	0.0
Consensus EPS	1.41	1.48	1.58	1.66
PE (x)	41.9	30.1	28.3	27.4
Dividend yield (%)	1.9	2.0	2.2	2.4
EV/EBITDA (x)	26.2	24.0	18.1	17.5
ROE (%)	9.7	12.9	11.6	8.5

52-WEEK PRICE (USD)



Source: Refinitiv IBES, HSBC estimates

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Financials & valuation: Aqua America

Buy

Financial statements

Year to	12/2018a	12/2019e	12/2020e	12/2021e
Profit & loss summary (USDm)				
Revenue	838	905	1,906	2,003
EBITDA	470	525	815	864
Depreciation & amortisation	-147	-160	-237	-260
Operating profit/EBIT	323	365	578	604
Net interest	-147	-84	-158	-170
PBT	178	281	420	434
HSBC PBT	176	281	420	434
Taxation	14	-14	-21	-22
Net profit	192	267	399	412
HSBC net profit	192	267	399	412
Cash flow summary (USDm)				
Cash flow from operations	369	340	675	676
Capex	-496	-500	-770	-770
Cash flow from investment	-640	-500	-5,045	-770
Dividends	-151	-162	-247	-267
Change in net debt	439	322	2,118	361
FCF equity	-127	-160	-95	-94
Balance sheet summary (USDm)				
Intangible fixed assets	53	53	928	928
Tangible fixed assets	6,718	7,058	10,991	11,501
Current assets	144	105	191	199
Cash & others	4	4	4	4
Total assets	6,961	7,262	12,156	12,674
Operating liabilities	1,546	1,420	1,545	1,558
Gross debt	2,564	2,886	5,003	5,364
Net debt	2,560	2,882	5,000	5,361
Shareholders' funds	2,009	2,114	4,765	4,910
Invested capital	5,365	5,792	10,561	11,067

Ratio, growth and per share analysis

Year to	12/2018a	12/2019e	12/2020e	12/2021e
Y-o-y % change				
Revenue	3.5	8.0	110.6	5.1
EBITDA	1.0	11.7	55.2	6.0
Operating profit	-1.8	12.9	58.4	4.5
PBT	-30.5	57.5	49.5	3.3
HSBC EPS	-20.0	39.4	6.3	3.3
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	6.8	6.2	6.7	5.3
ROE	9.7	12.9	11.6	8.5
ROA	4.5	5.1	5.8	4.7
EBITDA margin	56.1	58.0	42.8	43.1
Operating profit margin	38.6	40.3	30.3	30.1
EBITDA/net interest (x)	3.2	6.2	5.2	5.1
Net debt/equity	127.4	136.4	104.9	109.2
Net debt/EBITDA (x)	5.4	5.5	6.1	6.2
CF from operations/net debt	14.4	11.8	13.5	12.6
Per share data (USD)				
EPS Rep (diluted)	1.08	1.50	1.59	1.65
HSBC EPS (diluted)	1.08	1.50	1.59	1.65
DPS	0.85	0.91	0.99	1.07
Book value	11.29	11.88	19.04	19.62

Valuation data

Year to	12/2018a	12/2019e	12/2020e	12/2021e
EV/sales	14.7	13.9	7.7	7.5
EV/EBITDA	26.2	24.0	18.1	17.5
EV/IC	2.3	2.2	1.4	1.4
PE*	41.9	30.1	28.3	27.4
PB	4.0	3.8	2.4	2.3
FCF yield (%)	-1.3	-1.6	-1.0	-1.0
Dividend yield (%)	1.9	2.0	2.2	2.4

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2018a
GHG emission intensity*	n/a
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social Indicators	**12/2018a**
Employee costs as % of revenues	n/a
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	12/2018a
No. of board members	9
Average board tenure (years)	8.2
Female board members (%)	33.3
Board members independence (%)	88.9

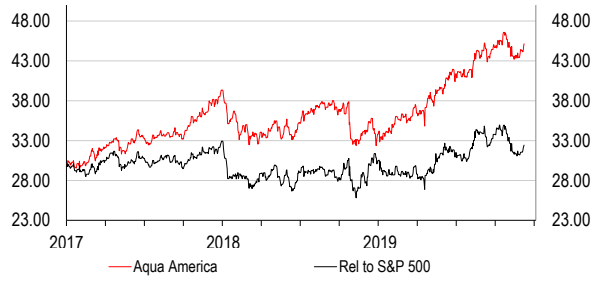
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	45.14	Free float	100%
Target price (USD)	47.50	Sector	Water Utilities
RIC (Equity)	WTR.N	Country/Region	United States
Bloomberg (Equity)	WTR US	Analyst	Verity Mitchell
Market cap (USDm)	9,743	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 05 Dec 2019

Expansion in progress

- Peoples transaction to be completed in early 2020
- Further expansion in PA through acquisition of DELCORA
- Maintain Buy rating; increase TP from USD45.5 to USD47.5

9M 2019 results summary

Aqua America (WTR) posted its 9M 2019 results on 5th November 2019. WTR posted growth of 7.7% and 13.1% in revenue and net income respectively. Employee-related costs, Peoples transaction-related expenses and growth-related costs were the main contributors to the increase in O&M expenses.

Aqua invested USD401.6m in the first nine months of the year to improve its infrastructure systems.

To date in 2019, the company's state subsidiaries in Illinois, New Jersey, North Carolina, Ohio, and Pennsylvania have received rate awards or infrastructure surcharges totalling an estimated increase to annualised revenues of USD59.8m. WTR currently has two rate case proceedings pending in Indiana totalling revenues of USD63,000. A dividend of USD0.2343 announced.

2019 outlook reaffirmed

- Adjusted income per diluted common share (non-GAAP) of USD1.45 to USD1.50
- Infrastructure investments of approximately USD550 million in 2019 for communities served by Aqua
- Infrastructure investments of approximately USD1.4 billion through to 2021 in existing operations to rehabilitate and strengthen systems
- Rate base compound annual growth rate of 7 percent through 2021
- Total customer growth of between 2 and 3 percent
- Closing of Peoples acquisition expected to occur in early 2020

DELCORA acquisition: a larger, deeper footprint in Pennsylvania

Aqua America announced in September that its Pennsylvania subsidiary, Aqua Pennsylvania Wastewater (Aqua), had signed an asset purchase agreement with the Delaware County Regional Water Quality Control Authority (DELCORA) to acquire the municipal authority's wastewater assets for cUSD276.5m. The transaction is subject to Pennsylvania Public Utility Commission (PUC) approval.

DELCORA serves a population of approximately 500,000 people in 42 municipalities in Southeast Pennsylvania. Aqua estimates that this represents the equivalent of 165,000 retail customers. The customer base consists of retail, commercial, and industrial customers and large wholesale agreements with municipal authorities. Its assets include 168 miles of combined and separate sewer mains, 14 miles of large-diameter force mains, and a 50-million gallon-per-

day wastewater treatment plant that serves the western part of its service territory. Wastewater from the eastern service territory (ESA) is treated by Philadelphia Water Department (PWD). This contract expires in 2028.

Under current arrangement with the PWD, Delcora could incur more than USD1.2bn in total costs through 2042, significantly increasing customer rates. Delcora is also building infrastructure necessary to divert ESA wastewater flows in its own plant. The majority of capex will be undertaken from 2026-28. WTR has experience with large/complex projects and already operates in many Delcora communities.

DELCORA is going to use the proceeds from WTR and put those into a trust, which will be used to offset customer rates for as long as possible given the upward pressure on rates from the investment above.

Pennsylvania PUC approval is required to complete this acquisition. Closing is expected to be in late 2020. This acquisition will be the largest municipal transaction for Aqua America and the largest water/wastewater municipal transaction in Pennsylvania's history.

Peoples transaction timeline

In March 2019, Aqua received regulatory approval for the Peoples transaction from the Kentucky Public Service Commission, and in April 2019, the company received approval from the West Virginia Public Service Commission. On June 26, 2019, the company filed a settlement agreement in the matter pending before the Pennsylvania Public Utility Commission.

On October 28, 2019, the administrative law judge rendered a recommended decision concluding that Aqua is technically, legally and financially fit to assume control of Peoples; that the acquisition of Peoples will affirmatively promote the service, accommodation, convenience or safety of the public in some substantial way; and recommended that the Pennsylvania Public Utility Commission issue all approvals necessary for Aqua to carry out the acquisition of Peoples.

The Commission will review the administrative law judge's recommendation and then issue a final order that is subject to appeal if a party so chooses. Aqua now expects the Peoples acquisition to close in early 2020.

Peoples transaction timeline

23-Oct-18	**WTR announces acquisition of Peoples**
13-Nov-18	WTR files merger application with PA and WV PUCs
20-Nov-18	WTR files merger application with KY PSC
28-Jan-19	Peoples filed a rate case for PA
8-Feb-19	WTR filed a rate case for settlement for PA
13-Mar-19	KY PSC approved merger application
27-Mar-19	Proposed merger settlement filed with WV PSC
29-Mar-19	WTR announced USD750m equity investment from CPPIB
Apr-19	WTR equity and debt offerings
Apr-19	WV PSC approved merger application
May-19	WTR PA rate case in effect
Jul-19	Peoples filed a rate case settlement for PA
28-Oct-19	PA ALJs recommended decision received
29-Oct-19	Peoples rate case in effect
Early 2020	Anticipated closing of the Peoples acquisition

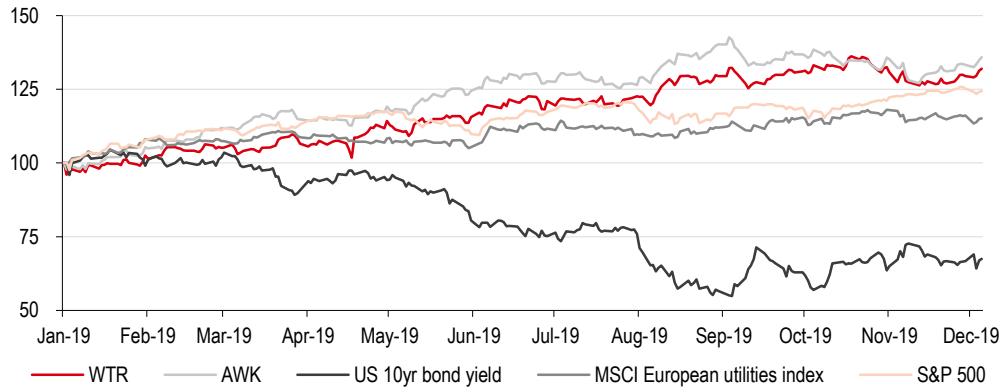
Source: Company presentation

Performance against peers

Aqua's share price has outperformed the S&P 500 by 8% since 1 January 2019. On 2020e PE, it trades at a discount to its water peer group but is in line with some of the US electricity utilities according to Refinitiv Datastream. This reflects, in our view, its future multi-utility status.

One more point to note is that the US Treasury 10-year yield has fallen sharply. WTR, as a defensive utility, should be inversely correlated to bond yields.

YTD performance of WTR vs AWK vs UST 10 yr vs MSCI European utilities index vs S&P 500



Source: Refinitiv Datastream

Valuation and risks

We value Aqua America via three methodologies: DCF, dividend yield and the average of PE multiples and SOP (rate-based) valuation. Taking the average of the three approaches gives us our target price of USD47.5 (previously USD45.5). We have rolled forward our estimates in all valuations detailed below.

In our DCF valuation, we have maintained our assumption of beta at 0.58 to be in line with its market peers and have rolled forward our valuation to FY2020e. In our multiples-based valuation, we have updated the multiples in line with the market peers. This results in an increase in PE multiple from 27.8x to 29.8x. Finally, in our yield valuation, we maintain our yield at 2% which is in line with its peers. Overall, these changes lead to an increased TP of USD47.5 from USD45.5. Our TP implies 5.2% upside; we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

Summary of valuation (USD)

Particulars	New	Previous
Current price as on 5-Dec-19	**45.1**	**NA**
DCF (rolled forward estimates)	47.5	46.0
Yield 2% (unchanged)	49.4	49.4
SOP & Peer multiple (updated peer multiples and rolled forward estimates)	45.8	41.0
Target price (average rounded)	**47.5**	**45.5**
Upside/ downside to target price	5.2%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity Valuation	USDm
Cost of debt		**+ DCF value**	**16,106**
Pre-tax cost of debt	3.9%	+ ST marketable assets	-
Marginal tax rate	11.0%	+ Value of associates	-
Cost of equity		+ Other assets	788
Risk-free rate	3.0%	**EV (asset side)**	**16,894**
Equity risk premium	3.0%	- Net debt (+ if Net cash)	(5,000)
Additional risk		- Quasi debt (pension)	-
Beta (unchanged)	**0.58**	- Value of minorities	0
Debt - 32%	3.5%	Total non-equity claims	(5,000)
Equity - 68%	4.7%	**Value of equity**	**11,894**
Cost of capital	**4.3%**	**Value per share (USD)**	**47.5**

Source: HSBC estimates

Sum-of-the-parts (SOP) and Multiples valuation

	2020e Rate base
Regulated water	
Pennsylvania	3,673
Ohio	363
Illinois	366
Texas	269
New Jersey	196
North Carolina	233
Indiana	95
Virginia	86
Regulated gas	2,733
Total	**8,014**
Price to rate base	16,027
Non-regulated 2020e PE multiple	13
Net debt 2020e, pensions & Minority	(5,000)
Estimated equity value	11,040
Estimated equity value per share (USD)	**44.1**
PE Multiple valuation	
2020e earnings	1.59
2020e PE sector average	29.8
Value per share	**47.5**
Average of rate base valuation and PE multiple valuation	**45.8**

Source: HSBC estimates

Downside risks

Aqua America fails to achieve the desired rate case revisions and infrastructure surcharges; it lacks organic growth from asset replacement; it cannot take advantage of the FV market legislation opportunity; its dividend grows at a lower rate than we assume.

It is not able to gain the Fair Market Value premium required in the systems it wants to acquire in Pennsylvania. Its current acquisitions of systems – New Garden and Limerick – are facing challenges to the premium proposed by Aqua.

Disclosure appendix

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The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

Prior to this date, HSBC's rating structure was applied on the following basis:

For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

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As of 05 December 2019, the distribution of all independent ratings published by HSBC is as follows:

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Sell	9%	(25% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

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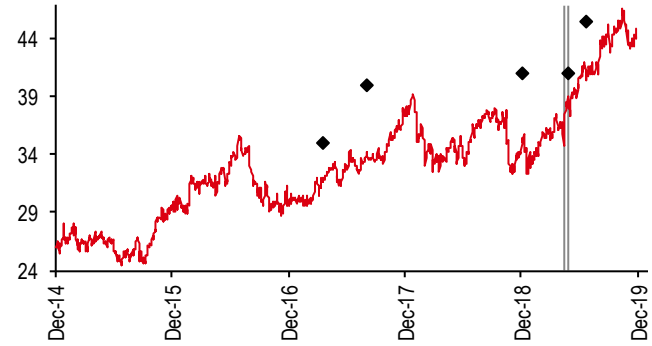
Share price and rating changes for long-term investment opportunities

Aqua America (WTR.N) share price performance USD Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	35.00	24 Mar 2017	Verity Mitchell
Price 2	40.00	08 Aug 2017	Verity Mitchell
Price 3	41.00	06 Dec 2018	Verity Mitchell
Price 4	Restricted	15 Apr 2019	
Price 5	41.00	30 Apr 2019	Verity Mitchell
Price 6	45.50	28 Jun 2019	Verity Mitchell

Source: HSBC

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Disclosure checklist

Company	Ticker	Recent price	Price date	Disclosure
AQUA AMERICA	WTR.N	44.90	04 Dec 2019	1, 5, 6

Source: HSBC

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[1134671]

HSBC Global Research

22 April 2020

Essential Utilities (WTRG US)

Buy: Acquisitions in the bag for growth

Equities
Water Utilities

United States

- Water and wastewater infrastructure business relatively unaffected by COVID-19
- Peoples deal completed; DELCORA on track for 2022; regulatory mechanisms to ease rate case lag; proforma 2020
- Maintain Buy rating; TP increased from USD47.5 to USD50.0

COVID-19 update: The American Water Works Association (AWWA) published the results of an online survey on the impact of the COVID-19 emergency on its member organisations on 10 April. According to the survey, utilities are reacting swiftly to the crisis to guarantee essential services and business continuity, but two thirds expect revenue/cash flow problems within the next two months. The two factors causing financial uncertainty are changes in water demand from non-domestic customers and customer payments during the coronavirus pandemic. However capital investment in asset rehabilitation remains relatively unaffected.

Essential Utilities (EU) has already made two significant acquisitions: The focus for 2020-2022 will be on integrating these and successfully delivering rate cases. Infrastructure surcharges and test years for rate cases help to reduce the regulatory lag. 52% of EU's capex is eligible for these. This provides clarity on the cash flows and reduces uncertainties around translation of rate base growth into earnings. With the completion of the Peoples deal and the gas heating season in Q1 lowering the seasonal contribution to earnings for Q2 and Q3, the company will be reporting earnings for 2020 on a pro-forma basis to improve transparency.

Maintain Buy rating with increased target price, from USD47.5 to USD50.0: We value Essential Utilities via three methodologies: DCF, dividend yield, and the average of PE multiple and SOP (rate-based) valuations. Taking the average of the three approaches gives us our target price of USD50.0 (previously USD47.5). In our DCF valuation, we have updated our beta assumption from 0.58 to 0.60 to be in line with market peers and have updated the model for FY2019 results. Our cost of capital is updated from 4.3% to 5.9%. These changes leads to a fall in the DCF valuation from USD47.5 to USD41.1. In our PE multiple-based valuation, we have updated the multiple in line with market peers, from 29.8x to 30.0x. This leads to an increase in the PE-multiple valuation, from USD45.8 to USD46.8. Our SOP valuation rises from USD44.1 to USD57.1, driven by the updated rate base, and the average of the two rises from USD45.8 to USD52. In our yield valuation, we update our yield from 2% to 1.75%, again in line with peers. This results in an increase in the Yield valuation from USD49.4 to USD57.8. Overall, these changes lead to an increase in our TP from USD47.5 to USD50.0. Our TP implies 15.3% upside and we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

MAINTAIN BUY

TARGET PRICE (USD)	PREVIOUS TARGET (USD)
50.00	**47.50**
SHARE PRICE (USD)	UPSIDE/DOWNSIDE
43.36	**+15.3%**
(as of 17 Apr 2020)	

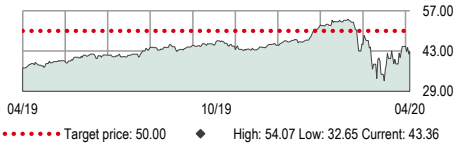
MARKET DATA

Market cap (USDm)	9,683	Free float	100%
Market cap (USDm)	9,683	BBG	WTRG US
3m ADTV (USDm)	67	RIC	WTRG.N

FINANCIALS AND RATIOS (USD)

Year to	12/2019a	12/2020e	12/2021e	12/2022e
HSBC EPS	1.04	1.56	1.68	1.81
HSBC EPS (prev)	1.50	1.59	1.65	na
Change (%)	-30.7	-2.0	1.7	na
Consensus EPS	1.48	1.56	1.64	1.77
PE (x)	41.7	27.8	25.9	23.9
Dividend yield (%)	2.2	2.3	2.5	2.7
EV/EBITDA (x)	21.9	17.0	16.2	15.4
ROE (%)	7.6	8.3	7.4	7.8

52-WEEK PRICE (USD)



Source: Refinitiv IBES, HSBC estimates

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This report must be read with the disclosures and the analyst certifications in the Disclosure appendix, and with the Disclaimer, which forms part of it.

Issuer of report: HSBC Bank plc

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Financials & valuation: Essential Utilities

Buy

Financial statements

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Profit & loss summary (USDm)				
Revenue	890	1,895	2,097	2,230
EBITDA	497	824	897	973
Depreciation & amortisation	-157	-239	-267	-284
Operating profit/EBIT	340	585	631	689
Net interest	-131	-153	-167	-188
PBT	212	432	463	501
HSBC PBT	209	432	463	501
Taxation	13	-35	-37	-40
Net profit	225	397	426	461
HSBC net profit	225	397	426	461
Cash flow summary (USDm)				
Cash flow from operations	339	706	707	754
Capex	-550	-950	-950	-950
Cash flow from investment	-605	-5,225	-950	-950
Dividends	-189	-257	-278	-300
Change in net debt	-1,352	3,108	521	496
FCF equity	-212	-244	-243	-196
Balance sheet summary (USDm)				
Intangible fixed assets	64	939	939	939
Tangible fixed assets	7,224	11,335	12,018	12,684
Current assets	2,011	2,154	2,182	2,201
Cash & others	1,869	1,869	1,869	1,869
Total assets	9,360	14,489	15,201	15,886
Operating liabilities	1,468	1,680	1,723	1,751
Gross debt	3,077	6,186	6,707	7,203
Net debt	1,208	4,317	4,838	5,334
Shareholders' funds	3,881	5,689	5,837	5,998
Invested capital	5,962	10,879	11,548	12,204

Ratio, growth and per share analysis

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Y-o-y % change				
Revenue	6.2	113.0	10.7	6.3
EBITDA	5.7	65.8	8.9	8.4
Operating profit	5.3	72.0	7.8	9.2
PBT	18.6	104.2	7.3	8.1
HSBC EPS	-3.4	50.2	7.3	8.1
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	6.4	6.4	5.2	5.3
ROE	7.6	8.3	7.4	7.8
ROA	4.1	4.5	3.9	4.1
EBITDA margin	55.9	43.5	42.8	43.6
Operating profit margin	38.2	30.9	30.1	30.9
EBITDA/net interest (x)	3.8	5.4	5.4	5.2
Net debt/equity	31.1	75.9	82.9	88.9
Net debt/EBITDA (x)	2.4	5.2	5.4	5.5
CF from operations/net debt	28.0	16.4	14.6	14.1
Per share data (USD)				
EPS Rep (diluted)	1.04	1.56	1.68	1.81
HSBC EPS (diluted)	1.04	1.56	1.68	1.81
DPS	0.94	1.01	1.09	1.18
Book value	17.97	22.36	22.94	23.58

Valuation data

Year to	12/2019a	12/2020e	12/2021e	12/2022e
EV/sales	12.2	7.4	6.9	6.7
EV/EBITDA	21.9	17.0	16.2	15.4
EV/IC	1.8	1.3	1.3	1.2
PE*	41.7	27.8	25.9	23.9
PB	2.4	1.9	1.9	1.8
FCF yield (%)	-2.2	-2.5	-2.5	-2.0
Dividend yield (%)	2.2	2.3	2.5	2.7

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2019a
GHG emission intensity*	n/a
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social Indicators	**12/2019a**
Employee costs as % of revenues	n/a
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	12/2019a
No. of board members	8
Average board tenure (years)	7.0
Female board members (%)	25
Board members independence (%)	87.5

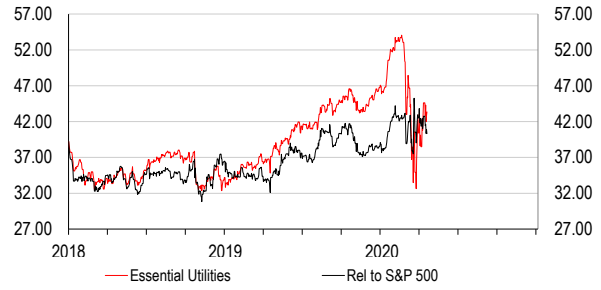
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	43.36	Free float	100%
Target price (USD)	50.00	Sector	Water Utilities
RIC (Equity)	WTRG.N	Country/Region	United States
Bloomberg (Equity)	WTRG US	Analyst	Verity Mitchell
Market cap (USDm)	9,683	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 17 Apr 2020

Acquisitions in the bag for growth

- Water and wastewater infrastructure business relatively unaffected by COVID-19
- Peoples deal completed; DELCORA on track for 2022; regulatory mechanisms to ease rate case lag; proforma 2020 results
- Maintain Buy rating; TP increased from USD47.5 to USD50.0

Uncertainties and risks due to COVID-19 pandemic

The American Water Works Association (AWWA) published the results of an online survey on the impact of the COVID-19 emergency on its member organisations on 10 April. According to the survey, utilities are reacting swiftly to the crisis to guarantee essential services and business continuity, but two thirds expect revenue/cash flow problems within the next two months. The two factors causing financial uncertainty are changes in water demand from non-domestic customers and customer payments during the coronavirus pandemic.

The two major challenges that investor-owned utilities identified were ensuring social distancing of the work force and supply chain issues for PPE. In terms of regulatory compliance, an issue that was noted was problems in accessing sampling sites. Most utilities have implemented measures to help customers: more than 90% have suspended water shut-offs, and nearly 50% have restored service to suspended accounts.

Three-pronged investment proposition

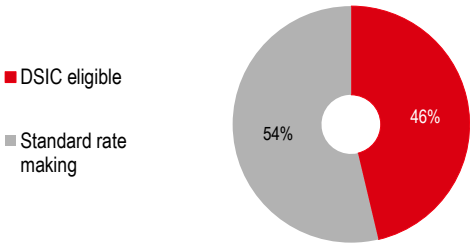
Essential Utilities has core competencies in infrastructure investment (pipes, plants, etc), regulatory affairs and operational excellence. Using these as pillars, Essential has created a 3-pronged growth strategy.

1. Municipal initiative: Driver of growing foundational water and wastewater business. This is the primary focus for the company right now.
2. Strategic M&A: Opportunistic pursuit of large, regulated utility/infrastructure targets – the company delivered on this by the Peoples gas acquisition recently completed and the DELCORA transaction which is expected to complete regulatory approvals by 2022.
3. MBAs (Market Based Activities): Complementary to regulated business. Capitalises on broader infrastructure renewals but is probably going to be less of a priority given the current challenges.

Attractive capex recovery mechanisms

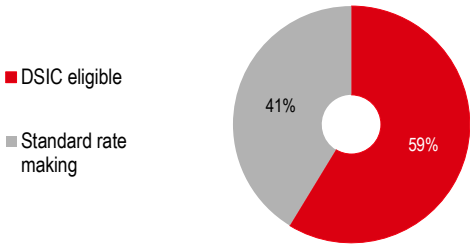
Infrastructure surcharges and test years for rate cases help to reduce regulatory lag. 52% of EU's capex is eligible for these. This provides clarity on the cash flows and reduces uncertainties around translation of the rate base growth into earnings.

Water capex: 2020-22 estimates



Source: WTRG company results presentations - FY2019

Gas capex: 2020-22 estimates



Source: WTRG company results presentations - FY2019

From the table below we can see that most of the states that Essential Utilities operates in have opted for these mechanisms, which is a positive development for the company.

State wise regulations for capex recovery

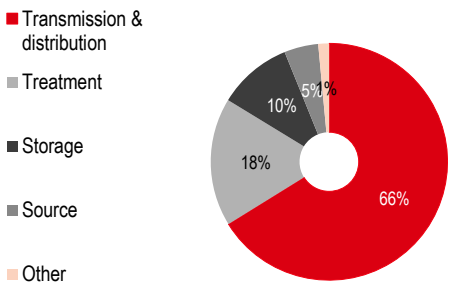
State	Allowed surcharge
Water	
Pennsylvania	7.5% W; 5%WW
Indiana	10%
Ohio	12.75% W; 9% WW
New Jersey	5%
Illinois	2.5% annual avg increase
North Carolina	5%
Gas	
Pennsylvania	5%
Kentucky	No cap

Source: WTRG company results presentations - FY2019

US water infrastructure needs offer opportunities for Aqua

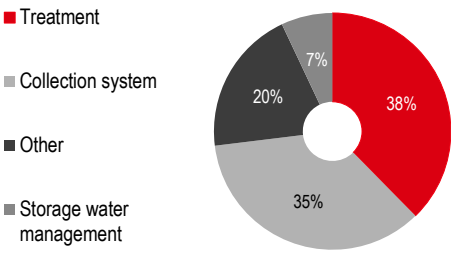
In the charts below we can see the EPA estimates of the US water infrastructure investment needs.

Water - USD473bn



Source: WTRG company results presentations - FY2019

Wastewater - USD271bn



Source: WTRG company results presentations - FY2019

Acquisitions – strong pipeline and primary focus for the company

From the table below we can see that, even with the major deal of DELCORA it has signed, Essential has a decent pipeline of acquisitions. However, due to current COVID-19 pandemic, the closure of some of these may well be delayed into 2021.

Acquisitions - closed and pending at FY2019 results

	State	Type	Total customers	Rate base (USD '000s)
Closed				
Skyline	Illinois	W / WW	752	3550
Phoenixville	Pennsylvania	W	529	2500
Grant Park	Illinois	WW	540	2300
Cheltenham	Pennsylvania	WW	9887	44558
Campbell	Ohio	W	3200	7535
Total			**14908**	**60443**
Pending				
New Garden	Pennsylvania	WW	2106	29500
East Norriton	Pennsylvania	WW	4952	21000
DELCORA	Pennsylvania	WW	198000	276500
Total			**205058**	**327000**

Source: WTRG company results presentations - FY2019

Guidance for 2020

The guidance for 2020 is as follows:

- Adjusted proforma income per diluted common share (non-GAAP) of USD1.53 to USD1.58. This illustrative guidance includes the full-year effects of the Peoples acquisition as if this transaction closed on January 1, 2020, by including an estimate of the results of Peoples for the period in 2020 prior to closing, excluding transaction-related expenses and the effects of transaction-related commitments to issue rate credits to utility customers.
- 3-year earnings CAGR 5-7% for 2019 through 2022, with the base being 2019 adjusted income per share (non-GAAP).

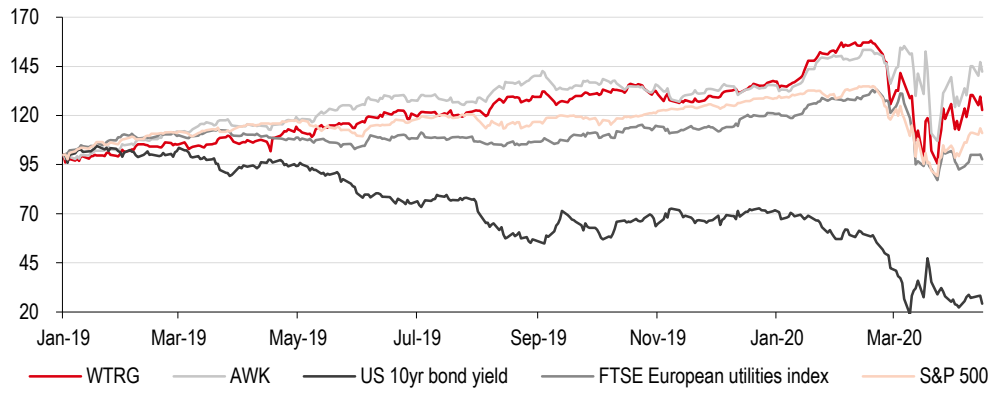
- Infrastructure investment of approximately USD550m in 2020 for communities served by the water operations.
- Infrastructure investment of approximately USD400m in 2020 for communities served by the gas operations.
- Infrastructure investment of approximately USD2.8bn through 2022 in existing water and gas operations to rehabilitate and strengthen systems.
- Rate base compound annual growth rate of 6 to 7% through 2022 in water; and 8 to 10% in gas through to 2022.
- Total annual water customer growth of between 2 and 3% on average, depending upon regulatory approval.

Performance against peers

Essential's share price has outperformed the S&P 500 by 12% since 1 January 2019. On 2020e PE, it is trading at a discount to its water peer group but in line with some of the US electricity utilities according to Refinitiv Datastream. This reflects, in our view, its future multi-utility status.

One more point to note is that the US Treasury 10-year yield has fallen sharply. WTRG, as a defensive utility, should be inversely correlated to bond yields.

Performance of WTRG vs AWK vs UST 10yr vs FTSE European utilities index vs S&P 500



Source: Refinitiv Datastream

Changes in estimates

We have updated our model for FY2019 results and the preliminary impact of COVID-19. We have also updated the model for Peoples proforma numbers for 2020 and included the DELCORA deal in our numbers from 2022. We have also updated the number of shares for 2020 to 254.4m from 215.9m in 2019 according to company guidance associated with the Peoples-related equity offering in 2019.

Change in estimates (USDm)

	2020e	2021e	2022e
EBIT			
Revised	585	631	689
Previous	578	604	
Change	*1%*	*4%*	
Net income			
Revised	397	426	461
Previous	399	412	
Change	*0%*	*3%*	
EPS (USD)			
Revised	1.56	1.68	1.81
Previous	1.59	1.65	
Change	*-2%*	*2%*	
DPS (USD)			
Revised	1.01	1.09	1.18
Previous	0.99	1.07	
Change	*2%*	*2%*	

Source: HSBC estimates

Valuation and risks

We value Essential Utilities via three methodologies: DCF, dividend yield, and the average of PE multiple and SOP (rate-based) valuations. Taking the average of the three approaches gives us our target price of USD50.0 (previously USD47.5). We have updated the model for FY2019 results.

- In our DCF valuation, we have updated our beta assumption from 0.58 to 0.60 to be in line with market peers. We have also updated the cost of debt from 3.9% to 8.5% and the marginal tax rate from 11% to 13%. These changes lead to updated cost of capital, from 4.3% to 5.9% and a fall in the DCF valuation from USD47.5 to USD41.1.
- In our PE multiple-based valuation, we have updated the multiple in line with market peers, from 29.8x to 30.0x. Our SOP valuation rises from USD44.1 to USD57.1, driven by updated rate base, and the average of the two rises from USD45.8 to USD52.
- In our Yield valuation, we update our yield from 2% to 1.75%, again in line with peers. This results in an increase in the Yield valuation from USD49.4 to USD57.8.

Overall, these changes lead to an increased TP from USD47.5 to USD50.0. Our TP implies 16.7% upside; we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

Summary of valuation (USD)

Particulars	New	Previous
Current price as on 17-Apr-20	**43.4**	**NA**
DCF (updated estimates, higher cost of capital)	41.1	47.5
Yield 1.75% (previously 2%)	57.8	49.4
SOP & Peer multiple (updated estimates and multiples)	51.9	45.8
Target price (average rounded)	**50.0**	**47.5**
Upside/ downside to target price	15.3%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity Valuation	USDm
Cost of debt		**+ DCF value**	**13,873**
Pre-tax cost of debt	8.5%	+ ST marketable assets	0
Marginal tax rate	13.0%	+ Value of associates	0
Cost of equity		+ Other assets	878
Risk-free rate	3.0%	**EV (asset side)**	**14,751**
Equity risk premium	3.0%	- Net debt (+ if Net cash)	(4,288)
Additional risk		- Quasi debt (pension)	0
Beta (previously 0.58)	**0.60**	- Value of minorities	0
Debt - 37%	7.8%	Total non-equity claims	(4,288)
Equity - 63%	4.8%	Value of equity	10,463
Cost of capital	**5.9%**	**Value per share (USD)**	**41.1**

Source: HSBC estimates

Sum-of-the-parts (SOP) and PE multiple valuations

USDm	2020e Rate Base
Regulated water	
Pennsylvania	3,682
Ohio	368
Illinois	382
Texas	319
New Jersey	214
North Carolina	245
Indiana	90
Virginia	83
Regulated gas	2,451
Total	**7,834**
Price to rate base (industry multiple)	18,802
Non-regulated (2020e peer average PE multiple)	9
Net debt 2020e, pensions & minority	(4,288)
Estimated equity value	**14,523**
Estimated equity value per share (USD)	**57.1**
PE multiple valuation	
2020e earnings per share (USD)	1.56
2020e PE sector average	30.0
Value per share	**46.8**
Average of rate base valuation and PE multiple valuation	**52.0**

Source: HSBC estimates

Downside risks

Essential Utilities fails to achieve the desired rate case revisions and infrastructure surcharges; it lacks organic growth from asset replacement; it cannot take advantage of the Fair Market Value legislation opportunity; its dividend grows at a lower rate than we assume.

It is not able to gain the Fair Market Value premium required in the systems it wants to acquire in Pennsylvania. Its current acquisitions of systems – New Garden and Limerick – are facing challenges to the premium proposed by Aqua.

Disclosure appendix

Analyst Certification

The following analyst(s), economist(s), or strategist(s) who is(are) primarily responsible for this report, including any analyst(s) whose name(s) appear(s) as author of an individual section or sections of the report and any analyst(s) named as the covering analyst(s) of a subsidiary company in a sum-of-the-parts valuation certifies(y) that the opinion(s) on the subject security(ies) or issuer(s), any views or forecasts expressed in the section(s) of which such individual(s) is(are) named as author(s), and any other views or forecasts expressed herein, including any views expressed on the back page of the research report, accurately reflect their personal view(s) and that no part of their compensation was, is or will be directly or indirectly related to the specific recommendation(s) or views contained in this research report: Verity Mitchell and Adam Dickens

Important disclosures

Equities: Stock ratings and basis for financial analysis

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From 23rd March 2015 HSBC has assigned ratings on the following basis:

The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

Our ratings are re-calibrated against these bands at the time of any 'material change' (initiation or resumption of coverage, change in target price or estimates).

Upside/Downside is the percentage difference between the target price and the share price.

Prior to this date, HSBC's rating structure was applied on the following basis:

For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

Rating distribution for long-term investment opportunities

As of 21 April 2020, the distribution of all independent ratings published by HSBC is as follows:

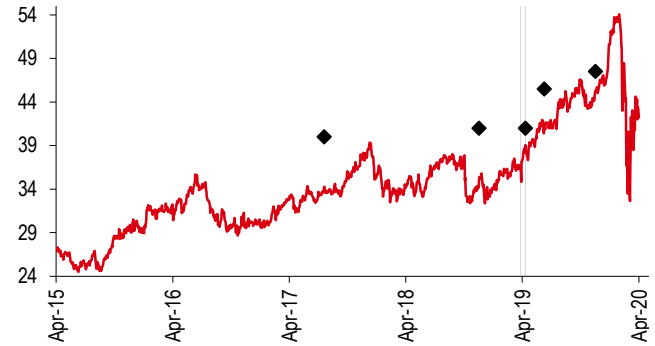
Buy	55%	(31% of these provided with Investment Banking Services)
Hold	36%	(30% of these provided with Investment Banking Services)
Sell	9%	(24% of these provided with Investment Banking Services)

For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

For the distribution of non-independent ratings published by HSBC, please see the disclosure page available at http://www.hsbcnet.com/gbm/financial-regulation/investment-recommendations-disclosures.

Share price and rating changes for long-term investment opportunities

Essential Utilities (WTRG.N) share price performance USD Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	40.00	08 Aug 2017	Verity Mitchell
Price 2	41.00	06 Dec 2018	Verity Mitchell
Price 3	Restricted	15 Apr 2019	
Price 4	41.00	30 Apr 2019	Verity Mitchell
Price 5	45.50	28 Jun 2019	Verity Mitchell
Price 6	47.50	06 Dec 2019	Verity Mitchell

Source: HSBC

To view a list of all the independent fundamental ratings disseminated by HSBC during the preceding 12-month period, please use the following links to access the disclosure page:

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Clients of HSBC Private Banking: www.research.privatebank.hsbc.com/Disclosures

HSBC & Analyst disclosures

Disclosure checklist

Company	Ticker	Recent price	Price date	Disclosure
ESSENTIAL UTILITIES	WTRG.N	42.24	20 Apr 2020	1, 5, 6

Source: HSBC

1 HSBC has managed or co-managed a public offering of securities for this company within the past 12 months.

2 HSBC expects to receive or intends to seek compensation for investment banking services from this company in the next 3 months.

3 At the time of publication of this report, HSBC Securities (USA) Inc. is a Market Maker in securities issued by this company.

4 As of 31 March 2020, HSBC beneficially owned 1% or more of a class of common equity securities of this company.

5 As of 29 February 2020, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of investment banking services.

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7 As of 29 February 2020, this company was a client of HSBC or had during the preceding 12 month period been a client of and/or paid compensation to HSBC in respect of non-securities services.

8 A covering analyst/s has received compensation from this company in the past 12 months.

9 A covering analyst/s or a member of his/her household has a financial interest in the securities of this company, as detailed below.

10 A covering analyst/s or a member of his/her household is an officer, director or supervisory board member of this company, as detailed below.

11 At the time of publication of this report, HSBC is a non-US Market Maker in securities issued by this company and/or in securities in respect of this company

12 As of 15 Apr 2020, HSBC beneficially held a net long position of more than 0.5% of this company's total issued share capital, calculated according to the SSR methodology.

13 As of 15 Apr 2020, HSBC beneficially held a net short position of more than 0.5% of this company's total issued share capital, calculated according to the SSR methodology.

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Additional disclosures

1 This report is dated as at 22 April 2020.

2 All market data included in this report are dated as at close 17 April 2020, unless a different date and/or a specific time of day is indicated in the report.

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Water Utilities

January 12, 2021

Essential Utilities Inc. (WTRG) - BUY

Positive Guidance Call Takeaways; Reiterate BUY Rating, $70 Fair Value

Price:	$48.18
Fair Value Estimate:	$70.00
52-Week Range:	$30.40 - $54.52
Market Cap (MM):	11,817
Shr.O/S-Diluted (mm):	245.3
Average Daily Volume:	1,053,887
Book Value:	$18.90
Dividend:	$1.00
Yield:	2.1%

FYE: Dec	2020E	2021E	2022E
EPS:	$1.58E	$1.67E	$1.78E
Prior EPS:	NC	NC	NC
P/E Ratio:	30.5x	28.9x	27.1x

Quarterly EPS:

Q1	$0.60A	$0.66E	$0.68E
Q2	$0.29A	$0.22E	$0.25E
Q3	$0.23A	$0.26E	$0.27E
Q4	$0.46E	$0.52E	$0.58E

EPS: adjusted

Quarterly Revenue (M):

Q1	$256A	$773E	$794E
Q2	$384A	$342E	$352E
Q3	$349A	$360E	$370E
Q4	$541E	$579E	$601E
Year:	$1,530E	$2,053E	$2,118E

PORTFOLIO MANAGER BRIEF

As the title of our note implies, the key takeaways from WTRG's guidance call for 2021 were all positive. Key areas focused on included earnings (2021 and long-term), capital allocation, emission reduction initiatives, and acquisitions. Given the 2021 EPS guidance range encompassed our pre-existing full year estimate, we've made no changes to our forecasts. We reiterate our BUY rating and $70 Fair Value on WTRG shares.

ANALYST NOTES

- 2021 EPS Guidance Range Encompassed Street Expectations. The expected 2021 EPS guidance range of $1.64 to $1.69 encompassed 7 of 9 published forecasts in FactSet. The company continues to see a 5-7% CAGR on a go forward basis from 2020 through 2023, and it also reiterated its 2020 adjusted EPS guidance range of $1.53 - $1.58. WTRG expects to report 4Q20 and full year 2020 results after market close on 2/24/21.
- Capital Allocation Heavily Tilted to Pennsylvania. For 2021, the capital budget is $1 billion, and of that amount, 55% ($550MM) is slated for water investment, 45% ($450MM) for gas. However, if we break out the CAPEX in terms of state allocation, it looks like approximately $875MM of the investment will occur in Pennsylvania, where WTRG gets its highest returns. One slide that caught our attention was #17, which highlights the breakout of pipe replacement through 2023. The acceleration in gas pipe replacement on a percentage basis is well above that of the water business and again is occurring in Pennsylvania.
- Emission Reductions Will Be Sizable. A fair amount of time was spent on emission reductions (Scope 1 and 2) across all operations. Using 2019 as a baseline, the Company expects a 60% reduction by 2035, and pledged to update stakeholders on the progress towards that goal every 6 months until achieved. Key elements for the gas distribution system include replacing 3,000 miles of leak prone gas distribution pipe, a gathering system repair and replacement program, accelerated leak detection and repair, fugitive gas reinjection during construction, and transitioning to CNG vehicles. For the water and wastewater operations, a commitment to source 100% renewable electricity for the States of Illinois, New Jersey, Ohio, and Pennsylvania by 2022.

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- Acquisition Pipeline Remains Strong. Building on 2020's successful acquisition program (12k new customers, $63MM rate base) in 2021 should be a fairly easy affair, given pending transactions total just shy of 225K customers and $420MM of rate base. The DELCORA transaction remains the "big prize" with its 198K customers and $276MM purchase price. The Company expects to close the DELCORA acquisition in 2Q21. WTRG is actively pursuing municipal opportunities totaling 340K total customers.
- Summary/Valuation. On-the-mark guidance, robust capital investment levels, a strong acquisition pipeline, visible earnings growth, aggressive emission reduction targets.....there was a lot more information in WTRG's "guidance call" than we expected. All the news was good and Essential Utilities continues to be our top pick in the water utility sector. Valuation remains compelling; at a P/E of 27x consensus 2022 forecasts, the shares trade 5 turns below the peer group and carry a sector-high dividend yield of 2.08%. We reiterate our BUY rating and $70 Fair Value, based on a target dividend yield of 1.5% applied to our 2021 estimated dividend of $1.06.

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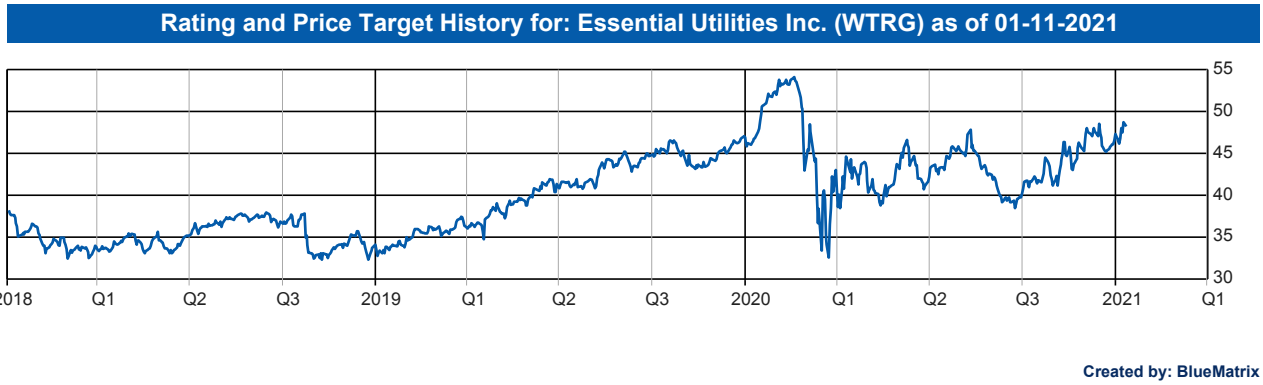

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			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	115	46.18	27	23.48
NEUTRAL [N]	134	53.82	16	11.94
SELL [S]	0	0.00	0	0.00

*Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.

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Water Utilities

May 11, 2020

Essential Utilities Inc. (WTRG) - BUY

Strong 1Q20 Results in a Transformational Quarter; Reiterate BUY Rating, $70 Fair Value

Price:	$40.30
Fair Value Estimate:	$70.00
52-Week Range:	$30.40 - $54.52
Market Cap (MM):	9,874
Shr.O/S-Diluted (mm):	245.0
Average Daily Volume:	1,377,749
Book Value:	$17.58
Dividend:	$0.94
Yield:	2.3%

FYE: Dec	2019A	2020E	2021E
EPS:	$1.47A	$1.58E	$1.66E
Prior EPS:		$1.56	$1.65
P/E Ratio:	27.4x	25.5x	24.3x

Quarterly EPS:

Q1	$0.28A	$0.60A	$0.66E
Q2	$0.37A	$0.23E	$0.23E
Q3	$0.48A	$0.25E	$0.26E
Q4	$0.34A	$0.50E	$0.51E

EPS: adjusted

Quarterly Revenue (M):

Q1	$201A	$256A	$773E
Q2	$219A	$325E	$342E
Q3	$244A	$352E	$360E
Q4	$226A	$571E	$579E
Year:	$890A	$1,504E	$2,053E

PORTFOLIO MANAGER BRIEF

WTRG's 1Q20 adjusted EPS results exceeded expectations, in what was probably the most transformational quarter in the Company's history. Q1 saw the final closing of the Peoples Gas transaction, and then a filing with the IRS for tax repair at Peoples Gas. Also completed was an application with Pennsylvania Public Utility Commission (PAPUC) for the DELCORA acquisition. In addition to that the Company changed its name and stock symbol, and then activated its emergency response plans to deal with COVID-19. From our viewpoint, the investment case for ownership of WTRG shares continues to strengthen; and given the current yield of 2.3% (highest in the water sector peer group), we reiterate our BUY rating and $70 Fair Value on WTRG shares.

ANALYST NOTES

1Q20 Results Above Forecasts. On the top line, revenues increased 27% YOY, driven by the addition of Peoples Gas and new rates/surcharges in the water segment. At the bottom line, WTRG chose to elect tax repair accounting methodology for most of the Peoples Gas operations, which generated a $5.9MM tax benefit in the quarter. All-in adjusted EPS of $0.60 was above our $0.53 estimate and consensus of $0.58.

Pennsylvania is Generating Significant Acquisition Activity. While the Company's been active across its geographic footprint in terms of acquisitions, the State of Pennsylvania has been particularly meaningful when it comes to acquiring assets recently. In Q1 the Peoples Gas transaction was completed, and next up is the Delaware County Regional Water Quality Control Authority (DELCORA) which serves 42 municipalities and 500,000 people. Beyond DELCORA, the Company has two more signed agreements in Pennsylvania (New Garden and East Norriton) which will add another 7,000+ customers.

Other substantial targets that have been discussed publicly as potential asset sales in the State include the cities of Pittsburgh, Harrisburg and the Chester Water Authority. All-in the Company has signed purchase agreements expected to add the equivalent of 205,058 water & wastewater customers, with all but 512 of them in the Keystone State. Essential also noted that Virginia recently passed fair market value legislation, which is now in place in all 8 states where Essential operates. We certainly expect competition for assets where opportunities exist, but WTRG should continue to get its fair share of acquisitions within its service territories.

RESEARCH ANALYST CERTIFICATIONS AND IMPORTANT DISCLOSURES ARE ON PAGES 3 - 4 OF THIS REPORT

COVID-19 Actions Mirror Industry-Wide Best Practices. WTRG's response to COVID-19 is mirroring utility industry best practices, including following Federal and local guidelines in the areas of health & safety. Those employees that can work remotely are doing so, and social distancing work practices are in place. The Company suspended customer shut-offs early after COVID-19 risks were identified, and is not entering customer homes for non-essential work. In terms of the balance sheet, WTRG increased liquidity via a $500MM 364 term loan in March.

Regulatory Update. YTD, the Company has completed rate case or surcharge filings for water operations in Illinois, North Carolina, Ohio and Virginia totaling $5.2MM in additional revenues. In the Natural Gas segment, surcharge filings have been completed in Kentucky and Pennsylvania totaling $977K. New base rates are expected shortly in Indiana, New Jersey, North Carolina and Ohio (total requests = $10.1MM).

Summary/Valuation. Successful completion of the Peoples Gas transaction, election of tax repair accounting methodology, additional expected benefits from catch-up tax repair deductions for past investments, the upcoming closing of the DELCORA transaction, a full pipeline of acquisition opportunities across all operating states, continued rate relief.....the list of expected positive impacts on WTRG's financials is quite extraordinary at this moment in time.

In terms of valuation, recall our view on the sector in general that as long as earnings growth continues under the regulated investment model, P/E's may fluctuate with general market conditions but over time dividend increases will continue to push share prices higher as long as 1) interest rates remain static or move lower and 2) yields on utilities compare favorably with other types of investments. We've noted some of our peers are bringing P/E multiple assumptions for utility shares lower and in some cases doing a "sum-of-the-parts" methodology, whereby each reporting segment gets its own multiple. We abandoned that methodology years ago because we found ourselves perpetually missing equity tops when yield (and dividend increases) became the primary focus for utility investors.

Returning to WTRG shares, we note the Company's primary service territory of Pennsylvania remains the most constructive in the U.S. (in our opinion) for both natural gas and water utilities. When we last revisited valuation in our industry piece back on October 7th, the U.S. 10-Year T-Note was at 1.53%. WTRG shares were trading at a P/E of 27x 2021 EPS estimates, for a yield of 2.06%. The Peoples Gas transaction had not closed (and actually dragged on a bit longer than expected), which introduced some minor element of regulatory risk. Fast forward to Friday: the U.S. 10-Year T-Note closed at 0.69%, WTRG shares are trading at a P/E of 24x 2021 EPS estimates, for a yield of 2.33%. The Peoples Gas transaction has now closed, tax repair accounting (and its bottom line benefits) are in place, and regulatory risk present in October is not a factor.

All-in, we believe P/E multiples will once again begin moving higher for all the water utilities, but especially for WTRG shares, given 1) the yield of 2.33%, versus the group average yield of 1.88%, 2) due to our expectations that interest rates will remain low, and 3) that the earnings bias is decidedly upward. The shares hit a 52-week high of $54.52 back on February 18th, and its a stronger Company with better earnings visibility today than it was just 3 months ago. Our view is that the need for yield has intensified, and will remain strong for the foreseeable future. We maintain our BUY rating and $70 Fair Value, based on a P/E of 42x our 2021 EPS estimate of $1.66.

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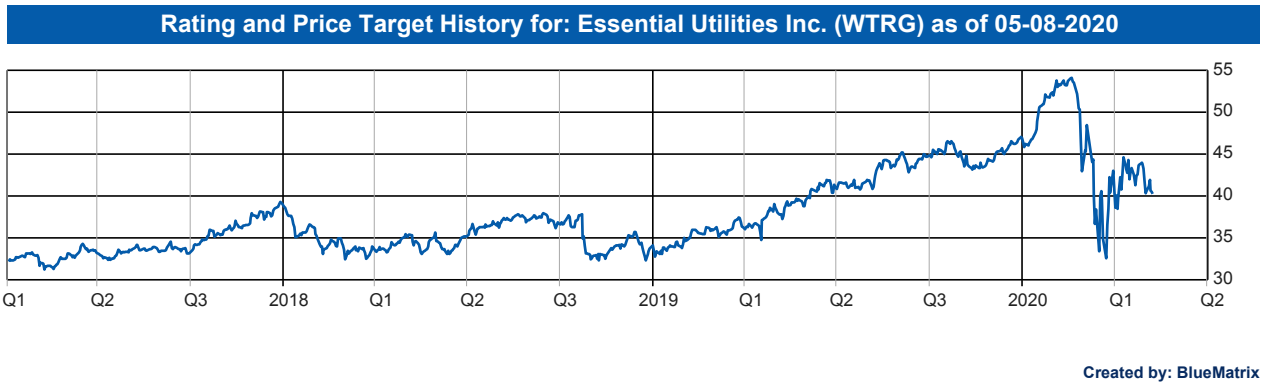
Price Charts



Janney Montgomery Scott Ratings Distribution as of 03/31/2020

			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	169	51.84	35	20.71
NEUTRAL [N]	156	47.85	22	14.10
SELL [S]	1	0.31	0	0.00

*Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.

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Water Utilities

May 11, 2021

Essential Utilities Inc. (WTRG) - BUY

2021 Off To A Strong Start; Reiterate BUY Rating, $70 Fair Value

Price:	$46.76
Fair Value Estimate:	$70.00
52-Week Range:	$37.37 - $48.89
Market Cap (MM):	11,924
Shr.O/S-Diluted (mm):	255.0
Average Daily Volume:	1,050,480
Book Value:	$18.90
Dividend:	$1.00
Yield:	2.1%

FYE: Dec	2020A	2021E	2022E
EPS:	$1.58A	$1.69E	$1.78E
Prior EPS:		$1.67	NC
P/E Ratio:	29.6x	27.7x	26.3x

Quarterly EPS:

Q1	$0.60A	$0.72A	$0.74E
Q2	$0.29A	$0.23E	$0.27E
Q3	$0.23A	$0.29E	$0.28E
Q4	$0.46A	$0.45E	$0.50E

EPS: adjusted

Quarterly Revenue (M):

Q1	$256A	$584A	$617E
Q2	$384A	$388E	$403E
Q3	$349A	$367E	$382E
Q4	$474A	$497E	$517E
Year:	$1,463A	$1,836E	$1,920E

PORTFOLIO MANAGER BRIEF

WTRG's 1Q21 EPS results were above our and consensus forecasts, as more favorable winter weather positively impacted the gas segment's results. Despite the outperformance, 2021 EPS guidance was maintained; we've adjusted our estimates to remain "within the lines" of the expected range. All-in, 2021 and 2022 look to be very good years for the Company from an earnings perspective, and our view is WTRG shares remain one of the best values in our coverage universe. We reiterate our BUY rating and $70 Fair Value.

ANALYST NOTES

- 1Q21 Results Nicely Above Expectations. Weather was very favorable in Q1 in southwestern Pennsylvania, which drove a strong performance from WTRG's Peoples Gas operations. Consolidated adjusted EPS of $0.72 was above our $0.66 estimate, which was also consensus.
- Acquisition Updates. The Company continues to push forward on its DELCORA acquisition, which remains in litigation. Delaware County Court has upheld the validity of the sale agreement, but Delaware County has appealed to the state court. WTRG is awaiting a judge's decision for that appeal, which could take six months or more. The Company expects to settle the forward sale agreement of the 6.7MM shares (proceeds to be used primarily for the DELCORA acquisition) no later than (and close to) August 10th, 2021, the last day it can do so.
- DELCORA aside, the pipeline of opportunities continues to be robust, with 395,000 customer connections being pursued. Fair market value legislation across the geographic service territory continues to benefit acquisition activity, with West Virginia and Kentucky the most recent states to pass this type of legislation. On the 1Q21 conference call, WTRG indicated that it expected to be active in Kentucky looking for transactions going forward.
    - Guidance Maintained. For 2021, WTRG's guidance remains as follows:
    - Net income per diluted common share of $1.64 to $1.69,
    - Earnings per share growth CAGR of 5 to 7% for 2020 through 2023,
    - Regulated water segment infrastructure investments of approximately $550 million in 2021,
    - Regulated natural gas segment infrastructure investments of approximately $450 million in 2021,
    - Infrastructure investments of approximately $3 billion through 2023 to rehabilitate and strengthen water, wastewater and natural gas systems,

RESEARCH ANALYST CERTIFICATIONS AND IMPORTANT DISCLOSURES ARE ON PAGES 3 - 4 OF THIS REPORT

  - Regulated water segment rate base compound annual growth rate of 6 to 7% through 2023,
  - Regulated natural gas segment rate base compound annual growth rate of 8 to 10% through 2023,
  - Average annual regulated water segment customer (or equivalent dwelling units) growth of between 2 and 3% from acquisitions and organic customer growth.

- Summary/Valuation. WTRG share prices have been performing better recently, but still lag versus the peer group. We thought a "sum-of-the-parts" valuation might be useful given the disconnect; the gas utility operations are the most difficult to value, given "pure-play" natural gas comparables to Peoples Gas are difficult to come by. We note that Centerpoint Energy (CNP, NR) recently announced the sale of several gas utility properties for 2.5x rate base. If we use the Peoples Gas rate base of $2.5B, applying a 2.5x rate base multiple would equal a $6.25B value. If we divide that by 255MM shares, that translates to a $24.51 per share value.
- The water utility operations present less of a challenge in terms of valuation, given several comparables exist. The most direct comp is likely American Water Works (AWK, BUY) which has sizable operations in Pennsylvania and New Jersey. Those shares command a 37x P/E on 2021 consensus EPS. If we use the midpoint of 2021 EPS guidance for WTRG shares and assume approximately 70% of EPS is derived from water utility operations, that gets us to $1.16 EPS x 37 P/E = $42.92. When added to the aforementioned $24.51 gas utility valuation, that would equate to a Fair Value of $67.43.
- Sum-of-the-parts analysis aside, we favor using dividend yield for water utilities. While we acknowledge that WTRG isn't a pure-play water utility, we believe its ability to increase and pay dividends is as predictable as any water utility in our coverage universe. Currently, the group average dividend yield (including WTRG) is 1.72%, but several water utilities are trading at our target yield of approximately 1.5%. Essential Utilities is currently trading at a yield of 2.15%, highest in the peer group. Given the Company's superior operating footprint (all constructive regulatory environments), we believe the forward earnings outlook is exceptionally strong and we expect the shares to trade to a 1.5% yield based on our 2022 estimated dividend of $1.05, which generates a Fair Value of $70. All-in, regardless of what valuation metric investors choose, the potential share values we've highlighted ($67 / $70) are both higher than yesterday's closing price of $46.76. We reiterate our BUY rating on WTRG shares and $70 Fair Value.

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IMPORTANT DISCLOSURES

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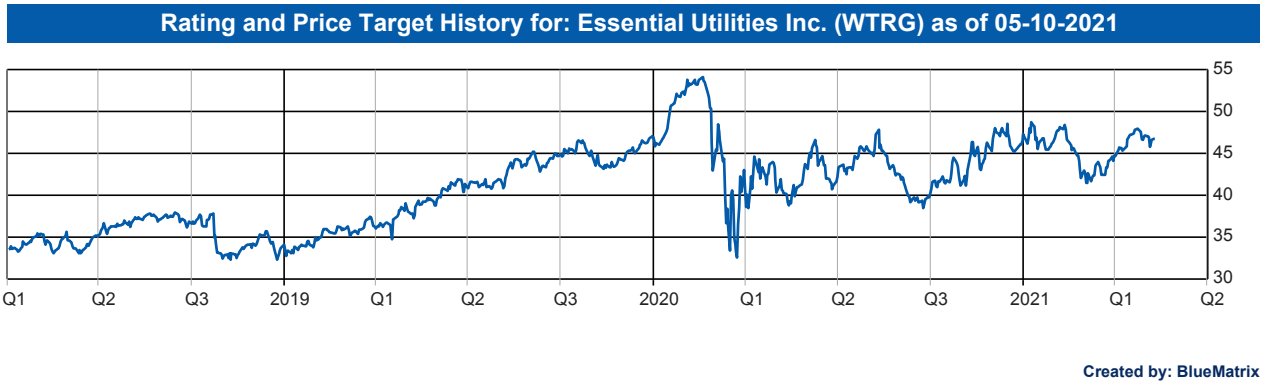
Price Charts



Janney Montgomery Scott Ratings Distribution as of 03/31/2021

			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	119	46.12	26	21.85
NEUTRAL [N]	105	40.70	7	6.67
SELL [S]	0	0.00	0	0
EXTENDED REVIEW [EXTRE]	34	13.18	10	29.41

*Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.

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Water Utilities

August 8, 2019

Aqua America, Inc. (WTR) - BUY

WTR: Solid Quarter, Strong Outlook; Maintain BUY Rating, $44 Fair Value

Price:	$42.06
Fair Value Estimate:	$44.00
52-Week Range:	$32.09 - $42.32
Market Cap (MM):	9,072
Shr.O/S-Diluted (mm):	215.7
Average Daily Volume:	1,024,918
Book Value:	$11.17
Dividend:	$0.94
Yield:	2.2%

FYE: Dec	2019E	2020E	2021E
EPS:	$1.50E	$1.56E	$1.70E
Prior EPS:	$1.39	$1.52	NC
P/E Ratio:	28.0x	27.0x	24.7x

Quarterly EPS:

Q1	$0.28A	$0.56E	$0.59E
Q2	$0.37A	$0.19E	$0.21E
Q3	$0.44E	$0.36E	$0.38E
Q4	$0.41E	$0.46E	$0.51E

Quarterly Revenue (M):

Q1	$201A	$681E	$706E
Q2	$219A	$392E	$408E
Q3	$357E	$380E	$397E
Q4	$560E	$596E	$618E
Year:	$1,345E	$2,048E	$2,129E

PORTFOLIO MANAGER BRIEF

WTR's 2Q19 results met expectations, with adjusted EPS of $0.37 meeting the consensus forecast. Quarterly results aside, new acquisition opportunities were a dominant topic during the 2Q conference call, and the pipeline of new opportunities appears to have grown substantially larger. We've made minor adjustments to our forward estimates based on the push-out of the Peoples Gas transaction (our estimates now include the combined entity beginning in 4Q19) and we maintain our BUY rating and $44 Fair Value on WTR shares.

ANALYST NOTES

- 2Q19 Results Inline with Expectations. At the top line, revenues of $219MM benefitted from growth ($4MM) and rates & surcharges ($4MM), with lower consumption providing somewhat of an offset (-$700K) and other items (-$300K). At the bottom line, adjusted EPS of $0.37 met the consensus forecast, but was below our $0.39 estimate.
- Potential Acquisition Opportunities Are Sizable (and Plentiful). Several large-scale acquisition opportunities have developed in Pennsylvania, which could add substantially to the company's size. During the quarter, WTR signed an exclusive agreement with DELCORA, a large municipal wastewater authority in southeastern PA serving 500K people in 42 municipalities. DELCORA and WTR have committed to exclusive discussions regarding DELCORA's potential acquisition. Also in play in Pennsylvania is the water, wastewater and stormwater systems for the City of Harrisburg, the state capital. Then there's the water system that comprises the Chester Water Authority, which Aqua America has pursued previously. A legal fight is taking place between the Authority and the City of Chester over who owns the assets; the city would like to entertain offers, the Authority wishes to stay independent. Overall, the acquisition environment continues to improve, aided by fair market value legislation across the company's geographic footprint.
- Summary/Valuation. With the Peoples Gas acquisition expected to close in the fall, we've already moved to combined estimates (Aqua + Peoples). We expect to continue to refine our forecasts as more information on timing and cost impacts become available, but we believe our estimates are reasonable given the data already available. The outlook for earnings growth (and dividend increases) looks particularly bright, and just on the base assets. Additional acquisitions of size (if they materialize) would likely add additional upside to our forecasts, given the company's disciplined approach when it comes to purchasing assets. In terms

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of valuation, WTR shares still have reasonable upside to our Fair Value of $44 (based on a P/E of 26x our 2021 EPS estimate of $1.70) , so we maintain our BUY rating, recommending investors add on dips, should they occur.

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Price Charts

Janney Montgomery Scott Ratings Distribution as of 06/30/2019

			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	179	55.59	40	22.35
NEUTRAL [N]	142	44.10	14	9.86
SELL [S]	1	0.31	0	0.00

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Water Utilities

September 18, 2019

Aqua America, Inc. (WTR) - BUY

DELCORA Acquisition Further Increases Pennsylvania Exposure; Reiterate BUY Rating, Fair Value to $50

Price:	$43.90
Fair Value Estimate:	$50.00
52-Week Range:	$32.09 - $45.50
Market Cap (MM):	9,474
Shr.O/S-Diluted (mm):	215.8
Average Daily Volume:	1,033,917
Book Value:	$17.73
Dividend:	$0.94
Yield:	2.1%

FYE: Dec	2019E	2020E	2021E
EPS:	$1.50E	$1.56E	$1.77E
Prior EPS:	NC	NC	$1.70
P/E Ratio:	29.3x	28.1x	24.8x

Quarterly EPS:			
Q1	$0.28A	$0.56E	$0.63E
Q2	$0.37A	$0.19E	$0.24E
Q3	$0.44E	$0.36E	$0.39E
Q4	$0.41E	$0.46E	$0.50E

Quarterly Revenue (M):			
Q1	$201A	$681E	$721E
Q2	$219A	$392E	$423E
Q3	$357E	$380E	$412E
Q4	$560E	$596E	$633E
Year:	$1,345E	$2,048E	$2,189E

PORTFOLIO MANAGER BRIEF

After the close yesterday, Aqua America announced its second large acquisition in the State of Pennsylvania within a one-year period. The company will pay $276.5MM for an estimated 165,000 retail wastewater customers from the Delaware County Regional Water Quality Control Authority (DELCORA). The announcement was widely anticipated, given previous disclosures that discussions were underway. We expect the deal to close in late 2020, and are making adjustments to our 2021 estimates to reflect anticipated benefits from the acquisition. We reiterate our BUY rating, and raise our Fair Value from $44 to $50, based on a P/E of 28x our 2021 EPS estimate of $1.77.

ANALYST NOTES

- DELCORA Acquisition As Good as it Gets. Pennsylvania has proven to be a target rich environment for Aqua America in terms of M&A, with the company once again announcing a sizable transaction. Following closely on the $4.3B Peoples Gas acquisition announcement, Aqua has come to terms with DELCORA, an expansive wastewater treatment system spanning 42 municipalities in the southeastern part of the state. The price ($276.5MM) looks very favorable, and given the number of estimated customers, likely will not generate goodwill. In the release, the company indicated the system needs $1.2B of investment through 2041, which amounts to meaningful CAPEX annually over the period. And of course, Aqua knows southeastern Pennsylvania extremely well, given its original roots dating back to its Philadelphia Suburban Corporation (previous ticker symbol PSC) days. We expect no problems with the transaction being approved by the Pennsylvania Public Utility Commission, and anticipate a closing in late 2020.
- Summary/Valuation. The last three sizable transactions - DELCORA, Peoples Gas and Limerick have all been in Aqua America's home state of Pennsylvania, which also happens to be the most constructive regulatory environment in the U.S., in our opinion. Returns are solid, the PAPUC has a great reputation of working with utilities to improve infrastructure and manage ratepayer costs, which we note cannot be said of all states across the country. We believe Aqua's demonstrated ability to significantly grow its presence (and future earnings) is worthy of a bump in its valuation, and we raise not only our 2021 EPS estimate, but our P/E multiple assumption. We reiterate our BUY rating and increase our Fair Value target from $44 to $50, based on a P/E of 28x our 2021 EPS estimate of $1.77.

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Price Charts

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Water Utilities

November 5, 2019

Aqua America, Inc. (WTR) - BUY

WTR: 3Q19 Results Above Expectations; Maintain BUY Rating, $70 Fair Value

Price:	$43.56
Fair Value Estimate:	$70.00
52-Week Range:	$32.09 - $46.90
Market Cap (MM):	9,400
Shr.O/S-Diluted (mm):	215.8
Average Daily Volume:	1,151,504
Book Value:	$17.73
Dividend:	$0.94
Yield:	2.2%

FYE: Dec	2019E	2020E	2021E
EPS:	$1.47E	$1.56E	$1.70E
Prior EPS:	$1.50	NC	$1.77
P/E Ratio:	29.6x	27.9x	25.6x

Quarterly EPS:

Q1	$0.28A	$0.56E	$0.63E
Q2	$0.37A	$0.20E	$0.19E
Q3	$0.48A	$0.30E	$0.28E
Q4	$0.34E	$0.53E	$0.60E

EPS: adjusted

Quarterly Revenue (M):

Q1	$201A	$672E	$711E
Q2	$219A	$392E	$423E
Q3	$244A	$367E	$398E
Q4	$226E	$597E	$635E
Year:	$890E	$2,028E	$2,168E

PORTFOLIO MANAGER BRIEF

WTR's 3Q19 EPS results were above expectations, with adjusted EPS of $0.48 above the consensus forecast of $0.44. The company also reiterated its full year adjusted EPS guidance range of $1.45 to $1.50. With the Peoples Gas transaction now anticipated to close in 4Q19 or early 1Q20, we've removed Peoples Gas forecasts from our 4Q19 estimates (but are maintaining them for 1Q20). With both the Peoples Gas and DELCORA acquisitions moving forward, normal M&A activity and continuing rate relief, we see significant growth in the years ahead. Valuation remains attractive, as well; with the shares trading at a P/E 26x our 2021 EPS estimate of $1.70 and yielding 2.1% (highest in the peer group) we reiterate our BUY rating and $70 Fair Value.

ANALYST NOTES

- 3Q19 Adjusted EPS Results Ahead of Expectations. On the top line, revenues of $244MM were just below consensus of $250MM but higher YoY by 7.7% as rates, growth and volume all positively contributed. The company continues to experience higher O&M expenses due to the Peoples Gas transaction, which negatively impacted GAAP EPS of $0.38. Adjusted 3Q19 EPS was $0.48, 9.4% higher YoY and well above the Street estimate of $0.44.
- Major Acquisitions Still Awaiting Closing. The Peoples Gas transaction is expected to close in late 2019 or early 2020, while DELCORA is expected late 2020. For Peoples Gas, the Administrative Law Judge assigned to the case rendered a positive decision, and recommended the PA Public Utility Commission approve the acquisition. The DELCORA transaction also requires PAPUC approval.
- Regulatory Update. In the company's geographic operating footprint, its received annual rate increases totaling $59.8MM across Illinois, New Jersey, North Carolina, Ohio and Pennsylvania. Peoples Gas filed a settlement agreement in its PA rate case in July 2019, and the PAPUC authorized a $59.5MM increase on October 3, 2019. New rates become effective January 1, 2020.
- Summary/Valuation. Aqua's ability to continue executing acquisitions both large and small sets the stage for continued earnings growth in the years ahead. For both its gas and water assets, the pipeline of opportunities remains robust, and our positive investment thesis remains decidedly bullish. We maintain our BUY rating and $70 Fair Value, based on a P/E of 41x our 2021 EPS estimate of $1.70. We note the shares have the highest yield in the peer group (2.14%) and dividend growth should continue to be mid-to-high single digits for the foreseeable future.

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Price Charts

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			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	171	52.78	37	21.64
NEUTRAL [N]	151	46.60	20	13.25
SELL [S]	2	0.62	0	0.00

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Water Utilities

November 5, 2020

Essential Utilities Inc. (WTRG) - BUY

3Q20 Results Just Above Expectations; Maintain BUY Rating, $70 Fair Value

Price:	$41.19
Fair Value Estimate:	$70.00
52-Week Range:	$30.40 - $54.52
Market Cap (MM):	10,098
Shr.O/S-Diluted (mm):	245.2
Average Daily Volume:	1,230,398
Book Value:	$18.91
Dividend:	$1.00
Yield:	2.4%

FYE: Dec	2020E	2021E	2022E
EPS:	$1.58E	$1.67E	$1.78E
Prior EPS:	NC	NC	NC
P/E Ratio:	26.1x	24.7x	23.1x

Quarterly EPS:

Q1	$0.60A	$0.66E	$0.68E
Q2	$0.29A	$0.22E	$0.25E
Q3	$0.23A	$0.26E	$0.27E
Q4	$0.46E	$0.52E	$0.58E

EPS: adjusted

Quarterly Revenue (M):

Q1	$256A	$773E	$794E
Q2	$384A	$342E	$352E
Q3	$349A	$360E	$370E
Q4	$541E	$579E	$601E
Year:	$1,530E	$2,053E	$2,118E

PORTFOLIO MANAGER BRIEF

WTRG's 3Q20 adjusted EPS results were just above our expectations ($0.23 vs. $0.22) which was also consensus. The Company refined its guidance, as it now expects 2020 adjusted EPS at the upper end of its previously communicated $1.53 to $1.58 range (it also expects an earnings growth CAGR of 5-7% for 2019 thru 2022). We've made only minor adjustments to our 2020 & 2021 estimates, and introduced 2022 forecasts. We maintain our BUY rating and $70 Fair Value, based on a P/E of 39x our 2022 EPS estimate of $1.78.

ANALYST NOTES

- 3Q20 Results Just Above Expectations. On the top line, revenues of $349MM were just above our $342MM estimate (consensus was $347MM). The upside in our model surprisingly came from the Gas segment, as our estimates already factored in increased volumes in the Water segment due to the hot & dry summer. OPEX in the quarter came in roughly inline with our forecasts, and adjusted EPS of $0.23 was $0.01 above our and the consensus forecast of $0.22.
- Updated (And Refined) Guidance. For 2020, WTRG now sees adjusted EPS at the upper end of its $1.53 to $1.58 range. The Company expects an earnings growth CAGR of 5-7% for 2019 through 2022. CAPEX remains on track for $550MM for the Water segment in 2020 ($400MM for the Natural Gas segment, including investments made before WTRG ownership). Going forward, it sees $2.8B of infrastructure investment thru 2022.
- Adjusting 2020/2021 Estimates; Introducing 2022 Forecasts. We've made only minor adjustments to our 2020/2021 estimates; for 2020, we were already at the high end of the Company's $1.53 - $1.58 guidance range. We took the $0.01 of EPS from 4Q20 out of the Natural Gas segment; NOAA forecasts for the Northeast see continuing above normal temperatures through the middle of November.
- Summary/Valuation. A solid quarter, healthy M&A activity (with a robust pipeline of opportunities), strong CAPEX profile and attractive valuation are all reasons we recommend Essential Utilities shares at current price levels. We also note that shares yield 2.43%, the highest in the water utility peer group. We maintain our BUY rating and $70 Fair Value, which is based on a P/E of 39x our 2022 EPS estimate of $1.78.

RESEARCH ANALYST CERTIFICATIONS AND IMPORTANT DISCLOSURES ARE ON PAGES 2 - 3 OF THIS REPORT

IMPORTANT DISCLOSURES

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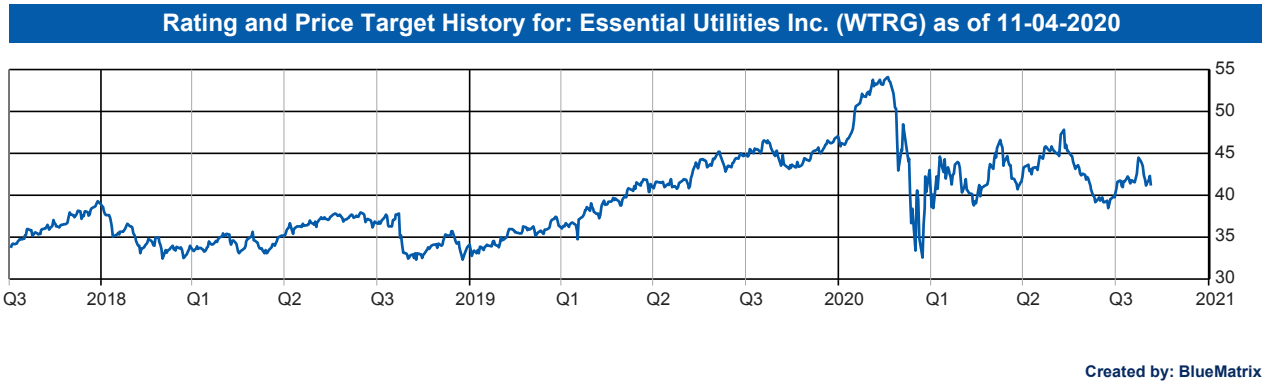

Janney Montgomery Scott Ratings Distribution as of 09/30/2020

			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	117	47.37	18	15.38
NEUTRAL [N]	130	52.63	11	8.46
SELL [S]	0	0.00	0	0.00

*Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.

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Michael Gaugler 215-665-1359 mgaugler@janney.com

Water Utilities

February 25, 2021

Essential Utilities Inc. (WTRG) - BUY

Strong Finish to 2020, Guidance For 2021 Compares Favorably; Reiterate BUY Rating, $70 Fair Value

Price:	$44.09
Fair Value Estimate:	$70.00
52-Week Range:	$30.40 - $52.00
Market Cap (MM):	10,815
Shr.O/S-Diluted (mm):	245.3
Average Daily Volume:	1,075,865
Book Value:	$18.90
Dividend:	$1.00
Yield:	2.3%

FYE: Dec	2020A	2021E	2022E
EPS:	$1.58A	$1.67E	$1.78E
Prior EPS:		NC	NC
P/E Ratio:	27.9x	26.4x	24.8x

Quarterly EPS:

Q1	$0.60A	$0.66E	$0.68E
Q2	$0.29A	$0.22E	$0.25E
Q3	$0.23A	$0.26E	$0.27E
Q4	$0.46A	$0.52E	$0.58E

EPS: adjusted

Quarterly Revenue (M):

Q1	$256A	$700E	$725E
Q2	$384A	$342E	$352E
Q3	$349A	$360E	$370E
Q4	$474A	$501E	$526E
Year:	$1,463A	$1,976E	$2,043E

PORTFOLIO MANAGER BRIEF

Essential Utilities 4Q20 adjusted EPS of $0.46 matched our estimate and was slightly ahead of consensus, and its 2021 EPS guidance range of $1.64 to $1.69 compares favorably to our our $1.67 forecast (also consensus). We've made minor adjustments to our forward estimates (see table, this page) and reiterate BUY rating and $70 Fair Value, based on a P/E of 39x our 2022 EPS estimate of $1.78. The shares yield 2.3%, highest in the water utility peer group.

ANALYST NOTES

- 4Q20 Adjusted EPS Met Expectations. On the top line, revenues of $474MM increased 109.7% YOY, benefitting from the Peoples Gas acquisition (+ $241MM) and increased volume, growth, rate and surcharge increases in the regulated water segment (+$10MM) while "other" items netted a -$3MM. On the bottom line, adjusted EPS of $0.46 matched our estimate and was a penny ahead of consensus.
- 2021 Guidance Update. For the full year, key guidance items include EPS ($1.64 to $1.69), EPS CAGR of 5% to 7% for 2020 through 2023, CAPEX of $550MM for the Water segment and $450MM for the Natural Gas segment. For the 2021 through 2023 period, CAPEX of $3B, which is expected to drive rate base compound annual growth of 6%-7% for the Water segment and 8% to 10% for the Natural Gas segment. Other items include Water segment customer growth of 2% to 3% (acquisitions and organic), reduction of Scope 1 and Scope 2 greenhouse gas emissions by 60% by 2035 and multiyear plans to achieve diverse supplier spend and employees of color.
- Regulatory Update. WTRG has received rate awards in NJ, NC, OH and PA of $8.5MM YTD. It has proceedings in VA and IN that would add an estimated $1.8MM in incremental revenues.
- Strong Acquisition Activity Continues. 2021 looks to be a very strong year for acquisitions, with the biggest announced transaction (DELCORA, 198K equivalent dwelling units) expected to receive a Pennsylvania Public Utility Commission (PAPUC) decision in March. All-in, Essential Utilities has six signed purchase agreements encompassing 227K equivalent dwelling units that will add $438MM in rate base when closed. The Company's pipeline of potential acquisitions represents 375K total water/wastewater customers. Its target for 2021 is to sign municipal deals totaling at least $100MM of rate base.

RESEARCH ANALYST CERTIFICATIONS AND IMPORTANT DISCLOSURES ARE ON PAGES 3 - 4 OF THIS REPORT

- Summary/Valuation. We remain perplexed as to why WTRG shares aren't trading at high price levels. The Company's executed in accordance with guidance, has a robust CAPEX plan for the next three years, expects 5%-7% earnings growth through 2023 and continues to close acquisitions of size, augmenting organic growth. Its regulatory risk is probably the lowest of any in the peer group with multi-state operations, and its yield at 2.3% is the highest. Within the water utility peer group, WTRG remains our top pick, and we reiterate our BUY rating and $70 Fair Value, based on a P/E of 39x our 2022 EPS estimate of $1.78. Our target yield for WTRG shares is 1.5% against an expected 2022 annualized dividend of $1.05.

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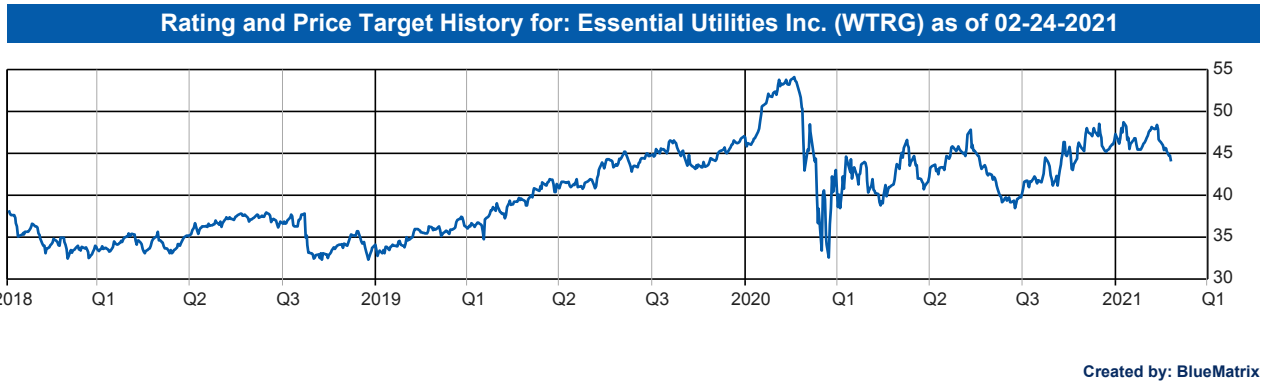
Price Charts



Janney Montgomery Scott Ratings Distribution as of 12/31/2020

			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	115	46.18	27	23.48
NEUTRAL [N]	134	53.82	16	11.94
SELL [S]	0	0.00	0	0.00

*Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.

Other Disclosures

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Water Utilities

February 28, 2020

Essential Utilities Inc. (WTRG) - BUY

4Q19 Results & 2020 Guidance On Target; Maintain BUY Rating, $70 Fair Value

Price:	$46.34
Fair Value Estimate:	$70.00
52-Week Range:	$34.79 - $54.52
Market Cap (MM):	9,999
Shr.O/S-Diluted (mm):	215.8
Average Daily Volume:	1,199,373
Book Value:	$17.90
Dividend:	$0.94
Yield:	2.0%

FYE: Dec	2019A	2020E	2021E
EPS:	$1.47A	$1.56E	$1.65E
Prior EPS:		NC	$1.70
P/E Ratio:	31.5x	29.7x	28.1x

Quarterly EPS:

Q1	$0.28A	$0.21E	$0.59E
Q2	$0.37A	$0.20E	$0.20E
Q3	$0.48A	$0.30E	$0.30E
Q4	$0.34A	$0.53E	$0.56E

EPS: adjusted

Quarterly Revenue (M):

Q1	$201A	$207E	$711E
Q2	$219A	$392E	$423E
Q3	$244A	$367E	$398E
Q4	$226A	$597E	$635E
Year:	$890A	$1,562E	$2,168E

PORTFOLIO MANAGER BRIEF

WTR's 4Q19 results met our expectations (top and bottom line), and forward proforma EPS guidance for 2020 was also on target. Looking forward, we've made minor adjustments to our forward estimates (see table, this page) and we maintain our BUY rating and $70 Fair Value on WTR shares.

ANALYST NOTES

- 4Q19 Results Met Expectations. Revenues of $226MM and adjusted EPS of $0.34 met our expectations (consensus was $222MM and $0.30, respectively). 4Q19 results for water utilities are a seasonally weak period and rarely impact water utility estimates or valuations.
- Peoples Gas Update; Just a Little Bit Longer. The Peoples Gas transaction is now expected to close on March 16, 2020, an unfortunate development given Q1 is the seasonally strongest period for Mid-Atlantic gas utilities.
- Long Awaited 2020 Guidance Arrives. Given the delays in closing the Peoples Gas transaction, Essential Utilities is offering pro-forma adjusted 2020 EPS guidance in a range of $1.53 to $1.58, which assumes ownership of Peoples Gas from January 1st (we assume management did this to provide a range of full year earnings potential and to aid analysts in modeling estimates). The company expects to see an EPS CAGR of 5%-7% over the next 3-year period.
- Adjusting Estimates. We made minor adjustments to our forward estimates (see table, this page). Those estimates are what we think the company will actually report on an adjusted basis, not pro-forma. Our proforma adjusted EPS is $1.56, with the difference between the two being the exclusion of gas results in 1Q20.
- Summary/Valuation. 4Q19 results and 2020 guidance turned out as anticipated. Rate case activity remains strong, with 3 states receiving rate awards and infrastructure surcharges totaling $4.8MM (the company has other rate activity pending in 4 states requesting $8.3MM). The acquisition pipeline remains full, and CAPEX trends are robust. 2020 is unfolding as we expected, which required minimal adjustments to estimates. In terms of valuation, we continue to forecast Essential's 2030 dividend at $1.93, which when pegged to our expected U.S. 10-year T-Note yield of 1.5%, generates a Fair Value of $70. We maintain our BUY rating on Essential Utilities.

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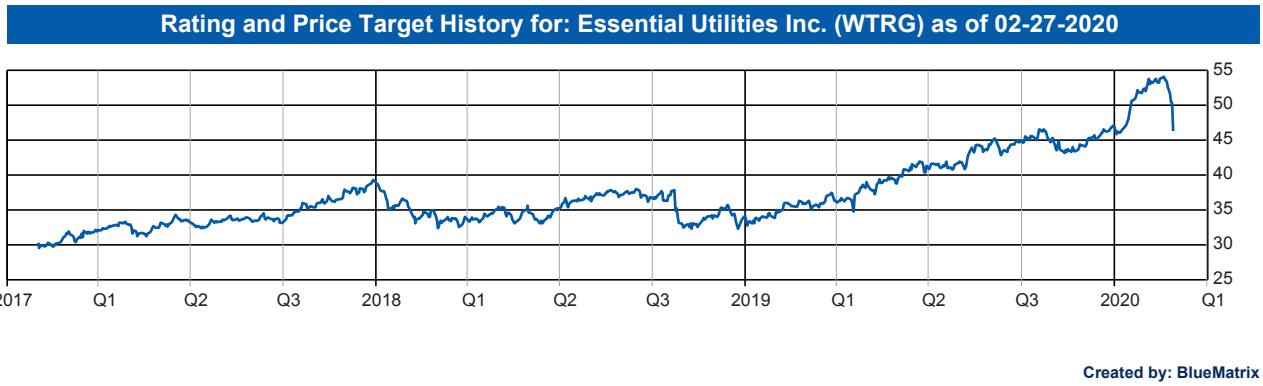

Janney Montgomery Scott Ratings Distribution as of 12/31/2019

			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	167	51.38	35	20.96
NEUTRAL [N]	157	48.31	23	14.65
SELL [S]	1	0.31	0	0.00

*Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.

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Water Utilities

March 5, 2020

Essential Utilities Inc. (WTRG) - BUY

Realigning 2020 Estimate Methodology; Maintain BUY Rating, $70 Fair Value

Price:	$48.45
Fair Value Estimate:	$70.00
52-Week Range:	$34.79 - $54.52
Market Cap (MM):	10,795
Shr.O/S-Diluted (mm):	222.8
Average Daily Volume:	1,309,471
Book Value:	$17.90
Dividend:	$0.94
Yield:	1.9%

FYE: Dec	2019A	2020E	2021E
EPS:	$1.47A	$1.56E	$1.65E
Prior EPS:		NC	NC
P/E Ratio:	33.0x	31.1x	29.4x

Quarterly EPS:

Q1	$0.28A	$0.53E	$0.59E
Q2	$0.37A	$0.20E	$0.20E
Q3	$0.48A	$0.30E	$0.30E
Q4	$0.34A	$0.53E	$0.56E

EPS: adjusted

Quarterly Revenue (M):

Q1	$201A	$207E	$711E
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Q4	$226A	$597E	$635E
Year:	$890A	$1,562E	$2,168E

PORTFOLIO MANAGER BRIEF

Upon review of consensus forecasts for 2020, we are changing our 1Q20 EPS methodology from adjusted actual of $0.21 to pro-forma of $0.53 to prevent any confusion among investors. We made this distinction in our 2/28 note when we indicated our pro-forma EPS estimate for 2020 was $1.56, and there is no change in that regard. We are simply moving all of our 2020 estimates to pro-forma.

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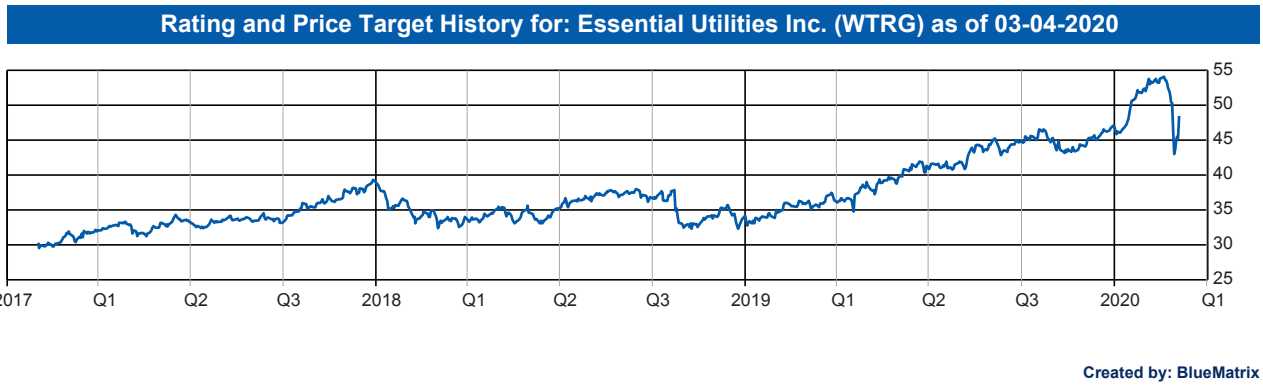

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			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	167	51.38	35	20.96
NEUTRAL [N]	157	48.31	23	14.65
SELL [S]	1	0.31	0	0.00

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Water Utilities

July 20, 2020

Essential Utilities Inc. (WTRG) - BUY

2Q20 Preview; Raising Estimates Due to Favorable Weather, Reiterate BUY Rating, $70 Fair Value

Price:	$44.71
Fair Value Estimate:	$70.00
52-Week Range:	$30.40 - $54.52
Market Cap (MM):	10,954
Shr.O/S-Diluted (mm):	245.0
Average Daily Volume:	1,139,007
Book Value:	$18.83
Dividend:	$0.94
Yield:	2.1%

FYE: Dec	2019A	2020E	2021E
EPS:	$1.47A	$1.58E	$1.67E
Prior EPS:		NC	$1.66
P/E Ratio:	30.4x	28.3x	26.8x

Quarterly EPS:

Q1	$0.28A	$0.60A	$0.66E
Q2	$0.37A	$0.28E	$0.23E
Q3	$0.48A	$0.24E	$0.26E
Q4	$0.34A	$0.46E	$0.52E

EPS: adjusted

Quarterly Revenue (M):

Q1	$201A	$256A	$773E
Q2	$219A	$352E	$342E
Q3	$244A	$342E	$360E
Q4	$226A	$541E	$579E
Year:	$890A	$1,491E	$2,053E

PORTFOLIO MANAGER BRIEF

We've increased our 2Q20 estimates materially (adjusted EPS from $0.23 to $0.28) based on favorable weather patterns for both the natural gas and water segments during the April-June time frame. Full year 2020 adjusted EPS guidance is currently $1.53 - $1.58; we see the potential for that range to tighten (to the upside) or be increased if favorable weather patterns continue. We maintain our BUY rating and $70 Fair Value on WTRG shares.

ANALYST NOTES

- Weather Should Positively Contribute to 2Q20 Results. April in the State of Pennsylvania was surprisingly cold, and we expect Essential's Peoples Gas segment results to benefit. We noted on the UGI Corp website UGI Corp weather that temperatures in April for its UGI Utilities segment (all in Pennsylvania) was 14% colder than normal in April and 23% colder in May.

  As Summer arrived, the weather changed quickly, and its been hot and dry through June and July. That should benefit Essential's water segment results, and we've raised our forecasts as a result. NOAA's 8-14 day outlook sees temperatures remaining above average across much of the United States, and a heatwave started this weekend in the Northeast.

- What Will WTRG Do With Full Year Guidance? Our previous 2Q20 adjusted EPS estimate was $0.23; now its $0.28. We were already at the high end of Company annual guidance before the change. 3Q20 weather is shaping up very nicely as well, with July hot and dry through the 19th, and the current NOAA forecast for that to continue through month-end. We've lowered our 4Q20 forecasts to remain within the Company's guidance range for the full year ($1.53 to $1.58), but we note that if we get a cold 4Q (like last year) WTRG is set-up to outperform its current guidance range.

- Summary/Valuation. Essential Utilities is off to good start in 2020. The closing of its Peoples Gas transaction, coupled with favorable weather patterns should allow it to deliver earnings at or above previous expectations. We still see plenty of upside to share prices; the 2.1% yield remains the highest in the water utility peer group, and with the U.S. 10YR T-Note yield 150bps lower, we continue to recommend accumulation at current levels. We reiterate our BUY rating and $70 Fair Value, based on a P/E of 42x our 2021 EPS estimate of $1.67 (which also equates to a 1.5% dividend yield in 2030 that assumes a 7.5% dividend CAGR).

RESEARCH ANALYST CERTIFICATIONS AND IMPORTANT DISCLOSURES ARE ON PAGES 2 - 3 OF THIS REPORT

IMPORTANT DISCLOSURES

Research Analyst Certification

I, Michael Gaugler, the Primarily Responsible Analyst for this research report, hereby certify that all of the views expressed in this research report accurately reflect my personal views about any and all of the subject securities or issuers. No part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views I expressed in this research report.

Janney Montgomery Scott LLC ("Janney") Equity Research Disclosure Legend

Essential Utilities Inc. currently is, or during the past 12 months was, a Janney Montgomery Scott LLC client. Janney Montgomery Scott LLC, provided investment banking related services.

Janney Montgomery Scott LLC currently acts as a market-maker in the securities of Essential Utilities Inc..

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Janney Montgomery Scott LLC intends to seek or expects to receive compensation for investment banking services from Essential Utilities Inc. and UGI Corporation in the next three months.

The research analyst is compensated based on, in part, Janney Montgomery Scott's profitability, which includes its investment banking revenues.

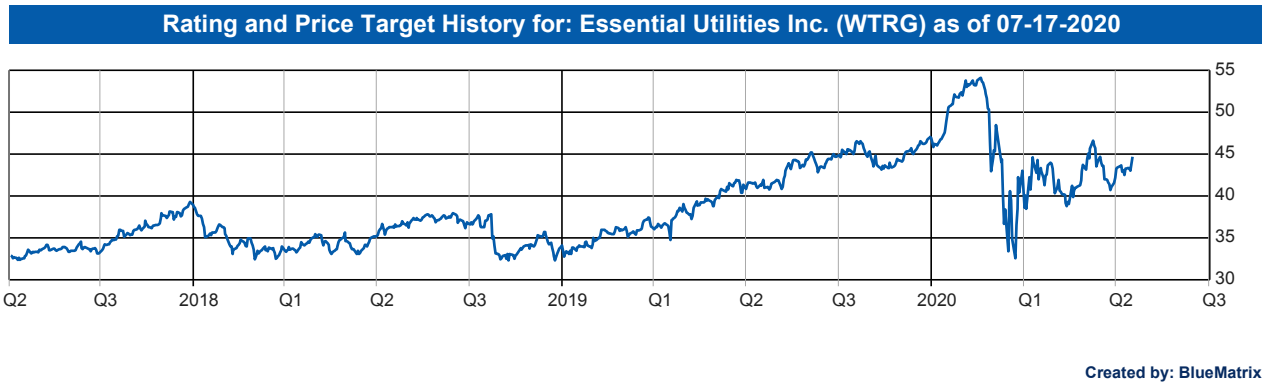
Definition of Ratings

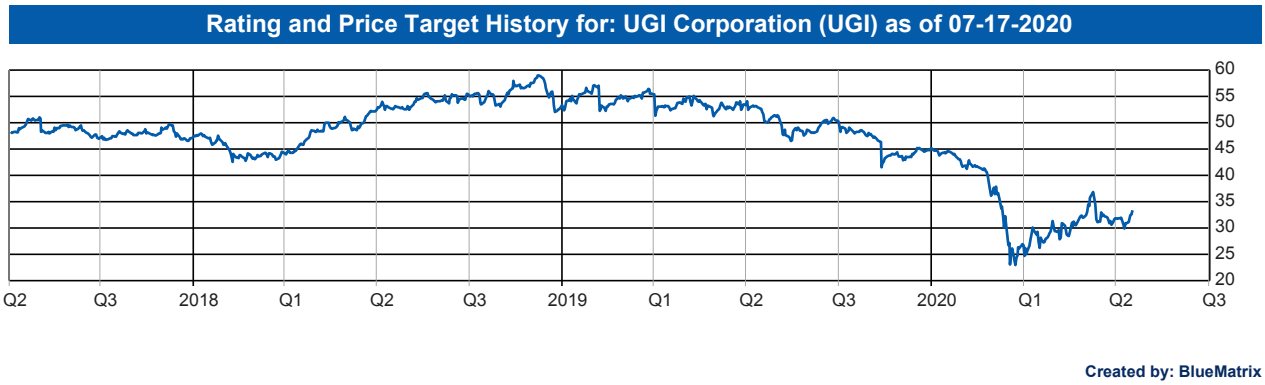
BUY: Janney expects that the subject company will appreciate in value. Additionally, we expect that the subject company will outperform comparable companies within its sector.

NEUTRAL: Janney believes that the subject company is fairly valued and will perform in line with comparable companies within its sector. Investors may add to current positions on short-term weakness and sell on strength as the valuations or fundamentals become more or less attractive.

SELL: Janney expects that the subject company will likely decline in value and will underperform comparable companies within its sector.

Price Charts





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Janney Montgomery Scott Ratings Distribution as of 06/30/2020

			IB Serv./Past 12 Mos.*	
Rating	**Count**	**Percent**	**Count**	**Percent**
BUY [B]	116	46.40	26	22.41
NEUTRAL [N]	133	53.20	21	15.79
SELL [S]	1	0.40	0	0.00

*Percentages of each rating category where Janney has performed Investment Banking services over the past 12 months.

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This report is for your information only and is not an offer to sell or a solicitation of an offer to buy the securities or instruments named or described in this report. Interested parties are advised to contact the entity with which they deal or the entity that provided this report to them, should they desire further information. The information in this report has been obtained or derived from sources believed by Janney Montgomery Scott LLC, to be reliable. Janney Montgomery Scott LLC, however, does not represent that this information is accurate or complete. Any opinions or estimates contained in this report represent the judgment of Janney Montgomery Scott LLC at this time and are subject to change without notice.

Investment opinions are based on each stock's 6-12 month return potential. Our ratings are not based on formal price targets, however, our analysts will discuss fair value and/or target price ranges in research reports. Decisions to buy or sell a stock should be based on the investor's investment objectives and risk tolerance and should not rely solely on the rating. Investors should read carefully the entire research report, which provides a more complete discussion of the analyst's views. Supporting information related to the recommendation, if any, made in the research report is available upon request.

Michael Gaugler 215-665-1359 mgaugler@janney.com

Water Utilities

August 7, 2020

Essential Utilities Inc. (WTRG) - BUY

Quarterly Results Above Expectations; Reiterate BUY Rating, $70 Fair Value

Price:	$45.56
Fair Value Estimate:	$70.00
52-Week Range:	$30.40 - $54.52
Market Cap (MM):	11,164
Shr.O/S-Diluted (mm):	245.0
Average Daily Volume:	1,148,358
Book Value:	$18.83
Dividend:	$1.00
Yield:	2.2%

FYE: Dec	2019A	2020E	2021E
EPS:	$1.47A	$1.58E	$1.67E
Prior EPS:		NC	NC
P/E Ratio:	31.0x	28.8x	27.3x

Quarterly EPS:

Q1	$0.28A	$0.60A	$0.66E
Q2	$0.37A	$0.29A	$0.23E
Q3	$0.48A	$0.22E	$0.26E
Q4	$0.34A	$0.47E	$0.52E

EPS: adjusted

Quarterly Revenue (M):

Q1	$201A	$256A	$773E
Q2	$219A	$352E	$342E
Q3	$244A	$342E	$360E
Q4	$226A	$541E	$579E
Year:	$890A	$1,491E	$2,053E

PORTFOLIO MANAGER BRIEF

WTRG's 2Q20 results exceeded our and consensus expectations both on the top and bottom line. Favorable weather and higher consumption patterns among residential customers offset negative impacts from COVID-19 across C&I segments, and with 3Q weather patterns that have been hot and dry (excluding Monday's wild storm across much of the Company's service territory), the set-up is there for WTRG to meet (or exceed) the top end of its 2020 guidance range, which it reaffirmed. We reiterate our BUY rating and $70 Fair Value, based on a P/E of 42x our 2021 EPS estimate of $1.67. We continue to use estimated dividend growth over a 10-year period pegged to a 1.5% U.S. 10-year T-Note yield to derive our valuation and corresponding P/E multiple.

ANALYST NOTES

- Nothing but Good News in 2Q. On the top line, revenues of $384MM were well above our forecast of $352MM (consensus was $371MM) as favorable weather (for both the natural gas and water segments) and higher residential water consumption offset negative impacts across the commercial and industrial segments. On the bottom line, EPS of $0.29 was just a touch above our $0.28 estimate, but well above consensus of $0.23.
- Acquisitions and CAPEX Tracking to Plan. Acquisitions and organic growth in 1H20 increased the company's customer count by 1.2% (full year target is 2-3%, all in the water segment). Essential has signed purchase agreements that will add the equivalent of over 200,000 water & wastewater customers ($300MM of rate base). The bulk of that growth is tied to its planned DELCORA acquisition, which is expected to close in early 2021. In terms of investments, $293MM in 1H20 thus far, with a target of $550MM in the Water segment. For the natural gas operations, $400MM is planned for 2020 (including capital invested prior to ownership).
- Dividend Increased 7%. Essential Utilities began the week by announcing a 7% dividend increase on Monday, inline with our previous expectations. We watch dividend increases closely, given we set our Fair Value assumptions based on dividend CAGR's aligned with an anticipated US 10YR TNOTE yield of 1.5% in 2030.
- Guidance Maintained. For full year 2020, the guidance highlights are: adjusted EPS in the range of $1.53 to $1.58, earnings growth CAGR of 5-7% for the 2019-2022 time period, and CAPEX of $2.8B through 2022.

RESEARCH ANALYST CERTIFICATIONS AND IMPORTANT DISCLOSURES ARE ON PAGES 3 - 4 OF THIS REPORT

- Summary/Valuation. Essential's first full quarter owning Peoples Gas generated better-than-expected results, which will likely boost investor confidence that it can hit its financial targets and integrate big acquisitions without hiccups. That should lead to expanded valuation metrics and higher share prices. The set-up for WTRG to outperform in 3Q is in place; weather has been near-perfect since the start of the quarter July 1st (excluding Monday's torrential rains up and down the East Coast); NOAA's 8-14 day weather forecasts are calling for a continuation of the trend in the Mid-Atlantic region, where the Company has significant customer concentrations. We reiterate our BUY rating and $70 Fair Value, based on a P/E of 42x our 2021 EPS estimate of $1.67. We continue to use estimated dividend growth over a 10-year period pegged to a 1.5% U.S. 10-year T-Note yield to derive our valuation and corresponding P/E multiple. Our anticipated dividend CAGR over the period is 7.5%.

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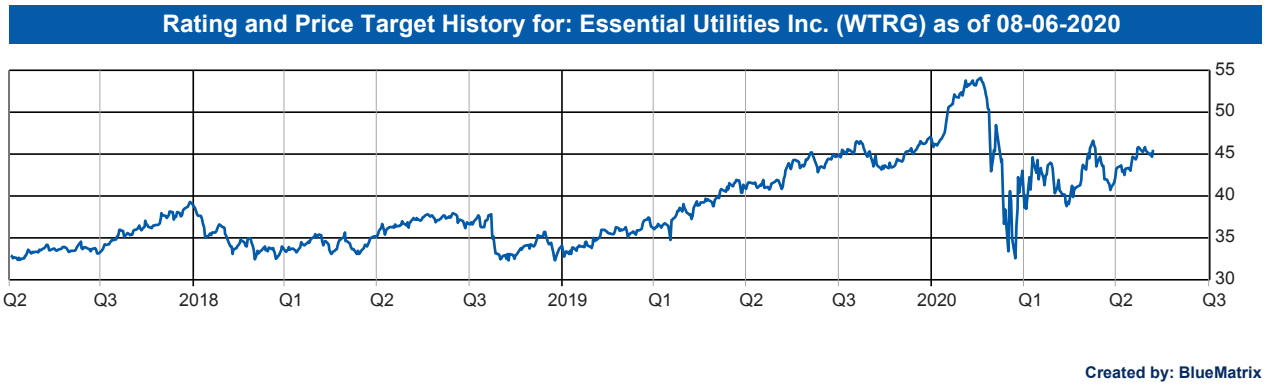

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1 July 2019

United States

EQUITIES

WTR US
Price (at 03:06, 29 Jun 2019 GMT)

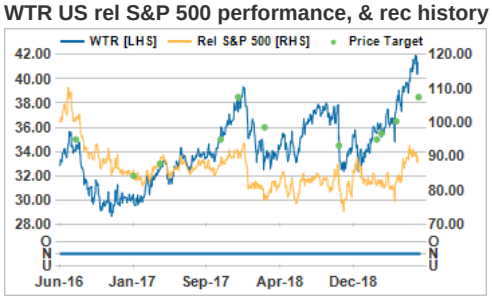
Neutral
US$41.37

Valuation - PER	US$	38.50
12-month target	US$	38.50
12-month TSR	%	-4.7
GICS sector		Utilities
Market cap	US$m	8,925
30-day avg turnover	US$m	40.8
Number shares on issue	m	215.7

Investment fundamentals

Year end 31 Dec		2018A	2019E	2020E	2021E
EPS adj	US$	1.41	1.30	1.51	1.65
EPS adj growth	%	4.5	-7.5	16.0	9.1
PER adj	x	29.4	31.8	27.4	25.1
Total DPS	US$	0.85	0.91	0.97	1.04
Total div yield	%	2.0	2.2	2.3	2.5

WTR US rel S&P 500 performance, & rec history



Note: Recommendation timeline - if not a continuous line, then there was no Macquarie coverage at the time or there was an embargo period.
Source: FactSet, Macquarie Research, July 2019
(all figures in USD unless noted)

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Aqua America (WTR US)
Not all news is good news

Key points

- Merger settlement is opposed by PAPUC's Staff.
- Peoples' gas settlement is only partial and doesn't seem to include a repair tax deduction.
- We remain on the sidelines, but boost TP to US$38.50 from US$36.50.

Event

- WTR (and AWK) have benefitted from nationalization concerns surrounding UK water utilities. Regulatory updates on WTR's pending merger with Peoples have been mixed, and so far the utilities haven't received even a tentative approval to use a repair tax deduction at Peoples. The latter seems essential for WTR to offer a positive earnings surprise for 2020 and beyond.

Impact

- **Non-unanimous merger settlement:** In early June, WTR agreed to a settlement in the Peoples merger with all but two interveners in the proceeding. The Staff of the PA PUC (I&E) disputes Peoples' treatment of a rural gas system of 1,600 connections (Goodwin/Tombaugh Gathering System), which for years has experienced gas leaks. WTR has agreed to spend US$120m in capex on the system and the spending would be recoverable through general rate cases. The I&E should present their position on the Goodwin/Tombaugh system on July 10, but for now we believe that the Staff wanted the system to be removed from Peoples' rate base and for the customers to be converted to propane, likely at Peoples' unrecoverable expense. WTR now expects an ALJ decision in late summer and the PAPUC decision by Oct/Nov.
- **Gas rate case settlement:** On Friday, Peoples reached a settlement in its pending gas rate case in PA. The settlement happened sooner than we had expected, though cancelled rate case hearings in late June suggested a settlement was imminent. We are waiting for the settlement to be made public, but for now it's our understanding that a main line replacement was excluded from the settlement and will continue to be litigated. Also, the rate case settlement doesn't seem to include any references to a future election of the repair tax deduction, which is essential to accelerate WTR's EPS growth following the Peoples deal.

Earnings and target price revision

- We updated our estimates to reflect the Peoples merger closing in late October. Our new '19/'20/'21 EPS estimates are US$1.30/1.51/1.65 vs US$1.47/1.54/1.62, respectively. We raised our TP to US$38.50 from US$36.50 to reflect a higher '21 anchor PEs for regulated water/gas utilities. Our new TP is based on 24.1x '21E water EPS plus 21.4x '21E gas EPS. Our previous TP was based on 22.8x '21E water EPS plus 21.0x '21E gas EPS.

Price catalyst

- 12-month price target: US$38.50 based on a PER methodology.
- Catalyst: Update on repair tax deduction for Peoples; 2019/2020 EPS guidance.

Action and recommendation

- We reiterate our Neutral rating.

Please refer to page 4 for important disclosures and analyst certification, or on our website www.macquarie.com/research/disclosures.

bcobrien@aquaamerica.com Ben O'Brien 07/01/19 02:00:16 PM Aqua America Inc

Fig 1 WTR: EPS proforma pending Peoples merger

	2019	2020	2021	2022
Water net income (US$m)	261.87	274.25	288.13	305.00
Gas net income (US$m)	48.14	146.16	167.76	184.54
Incremental parent interest expense after tax (US$m)	-10.5	-31.9	-31.6	-36.0
Total EPS (US$)	1.30	1.51	1.65	1.76
S/O (m)	231	257	257	257
EPS accretion vs standalone EPS (US$)	-0.17	-0.03	0.04	0.06
Water EPS	87%	71%	68%	67%
Gas EPS	13%	29%	32%	33%
Water EPS (US$)	1.13	1.07	1.12	1.19
Water PE multiple		25.3x	24.1x	22.8x
Equity value of water per share		26.95	26.96	27.11
Gas EPS (US$)	0.16	0.44	0.53	0.58
Gas PE multiple		23.1x	21.4x	19.7x
Equity value of gas per share		10.27	11.33	11.37
Total equity value per share ($)		**37.22**	**38.29**	**38.49**

Source: Macquarie Capital (USA), July 2019

Fig 2 WTR: Financial projections (US$ m except per-share data)

	2018	2019E	2020E	2021E
EBITDA	470	606	764	820
EBIT	323	454	601	648
Net interest expense	99	125	163	162
Ordinary Profit Before Tax	252	352	461	509
Income tax	1	51	73	85
Net profit	251	301	388	423
S/O (m)	**178**	**231**	**257**	**257**
Diluted EPS	**1.41**	**1.30**	**1.51**	**1.65**
DPS	**0.85**	**0.91**	**0.97**	**1.04**
Cash	5	5	5	5
Receivables	101	128	148	156
Inventory	14	18	18	18
Other short-term assets	16	16	16	16
Other-long term assets	801	801	801	801
Property, plant, and equipment	5,808	6,206	6,473	6,731
Total assets	**6,746**	**7,174**	**7,461**	**7,727**
Financial liabilities	117	117	117	117
Operating liabilities	64	81	82	84
Other liabilities	108	108	108	108
Deferred credits	2,096	2,110	2,124	2,138
Long-term debt	1,975	2,254	2,248	2,489
Shareholders' equity	2,385	2,503	2,781	2,791
Total liabilities and equity	**6,746**	**7,174**	**7,461**	**7,727**
Net income	251	301	388	423
D&A, goodwill amortisation	147	152	163	172
Other non-cash elements	25	25	25	25
Funds from operations	423	478	577	621
Non-cash working capital	8	43	22	9
Operating cash flow	430	522	599	630
Net investments in fixed assets	-555	-550	-430	-430
Net investments in financial assets	0	0	0	0
Free cash flow before dividends	-125	-28	169	200
Dividends paid	-151	-210	-250	-268
Free cash flow after dividends	-276	-238	-81	-67
Changes in capital	2	2	2	2
Changes in financial debt	273	235	78	64
Adjustment for minorities / miscellaneous	1	1	1	1
Increase in cash	1	0	0	0

Source: Company data, Macquarie Capital (USA), July 2019

Other stock mentioned: American Water Works (AWK US, US$116, Outperform, TP US$121)

bcobrien@aquaamerica.com Ben O'Brien 07/01/19 02:00:16 PM Aqua America Inc

Macquarie Quant Alpha Model Views

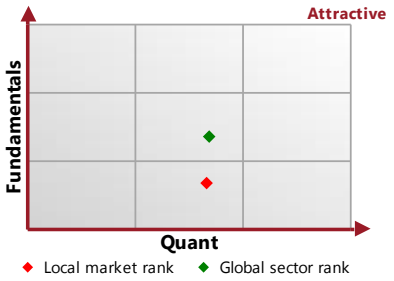
The Quant View page below has been derived from models that are developed and maintained by Sales and Trading personnel at Macquarie. The models are not a product of the Macquarie Research Department.

The quant model currently holds a marginally positive view on Aqua America. The strongest style exposure is Price Momentum, indicating this stock has had strong medium to long term returns which often persist into the future. The weakest style exposure is Valuations, indicating this stock is over-priced in the market relative to its peers.

197/448

Global rank in Utilities

% of BUY recommendations	67% (6/9)
Number of Price Target downgrades	0
Number of Price Target upgrades	2

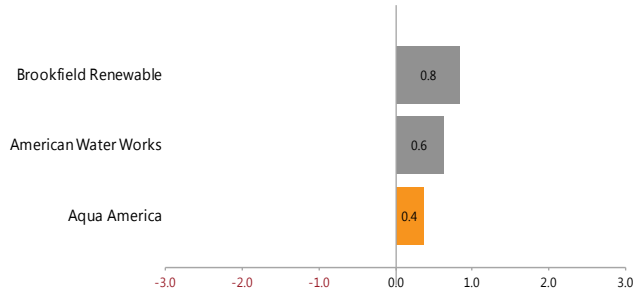


Displays where the company's ranked based on the fundamental consensus Price Target and Macquarie's Quantitative Alpha model.

Two rankings: Local market (United States) and Global sector (Utilities)

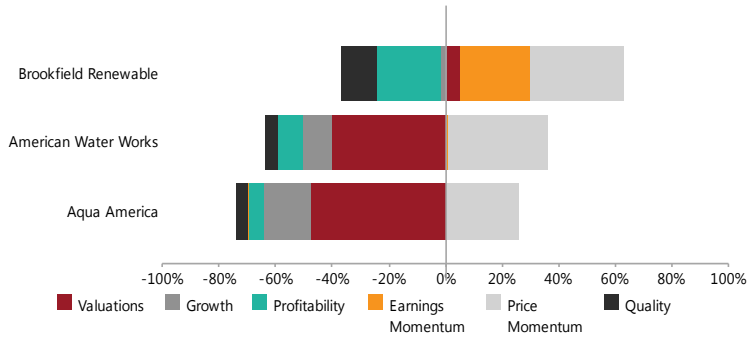
Macquarie Alpha Model ranking

A list of comparable companies and their Macquarie Alpha model score (higher is better).



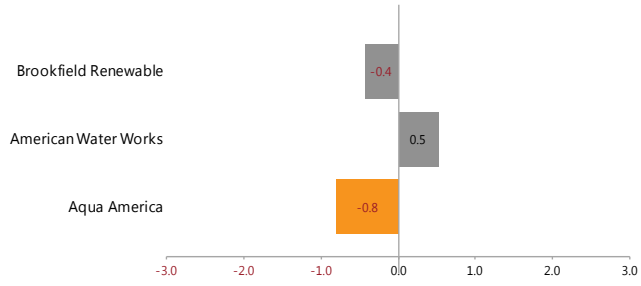
Factors driving the Alpha Model

For the comparable firms this chart shows the key underlying styles and their contribution to the current overall Alpha score.



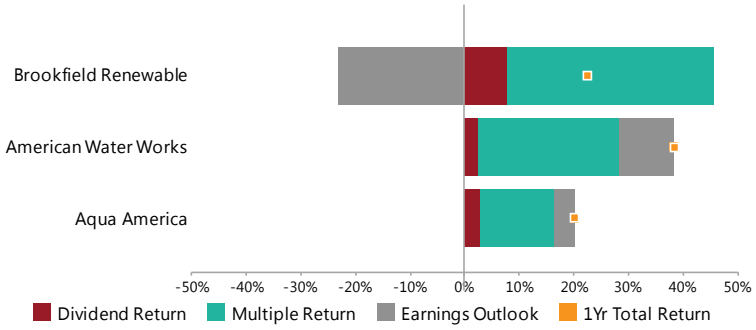
Macquarie Earnings Sentiment Indicator

The Macquarie Sentiment Indicator is an enhanced earnings revisions signal that favours analysts who have more timely and higher conviction revisions. Current score shown below.



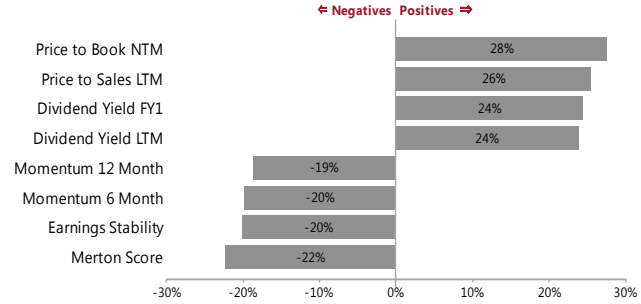
Drivers of Stock Return

Breakdown of 1 year total return (local currency) into returns from dividends, changes in forward earnings estimates and the resulting change in earnings multiple.



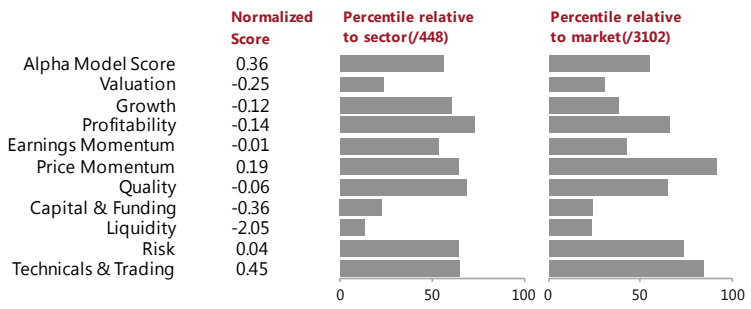
What drove this Company in the last 5 years

Which factor score has had the greatest correlation with the company's returns over the last 5 years.



How it looks on the Alpha model

A more granular view of the underlying style scores that drive the alpha (higher is better) and the percentile rank relative to the sector and market.



Source (all charts): FactSet, Thomson Reuters, and Macquarie Quant. For more details on the Macquarie Alpha model or for more customised analysis and screens, please contact the Macquarie Global Quantitative/Custom Products Group (cpg@macquarie.com)

bcobrien@aquaamerica.com Ben O'Brien 07/01/19 02:00:16 PM Aqua America Inc

Important disclosures:

Recommendation definitions

Macquarie – Asia, USA, Europe and Mazi Macquarie (SA):
Outperform – expected return >10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie - Australia/New Zealand
Outperform – expected return >10%
Neutral – expected return from 0% to 10%
Underperform – expected return <0%

Note: expected return is reflective of a Medium Volatility stock and should be assumed to adjust proportionately with volatility risk

Volatility index definition*

This is calculated from the volatility of historical price movements.

Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

Medium – stock should be expected to move up or down at least 30–40% in a year.

Low–medium – stock should be expected to move up or down at least 25–30% in a year.

Low – stock should be expected to move up or down at least 15–25% in a year.
* Applicable to select stocks in Asia/Australia/NZ

Recommendations – 12 months
Note: Quant recommendations may differ from Fundamental Analyst recommendations

Financial definitions

All "Adjusted" data items have had the following adjustments made:
Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
Excluded: non-recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

EPS = adjusted net profit / efpowa*
ROA = adjusted ebit / average total assets
ROA Banks/Insurance = adjusted net profit /average total assets
ROE = adjusted net profit / average shareholders' funds
Gross cashflow = adjusted net profit + depreciation
*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

Recommendation proportions – For quarter ending 31 March 2019

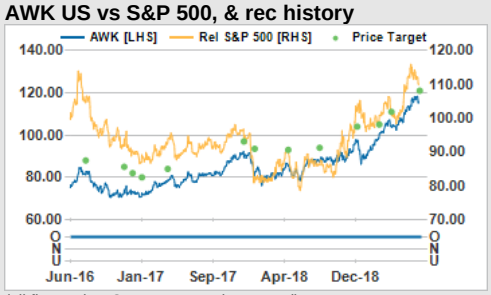
	AU/NZ	Asia	RSA	USA	CA	EUR	
Outperform	48.45%	56.50%	47.06%	51.94%	68.53%	51.76%	(for global coverage by Macquarie, 3.69% of stocks followed are investment banking clients)
Neutral	35.27%	30.15%	32.94%	42.78%	24.48%	38.19%	(for global coverage by Macquarie, 2.76% of stocks followed are investment banking clients)
Underperform	16.28%	13.35%	20.00%	5.28%	6.99%	10.05%	(for global coverage by Macquarie, 0.89% of stocks followed are investment banking clients)

Note: This table does not reflect the announced cessation of research services effective April 29, 2019, through our affiliate Macquarie Capital Markets Canada Ltd.

WTR US vs S&P 500, & rec history

(all figures in USD currency unless noted)

AWK US vs S&P 500, & rec history



(all figures in USD currency unless noted)

Note: Recommendation timeline – if not a continuous line, then there was no Macquarie coverage at the time or there was an embargo period.
Source: FactSet, Macquarie Research, July 2019

12-month target price methodology

WTR US: US$38.50 based on a PER methodology

AWK US: US$121.00 based on a Sum of Parts methodology

Company-specific disclosures:

Important disclosure information regarding the subject companies covered in this report is available at www.macquarie.com/research/disclosures.

Date	Stock Code (BBG code)	Recommendation	Target Price
01-Jul-2019	WTR US	Neutral	US$38.50
22-Apr-2019	WTR US	Neutral	US$36.50
06-Mar-2019	WTR US	Neutral	US$35.50
20-Feb-2019	WTR US	Neutral	US$35.00
24-Oct-2018	WTR US	Neutral	US$34.50
05-Mar-2018	WTR US	Neutral	US$36.00
12-Dec-2017	WTR US	Neutral	US$38.50
18-Oct-2017	WTR US	Neutral	US$35.00
11-Apr-2017	WTR US	Neutral	US$33.00
18-Jan-2017	WTR US	Neutral	US$32.00
21-Jul-2016	WTR US	Neutral	US$35.00

Target price risk disclosures:
WTR US: Our US$38.50 TP is based on 25x our proforma '21 water EPS and 21.2x proforma '21 gas EPS. Risks include: regulatory conditions for the Peoples acquisition, outcomes of pending and future rate cases, especialy in PA, cost controls, municipal M&A, and the level of market interest rates.
AWK US: Our US$111 TP is based on our 2021 SOTP. Risks to the downside include: the slower pace of future municipal acquisitions, lower cost efficiencies, and slower growth in non-regulated operations.

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Analyst certification:
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This publication was disseminated on 01 July 2019 at 07:34 UTC.

8 August 2019

United States

EQUITIES

WTR US
Price (at 22:52, 07 Aug 2019 GMT)

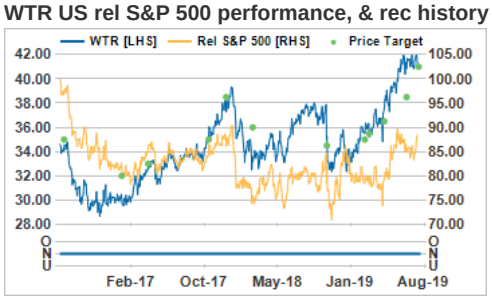
Neutral
US$42.06

Valuation - PER	US$	41.44
12-month target	US$	41.00
12-month TSR	%	-0.3
GICS sector		Utilities
Market cap	US$m	9,072
30-day avg turnover	US$m	37.3
Number shares on issue	m	215.7

Investment fundamentals

Year end 31 Dec		2018A	2019E	2020E	2021E
EPS adj	US$	1.41	1.30	1.54	1.68
EPS adj growth	%	4.5	-7.3	17.8	9.1
PER adj	x	29.9	32.3	27.4	25.1
Total DPS	US$	0.85	0.91	0.97	1.04
Total div yield	%	2.0	2.2	2.3	2.5

WTR US rel S&P 500 performance, & rec history



Note: Recommendation timeline - if not a continuous line, then there was no Macquarie coverage at the time or there was an embargo period.
Source: FactSet, Macquarie Research, August 2019
(all figures in USD unless noted)

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Aqua America (WTR US)
Pipe dream

Key points

- As a pure-play water utility, WTR would likely be trading 12% higher than currently.
- Peoples deal seemed based on repair tax deduction, but WTR is still studying it.
- Then again, repair tax deduction would just pull forward future earnings.

Event

- We've been watching WTR's pursuit of a gas utility from afar. For now, it seems like WTR's stock would likely be trading 12% higher than currently if the company had just remained a pure-play water utility. The repair tax deduction at Peoples Gas in PA could change the math, but that's likely months away.
- WTR's 2Q19 EPS of US$0.37 was in line with consensus, but excluded a US$0.02 dilution related to the higher share count associated with the Peoples deal. Inclusive of the dilution, WTR's results were in line with our US$0.35 expectation.

Impact

- **A trade-off between PE and EPS growth:** For the five years before the Peoples deal announcement, WTR traded on par with AWK on FY2 PE, though WTR grew EPS at a 4% CAGR over this period and AWK at almost 9%. If WTR had remained a pure-play water utility growing at 4-4.5% annually and the PE parity persisted, we estimate WTR would now be trading at ~US$47/share or almost 12% higher than yesterday's close. WTR currently trades at a 10% '20 PE discount to AWK on our US$1.54/sh '20 proforma EPS, though the deal is EPS neutral then.
- **Repair tax deduction at Peoples:** The diversification into the gas sector was widely expected to weigh on WTR's PE multiple, but in exchange was to align WTR's EPS growth with the 7% water rate base growth, which should happen by '21, we believe. The growth rate could be even higher depending on the repair tax deduction in PA for Peoples, but for now the US$265m (and counting) in deal fees hasn't created much shareholder value, we believe. Peoples Gas' rate case settlement in PA does not include a repair tax deduction, and WTR plans to pursue it only in '20 once it completes the assessment of how much of Peoples' capex would qualify for repair tax expensing. The repair tax was likely the core assumption underpinning the deal's EPS accretion.

Earnings and target price revision

- We raise our estimates to reflect a lower fully diluted share count assuming conversions of tangible equity units at higher stock prices. Our new '19/'20/'21 EPS estimates are US$1.30/1.54/1.68 vs US$1.30/1.51/1.65 previously. We raise our TP to US$41 from US$38.50. The TP remains based on 1.4x our '21 PE anchor for electric utilities for water and 1.2x for WTR's gas business.

Price catalyst

- 12-month price target: US$41.00 based on a PER methodology.
- Catalyst: Analyst day (Dec 5).

Action and recommendation

- We reiterate our Neutral rating.

Please refer to page 4 for important disclosures and analyst certification, or on our website www.macquarie.com/research/disclosures.

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Fig 1 WTR: EPS proforma pending Peoples merger

	2019E	2020E	2021E	2022E
Water net income (US$m)	261.87	274.25	288.13	305.00
Gas net income (US$m)	48.14	146.16	167.76	184.54
Incremental parent interest expense after tax (US$m)	-10.5	-31.9	-31.6	-36.0
Total EPS (US$)	1.30	1.54	1.68	1.79
S/O (m)	230	253	253	253
EPS accretion vs standalone EPS (US$)	-0.16	0.00	0.06	n/a
Water EPS	87%	71%	68%	67%
Gas EPS	13%	29%	32%	33%
Water EPS (US$)	1.14	1.08	1.14	1.21
Water PE multiple		27.2x	25.9x	24.6x
Equity value of water per share		29.48	29.50	29.66
Gas EPS (US$)	0.16	0.45	0.54	0.59
Gas PE multiple		23.8x	22.2x	20.6x
Equity value of gas per share		10.73	11.95	12.12
Total equity value per share		**40.21**	**41.44**	**41.78**

Source: Macquarie Capital (USA), August 2019

Fig 2 WTR: Financial projections (US$m except per share data)

	2018	2019E	2020E	2021E
EBITDA	470	605	765	821
EBIT	323	453	602	649
Net interest expense	99	125	163	162
Ordinary Profit Before Tax	252	351	462	510
Income tax	1	51	74	85
Net profit	251	300	389	424
S/O (m)	**178**	**230**	**253**	**253**
Diluted EPS	**1.41**	**1.30**	**1.54**	**1.68**
DPS	**0.85**	**0.91**	**0.97**	**1.04**
Cash	5	716	293	5
Receivables	101	128	148	156
Inventory	14	18	18	18
Other short-term assets	16	16	16	16
Other-long term assets	801	801	801	801
Property, plant, and equipment	5,808	6,206	6,473	6,731
Total assets	**6,746**	**7,884**	**7,749**	**7,727**
Financial liabilities	117	117	117	117
Operating liabilities	64	81	82	84
Other liabilities	108	108	108	108
Deferred credits	2,096	2,110	2,124	2,138
Long-term debt	1,975	2,254	2,248	1,904
Shareholders' equity	2,385	3,214	3,069	3,376
Total liabilities and equity	**6,746**	**7,884**	**7,749**	**7,727**
Net income	251	300	389	424
D&A, goodwill amortisation	147	152	163	172
Other non cash elements	25	25	25	25
Funds from operations	423	477	577	622
Non-cash working capital	8	43	22	9
Operating cash flow	430	521	600	631
Net investments in fixed assets	-555	-550	-430	-430
Net investments in financial assets	0	0	0	0
Free cash flow before dividends	-125	-29	170	201
Dividends paid	-151	-209	-246	-263
Free cash flow after dividends	-276	-238	-76	-62
Changes in capital	2	1,298	2	2
Changes in financial debt	273	-350	-350	-228
Adjustment for minorities / miscellaneous	1	1	1	1
Increase in cash	1	711	-423	-288

Source: Company data, Macquarie Capital (USA), August 2019

Stocks mentioned:

American Water Works (AWK US, US$117.42, Outperform, TP: US$121.00)

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Macquarie Quant Alpha Model Views

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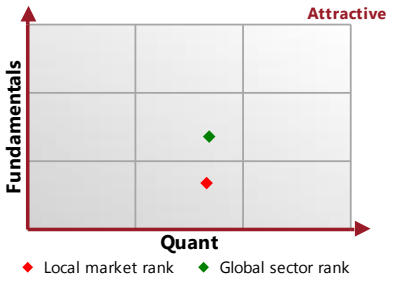
The quant model currently holds a marginally positive view on Aqua America. The strongest style exposure is Price Momentum, indicating this stock has had strong medium to long term returns which often persist into the future. The weakest style exposure is Valuations, indicating this stock is over-priced in the market relative to its peers.

197/448

Global rank in Utilities

% of BUY recommendations	67% (6/9)
Number of Price Target downgrades	0
Number of Price Target upgrades	2

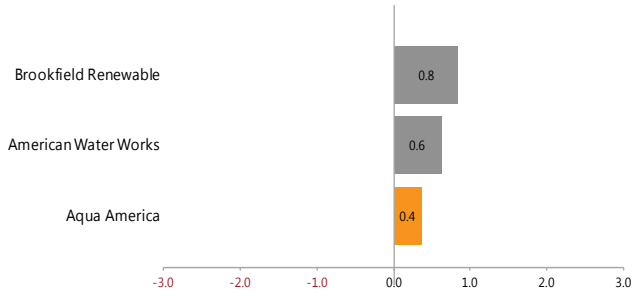


Displays where the company's ranked based on the fundamental consensus Price Target and Macquarie's Quantitative Alpha model.

Two rankings: Local market (United States) and Global sector (Utilities)

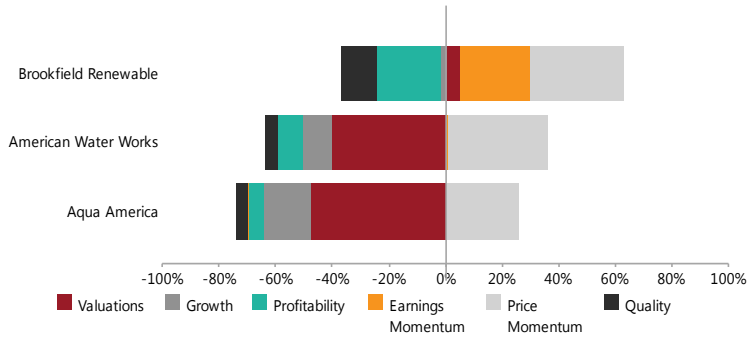
Macquarie Alpha Model ranking

A list of comparable companies and their Macquarie Alpha model score (higher is better).



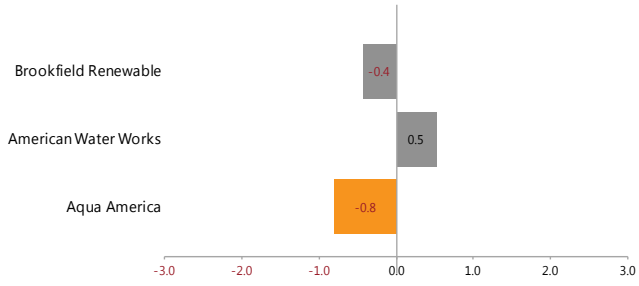
Factors driving the Alpha Model

For the comparable firms this chart shows the key underlying styles and their contribution to the current overall Alpha score.



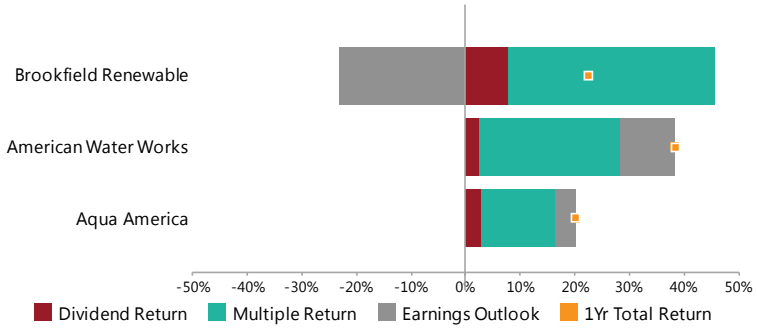
Macquarie Earnings Sentiment Indicator

The Macquarie Sentiment Indicator is an enhanced earnings revisions signal that favours analysts who have more timely and higher conviction revisions. Current score shown below.



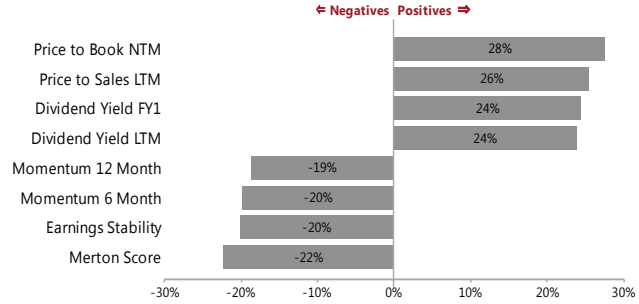
Drivers of Stock Return

Breakdown of 1 year total return (local currency) into returns from dividends, changes in forward earnings estimates and the resulting change in earnings multiple.



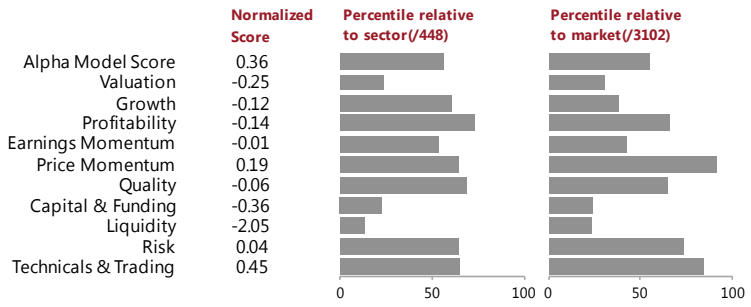
What drove this Company in the last 5 years

Which factor score has had the greatest correlation with the company's returns over the last 5 years.



How it looks on the Alpha model

A more granular view of the underlying style scores that drive the alpha (higher is better) and the percentile rank relative to the sector and market.



Source (all charts): FactSet, Thomson Reuters, and Macquarie Quant. For more details on the Macquarie Alpha model or for more customised analysis and screens, please contact the Macquarie Global Quantitative/Custom Products Group (cpg@macquarie.com)

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Important disclosures:

Recommendation definitions

Macquarie – Asia, USA, Europe and Mazi Macquarie (SA):
Outperform – expected return >10%
Neutral – expected return from -10% to +10%
Underperform – expected return <-10%

Macquarie - Australia/New Zealand
Outperform – expected return >10%
Neutral – expected return from 0% to 10%
Underperform – expected return <0%

Note: expected return is reflective of a Medium Volatility stock and should be assumed to adjust proportionately with volatility risk

Volatility index definition*

This is calculated from the volatility of historical price movements.

Very high–highest risk – Stock should be expected to move up or down 60–100% in a year – investors should be aware this stock is highly speculative.

High – stock should be expected to move up or down at least 40–60% in a year – investors should be aware this stock could be speculative.

Medium – stock should be expected to move up or down at least 30–40% in a year.

Low–medium – stock should be expected to move up or down at least 25–30% in a year.

Low – stock should be expected to move up or down at least 15–25% in a year.
* Applicable to select stocks in Asia/Australia/NZ

Recommendations – 12 months
Note: Quant recommendations may differ from Fundamental Analyst recommendations

Financial definitions

All "Adjusted" data items have had the following adjustments made:
Added back: goodwill amortisation, provision for catastrophe reserves, IFRS derivatives & hedging, IFRS impairments & IFRS interest expense
Excluded: non recurring items, asset revals, property revals, appraisal value uplift, preference dividends & minority interests

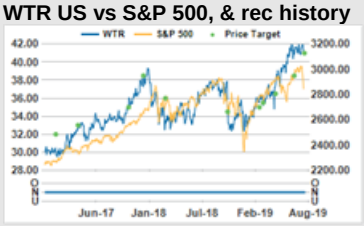
EPS = adjusted net profit / efpowa*
ROA = adjusted ebit / average total assets
ROA Banks/Insurance = adjusted net profit /average total assets
ROE = adjusted net profit / average shareholders funds
Gross cashflow = adjusted net profit + depreciation
*equivalent fully paid ordinary weighted average number of shares

All Reported numbers for Australian/NZ listed stocks are modelled under IFRS (International Financial Reporting Standards).

Recommendation proportions – For quarter ending 30 June 2019

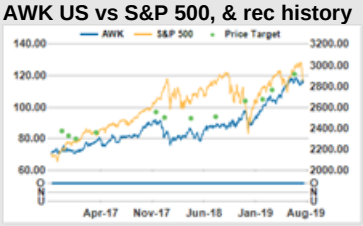
	AU/NZ	Asia	RSA	USA	EUR	
Outperform	47.41%	58.03%	49.38%	52.16%	51.95%	(for global coverage by Macquarie, 3.22% of stocks followed are investment banking clients)
Neutral	36.30%	29.24%	32.10%	42.65%	40.69%	(for global coverage by Macquarie, 3.02% of stocks followed are investment banking clients)
Underperform	16.30%	12.74%	18.52%	5.19%	7.36%	(for global coverage by Macquarie, 0.96% of stocks followed are investment banking clients)

WTR US vs S&P 500, & rec history



(all figures in USD currency unless noted)

AWK US vs S&P 500, & rec history



(all figures in USD currency unless noted)

Note: Recommendation timeline – if not a continuous line, then there was no Macquarie coverage at the time or there was an embargo period.
Source: FactSet, Macquarie Research, August 2019

12-month target price methodology

WTR US: US$41.00 based on a PER methodology

AWK US: US$121.00 based on a Sum of Parts methodology

Company-specific disclosures:
WTR US: The primary analyst has not visited this company's material operations and development assets within the past year.
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Clients receiving this report can additionally access previous recommendations (from the year prior to publication of this report) issued by this report's author at https://www.macquarieinsights.com.

Date	Stock Code (BBG code)	Recommendation	Target Price
01-Jul-2019	WTR US	Neutral	US$38.50
22-Apr-2019	WTR US	Neutral	US$36.50
06-Mar-2019	WTR US	Neutral	US$35.50
20-Feb-2019	WTR US	Neutral	US$35.00
24-Oct-2018	WTR US	Neutral	US$34.50
05-Mar-2018	WTR US	Neutral	US$36.00
12-Dec-2017	WTR US	Neutral	US$38.50
18-Oct-2017	WTR US	Neutral	US$35.00
11-Apr-2017	WTR US	Neutral	US$33.00
18-Jan-2017	WTR US	Neutral	US$32.00
21-Jul-2016	WTR US	Neutral	US$35.00

Target price risk disclosures:
WTR US: Our US$41 TP is based on 25.9x our proforma '21 water EPS and 22.2x proforma '21 gas EPS. Risks include: regulatory conditions for the Peoples acquisition, outcomes of pending and future rate cases, especialy in PA, cost controls, municipal M&A, and the level of market interest rates.
AWK US: Our US$121 TP is based on our 2021 SOTP. Risks to the downside include: the slower pace of future municipal acquisitions, lower cost efficiencies, and slower growth in non-regulated operations.

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Sensitivity analysis:
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Analyst certification:
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Marquis, Renee T

From: Tucker, Shelby <SPARC@rbccm.com>
Sent: Monday, January 11, 2021 9:23 AM
To: Marquis, Renee T
Subject: [EXTERNAL] Essential Utilities (WTRG): Initiates 2021 guidance in line with RBC and consensus, reaffirms 2020 guidance, introduces voluntary emissions reductions goals (RBC SPARC)

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RBC Capital Markets — RBC Insight — Research

Essential Utilities (WTRG): Initiates 2021 guidance in line with RBC and consensus, reaffirms 2020 guidance, introduces voluntary emissions reductions goals

Sentiment Indicator : positive

Produced by Tucker, Shelby (RBC Capital Markets, LLC) on Monday, January 11, 2021, 09:18 AM ET

Disseminated on Monday, January 11, 2021, 09:22 AM ET

Our view: WTRG introduced 2021 EPS guidance of $1.64-$1.69, in line with our estimate of $1.68 and consensus of $1.67. Management also reaffirmed its guidance to the upper end of its 2020 EPS range of $1.53-$1.58. WTRG announced its voluntary goal of reducing 60% of its Scope 1 and Scope 2 emissions by 2035 off 2019 levels, which applies to all its operations across gas, water and wastewater. On the guidance call today, we look forward to management's comments on DELCORA, updates on the proceeding for the catch-up portion of repair tax at Peoples, the timing of drawing down equity from its forward sale and the acquisition pipeline.

Essential Utilities (WTRG, Outperform, $48.72) initiated 2021 EPS guidance of $1.64-$1.69 and reaffirmed its 2020 EPS guidance to the upper end of the $1.53-$1.58 range. We are at $1.57.

DELCORA updates. Following the judge's ruling in December that upheld the validity of DELCORA's asset purchase agreement, WTRG expects a PA PUC Administrative Law Judge recommended decision in January and the DELCORA acquisition to close in the 2Q21.

Slight upward adjustments to capex and rate base. Estimated 2021 capex is $1 billion, compared to the 2020 capex spend of $950 million. The 2021-2023 capex plan stands at $3 billion, an increase from the 2020-2022 plan of $2.8 billion. This results in higher gas rate base estimates in 2021 and 2022 by $100 million and a higher 2022 water rate base estimate by $100 million. 2023 combined water and gas rate base is now estimated at $9.8 billion. Water rate base is still expected to grow at a 6-7% CAGR, excluding acquisitions, and gas is expected to grow at a 8-10% CAGR.

Conference call today at 11:00am ET. Dial in at (800)-367-2403, passcode 1177890.

Company Name	Exchange	Ticker	Rating	Risk Qualifier	Price Target	Currency	Price	Price Date
Essential Utilities Inc	NYSE	WTRG US	Outperform	Not Assigned	49.00	US Dollar	48.72	11 Jan 2021 08:29:00 ET

RBC Capital Markets, LLC
Shelby Tucker (Analyst) | (212) 428-6462 | shelby.tucker@rbccm.com

Visit our Research Portal here

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EQUITY RESEARCH INITIATION

Capital Markets

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Shelby Tucker, CFA (Analyst)
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shelby.tucker@rbccm.com

April 24, 2020

Essential Utilities Inc

Water and Gas Do Mix After All; Initiating at Outperform

Our view: We fundamentally see Essential Utilities as trading at a discount to its 70% water/30% gas mix. While it has lost some of its ESG/water valuation veneer when it acquired Peoples Gas, we believe the "punishment does not fit the crime". Peoples is a fast-growing gas utility; the water segment should grow through active consolidation. Our sum-of-the-parts suggests $49 of value, which justifies our Outperform rating.

Key points:

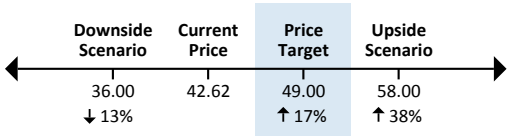
- **Essential Utilities is still primarily a water utility.** Essential Utilities (WTRG, formerly known as Aqua America) owns the second largest water utility in the country behind American Water Works. As such, it partakes in many of the broad themes that dominate the water sector: tremendous infrastructure upgrade needs, consolidation including municipal roll-ups, and, for the most part, supportive regulation. Seven out of the eight states in which WTRG's water segment, Aqua, operate have Fair Market Value legislation. Given this, we expect the company to continue to be active in water acquisitions, as exemplified by its $276.5 million pending acquisition of DELCORA, a wastewater municipal provider in Pennsylvania. Our model assumes ~$100 million of annual water acquisitions.
- **Peoples Gas is the right vehicle.** After a lot of fits and starts, WTRG finally closed mid-March its acquisition of Peoples Gas (PNG), a gas utility (LDC) with operations in Pennsylvania, West Virginia, and Kentucky. While investors can debate the wisdom for a water utility to buy a gas utility, we would be hard pressed to find a gas LDC that offers as many opportunities as Peoples does for WTRG. Both are anchored in PA, thus sharing common regulatory relationships, but PNG is in Western PA while Essential's Aqua America covers Eastern PA. This may open opportunities for WTRG to connect with water systems in the west that might have been hard to achieve otherwise. Furthermore, opportunities may exist in WV and KY for water consolidation, although Aqua is not in those states. Furthermore, Peoples Gas has multi-decade backlog of pipeline replacement that should assume strong growth for years to come.
- **Mix of business suggests $49 price target.** We believe that the best way to value the company is by assigning parent costs proportionally to Aqua and to Peoples then assign respective P/E multiples. Our base low-growth (secular) forward P/E multiples for water and gas are 24.9x and 19.3x, respectively. Given that both utilities are growing better than 4% and 3.5%, respectively, we assign a 25% premium for Aqua and 30% for People, to arrive at a blended 29.1x P/E multiple.

Outperform

NYSE: WTRG; USD 42.62

Price Target USD 49.00

Scenario Analysis*



*Implied Total Returns

Key Statistics

Shares O/S (MM):	245.0	Market Cap (MM):	10,442
Dividend:	0.92	Yield:	2.2%
		Avg. Daily Volume:	1,411,456

RBC Estimates

FY Dec	2019A	2020E	2021E	2022E
EPS, Adj Diluted	1.47	1.21	1.67	1.78
P/AEPS	29.0x	35.2x	25.5x	23.9x
DPS	0.91	0.97	1.04	1.11
Div Yield	2.1%	2.3%	2.4%	2.6%

All values in USD unless otherwise noted.

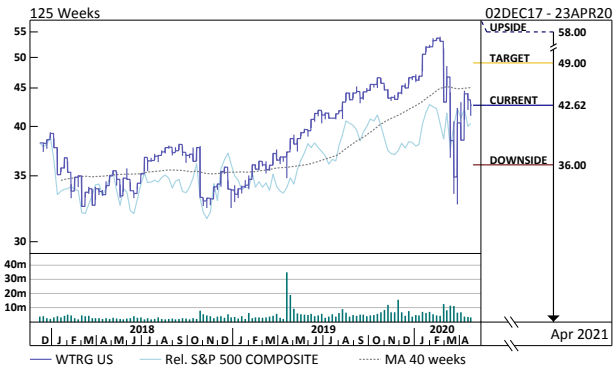
Disseminated: Apr 24, 2020 00:45ET; Produced: Apr 24, 2020 00:36ET Priced as of prior trading day's market close, EST (unless otherwise noted).

For Required Conflicts Disclosures, see Page 37.

RBC Capital Markets appreciates your consideration in the 2020 Institutional Investor All-America Research Team survey.

Target/Upside/Downside Scenarios

Exhibit 1: Essential Utilities, Inc.



Source: Bloomberg and RBC Capital Markets estimates for Upside/Downside/Target

Price target/base case

We derive our $49 price target by taking our 2021 EPS of $1.67 and using a sum of parts to account for the water and gas operating segments. We apply a 25% premium to our base multiple of 24.9x P/E for water utilities and a 30% premium to our base multiple of 19.3x P/E for gas utilities, given both utilities' greater-than-average growth rates.

Upside scenario

Our upside value of $58 assumes that WTRG executes on greater-than-expected M&A and sees even stronger-than-projected base growth at Peoples. To our 2021E EPS of $1.67 we apply 50% premium to our base multiple of 24.9x P/E for water utilities and a 50% premium to our base multiple of 19.3x P/E for gas utilities.

Downside scenario

Our downside value of $36 assumes the company does not execute on as much M&A as we forecast and that its credit metrics weaken over time, causing the company to issue equity and potentially dilute its share price. To our 2021E EPS of $1.67 we apply -10% discount to our base multiple of 24.9x P/E for water utilities and use our base multiple of 19.3x P/E for gas utilities.

Investment summary

WTRG's acquisition of Peoples and expansion into the natural gas industry creates a strong platform for future growth. We expect to see a significant amount of organic growth at Peoples as well as growth through acquisitions at the water segments. We believe WTRG's water and gas presence in ten states sets it up nicely to expand its footprint. The growing presence of Fair Market Value legislation that allows IOUs to purchase municipal systems at fair value without incurring meaningful goodwill provides a strong backdrop that should encourage transactions. We are initiating coverage with a $49 price target and an Outperform rating.

Potential catalysts:

- Increased adoption of Fair Market Value legislation opens up greater opportunities for WTRG to transact.
- Greater geographic footprint proves advantageous from an M&A standpoint, increasing the amount of acquisitions.

Risks to call:

- Lower-than-anticipated adaptation of fair market value principles across the country could dampen expectations.
- M&A transactions could require greater equity than we forecast, or could result in a weaker balance sheet than we expect.
- Less favorable regulations or disruptions within public utility commissions could weigh on growth.
- Climate variability may cause increased volatility in weather and may impact water usage and related revenue, which may not be recoverable through rates.
- Continued lockdown from coronavirus could impact revenues, through higher bad debt expenses.
- ESG investing continues to gain traction, but WTRG does not meet certain ESG criteria due to Peoples, which makes it harder to benefit from these increased flows.

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Key Questions

		Our view
1.	**Is it worth getting into the stock when it is trading at 27.0x NTM P/E?**	The answer depends on how much premium is attributed to ESG for a water-gas multi-utility. In our sum-of-the-parts analysis, we expect water/gas to contribute 70%/30% to 2021E EPS of $1.67. For water valuation, we look to the industry leader American Water Works (NYSE: AWK), which we have assumed a 35% premium above the water base P/E of 24.9x. While Aqua doesn't have the size of AWK, we believe rate base is supported by substantial capex opportunities. Nonetheless, the introduction of natural gas removes some of the ESG appeal. We apply a 25% premium to our water base P/E of 24.9x, resulting in a P/E multiple of 31.1x. Gas valuation is more straightforward. We apply a 30% premium to our gas base P/E of 19.3x, resulting in a P/E multiple of 25.1x, which we consider appropriate due to above-average rate base growth. The sum of the parts results in a blended P/E of 29.4x and total potential return of 17.0% inclusive of a 2.2% dividend yield. Our valuation suggests an attractive entry point.
2.	**What does water-gas combo mean to Essential?**	While the addition of PNG doesn't alter the regulated utility model and should be earnings accretive, it challenges the way we think about valuation as noted above. On a standalone basis, it seems clear to us that PNG now deserves a premium to valuation from its higher-than-average rate base growth (the company expects to see an 8-10% CAGR between 2019 and 2022, vs. peer utility average of 6-7%) following a period of underinvestment. On a consolidated basis, while Aqua remains a solid business, we could contemplate a discount to the lofty valuation that a pure-play water utility typically enjoys, with the involvement of natural gas and a less stellar balance sheet. In some way, the lack of an appropriate comp for a water and gas combo suggest that we are in uncharted territory.
3.	**How do balance sheet metrics fare post-PNG merger?**	Balance sheet looks less padded. We expect Essential to focus on deleveraging over the next few years. We see FFO-to-debt stabilizing in low-teens and debt-to-capital in the mid-fifties by 2023. Compared to water peers, these metrics seem may be on the lower end. However, thresholds for water utilities tend to be lower, with FFO-to-debt threshold at the 9-10% range. Currently, bonds at Essential and PNG are rated A/Baa2 and A/Baa1.
4.	**Will Fair Market Value legislation continue to expand?**	The rise of fair market value is becoming the preferred alternative to the traditional depreciated original cost method, providing mutually beneficial outcomes to both the buyer and seller of municipal systems. Sellers are able to capture the true value of their assets while buyers are allowed to add the total purchase price to rate base, without padding goodwill, dubbing the premium an "acquisition adjustment".
5.	**What are the unique characteristics of the water utility sector vs its electric and gas peers?**	The industry is 2x more capital intensive than the electric sector and 3x more than the gas sector. Despite this, water utilities generally spend the least amount of O&M dollars to maintain their assets. Over the past 20 years, water utility O&M expenses as a percent of PP&E averaged 20% compared to gas utilities of 40% and electric utilities of 60%. Further, the net PP&E to revenues ratio for investor-owned water utilities is about 5.0x, compared to electric utilities of 3.4x and natural gas utilities of 2.3x. In our view, this showcases the importance of infrastructure spending as a key characteristic of the industry's cost structure, making it difficult to reduce capital costs.

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Investment Summary

Essential Utilities Inc. (f.k.a. Aqua America, Inc.) is the second largest water and wastewater utility in the U.S., with a market capitalization of $10.6 billion. Before its entry into natural gas, Essential generated virtually all of its revenues through its regulated water utility segment (99.6% of sales) as of 2019, serving an estimated three million customers located primarily in states along the Rust Belt and Texas. On February 3, 2020, the company changed its corporate name to Essential Utilities Inc. following the acquisition of Peoples Natural Gas (PNG), and transformed into gas-water multi-utility with an expanded footprint. We expect water to remain the main contributor to earnings (70%) in 2020, though there are compelling growth opportunities across both segments. To a smaller extent, Essential also operates certain non-utility activities through Aqua Resources and Aqua Infrastructure.

Initiating coverage with $49 price target and Outperform rating. We view Essential as a solid water and gas multi-utility with substantial rate base investment opportunities in both segments. Post-merger with Peoples Natural Gas, Essential extends its operating territory to 10 states including the rust belt and Texas, with a combined rate base of $7.3 billion. The company remains deeply rooted in Pennsylvania, where 66% of combined customers are located. With the addition of PNG, Essential doubles its annual capex to ~$1 billion for 2020. From 2019 through 2022, the company expects to see to its water rate base grow at a 6-7% CAGR and its gas rate base to grow at an 8-10% CAGR. On a consolidated basis, we expect EPS to grow at a 6-7% CAGR during this time frame, an increase from a 4% CAGR between 2015 and 2019 as a pure-play water utility.

We view the regulatory environment in which Essential operates as constructive. More than half of Essential's annual capex is eligible for automatic recovery through surcharges. Further, at the water utilities, seven out of eight states have adopted the so-called Fair Market Value legislation (FMV). Under FMV, goodwill is added to rate base instead of being hung up on the balance sheet. This in turn encourages industry consolidations. Of course, not all deals are created equally. On average, we estimate $0.01 EPS accretion for every $50 million acquisition spend. Including DELCORA's $300 million acquisition (expected close early 2021), Essential has identified opportunities of various sizes that could add up to 320,000 customers, or ~10% of existing total. We also point to the eligibility of tax repair treatment which makes the PNG transaction particularly earnings accretive. Upon election with the IRS, the treatment allows previously capitalized repair costs to be expensed, resulting in higher deductions and lower tax expense without jeopardizing customer bills. An additional look-back deduction would also eligible, but requires some form of approval from the Pennsylvania PUC. We think the ability to stay away from rate cases, as in the case of Aqua Pennsylvania is especially valuable.

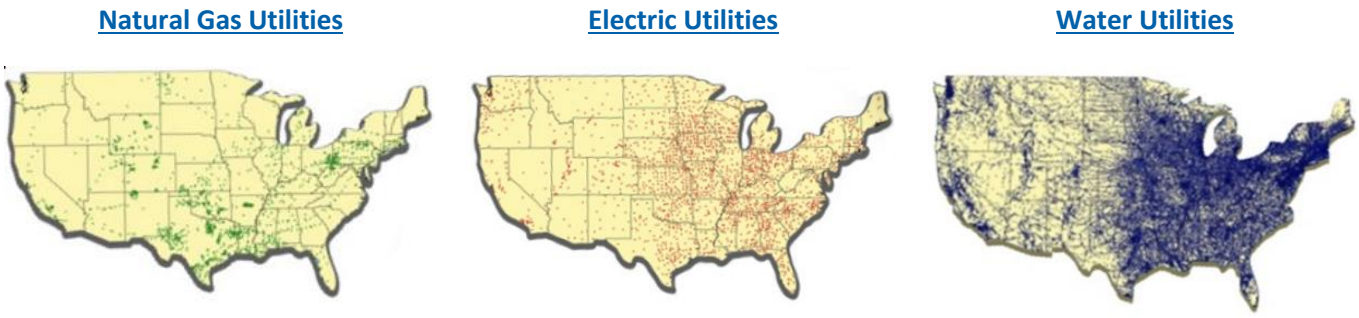
In our view, water and gas is a winning combo. Water remains Essential's core business and enjoys the benefits of an ESG play. Gas, via PNG, provides fast, complementary growth which differentiates Essential from water peers. While 2020 could be an "off-year" with a partial contribution from PNG and management focused on deleveraging, we see Essential getting back on track in 2021. The market has penalized the stock for introducing natural gas in the picture. We believe the "punishment does not fit the crime" and are bullish on the stock. We also recognize that the ESG investing movement has hit a temporary pause. As markets find some degree of normalcy – not necessarily recovery – we expect the movement to regain steam. We see Essential as one of the main beneficiaries of that trend despite its gas business.

Investment Highlights

Municipal acquisitions drive accretion

Fragmented industry ripe for municipal acquisitions. The U.S. water and wastewater industry is heavily commoditized. The fragmented nature of the water industry is highlighted by the roughly 50,000 water systems in the U.S. and about 15,000 community wastewater systems compared to 1,400 gas systems and 3,800 electric systems. Roughly 84% and 98% of the U.S. population is served by municipal water systems and wastewater systems, respectively, according the Environmental Protection Agency (EPA). This underscores the thirst for industry consolidation, in our view. Notably, investor-owned utilities only serve about 16% of the total population.

Exhibit 2: U.S. water among the most fragmented utility sectors



Source: Enviornmental Protection Agency and Energy Information Administration

Fair Market Value legislation has encouraged deal-making. Municipal acquisitions have become a popular theme over the last several years driven by a more favorable regulatory backdrop. The rise of FMV assessment of water and wastewater systems is becoming the preferred alternative to the traditional depreciated original cost method, providing mutually beneficial outcomes to both the buyer and seller of municipal systems. Sellers are able to capture the true value of their assets while buyers are allowed to add the total purchase price to rate base, without padding goodwill, dubbing the premium an “acquisition adjustment”. Currently, 12 states have implemented the measure. We estimate every $50 million (in line with historical average) that Essential deploys towards municipal acquisitions adds a run rate $0.01 to EPS. Kentucky is the only state under Essential’s operating jurisdiction that has not enacted FMV legislation.

Infrastructure surcharges permit rate adjustments outside of rate cases

Regulatory mechanisms that permit investor-owned utilities to adjust rates outside of general rate cases are referred to as infrastructure surcharges. These surcharges generally permit recovery of capital investments multiple times a year, and creates significant flexibility between rate cases. While the main benefit is to reduce regulatory lag, surcharges also allows utilities to stay away from a full rate case which subjects their rate base ROE and equity ratio to review by state commissions. In some way, utilities are able to preserve outperformance by avoiding rate cases. Surcharges come in many forms and are specific to states. For Essential, the main surcharges are the Distribution System Improvement Charge (DSIC), the Water and Sewer System Improvement Charge (WSSIC), and the Qualifying Infrastructure Plant Surcharge (QIPS). Post-PNG transaction, the Pipeline Replacement Program (PRP) also became available. The chart below illustrates the various mechanisms by state and their respective allowed surcharge.

Exhibit 3: Various surcharges employed by Essential, by state

AQUA

State	PA	IN	OH	NJ	IL	NC
Mechanism	DSIC	DSIC	SIC	DSIC	QIPS	WSSIC
Allowed Surcharge	7.5% W 5% WW	10%	12.75% W 9% WW	5%	2.5% average annual increase	5%

PEOPLES

State	PA	KY
Mechanism	DSIC	PRP
Allowed Surcharge	5%	No cap

Source: Company Presentation

Management estimates 52% of total capex between 2020 and 2022 are surcharge-eligible, while the remaining 4% must go through standard rate making. By segment, 46%/58.7% are surcharge-eligible for water/gas. We view these statistics a key component of Essential's robust capital program and long-term EPS growth.

Outsized rate base expansion; PNG as a new platform for growth

The Peoples acquisition creates a strong growth opportunity. Under its previous ownership, Peoples was severely underinvested in and now requires significant upgrades to its infrastructure. The system requires nearly 3,000 miles of gas pipeline replacement. With its accelerated pipe replacement program, the company expects rate base to grow organically at an 8-10% CAGR over the next three years. The election of repair tax at Peoples further increases earnings potential, which we discuss in more detail further down.

The acquisition of PNG represents new but complementary territory to the core water business. Peoples serves territories in Pennsylvania, Kentucky, and West Virginia. Aqua Pennsylvania's footprint is in the eastern side of PA while Peoples, headquartered in Pittsburgh, serves territories on the western side of PA. We believe the company's entrance into the gas industry will help grow its water business as well. Essential will likely be able to take advantage of its increased presence in the Pittsburgh area and entry into new states, and will find a way to aggregate more water assets.

Financial Outlook

Earnings outlook

The company forecasts rate base at its water utilities to grow at a 6-7% CAGR from 2019 through 2022 excluding rate base growth from acquisitions. Its capex is driven by investment in pipeline replacement, water treatment, and metering and IT development. Peoples Gas rate base is expected to grow at an 8-10% CAGR 2019 through 2022, as its aging distribution infrastructure requires significant pipeline replacement. Our 2020 through 2023 earnings per share estimates are $1.21, $1.67, $1.78, and $1.89. Our estimate of $1.21 reflects a partial year of earnings from Peoples as well as the effects of share dilution from 2019 financing. The $0.46 cent EPS increase in 2021 reflects a full year of earnings from Peoples, compared to three quarters in 2020. We expect earnings to increase at a +6.5% CAGR through 2023 based off 2019 adjusted EPS of $1.47. Breaking down the estimates by segment, water contributes ~64% of earnings and gas contributes ~36%. Our estimates reflect investment and continued acquisitions at its water utility and growth through investment at its gas segment. Our +6.5% EPS outlook compares to Essential's historical 4.0% EPS CAGR (2015-2019).

Dividend growth outlook

Essential has increased its common stock dividend at a 7.2% CAGR over the past four years. Our 2020 through 2023 dividend per share estimates are $0.97, $1.038, $1.110, and $1.188 and imply a DPS CAGR of 7%. The historical and forecasted payout remains in the 60%-65% range, excluding the 2020 estimate which is significantly higher due to a partial year of earnings from Peoples Gas.

Exhibit 4: Historical and projected dividend including forecasted EPS

	2018	2019	2020E	2021E	2022E	2023E
Dividend Per Share	$0.847	$0.907	$0.970	$1.038	$1.110	$1.188
Dividend Growth	*7.0%*	*7.0%*	*7.0%*	*7.0%*	*7.0%*	*7.0%*
Adjusted EPS	**$1.07**	**$1.47**	**$1.21**	**$1.67**	**$1.78**	**$1.89**
Dividend Payout Ratio	*79.1%*	*61.7%*	*80.1%*	*62.2%*	*62.5%*	*62.8%*

Source: Company data, RBC Capital Markets estimates

Sources of funds

We expect Essential to fund its capital expenditures through mostly new debt issuances and retained earnings. Regarding water M&A transactions, we expect the company to finance these transactions through a mixture of debt and equity. In 2020 we model ~$330 million equity in the second half of the year to finance its acquisitions including DELCORA, which is expected to be completed in late 2020 or early 2021. In the following years, we model a base of $50 million of equity, in some years issuing larger block amounts of equity to ensure its credit grade ratings. Historically, capex has been the largest use of cash followed by the dividend payout. Water acquisitions only accounted for ~7% of total capital deployment, but we expect this allocation to increase in future years. We do not model out any M&A transactions at Peoples, as we believe management is being careful about maintaining an earnings mix that is more heavily weighted from water operations.

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Exhibit 5: Sources and uses of funds

	2018	2019	2020E	2021E	2022E	2023E
Free Cash Flow						
Cash Flow from Operations	369	339	576	769	822	878
Common Stock Dividend	(151)	(189)	(249)	(273)	(293)	(315)
Retained Free Cash Flow	**218**	**150**	**327**	**496**	**529**	**563**
Acquisitions	(146)	(60)	(3,515)	(327)	(100)	(100)
Capital Expenditures	(496)	(550)	(810)	(960)	(969)	(979)
Net Free Cash Flow	**(424)**	**(460)**	**(3,998)**	**(790)**	**(540)**	**(516)**
Sources of Funds						
Net Long Term Debt Issuances	1,332	1,409	1,100	950	1,100	650
Net Short Term Debt Issuances	12	10	-	(10)	40	-
Common Equity Issuances	5	1,272	1,050	50	50	50
Net Debt and Equity Issuances	**1,349**	**2,692**	**2,150**	**990**	**1,190**	**700**
Ending Cash Balance	4	1,869	18	13	12	18

Source: Company data, RBC Capital Markets estimates

Credit metrics

Essential is rated A by S&P and Baa2 by Moody's. At the subsidiary level, Aqua is rated A+ and Peoples is rated A. Prior to the acquisition, the company's debt to cap ratio was maintained between 50% and 55%. In future years, we expect this ratio to trend higher and sit around the mid-fifties. Following 2020, we expect FFO-to-debt to be in the low teens, sitting around 13.4% in 2021. We see this move down to ~12% in the following years, which could point to a need to issue a larger amount of equity in 2023. This compares to its four-year historical average of around 20%.

While these metrics seem weak from a gas and electric utility perspective, water utilities may maintain their investment grade rating while having significantly higher debt to cap ratios and lower FFO-to-debt. A water utility may maintain an investment grade rating with a debt to cap as much as 60% and a FFO-to-debt as low as 9%. We expect Essential to remain comfortably far away from hitting these thresholds, and will continue to issue equity to maintain its solid credit metrics as it pursues additional acquisitions.

Exhibit 6: WTRG credit metrics

	2018	2019	2020E	2021E	2022E	2023E
Total Debt to Cap	55.7%	53.2%	51.9%	53.7%	54.5%	55.0%
EBIT Interest Coverage	3.3x	3.4x	2.6x	2.9x	2.9x	2.9x
FFO Interest Coverage	3.9x	3.4x	2.9x	3.2x	3.2x	3.2x
FFO to Net Debt	16.1%	7.1%	10.3%	13.4%	12.1%	11.9%
Discretionary Cash Flow to Debt	-10.9%	-7.7%	-7.8%	-6.7%	-6.0%	-5.3%

Source: Company data, RBC Capital Markets estimates

Repair tax is back on the table

Repair tax drove outsized EPS growth between 2013 and 2016 mostly for Aqua Pennsylvania. Essential now plans on electing repair tax for PNG in Pennsylvania. The mechanism has the benefits of keeping customer rates stable while increasing investments (and returns) without having the need to file for a lengthy rate case. For this reason, Essential has been able to stay out of a rate case on the water side since 2012, coupled with the implementation of

distribution surcharge mechanisms, which we had touched on in this report. In a nutshell, the repair tax allows certain maintenance costs previously capitalized to be expensed, effectively increasing deductions on a *tax basis* and improving cash flows. The Pennsylvania PUC then allows flow through tax accounting treatment that lets tax savings flow through to the income statement resulting in a lower effective tax rate and elevated earnings. Essential collects from customers at the statutory tax rate per the existing revenue requirement, but is expected to pay less to the tax authority. The impact is akin to a tax deferral as the benefit is the Thought in a different way, Essential collects the cost of taxes as new investments will bear the cost of higher taxes via the rate.

The amount of deduction is divided into two parts, ongoing deductions and a catch-up deduction for those costs that incurred in the past. Ongoing deductions are straightforward with Essential filing the election with the IRS. Management currently expects 8 to 12 cents of earnings accretion on a run-rate basis. The terms of the catch-up deduction would require approvals from the Pennsylvania state commission. As a reference point, the previous case with Aqua Pennsylvania allowed the deduction to be amortized over 10 years.

Balance Sheet and Expected Capital Deployment

Strong credit metrics to begin with. PNG brings metrics back to industry average. Essential's debt is rated A by S&P and Baa2 by Moody's, which is in line with the water industry. However, credit metrics look superior relative to peers excluding PNG, with debt-to-cap tracking low 50s and FFO-to-debt between high teens and low 20s in the past five years. To put these figures into perspective, AWK, a close peer to Essential before the PNG transaction, features a debt-to-capital ratio just below 60% and FFO-to-debt of mid to high teens during the same period.

Post-PNG transaction, we believe Essential's credit metrics could track closer to levels at AWK. We expect FFO-to-debt to stabilize in lower mid-teens and debt-to-capital at mid-50s, in line with company guidance of 12-14% and 50-55%, respectively. We believe towards 2023 the metrics will track farther away from the company's comfort levels, which may incentivize an equity issuance around that time. It is important to note that while credit agencies have typically considered 11-12% FFO-to-debt as the threshold for investment grade (BBB/Baa2) ratings for gas utilities, their threshold for water utilities is typically even lower in the 9-10% range. Due to the regulated nature of utilities, companies are able to flex their balance sheet to levels that would generally perceived as alarming in other industries. We also give consideration to the fact that PNG's debt (A/Baa1) is rated similarly to Essential (A/Baa2) and do not anticipate any material deterioration after the acquisition. The following summary shows credit ratings among Essential, Aqua America and PNG.

Exhibit 7: Current credit ratings for Essential, Aqua American and PNG

	S&P Global Ratings		Moody's	
	Issuer	Issuance	Issuer	Issuance
Essential	A	A-	Baa2	Baa2
AQUA (PA Subsidiary)	A	A+	--	--
PEOPLES	A	A	Baa1	Baa1

Source: Company Presentation

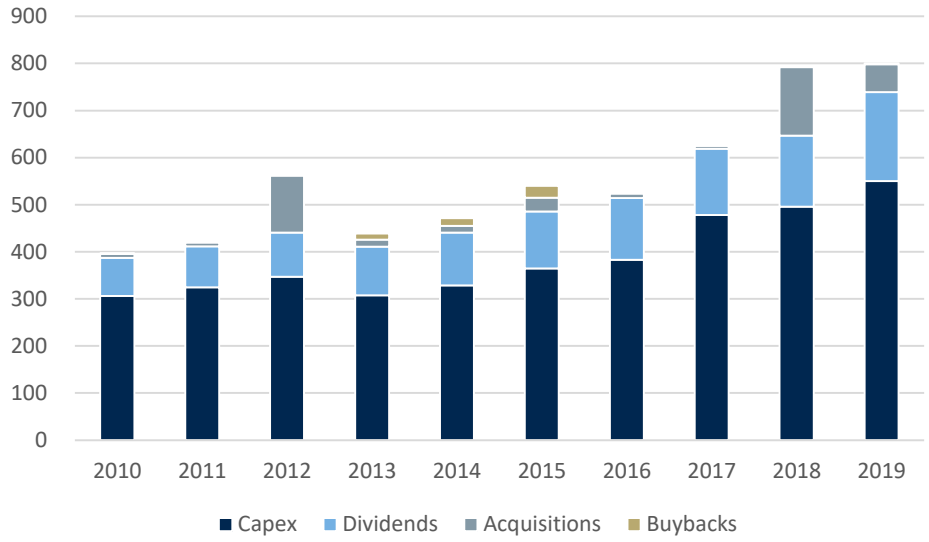
Capital deployment

Tapering expectations on dividends. Essential announced an annualized $0.94/share dividend payment in 2019. Between 2014 and 2019, dividends had achieved 7.3% CAGR along with healthy growth in earnings per share. In our outlook, we estimate dividend to grow in the 6-7% range in near term coupled with acquisitions that are in the $100 million range. Eventually, growth should taper off and fall in line with EPS growth, which we anticipate to be in the 6.0-6.5% range. We believe this enables Essential to manage a payout in the low 60s, in line with company guidance of 60-65% dividend payout. While the range is still a step up from water utility peers, which typically have payout ratios 50-60%, and is more in line with gas utility peers, we believe our estimate represents stabilizing ground after the PNG transaction.

Minimal share buybacks. Since 2010, buybacks averaged ~1% of total capital deployment. An abundance of capital projects in the water industry have stymied the need for buybacks to return capital to shareholders. Given our view of further consolidation in the industry and massive infrastructure upgrade opportunities in water pipes, we don't see buyback activity in the cards anytime soon.

Acquisitions remains a relatively small component; focus turns to organic growth following PNG transaction. Acquisitions have generally not been a large piece of capital deployment. Since 2010, acquisitions totaled 7.5% of overall capital deployment. We believe M&A could be somewhat limited now given the need to deleverage and preserve the strength of the balance sheet as Essential embarks into the gas distribution business. Management sees roughly $100 million of acquisitions per year but could inch higher if a larger deal were to close. The water industry is ripe for consolidation, in our view. We like the roll-up of municipal deals despite accretion being relatively modest. Assuming $100 million of deals, a blended 50% equity ratio and 10% ROE yields 3 cents of accretion on an increasing base, or +2% on current 2020E consensus.

Exhibit 8: Capital deployment, 2010-2019

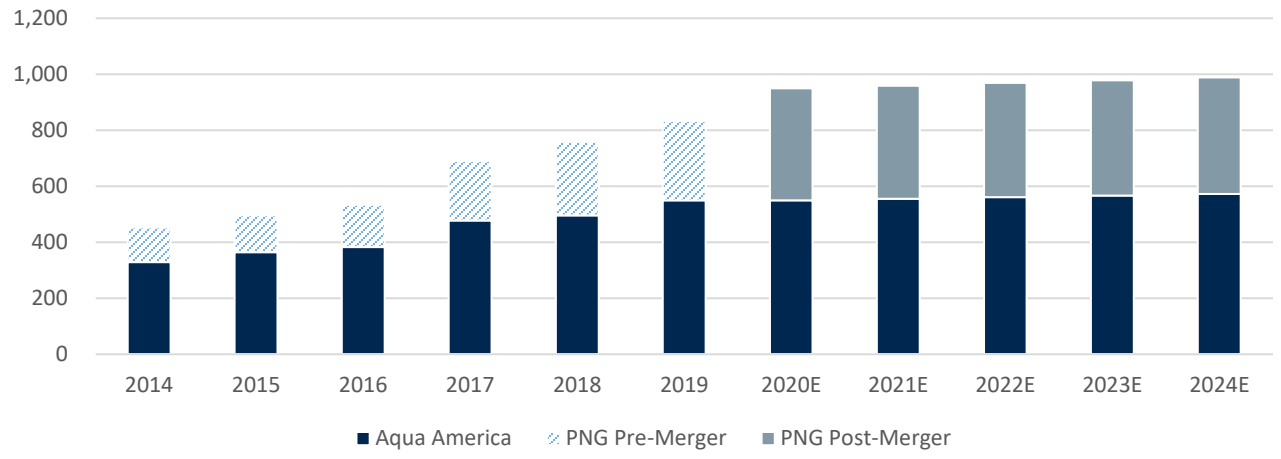


Source: Company 10K

Capital expenditures ramp up in 2020, post-PNG transaction. Core business has a healthy runway, expected to invest $1 billion infrastructure annually with a solid, organic rate base growth of 6-7% for water and 8-10% for gas. Further, more than half (52%) is recoverable through surcharges and the rest through rate cases. We view opportunities for infrastructure upgrade for both gas and water favorably. To put this into perspective, PNG plans to renew about 189 miles of pipeline per year under the long-term infrastructure investment program (LTIIP). Based on current capex expectations for 2020 of $400 million, this implies $2 million per mile of pipe. Management has indicated that there are nearly 3,000 miles of gas main suitable for replacement in Pennsylvania alone. In water and wastewater, the EPA estimates $471 billion and $271 billion worth of infrastructure investments needed as of today, respectively. We acknowledge that all pipes are not created equal and warrant different levels of investment based on deterioration. The opportunities are strongly outlined, however. We remain positive on the regulatory environment for both water and gas.

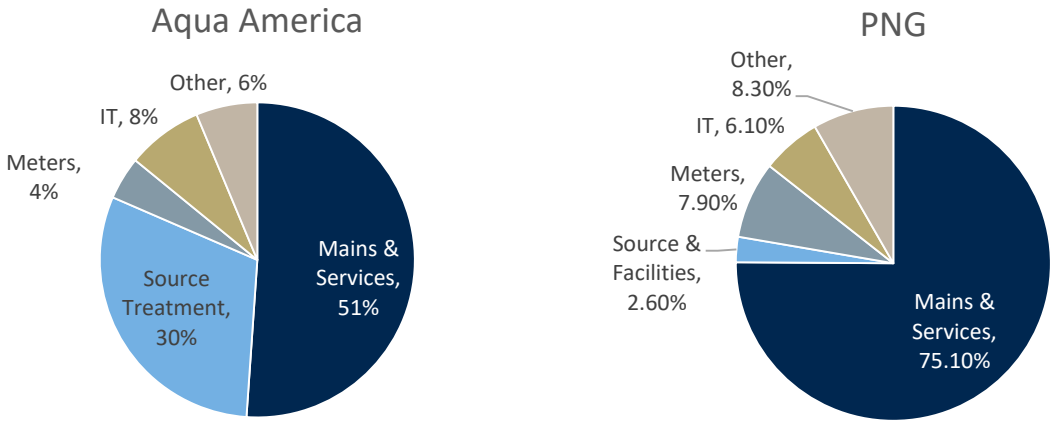
A counterweight to our capex expectations is the temptation to overgrow the gas utility. While gas investments typically generates a better return (8-10% ROE range, vs. 5-6% for water), we believe management could limit the growth in gas giving consideration to valuation of the overall utility. Earnings accretion from gas investments could erode the premium valuation that Essential enjoys from Aqua America. This is especially relevant to some investors who are concerned with ESG considerations. For 2020, we expect the gas/water capex mix to be 42%/58%. Going forward, we believe the ratio could remain static over even tilt towards water.

Exhibit 9: 2020 capex ramps up to $1 billion, slated to invest $2.8 billion, 2020E-2022E



Source: Company Presentation, RBC Capital Markets estimates

Exhibit 10: Infrastructure investments, 2020E-2022E



Source: Company Presentation

Financing

The company plans to finance its acquisitions with a mixture of debt and equity. The company has indicated that an equity issuance of ~$300 million will likely come in late 2020 as the company finances the DELCORA and other acquisitions. In 2020 and 2021 we will see the dilutive effects issuances used to fund the PNG and DELCORA transactions. Looking forward, we model $100 million in acquisitions every year, $50 million of which would be funded through equity.

Upcoming notable acquisitions

DELCORA acquisition should provide upside. In September 2019, Essential (then Aqua America) announced the acquisition of DELCORA wastewater assets for $276.5 million. The acquisition represents the largest municipal acquisition in the company's history. DELCORA is a wastewater authority that treats water for smaller municipal systems that have their own

distribution systems. DELCORA has around 15,000 customers, but the end-use customers of those municipalities total around 200,000. This generates a significant amount of follow-on opportunities to acquire the distribution wastewater systems that DELCORA serves. As with other municipal acquisitions, the company expects to see an earnings lag. Rates at municipal water and wastewater systems are significantly lower than those of investor-owned utilities. Municipalities may not be earning a return, paying taxes, or have other financial commitments, which lowers costs to the end-use customers. The company expects DELCORA to go into the Pennsylvania rate case that will most likely be filed in 2021. With new rates effective thereafter, the company expects full earnings from DELCORA in 2022.

Regulatory jurisdiction

Most of Essential's water, wastewater and now gas utility operations are subject to regulation from state commissions. As these commissions regulate billing rates and terms of services, and approval of rate cases and surcharges, they exert power over the profitability of Essential. Individual policies vary across commissions, and depend on the policies of the state. Essential has historically maintained constructive relationships with them, especially in the home ground Pennsylvania. The following is list of utility commissions within Essential's operating jurisdictions.

Exhibit 11: State utility commissions

State	Utility Commission
Pennsylvania	Pennsylvania Public Utility Commission
Ohio	Public Utilities Commission of Ohio
Texas	Public Utility Commission of Texas
Illinois	Illinois Commerce Commission
North Carolina	North Carolina Utilities Commission
New Jersey	New Jersey Board of Public Utilities
Inidiana	Indiana Utility Regulatory Commission
Virginia	Virginia State Corporation Commission
West Virginia	Public Service Commission of West Virginia
Kentucky	Kentucky Public Service Commisssion

Source: Company 10K

Risks to Rating and Price Target

Less favorable regulatory backdrop. Lower-than-anticipated adaptation of FMV principles across the country could dampen expectations and weigh on growth in the long run. Changes in or less favorable regulations or disruptions within public utility commissions could also weigh on growth.

Integration of PNG takes longer than expected. In that case, we could see higher O&M expenses in 2020 and possibly spilling into 2021. This could hinder Essential's progress to deleverage the company, on a FFO-to-debt basis. However, we view Essential to have a strong leadership with a highly experienced management team which has managed consolidations frequently in the past and believe the integration should proceed as planned.

Poor leverage metrics leads to credit downgrade. As we had noted earlier in the report, we see leverage metrics deteriorating dramatically in 2020. Despite stabilizing in 2021, these metrics cut close to rating thresholds for water utilities. Plus, we are aware of credit rating agencies' sector-wide downgrade, putting even more pressure on companies like Essential. Debt at Essential and PNG are one to two notches away above non-IG rating. Should leverage metrics deteriorate more than expected, we see a credit downgrade weighing down the stock.

Natural gas segment decreases appeal from an ESG perspective. We believe Essential's attractiveness from an ESG standpoint has lessened now that it has entered the natural gas sector. As ESG investing becomes more main stream, we expect to see greater flows into the water sector from specialized funds and awareness of ESG metrics. Water utilities, which have historically traded at a premium to electric and gas utilities, will likely see even higher premiums due to increased investor appetite. We believe that scarcity will partially mitigate the negative impact of its gas segment. There are under ten pure-play water utilities, and Essential had the second-largest water footprint when its operations were only in the water sector. We believe Essential still maintains ESG appeal, but will not benefit as much from the ESG interest as its pure-play water counterparts.

Decrease in water supply and material changes in water usage patterns. Climate variability may cause increased volatility in weather and may impact water usage and related revenue, which may not be recoverable through rates. Increased frequency of rainfall during the warmer months could also weigh on water usage and lead to lower revenues.

Decarbonisation hinders growth opportunities at the gas utility. The transition to electrification may be a risk to growth at Peoples as cities and states take stronger stances on GHG targets and continue to promote decarbonisation and electrification. Legislation and initiatives have encouraged the use of electric appliances and heating systems over traditional gas-based systems. One city in California even banned new gas connections in commercial and residential buildings. The gas distribution system is primarily decoupled, which separates volumes from earnings. This protects Peoples here from a volumes per customer standpoint, but the risk of decarbonisation comes from less connection growth. This discouragement of gas consumption could prevent the company from adding connections and potentially cause it to lose revenues if a customer were to switch entirely to an electric system. The company benefits from a customer count perspective since it charges fixed infrastructure costs, regardless of how much the ratepayer consumes. We believe states in which Peoples operates – PA, WV, and KY – are less likely to discourage the use of natural gas in the near future. However, emissions initiatives down the road could put downward pressure on the stock.

Delays in closing DELCORA. The company expects the DELCORA acquisition to close in late 2020 or early 2021. A delay in the DELCORA acquisition related to COVID-19 or for other reasons could negatively impact earnings in 2022 and onwards. If the acquisition is not

completed before the company goes into its Pennsylvania rate case in 2021, they may risk not being able to file for new rates at DELCORA. The company expects full earnings contributions from DELCORA in 2022, after new rates are implemented. If DELCORA does not make it into the rate case, the company will continue under-earn on the asset until the next rate case since rates for municipal systems are considerably lower than those of investor-owned utilities.

Extension of coronavirus lockdown could further hurt the economy and increase bad debt expenses. Utilities in general have means to recover incurred costs, though they may need to finance these costs while waiting for the commissions to determine the proper recovery mechanism, if permitted. As more customers face hardship, it would put pressure on their ability to pay their bills, including the utility bills. This, in turn, would translate into a revenue shortfall that could create a cash shortfall. We anticipate that commissions will allow these costs to be treated as a regulatory asset to be recovered over time.

Valuation

Outperform, $49 PT

Valuation framework supports high base multiple. To derive our valuation for water, we turn to the dividend discount model (DDM), which we use to calculate the sustainable value of a low-growth utility. We use the parameters that we use for gas utilities for market return (9.75%), beta (0.55), risk-free rate (3.5%), and dividend payout ratio (64%). We have changed our growth assumption to 4% for water from 3.5% for natural gas and we add a 10% ESG/water premium. This results in a base P/E for a low growing water utility at 24.9x forward P/E.

We arrive at our $49 price target using a sum-of-parts method. We apply a 25% premium to our base multiple of 24.9x P/E for water utilities and a 30% premium to our base multiple of 19.3x P/E for gas utilities. We believe both business warrant premiums due to strong growth prospects and footprints in states with constructive regulatory environments. Our price target of $49 implies a total return of ~17% and justifies our Outperform rating.

Valuation considerations

WTRG is currently trading at a 4-turn discount to water peers on 2021E EPS, despite having the second-largest water footprint. This is likely due to the loss of the benefit from the water premium that bolsters its pure-play peers as a result of Essential's plunge into natural gas. We believe the company has a solid earnings mix of 70%-30% water and a premium should still be warranted due to water segments; Essential operates the second largest water business and maintains around 25% of market cap.

We also believe that Peoples creates a strong platform for growth at both the gas and water segments. The multi-decade backlog of pipeline replacement requires significant and accelerated investment that will generate low risk organic rate base growth. Turning to the water segment, we think the water business is well-positioned to further expand its water business. We expect to see the majority of future acquisitions coming from Pennsylvania, which represents Essential's largest water and gas operating segments. We believe Essential's expansion into Western PA due to the Peoples acquisition will further secure the company's presence in the state and help drive acquisition growth for Aqua PA. The acquisition of DELCORA, whose service territories overlap with those incorporated in Aqua PA's footprint, will further increase Essential's presence in PA.

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Company Overview

Essential Utilities Inc. (f.k.a. Aqua America, Inc.) is the second largest water and wastewater utility in the U.S., measured by market capitalization. Before its entry into the natural gas industry, Essential generated virtually all of its revenues through its regulated water utility segment (99.6% of sales), serving an estimated three million customers located primarily in states along the rust belt and Texas. Essential's customer base is primarily residential (58%), followed by commercial (16%), wastewater (12%) and other (14%) customers. Essential's growth has been marked by several key transactions, including the acquisition of Peoples Natural Gas Company, LLC ("PNG") in 2020, regulated water operations in Ohio from American Water Works in 2012, regulated water operations from AquaSource in 2003 and the merger with Consumers Water Company in 1999. On February 3, 2020, the company changed its corporate name to Essential Utilities Inc. and extends services to 747,000 gas customers and expands its footprint to include Kentucky and West Virginia. As a complement to their primary regulated business, Essential also operates certain non-utility activities through Aqua Resources and Aqua Infrastructure.

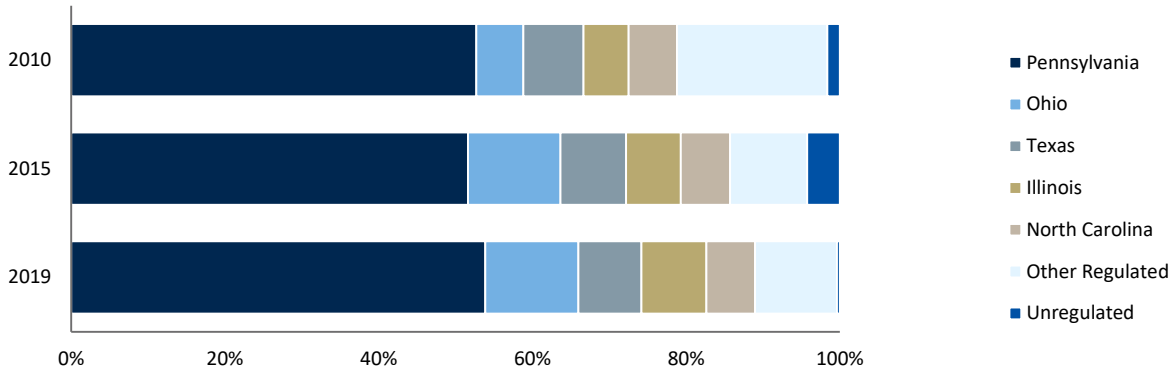
Exhibit 12: Company footprint, including Peoples Natural Gas transaction

Source: Company reports

Regulated water business

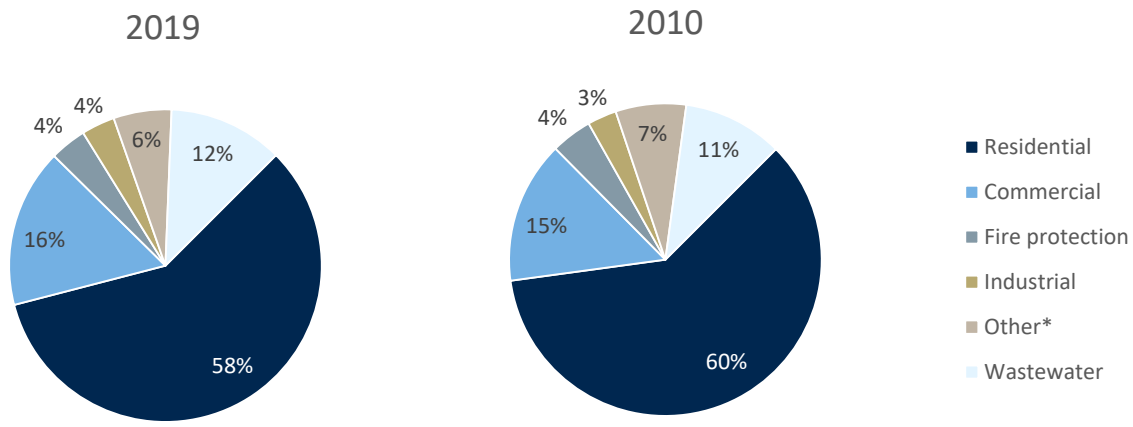
Essential generates virtually all of its revenues through its regulated water business, which serves water and wastewater customers in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana and Virginia. Historically, Pennsylvania is the main operating jurisdiction, accounting for 54% of operating revenues in 2019. Ohio, Texas, and Illinois contribute to the majority of the remaining share of revenues. Over the past decade, the percentage share across these states have remained largely in line year-over-year. Customer growth for the business has been robust, recording 1.8% CAGR in the trailing five years. The majority of customers for water services are residential (58% in 2019), followed by commercial (16%) and wastewater clients (12%).

Exhibit 13: 2019 regulated water segment revenues by state



Source: Company Presentation

Exhibit 14: Regulated water segment revenues by customer class

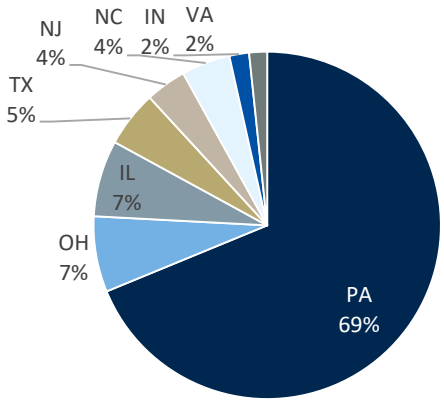


Source: Company Presentation

Water and wastewater service customers are subject to regulation by their respective state utility commissions, which determine billing rates and terms of service, among other regulatory matters. The regulated water business is dependent on water consumption which, in turn, is dependent on weather and temperature conditions much like electric and gas utilities. Generally, dry weather and high temperatures increase water consumption while above-average rainfall and low temperatures decrease water consumption. Given a regulated industry, local authorities may impose consumptions limits which could impact Essential's performance. Operating revenues for the regulated water business and operating revenues as a percentage of total were $805 million/$835 million/$886 million and 99.6%/99.6%/99.4% for 2017/2018/2019.

Utility growth is often referenced by growth in rate base. Between 2020 and 2022, rate base for water and gas are slated to ramp up at 6-7% CAGR to $6.5 billion and 8-10% CAGR to $3.0 billion, respectively. The following chart illustrates the relative sizes of water rate base as of 2018 by state.

Exhibit 15: Essential regulated water utility rate base as of 2018



Source: Company Presentation

Market-based activities

Essential conducts competitive, non-utility businesses through Aqua Resources and Aqua Infrastructure: Aqua Resources manages a water system operating and maintenance contract and offers other water solutions to customers; Aqua Infrastructure provides non-utility raw water supply services for firms in the natural gas drilling industry. Together, these businesses make up less than 0.5% of operating revenues hence immaterial to Essential's overall performance, in our view. The company's direction is consistent with a pure-play regulated utility and we believe the strategy will continue in the foreseeable future.

Peoples Natural Gas

Peoples Natural Gas ("PNG") is the largest natural gas distribution company in Pennsylvania with $2.3 billion rate base as of 2019 year-end. The company serves 747,000 customers across the Pennsylvania (93% of customers), West Virginia and Kentucky. The company's infrastructure is deeply rooted in these states, with 15,000 miles of distribution pipeline, 2,400 miles of gathering pipeline and 310 miles of intrastate transmission pipeline as of 2019. PNG is fully regulated, with 98% of earnings generated through its gas distribution business.

In October 2018, Aqua America announced the intent to acquire PNG for $4.275 billion in an all-cash transaction. The transaction closed on March 16, 2020. Much like other regulated utilities, PNG is regulated by various state commissions which determine customer tariff rates, terms of services and mergers and acquisition-related matters. On a regular basis, PNG files rate increase requests, either via riders or rate cases, to recover and earn a fair return on infrastructure spending. As with the regulated water business, the regulated gas distribution business is dependent on weather conditions and is seasonal by nature. Generally, colder weather increases gas consumption and warmer, milder weather decreases consumption. Certain states provide mechanisms that decouple gas sales from weather effects and helps smooth out earnings of gas utilities. While Pennsylvania and Kentucky offer decoupling, West Virginia does not. Given the high concentration of customers in Pennsylvania, we view the utility to be well-insulated from mild weather.

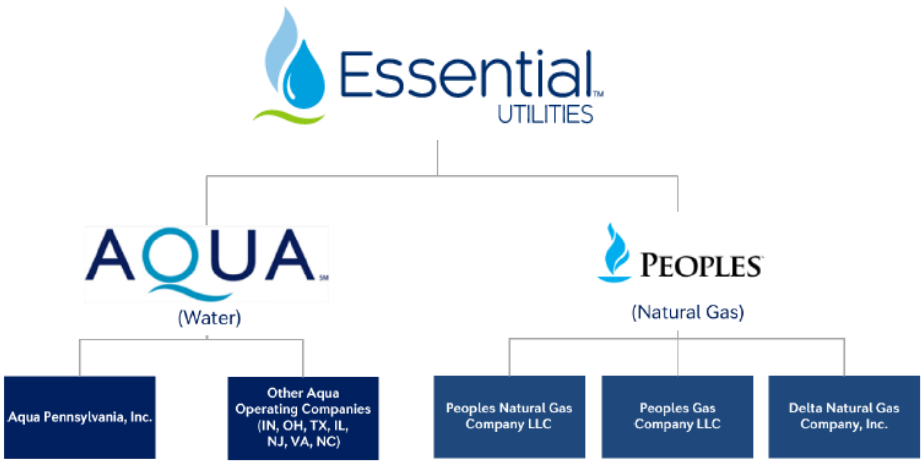
Management has indicated that it expects the business mix to stand at 70% water and 30% gas. It has also been made clear that the company wants to maintain its water-heavy earnings contribution, and will be very selective about any potential gas acquisitions moving forward.

We believe the mix of the two segments is crucial from a valuation standpoint, as this balance will play a significant role in how the stock trades compared to its utility peers.

Corporate structure – Essential Utilities

Despite consolidation in the past decades, Essential features a rather simple corporate structure. Aqua Pennsylvania, which provides regulated water and wastewater services in the state, is the largest entity within the structure and contributes to 54% of consolidated operating revenues. The figure below is a representation of the corporate structure after the PNG acquisition.

Exhibit 16: Essential Utilities corporate structure



Source: Company 10K

Management Team

Extensive industry experience. WTRG's management team has deep experience in the water utility industry, with most key executive officers serving in strategic roles at the company for extensive periods of time. We find the experience in mergers and acquisitions particularly valuable for the company, as it industry positions itself for further consolidation. The officers of Essential Utilities include:

Christopher H. Franklin – Chairman; President and Chief Executive Officer

Mr. Franklin has served as chief executive officer of Essential Utilities since July 2015 and as chairman since December 2017. Mr. Franklin was previously president and chief operating officer, regulated operations. A 20-plus-year veteran of the company, Mr. Franklin has held executive roles in public affairs, customer operations and as regional president of the company's southern and mid-western operations, where he managed eight states. While holding that post, Mr. Franklin significantly increased the performance and earnings power of these diverse state operations, while simultaneously serving as senior vice president of the company's corporate and public affairs, where he was also responsible for the company's federal, state and municipal legislative affairs, investor relations, and communications

Daniel J. Schuller – Executive Vice President and Chief Financial Officer

Mr. Schuller is executive vice president and chief financial officer for Essential. Before becoming Deputy CFO, Mr. Schuller served as Executive Vice President, Strategy and Corporate Development for Aqua America and was responsible for Aqua's strategic growth initiatives.

Mr. Schuller came to Aqua America from J.P. Morgan Asset Management – Infrastructure Investments Group where he had been an investment principal since 2007, providing strategic leadership as a director of portfolio companies including SouthWest Water Company—of which he was responsible for the 100 percent stake held by J.P. Morgan-advised investors—and Summit Utilities. Specifically for SouthWest Water, Mr. Schuller guided the company's turnaround and led its growth strategy, assessing both organic growth and acquisition opportunities. Prior to joining J.P. Morgan, Schuller was a manager at Mars & Co., an international strategy/general management consulting firm, where he led consulting engagements related to growth and profitability for Fortune 500 companies and conducted due diligence for private equity firms.

Richard S. Fox – Executive Vice President and Chief Operating Officer

Mr. Fox was named chief operating officer of Essential Utilities in July 2015. Prior to being appointed COO, he had been regional president for Aqua America since January 2012, heading all of Aqua America's utility operations in Texas, Illinois, North Carolina, Indiana and Virginia. Prior to assuming the role of regional president, he was vice president, customer operations, where he was responsible for all customer service operations for Aqua America's regulated operating subsidiaries, including the company's national customer call centers, national meter operations, and company-wide billing and collections.

Christopher P. Luning – Executive Vice President, General Counsel, and Secretary

Mr. Luning assumed the role of executive vice president, general counsel, and secretary for Essential Utilities in 2012. Mr. Luning is the company's chief legal counsel and oversees and provides strategic direction for the company's legal, human resources, internal audit, and safety departments. He provides direction on all parent company and its subsidiary matters, including corporate governance and board matters. Previously, he held the position of vice president, corporate development and was responsible for leading the Aqua America's corporate development activities, contributing to the company tripling its customer base in the previous 10-year period.

Matthew R. Rhodes – Executive Vice President, Strategy and Corporate Development

Mr. Rhodes was named executive vice president, strategy and corporate development for Essential in June 2018. Prior to this role, Mr. Rhodes served 11 years as a managing director in the investment banking division at Goldman Sachs in the global natural resources group focused on mergers and acquisitions for electric and gas utility clients. Prior to that role, Mr. Rhodes worked at Bank of America and Duke Capital Partners. Mr. Rhodes is the executive sponsor the Essential Utilities' Women Resource Group.

Robert A. Rubin – Senior Vice President, Controller and Chief Accounting Officer

Mr. Rubin was appointed senior vice president, controller and chief accounting officer (CAO) of Essential in January 2012 after having served as chief accounting officer since March 2004 and as controller for the previous five years. As CAO, Mr. Rubin is responsible for Essential's external and internal financial reporting, including that required by the Securities Exchange Commission and Sarbanes Oxley regulations. He is also responsible for taxes, coordinating external audits, corporate accounting and maintaining compliance with accounting standards and principles throughout the company.

Water Utilities in a Splash

Water is the most essential of utility services. The defensiveness of a utility sub-sector is partially defined by its ability to maintain a rate-regulated business model that creates predictable earnings and cash flows, thus allowing for a steady and foreseeable dividend. Fifty years ago, the telecommunication industry was a steady utility until competition was introduced and cellular technology disrupted it. Even twenty years ago, the generation portion of the electric industry was partially deregulated. It is conceivable that in a few decades electricity could be produced locally, thus not requiring a network of wires. Water, on the other hand, cannot be locally produced everywhere. Its pipelines form the least by-passable network among utilities. While most utility services are viewed as essential by the authorities, we believe that a premium consideration is placed on water utilities.

The U.S. water and wastewater industries are ripe for outsized investment opportunities driven by an aging infrastructure. The EPA estimates water utilities will need to invest ~$384 billion in pipes, treatment plants, and storage tanks over the next twenty years due to decades of under-investment. A competing study produced by the America Water Works Association (AWWA) estimates water infrastructure needs will total more than $1 trillion over the same timeframe, assuming pipes are replaced at the end of their service lives. As it stands today, U.S. water systems were slapped with a D+ grade from the American Society of Civil Engineers.

Municipal acquisitions drive accretion opportunities. The EPA estimates 84% of the community water market is serviced by municipalities and 98% of the wastewater systems are government-owned. Contrast that with the electric utilities sector, where investor-owned utilities (IOUs) served 72% of all electricity customers in 2017, according to Energy Information Administration (EIA), a division of the U.S. DOE. Acquisitions of municipalities have been a driver of growth for the water IOUs, having helped the nine largest companies collectively increase earnings at a 7%+ CAGR over the past ten years. Increasingly, states are creating incentives to facilitate such acquisitions, through Fair Market Value (FMV) legislation, which we will cover later. In our view, acquisitions resulting from fair market legislation will only become more prevalent and allow municipalities to focus on other community priorities.

Water lowest risk among utilities; argues for higher valuation. While water headlines can be scary (witness the Flint, Michigan disaster), most of the headlines come from poorly managed municipalities. Water investor-owned utilities (IOUs) do not suffer interruption of service like electric blackouts, the rare gas pipeline explosion, or the more numerous gas leaks. Regulatory outcomes are generally less contentious, with a greater usage of surcharges to grow revenues. The rating agencies recognize the lower risk as their thresholds for credit ratings are lower than those applied to other utilities. All else being equal, the FFO/debt for water utilities can drop to 10% or less and still retain an investment grade rating, a feat less likely to happen for electric utilities. A lower risk typically will lead to a lower discount rate and therefore a higher multiple.

ESG meaningful underlying driver for premium valuation. We believe that ESG (Environment, Social, and Governance) investing will continue to gain traction among fund managers, thus preserving a premium valuation for water utilities. On the environment side of the ledger, water utilities have the lowest carbon footprint of all utilities. Social issues revolve around the product that water utilities provide at a reasonable price. Governance issues are more akin to other industries. For example, while some companies separate the CEO and Chairman role, others do not. While more traditional ESG investors might be precluded from investing in gas/electric utilities due to nuclear assets, gas pipelines, or other aspects of the business model, we do not see a similar restriction on water utilities. Perhaps more importantly, we believe the increasing importance of ESG and the lack of publicly traded pure-play water stocks should only serve to further increase the premium valuations for companies in the industry.

Water Utilities: Industry Overview

Crippling and Aging Water Infrastructure

The average U.S. consumer has grown accustomed to the luxury of receiving clean drinking water and the management of wastewater, with little regard for the complicated and expansive systems necessary to deliver these services. For context, the United States has 1.2 million miles of drinking water supply mains and about an equal amount of sewer pipes. According to the Environmental Protection Agency (EPA) these systems are in dire need of investment, but the general public often has stark views over rising water prices, despite paying less than $0.01 per gallon. Further, water is generally the lowest percentage utility cost per household, despite being labeled as the most important service that customers receive (notably ahead of electricity and heat), according to a study conducted by Xylem Inc. (covered by Deane Dray). The discrepancy between necessary infrastructure investments and customer pushback over the rising cost of water will likely result in a dramatic shift in the way that water is priced in the future. In order for this to happen, water pricing must be restructured to cover the full costs of treatment and delivery to consumers, including expenses related to building, operating and maintaining and replacing water systems.

EPA regulates the industry at the federal level; PUCs at the state level. The EPA is tasked with setting the water quality standards while the state economic regulatory agencies, generally referred to as Public Utility Commissions (PUCs) govern the price impact of water services for investor-owned utilities. Investor-owned utilities are granted authority by each state's PUC to operate in a service area while receiving some protection from competition in exchange for quality and reliable service. The utility is entitled to a reasonable rate of return (allowed return) on prudently invested capital and can recover operating expenses. This is accomplished through rate cases.

Investments are passed onto rates via rate cases. In most states, municipal-owned water utilities generally set their own rates and do not have to go through a state PUC approval process. Political leaders are often reluctant to increase rates as that may cause unpopular opposition from voters. Thus, needed but costly infrastructure repairs may be postponed or avoided in order to keep rates low. Meanwhile, state PUC regulation of investor-owned utilities helps promote necessary infrastructure investment, rehabilitation and/or replacement, and maintenance. It does so not only by enforcing the utility's obligation to provide safe and reliable service, but also by setting rates that cover the costs of providing that service, including a fair return on invested capital.

Water is generally a good value proposition for customers

Most customers don't understand the water framework, but view water as essential. It is a fair characterization to admit that most U.S. customers overlook the value of the water that comes out of their faucets. Ratepayers of municipal systems or investor-owned utilities generally don't think about the pathway of how their water arrives in their homes or how it is treated and to what extent before being delivered. Ratepayers living in rentals may be so disassociated with water bills, they may often not be aware of the cost or dynamics of clean water, but even when paid directly ratepayers scuffle over paying on average less than a token penny per gallon of water vs a typical water bottle costing $1.50.

The average household pays roughly $540 a year for water and wastewater services compared to about $730 for soft drinks alone. In addition, water and wastewater services are typically the lowest percentage utility cost per household, representing about 12% of bills, compared to gas at 18%, telephone at 33%, and electricity at 37%. This historical underpricing of water is largely driven by lingering public perceptions that water is a fundamental human need supplied by the earth itself, i.e. free. These consumer perceptions have prevented

municipal utilities from attracting the necessary capital required to upgrade and maintain networks. Unfortunately, under-investment and inadequate water systems and/or lack of governance have caused instances like Flint, Michigan to occur, rendering national attention given the detrimental health and wellness effects of contaminated water. The water crisis in Flint displayed the disastrous consequences of lead contamination, but importantly also outlined the many other competing agendas that water utilities wrestle with including: (1) managing other drinking containments; (2) supervising wastewater treatment; and (3) handling storm water overflows. Notably, the EPA estimates 1.8 million to 3.5 million people per annum become ill from recreational contact to contaminated water. Further, the EPA estimates that about 850-900 billion gallons of untreated sewage is discharged into waterways every year due to aging pipes and inadequate resources.

Resulting from decades of underinvestment, water's aging infrastructure is in dire need of investment compounded by being the most capital intensive utility subsector. These challenges present ample investment opportunities for investor-owned utilities. The EPA estimates that $775 billion is needed to be invested in water and wastewater through 2040 due to decades of under-investment. A competing study produced by the American Water Works Association (AWWA) estimates water infrastructure needs will total more than $1 trillion over a similar timeframe, assuming pipes are replaced at the end of their service lives. As it stands today, U.S. water systems were slapped with a D+ grade and drinking water systems received a D rating from the American Society of Civil Engineers. Encouragingly, IOUs are increasing liaising with municipalities in mutual efforts to tackle the crippling and aging water infrastructure deficiencies. One of the tools is Fair Market Value legislation that we will be addressing in the next section.

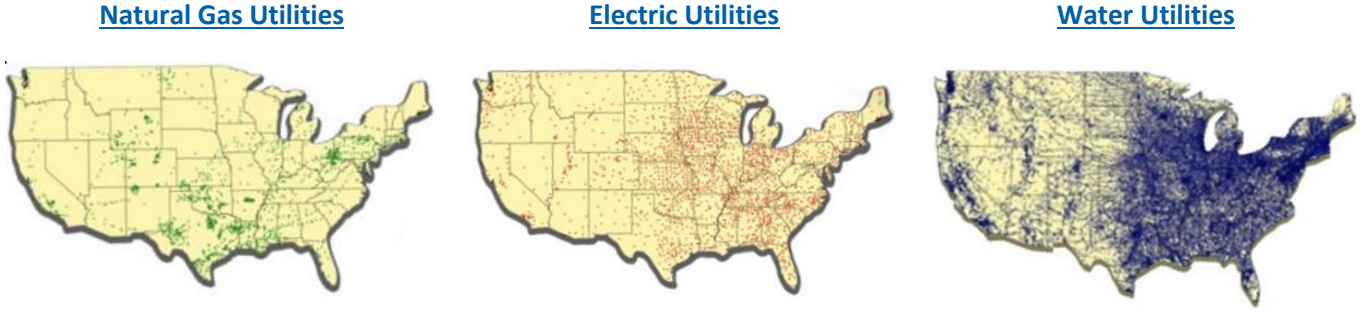
Only a fraction of the contaminants are regulated by the EPA

The EPA only regulates a fraction of the emerging water contaminants presenting a massive gap between the number of chemicals and the amount that are currently regulated. On a global scale, there are roughly 144 million chemicals registered under the Chemicals Abstracts Service. New chemicals are formed rapidly, roughly every 2.5 seconds, caused by a breakdown of existing chemicals. Further, there are about 1,400 microbial pathogens that are managed by water providers and only about 6% are regulated by the EPA. This doesn't mean that consumers aren't focused on the quality of water. For example, perfluorinated compounds (PFCs) were found in 162 water systems across the U.S. impacting 15 million people in 2017. PFCs are known to bioaccumulate and persist in the environment, and animal studies indicate that they are toxic, affecting reproduction and development, despite showing limited health effects in people. To augment to reality of not covering all bases, water utilities are increasingly implementing artificial intelligence (AI) and machine learning technologies to detect a broader range of contaminants.

Highly fragmented industry ripe for consolidation

The U.S. water and wastewater industry is heavily commoditized. The fragmented nature of the water industry is highlighted by roughly 50,000 water systems in the U.S. and about 15,000 community wastewater systems compared to 1,400 gas systems and 3,800 electric systems. Further, roughly 84% and 98% of the U.S. population is served by municipal water systems and wastewater systems, respectively. Additionally, half of the water and wastewater systems serve a population of less than 500, which generally don't provide enough scale that could warrant IOU interest.

Exhibit A: U.S. water among the most fragmented utility sectors



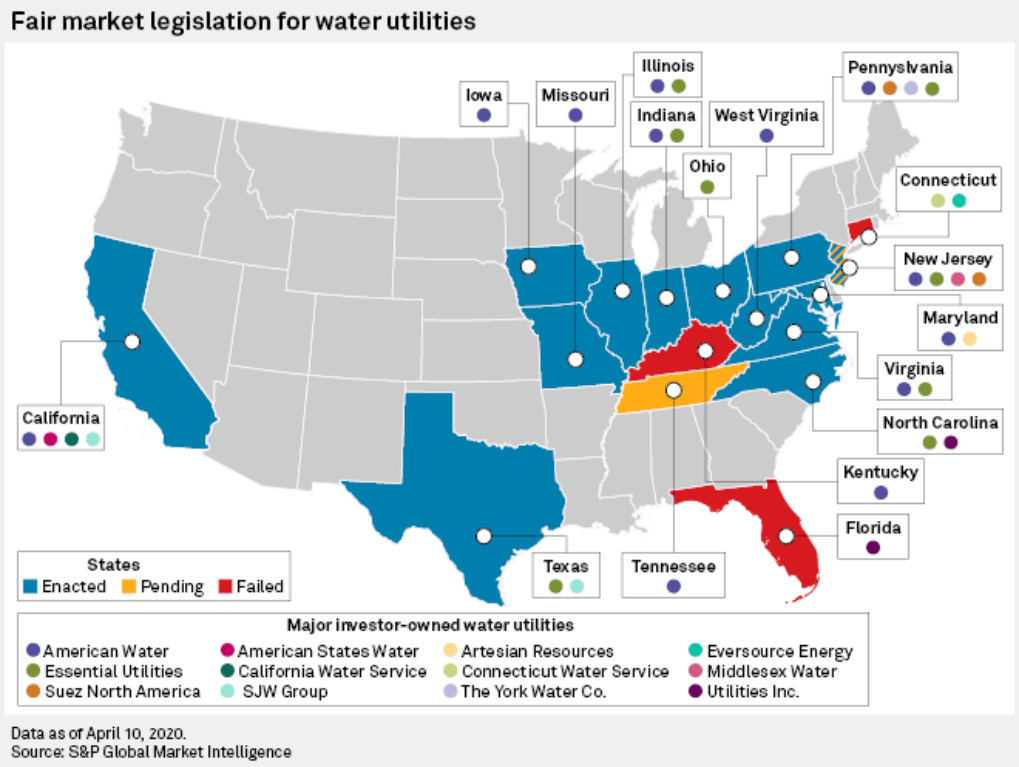
Source: Enviornmental Protection Agency and Energy Information Administration

Fair Market Value Legislation is leading to more deal-making

Fair market value assessment of water and wastewater systems is increasingly becoming a preferred alternative to the traditional depreciated original cost method, providing mutually beneficial outcomes to both the buyer and seller of municipal systems. Sellers are able to capture the true value of their assets while buyers are allowed to add the total purchase price to rate base, without padding goodwill, dubbing the premium an "acquisition adjustment". California became the first state to adopt fair market value legislation in 1997 following the passage of SB 1268. Since California's approval, eleven other states have adopted comparable approaches including Indiana, Missouri, Illinois, Iowa, Ohio, Pennsylvania, New Jersey, Maryland, and North Carolina, Texas, and Virginia. These states have subsequently turned into prime battlegrounds for IOUs fetching acquisition targets, further labeling the water industry as "ripe for consolidation". We believe that this legislation has already proven to and will continue to encourage consolidation in the water and wastewater industry. In our view, further acquisitions of municipal networks will provide operators with an option to exit the management of deteriorating water and wastewater assets, offer the ability to focus on other community priorities, and forfeit the need to comply with ever increasing environmental regulations despite having limited technical expertise. Of the 20,000 municipal water systems that are possible acquisition targets, we believe only a fraction of these are scalable enough to warrant acquisition consideration from IOUs. Companies are generally limited to their core operating states, and the acquired customer count generally needs to pass certain thresholds to be considered a viable takeout candidate.

The idea behind FMV is to create a win-win for IOUs and municipalities. In the utility world, regulators generally do not allow the acquiring company to earn on the full amount that it paid to acquire another company, if a premium is involved. Goodwill in essence becomes a stranded asset. In other industries, to the extent that you can create cost savings through synergies, paying the premium may be justified. However, utility rates are set by regulators that do not allow the company to keep the savings once a rate case is filed. These issues tend to cap the amount that companies are willing to pay for utility assets. The legislation allows IOUs to add approved goodwill to the rate base when buying a municipality or cooperative in states that feature FMV. It allows the acquiring companies to provide a better incentive for the municipality to sell its under-invested assets, while allowing the company a better opportunity to earn a fair return on the acquisition capital.

Exhibit B: Fair market value state legislation and investor-owned water utility footprints

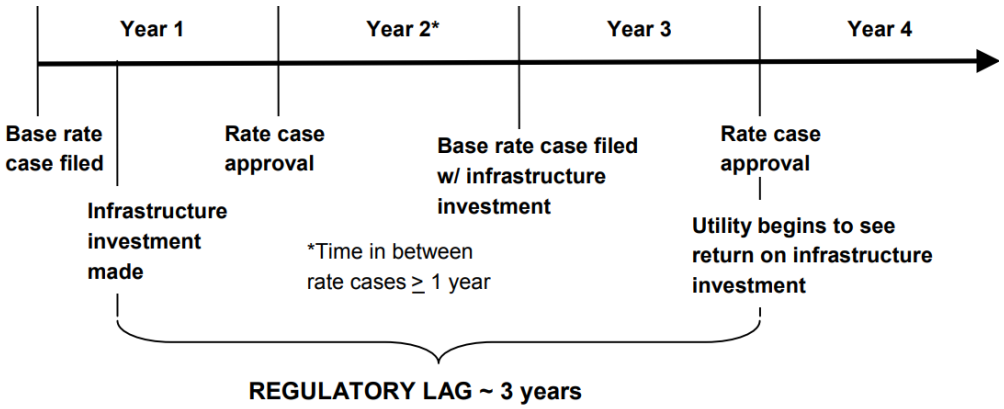


Source: Company reports, S&P Global Market Intelligence

Distribution system improvement charge

Water utilities are roughly 2x more capital intensive than their electric peers and 3x than their gas peers. As a result, repairing and replacing water and wastewater infrastructure has proven to be economically and politically challenging, primarily reflecting the impact on customer rates. To reflect this, public utility commissions (PUCs) have established infrastructure replacement surcharge programs to encourage water and wastewater infrastructure investments. Surcharge programs allow utilities to recover costs in a timelier fashion, effectively allowing them to extend the timeline between filing general rate cases, generally referred to as a stay-out. Surcharges also drive moderate base rate increases for customers, resulting in reduced customer rate shocks. Further, surcharge mechanisms help mitigate regulatory lag. Typically when a regulated water utility invests in a project, it seeks a return by filing for base rate increases through a rate case. Often, this process can be lengthy resulting in the aforementioned regulatory lag, a term coined from the time an investment is made until a utility is able to earn a return on that investment. This lag can obstruct a utilities ability to attract capital, weigh on its credit metrics, and may potentially limit necessary investments in systems.

Exhibit C: Impacting of regulatory lag



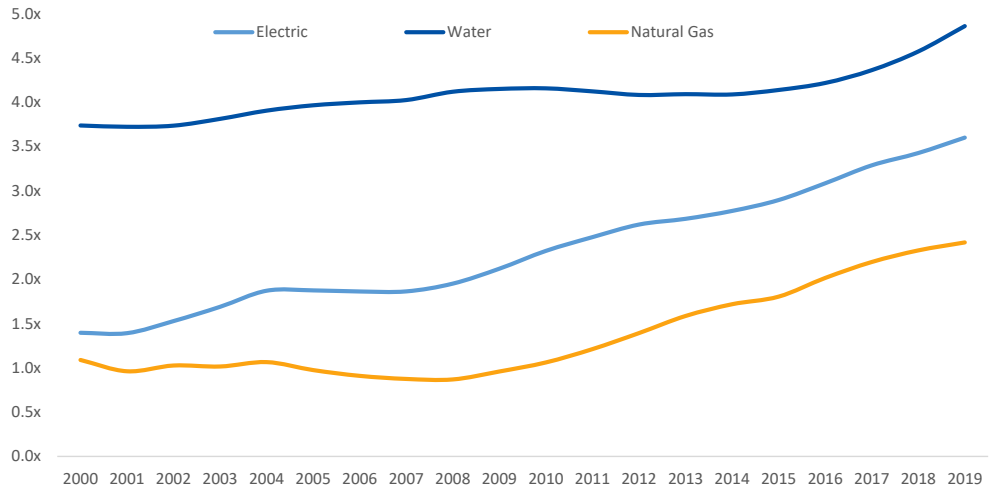
Source: American Water Works White Papers

Regulatory lag tends to have an especially adverse impact for water utilities, and consequently lead to sub-par returns during periods of heavy capital investment, due to the highly capital intensive nature of the businesses. The figure below demonstrates this dynamic. For illustrative purposes, the example showcases a historical test year (investments made during the rate case filing year would not be included in that rate case due to the investments falling outside of the test year). Assuming a general one-year timeline to conduct rate case proceedings, a utility would essentially be disallowed to earn a return on its first year's investments until year three. Surcharge rates are adjusted periodically based on infrastructure projects currently in progress or expected to be complete, but are typically reset to zero when a new base rate case begins, effectively rolling the surcharge based investments into the rate base. Further, surcharge rates are typically capped at 5.0% and 7.5% of a utility's annual revenue.

Capital intensity drives sustainable rate base growth

We believe the water utility sector has several unique and characteristics compared to the electric and gas sectors, particularly as it relates to return-generating projects and the associated revenue requirements to maintain infrastructure investments. Capital costs are mainly concentrated in pumping equipment, treatment facilities, and distribution systems. As noted previously, water utilities are roughly 2.0x more capital intensive than their electric peers and 3.0x more than their gas peers. Further, the net PP&E to revenues ratio for investor-owned water utilities is about 5.0x, compared to electric utilities of 3.4x and natural gas utilities of 2.3x. In our view, this ratio showcases the importance of infrastructure spending as a key characteristic of the industry's cost structure, and therefore making it difficult to pare back and reduce capital costs. Even as companies continue to drive their efficiency ratios lower, notably American Water Works and Aqua America, operating costs can only offset capital costs to a limited extent. In the figure below, we highlight the delta between the net utility PP&E to revenues of the three utility sub-sectors.

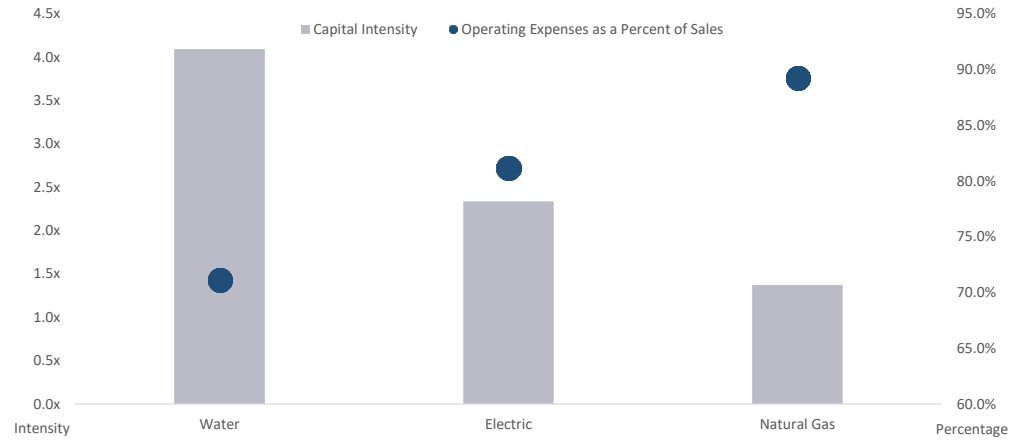
Exhibit D: Net utility PP&E to revenues



Note: Water, Natural Gas, and Electric Peers Include:
Water Peers: ARTNA, AWK, AWR, CWT, MSEX, SJW, WTRG, YORW
Natural Gas Peers: ATO, CPK, NJR, NWN, OGS, SJI, SR, SWX
Electric Peers: AEE, AEP, ED, ES, EVRG, PNM, PNW, PPL, SO, WEC, XEL
Source: Company reports

Despite the aforementioned capital intensive nature of the water utility sector, on a relative basis, companies generally spend the least amount of O&M dollars to maintain their assets vs electric and gas peers. To put this into perspective, over the past twenty years, water utility O&M expenses as a percent of PP&E averaged 20% compared to gas utilities at 40% and electric utilities at 60%. This leads us to believe that more water utility revenues are geared towards return-generating investments vs electric and gas peers which allocate a greater portion of expenses towards pass through costs that generally do not generate a return. This suggests to us that any incremental O&M savings could lead to further investment in capex dollars which eventually translate to higher rate base and earnings growth.

Exhibit E: Capital intensity and O&M expenses by utility sub-sector



Note: Water, Natural Gas, and Electric Peers Include:
Water Peers: ARTNA, AWK, AWR, CWT, MSEX, SJW, WTRG, YORW
Natural Gas Peers: ATO, CPK, NJR, NWN, OGS, SJI, SR, SWX
Electric Peers: AEE, AEP, ED, ES, EVRG, PNM, PNW, PPL, SO, WEC, XEL
Source: FactSet, Company reports, RBC Capital Markets

Environmental, Social Responsibility, and Governance

Environmental, social responsibility, and governance (ESG) principles are increasingly becoming mainstream components of investment decisions. The Global Sustainable Investment Alliance Review estimates that $17.5 trillion of sustainable-investing AUM globally proactively consider ESG components alongside financial analysis when contemplating investment decisions. To this extent, water utilities are stewards of a critical natural resource which has naturally drawn a connection to ESG principles. We believe American Water has established itself as the ESG template within the utility industry, ranking 23rd on Barron's most sustainable companies list, and the highest ranked utility.

The water utility industry generally scores higher in ESG than its electric/gas counterparts for a variety of reasons. The inherent asset profile for water utilities is considered superior to the asset profile of electric and gas utilities, principally due to the lack of coal, nuclear, natural gas, and pipelines. Additionally, water assets generally are considered higher-quality and safer.

The Sustainable Accounting Standards Board (SASB) provides a framework for analyzing ESG factors among electric, gas, and water utilities. In SASB's Materiality Map, which highlights various dimensions and general issues that would be material in evaluating a company's ESG profile, there are only two general issues that are considered material across electric, gas, and water utilities: Access & Affordability and Business Model Resilience. This highlights the inherent differences among the business profiles, in our view.

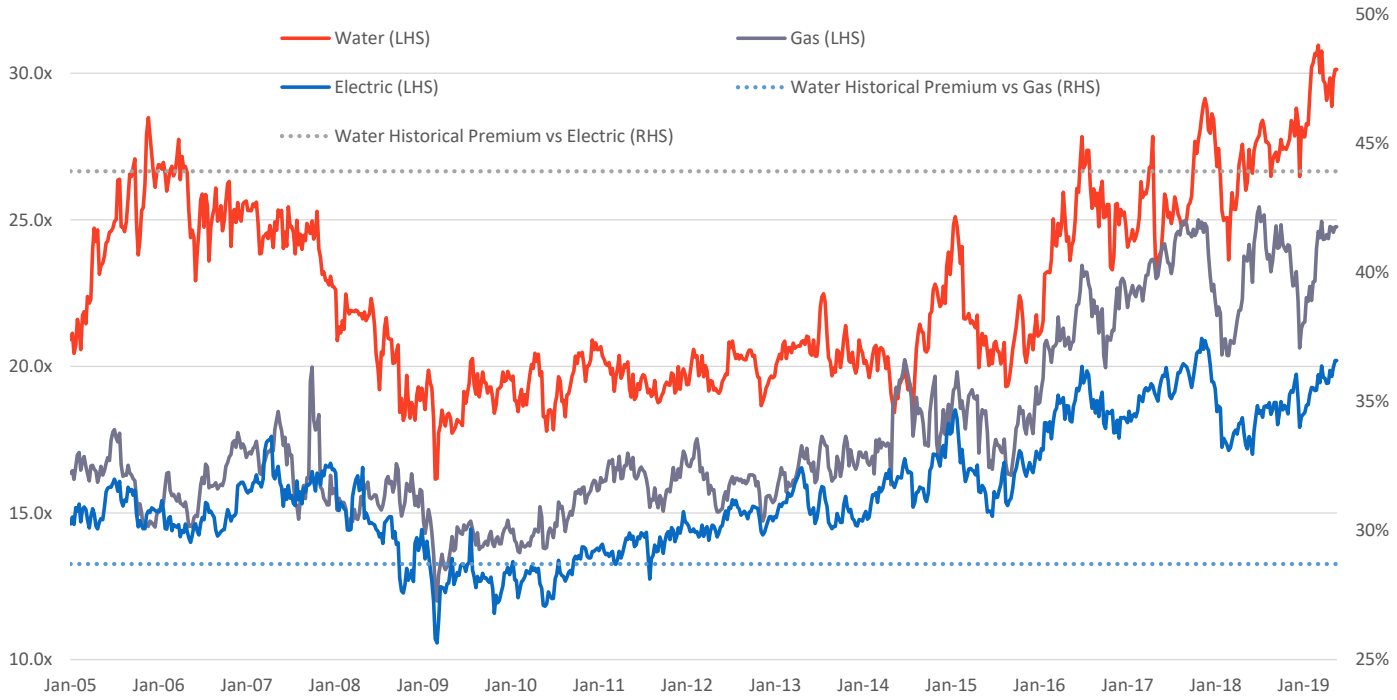
While we recognize that water utilities' environmental aspects are generally accepted as superior to electric/gas utilities, this is not the whole ESG story. When analyzing the ESG profiles of water utilities, it is important to compare water utilities among water utilities, meaning the E becomes less important on a relative basis. To us, key factors to consider include disclosure/quality of data (reporting under SASB standards, issuing sustainability reports, etc.), customer rates at or below national average, diversity of employees and Boards of Directors, and separation of CEO/Chairman.

Valuation Considerations

You Get What You Pay For

Utilities are commonly known for driving predictable earnings growth, and therefore it is common practice to use the price-to-earnings (P/E) ratio to calculate the value of utility equities. Valuations are also driven by utilities' established incumbent status, high barriers to entry, low commodity price exposure, increasing regulatory support, and steady (although generally declining) regulated returns. To this extent, regulated water, electric, and natural gas utilities have historically established what we view as 'entitled' multiples that vary quite a bit from one another. However, these utilities generally do not trade away from their respective peers (water, electric, gas) often, and instead stay within a fairly narrow band of valuation. Over the past fifteen years, water utilities averaged a ~23.0x next-twelve-month P/E ratio, reflecting a +30% premium to its natural gas peers, and a +45% premium vs its electric peers over the course.

Exhibit F: Water, natural gas, and electric utility peers forward P/E ratios



Note: Water, Natural Gas, and Electric Peers Include:
Water Peers: ARTNA, AWK, AWR, CTWS, CWT, MSEX, SJW, WTRG, YORW
Natural Gas Peers: ATO, CPK, NJR, NWN, OGS, SJI, SR, SWX
Electric Peers: AEE, AEP, ED, ES, EVRG, PNM, PNW, PPL, SO, WEC, XEL
Source: FactSet, RBC Capital Markets estimates

We believe structural differences between water utilities and their peers, which include several other factors, have contributed to the lofty historical premium. We highlight some of our observations below:

Naturally lower risk assets. Despite being the most capital intensive utility sector, water utilities are naturally lower risk assets and therefore command higher valuation multiples relative to their electric and natural gas peers. Recent PG&E investor capitulation following the devastating November 2018 Camp Fire, the natural gas explosions plaguing NiSource, or implications of fracking remind us of the elevated risks natural gas and electric utility peers absorb.

We believe prices may be moving higher. Until water is priced in a way that encourages wise use, reflects the true cost of delivering it, and allows for adequate replacement of that infrastructure, Americans will continue to take water for granted, and the infrastructure that makes it so easy for them to do so will continue to deteriorate.

Municipal acquisitions drive positive estimate revisions. Municipal acquisitions, and in particular fair market value legislation allow municipalities to be acquired for fair market prices. In turn, acquirers can add the total purchase price to the rate base, allowing water utilities to earn a return on the full rate base, without padding goodwill on the balance sheet. We estimate every $100 million deployed towards municipal acquisitions adds roughly $5 million to net income, assuming a best case scenario of regulatory lag.

Pure-play scarcity multiple applied to water peers. To a certain extent, water utility valuations are also driven by "scarcity value". This leaves funds with investment specific mandates a small selection of water utilities to invest in. There are only nine publicly traded water utilities, including Essential Utilities. Reflecting this treatment, we observed forced-selling in Essential Utilities (formerly known as Aqua America) shares in conjunction with its October 2018 Peoples Gas acquisition announcement for $4.5 billion.

Bite-sized enterprise values draw takeout considerations. The total market capitalization of publicly traded water utilities stands at roughly $44 billion vs ~$57 billion for their natural gas peers and ~$816 billion for their electric and multi-utility peers. We note that American Water Works and Essential Utilities represent about 78% of the aggregate water utility market capitalizations. In our view, this reflects the relatively bite-sized enterprise values of water utilities, despite above-average P/E ratios. To date, we've only observed Essential Utilities willing to dilute its pure-play water multiple with the announcement of its Peoples Gas acquisition, but we wouldn't rule out water acquisitions by electric and gas utilities. For now, the valuation multiple disparities present challenges to structure accretive acquisitions though we have seen more electric and gas utilities ramp up their respective ESG efforts which we believe could lead to higher valuation multiples for these entities.

Environmental, Social, and Governance (ESG) characteristics drive higher multiples. We believe utilities that have deliberately applied ESG principles fetch higher valuation multiples. The ESG model is easily implemented in the water framework given the very nature of the business models and strategic visions balance the provision of essential services with environmental stewardship, affordability, and financial integrity. To this tune, we believe ESG-focused companies generally exhibit higher quality of earnings driven by lower earnings volatility and higher return on equity. These characteristics have also drive higher P/E ratios.

Distribution Surcharge Infrastructure Changes (DSIC) arguably shift risks away from investors. Water utilities are known to stay out of rate cases and we believe this is a function of DSIC. Surcharges are reset to zero during the next rate or in the event that a company exceeds its allowed ROE.

Valuation framework

Inherent higher growth and ESG premiums lead to sustainably greater valuations. Our valuation framework for utilities is derived from the dividend discount model, where we assume a run rate risk free at 3.5% (well above the current 10-year Treasury yield of 0.65%). Exhibit G below shows the base P/E calculation that we employ for a traditional slow-growing electric utility.

Exhibit G: 3%-growing electric utility starts with a 17.8x forward P/E multiple

Cost of Equity Calculation		Absolute P/E Calculation	
Market Premium	6.3%	Dividend Payout Ratio	66.0%
Regulated Electric Beta	0.53	Dividend/Share Growth (g)	3.0%
10-Yr Treasury	3.50%	ESG premium	0.0%
Return on Equity (k)	6.8%	**RBC's Sustainable P/E**	**17.8x**

Source: Bloomberg; FactSet; RBC Capital Markets

We note that the above calculation tries to capture the long-term run rate utility, which, absent the heavy infrastructure requirements that exist in the electric business today, would likely grow only 3% a year, versus the foreseeable growth of 5%-6% a year.

There are only three variables that change for the water sector. One, we were somewhat surprised that the water utility beta is roughly in line to slightly higher than the electric beta. It may be due to the fact that the majority of water utilities are small to mid cap stocks, which can exhibit greater volatility. Two, the underpinning secular growth of the water sector is greater. We have assumed that a slow growing water company should manage to grow 4% per year. And three, we are introducing an ESG premium to our valuation with the launch of our water utility roll-out. We assume that the group starts with a 10% premium due to a combination of ESG investors and water funds that enhance the scarcity value of water stock. When we factor all that in, we arrive at a base P/E of 24.9x, as shown below. From there, we add a premium or discount based on numerous factors, including: quality of regulation, higher/lower growth rate expectation, quality of earnings/cash flow/credit, etc.

Exhibit H: 4%-growing water utility starts with a 24.9x forward P/E multiple

Cost of Equity Calculation		Absolute P/E Calculation	
Market Premium	6.3%	Dividend Payout Ratio	64.0%
Regulated Water Beta	0.55	Dividend/Share Growth (g)	4.0%
10-Yr Treasury	3.50%	ESG/water premium	10.0%
Return on Equity (k)	6.9%	**RBC's Sustainable P/E**	**24.9x**

Source: Bloomberg; FactSet; RBC Capital Markets

Essential Utilities, Inc.	Shelby G. Tucker, CFA; RBC Capital Markets
Consolidated Income Statement	**+1 (212) 428-6462; shelby.tucker@rbccm.com**

Fiscal Year Ending December 31,
($ in millions, except per share amounts)

INCOME STATEMENT	2018	2019	2020E	2021E	2022E	2023E
Revenues						
Adjusted Regulated Water Revenues	814.5	886.4	961.6	1,047.0	1,116.8	1,188.6
Regulated Natural Gas Revenues	-	-	611.8	982.8	1,030.6	1,085.6
Purchased Water	20.2	20.0	20.0	20.0	20.0	20.0
Other	3.5	3.3	5.0	5.0	5.0	5.0
Non-Recurring Revenues	-	-	-	-	-	-
Operating Revenues	**838.1**	**889.7**	**1,598.4**	**2,054.8**	**2,172.4**	**2,299.1**
Operating Expenses						
Purchased Water	(20.2)	(20.0)	(20.0)	(20.0)	(20.0)	(20.0)
Purchased Gas	-	-	(238.6)	(373.5)	(381.3)	(401.7)
Operations and Maintenance	(272.1)	(313.1)	(486.2)	(573.9)	(601.8)	(629.2)
Other Operations and Maintenance	(16.2)	(18.1)	(15.0)	(15.0)	(15.0)	(15.0)
Operations and Maintenance	(308.5)	(333.1)	(521.2)	(608.9)	(636.8)	(664.2)
Depreciation	(146.0)	(158.2)	(240.5)	(293.2)	(316.0)	(339.1)
Amortization	(0.6)	1.7	(0.5)	(0.5)	(0.5)	(0.5)
Taxes, Other than Income Taxes	(59.8)	(60.0)	(75.9)	(88.8)	(95.4)	(102.1)
Non-Recurring Operating Expenses	-	-	-	-	-	-
Operating Expenses	**(514.9)**	**(549.5)**	**(1,076.8)**	**(1,364.9)**	**(1,430.1)**	**(1,507.5)**
Operating Income	**323.2**	**340.2**	**521.6**	**689.9**	**742.4**	**791.6**
EBITDA	**469.9**	**496.6**	**762.6**	**983.6**	**1,058.9**	**1,131.2**
Adjusted EBITDA	**409.9**	**467.1**	**764.6**	**985.6**	**1,060.9**	**1,133.2**
Interest Expense	(98.9)	(100.0)	(201.7)	(237.2)	(256.8)	(271.2)
Allowance for funds during construction	13.0	16.2	16.0	16.0	16.0	16.0
Change in fair value of interest rate swap agreements	(59.779)	(23.742)				
Gain on sale of other assets	0.7	0.9	-	-	-	-
Equity (earnings) loss in joint venture	2.1	2.2	2.0	2.0	2.0	2.0
Other	(61.8)	(48.0)	-	-	-	-
EBT	**118.5**	**187.8**	**337.9**	**470.7**	**503.6**	**538.4**
Income Taxes	13.7	13.0	(27.6)	(32.7)	(34.9)	(37.2)
Effective Tax Rate	-11.5%	-6.9%	8.2%	6.9%	6.9%	6.9%
Income from Continuing Operations	**132.2**	**200.8**	**310.3**	**438.0**	**468.7**	**501.2**
Income from Discontinued Ops.	-	-	-	-	-	-
Net Income (GAAP)	**132.2**	**200.8**	**310.3**	**438.0**	**468.7**	**501.2**
Adjustments	58.8	39.0	-	-	-	-
Adjusted Net Income	**191.0**	**239.8**	**310.3**	**438.0**	**468.7**	**501.2**
Earnings Growth						
Adjusted Earnings Per Share - Diluted	**$1.07**	**$1.47**	**$1.21**	**$1.67**	**$1.78**	**$1.89**
EPS Growth	*-20.4%*	*37.3%*	*-17.6%*	*37.7%*	*6.5%*	*6.5%*
Dividend per common share	$0.8474	$0.9066	$0.9700	$1.0378	$1.1104	$1.1882
Payout Ratio	*79.1%*	*61.7%*	*80.1%*	*62.2%*	*62.5%*	*62.8%*
Dividend Growth	*7.0%*	*7.0%*	*7.0%*	*7.0%*	*7.0%*	*7.0%*
Basic Common Shares Outstanding	177.9	215.6	255.8	262.1	263.2	264.2
Diluted Common Shares Outstanding	178.4	215.9	256.3	262.6	263.7	264.7

Source: Company Reports, RBC Capital Markets Estimates

RBC Capital Markets

Essential Utilities, Inc.	Shelby G. Tucker, CFA; RBC Capital Markets
Consolidated Statements of Cash Flow and Balance Sheet	**+1 (212) 428-6462; shelby.tucker@rbccm.com**

Fiscal Year Ending December 31,

($ in millions, except per share amounts)

CASH FLOW DATA	2018	2019	2020E	2021E	2022E	2023E
Operating Activities						
Net Income (from continuing operations)	192.0	224.5	310.3	438.0	468.7	501.2
Depreciation and Amortization	146.7	156.5	241.0	293.7	316.5	339.6
Deferred Income Taxes	(15.0)	(10.4)	12.5	25.0	25.0	25.0
Provision for Doubtful Accounts	5.3	5.3	5.0	5.0	5.0	5.0
Stock Based Compensation	7.6	7.4	7.0	7.0	7.0	7.0
Gain on Sale of Utility System, Other Assets	(0.7)	(1.3)	-	-	-	-
Loss and settlement on interest rate swap agreements	59.779	(59.8)				
Equity loss in Joint Venture	-	-	-	-	-	-
Working Capital	(17.5)	0.8	-	-	-	-
Pension and other Postretirement Benefit Contributions	(14.2)	(8.6)	-	-	-	-
Other	4.5	24.2	-	-	-	-
Cash Flow from Operations	**368.5**	**338.5**	**575.8**	**768.7**	**822.2**	**877.8**
Investing Activities						
Capital Expenditures	(495.7)	(550.3)	(810.0)	(959.5)	(969.1)	(978.8)
Acquisitions, Net	(145.7)	(59.7)	(3,515.0)	(326.5)	(100.0)	(100.0)
Additions/Release of Funds Related to Construction Activity	-	-	-	-	-	-
Net Proceeds from Sale of Utility Systems	0.7	2.9	-	-	-	-
Proceeds from Note Receivable	-	-	-	-	-	-
Other - Investing	0.9	2.5	-	-	-	-
Cash Flow from Investing	**(639.8)**	**(604.6)**	**(4,325.0)**	**(1,286.0)**	**(1,069.1)**	**(1,078.8)**
Financing Activities						
Customer Advances and Contributions in Aid of Construction	7.5	9.1	10.0	10.0	10.0	10.0
Repayment of Customers' Advances	(6.2)	(6.8)	(6.0)	(6.0)	(6.0)	(6.0)
Net Proceeds of Short Term Debt	11.8	10.3		(10.0)	40.0	-
Proceeds From Long Term Debt	1,331.9	1,409.3	1,100.0	950.0	1,100.0	650.0
Repayments of Long Term Debt	(914.1)	(1,048.5)	(7.4)	(208.9)	(655.4)	(182.4)
Proceeds From Issuance of Common Stock	5.2	1,272.1	1,050.0	50.0	50.0	50.0
Proceeds From Exercised Stock Options	1.5	1.9	-	-	-	-
Proceeds from tangible equity unit issuance	-	673.6	-	-	-	-
Stock Base Compensation Windfall Tax Benefit	-	-	-	-	-	-
Repurchase of Common Stock	(2.6)	(1.9)	-	-	-	-
Dividends Paid on Common Stock	(150.7)	(188.5)	(248.6)	(272.5)	(292.8)	(314.5)
Other	(13.4)	0.8	-	-	-	-
Cash Flow from Financing	**270.7**	**2,131.4**	**1,897.9**	**512.6**	**245.8**	**207.1**
Beginning Cash Balance	4.2	3.6	1,868.9	17.7	13.0	11.9
Change in Cash	(0.6)	1,865.3	(1,851.2)	(4.7)	(1.2)	6.1
Ending Cash Balance	**3.6**	**1,868.9**	**17.7**	**13.0**	**11.9**	**17.9**

Source: Company Reports, RBC Capital Markets Estimates

RBC Capital Markets

Essential Utilities, Inc.	Shelby G. Tucker, CFA; RBC Capital Markets
Consolidated Statements of Cash Flow and Balance Sheet	**+1 (212) 428-6462; shelby.tucker@rbccm.com**

Fiscal Year Ending December 31,
($ in millions, except per share amounts)

BALANCE SHEET DATA	2018	2019	2020E	2021E	2022E	2023E
ASSETS						
Cash & Equivalents	3.6	1,868.9	17.7	13.0	11.9	17.9
Accounts Receivable	101.2	67.1	191.8	246.6	260.7	275.9
Inventory, Materials and Supplies	15.8	40.5	32.0	41.1	43.4	46.0
Gas Stored - Current Portion		18.4				
Prepayments and Other Current Assets	26.5	17.8	17.8	17.8	17.8	17.8
Total Current Assets	**147.2**	**2,012.7**	**259.3**	**318.5**	**333.8**	**357.6**
Property, Plant and Equipment						
Property, Plant & Equipment, gross	7,648.5	8,201.9	12,644.2	13,930.2	14,999.3	16,078.1
Less: Accumulated Depreciation	(1,718.1)	(1,856.1)	(3,310.8)	(3,604.5)	(3,921.0)	(4,260.6)
Property, Plant and Equipment, net	**5,930.3**	**6,345.8**	**9,333.4**	**10,325.7**	**11,078.3**	**11,817.5**
Regulatory Assets	788.1	878.1	1,181.6	1,181.6	1,181.6	1,181.6
Deferred Charges and Other Assets, Net	39.2	42.7	56.5	14.3	21.6	29.9
Investment in Joint Venture	7.0	6.0	6.0	6.0	6.0	6.0
Funds Restricted for Construction Activity	-	-	-	-	-	-
Goodwill and Intangibles	52.7	63.8	2,369.9	2,369.9	2,369.9	2,369.9
Operating lease right of use	-	12.9	68.8	68.8	68.8	68.8
Total Long Term Assets	**6,817.3**	**7,349.2**	**13,016.2**	**13,966.3**	**14,726.1**	**15,473.6**
TOTAL ASSETS	**6,964.5**	**9,362.0**	**13,275.5**	**14,284.8**	**15,060.0**	**15,831.3**
LIABILITIES						
Current Maturities of Long-Term Debt	144.5	105.1	208.9	780.4	182.4	51.5
Loan Payable	15.4	25.7	25.7	15.7	55.7	55.7
Accounts Payable	77.3	74.9	82.4	90.7	99.7	109.7
Accrued Interest	23.3	29.8	32.8	36.1	39.7	43.7
Accrued Taxes	22.2	22.8	25.1	27.6	30.3	33.3
Regulatory liabilities - current portion	-	-	-	-	-	-
Other Current Liabilities	116.1	60.6	66.6	73.3	80.6	88.7
Total Current Liabilities	**399.0**	**318.8**	**441.5**	**1,023.7**	**488.5**	**382.6**
Long Term Liabilities						
Long Term Debt, Excluding Current Portion	2,398.5	2,943.3	5,587.5	5,757.1	6,799.7	7,398.2
Deferred Income Taxes and Investment Tax Credits	845.4	936.2	948.7	973.7	998.7	1,023.7
Customers' Advances for Construction	93.3	95.6	105.6	115.6	125.6	135.6
Regulatory Liabilities	531.0	517.6	517.6	517.6	517.6	517.6
Other	97.2	102.5	102.5	102.5	102.5	102.5
Operating lease liabilities	-	11.6	11.6	11.6	11.6	11.6
Contributions in Aid for Construction	590.7	555.5	555.5	555.5	555.5	555.5
Total Deferred Credit and Other Liabilities	**4,556.2**	**5,162.3**	**7,829.0**	**8,033.6**	**9,111.2**	**9,744.7**
Total Liabilities	**4,955.1**	**5,481.1**	**8,270.5**	**9,057.3**	**9,599.6**	**10,127.2**
Shareholders' Equity						
Common Stock	90.6	111.9	118.9	125.9	132.9	139.9
Capital in Excess of Par Value	820.4	2,636.6	3,686.6	3,736.6	3,786.6	3,836.6
Retained Earnings	1,174.2	1,210.1	1,271.8	1,437.3	1,613.1	1,799.8
Treasury Stock	(75.8)	(77.7)	(77.7)	(77.7)	(77.7)	(77.7)
Accumulated Other Comprehensive Income	-	-	5.4	5.4	5.4	5.4
Noncontrolling interests	-	-	-	-	-	-
Stockholder's Equity	**2,009.4**	**3,880.9**	**5,005.0**	**5,227.5**	**5,460.4**	**5,704.1**
TOTAL LIABILITIES AND EQUITY	**6,964.5**	**9,362.0**	**13,275.5**	**14,284.8**	**15,060.0**	**15,831.3**

Source: Company Reports, RBC Capital Markets Estimates

RBC Capital Markets

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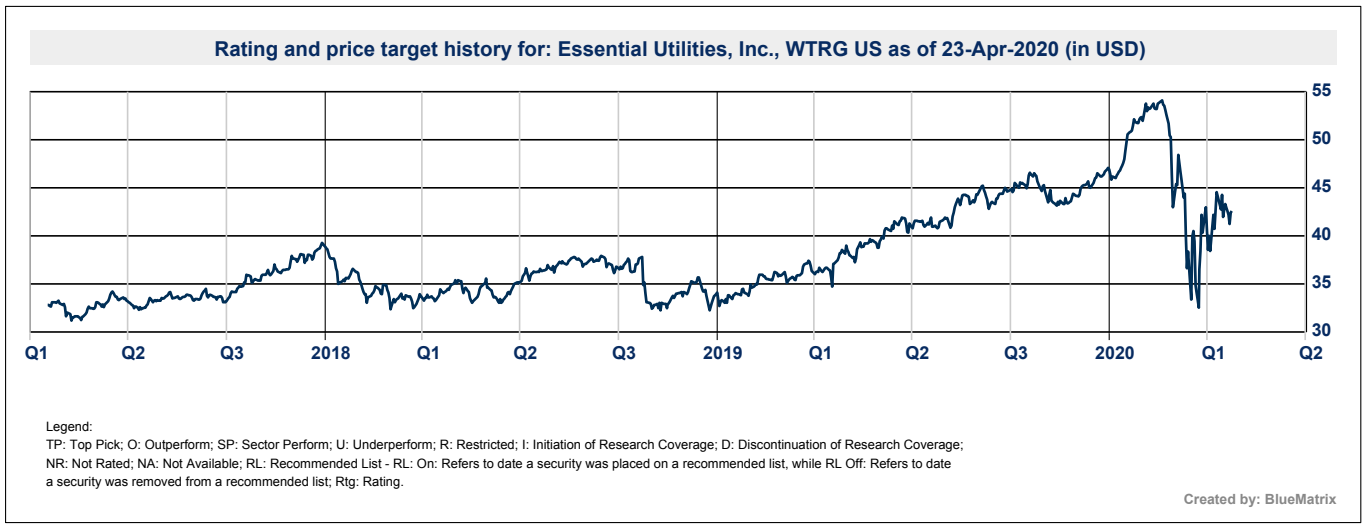
Distribution of ratings
RBC Capital Markets, Equity Research
As of 31-Mar-2020

			Investment Banking Serv./Past 12 Mos.	
Rating	Count	Percent	Count	Percent
BUY [Outperform]	755	51.64	220	29.14
HOLD [Sector Perform]	619	42.34	126	20.36
SELL [Underperform]	88	6.02	11	12.50



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Essential Utilities, Inc.

Valuation

Our $49 price target assumes WTRG trades at a 29.4x P/E multiple on our 2021 estimate of $1.67. This multiple represents a 25% premium to our base multiple of 24.9x P/E for water utilities and a 30% premium to our base multiple of 19.3x P/E for gas utilities. The implied return to our $49 price target supports our Outperform rating.

Risks to rating and price target

- Lower-than-anticipated adaptation of fair market value principles across the country could dampen expectations.
- M&A transactions could require greater equity than we forecast, or could result in a weaker balance sheet than we expect.
- Less favorable regulations or disruptions within public utility commissions could weigh on growth.
- Climate variability may cause increased volatility in weather and may impact water usage and related revenue, which may not be recoverable through rates.
- Continued lockdown from coronavirus could impact revenues, through higher bad debt expenses.
- ESG investing continues to gain traction, but WTRG does not meet certain ESG criteria due to Peoples, which makes it ineligible to benefit from these increased flows.

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January 12, 2021
Company Update
Utilities

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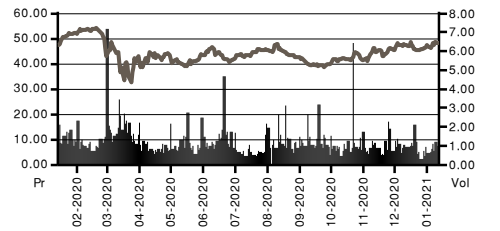
Rating:	**Neutral**
Price Target:	**N/A**

Price Target Metrics:
N/A

Current Price:	**$48.18**
Float:	244.8MM
Diluted Shares:	254.4MM
Short Interest:	9.8MM
Average Daily Volume:	920k
52 Week Range:	$30.40 - $54.52
Market Cap:	**$12,259MM**
Cash and Investments:	$5MM
Debt:	$5MM
Enterprise Value:	$12,259MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New	2023
EPS (Diluted)							
Q1 (Mar)	$0.60	$0.60A	$0.62	$0.62E	$0.63	$0.61E	$0.58E
Q2 (Jun)	$0.29	$0.29A	$0.31	$0.30E	$0.30	$0.29E	$0.28E
Q3 (Sep)	$0.23	$0.23A	$0.27	$0.27E	$0.30	$0.30E	$0.33E
Q4 (Dec)	$0.45	$0.45E	$0.46	$0.48E	$0.55	$0.58E	$0.71E
FY	$1.58	$1.58E	$1.66	$1.67E	$1.78	$1.78E	$1.90E
P/E		**30.5x**		**28.9x**		**27.1x**	**25.4x**
Dividends Per Share							
FY	$0.970	$0.970E	$1.038	$1.038E	$1.111	$1.111E	$1.188E
Dividend Yield		**2.0%**		**2.2%**		**2.3%**	**2.5%**

Essential Utilities, Inc.

(NYSE: WTRG)

Stock fully valued given market valuations of gas LDCs

Summary:
WTRG's 8.2%/10% water/gas rate base CAGR for 2020-2023 is very impressive, but fully reflected in its current share price, we believe, especially given the ongoing de-rating of gas LDCs, even those with premium rate base/earnings growth prospects. Yesterday, WTRG hosted its 2021 earnings guidance call. The midpoint of its $1.64-1.69 EPS guidance range is in line with consensus expectations.

Highlights

Strong momentum in water/wastewater municipal M&A: WTRG has $420.5MM in pending muni M&A deals on the water/wastewater side, including the $276MM DELCORA transaction which seems likely now that courts have upheld Aqua PA's purchase agreement for the asset. The deals should start boosting WTRG's water earnings in 2022/2023 assuming Aqua PA completes its next water rate case by mid-2022. That's reflected in our model which is based on an 8% water rate base CAGR for 2020-2023. Biden's likely infrastructure spending plan seems unlikely to derail the consolidation of the water/wastewater sector especially in states with the fair value legislation.

De-rating of stocks of gas LDCs: The marginal investor in stocks of US utilities continues to have a strict ESG screen hence the ongoing de-rating of stocks of gas LDCs. Among stand-alone gas LDCs, there is some P/E differentiation between strong (such as ATO or OGS) and weak EPS growers (such as SJI or NJR), but even the premium growers currently trade at a slight 3% discount to an average electric utility on 2023 EPS and at a 46% discount to an average water utility. With an 8-10% rate base CAGR for 2020-2023, WTRG's gas LDC is a fast grower, but that means it deserves to trade at just 16.5x 2023 EPS. A third of WTRG's 2023 EPS should come from gas which is the third highest in our coverage (after ATO and CMS) even after incorporating the DELCORA wastewater transaction.

Tweaking 2021 estimates, adding 2023 estimates: We raised our 2021 EPS estimate to $1.67 from $1.66 to reflect a slightly higher water rate base projection. Our 2022 EPS is unchanged as we added $300MM in equity in 2022 which fully offset the slightly higher water rate base estimate. We introduced our 2023 EPS of $1.90 which also reflects ~ $300MM in equity for that year. That should be enough to fund WTRG's current growth capex assuming the company is able to avoid paying federal cash taxes under Biden's proposed 15% minimum corporate income tax. We don't have PTs for Neutral-rated stocks, but to us, WTRG's current market valuation fully reflects its premium water/gas EPS growth prospects.

Company Description:
WTRG owns and operates water utilities (1 million accounts) and gas utilities (0.74 million accounts) in 10 states though mainly PA.

WTRG: EPS breakdown by segment ($)

WTRG	2019A	2020E	2021E	2022E	2022E	20-'23 CAGR
Regulated water utilities	1.47	1.10	1.15	1.25	1.31	
Regulated gas utilities	0.00	0.54	0.63	0.69	0.74	
Parent	0.00	-0.06	-0.12	-0.16	-0.15	
Total EPS	**1.47**	**1.58**	**1.67**	**1.78**	**1.90**	**6.4%**
DPS	**0.91**	**0.97**	**1.04**	**1.11**	**1.20**	**7.2%**
Dividend payout	62%	61%	62%	62%	63%	

Source: Company data for 2019; Seaport Global Securities

WTRG	2019A	2020E	2021E	2022E	2023E
Operational EBITDA	505	874	928	1,018	1,070
Operational EBIT	349	610	647	713	747
Net interest expense	100	202	210	233	223
Ordinary Profit Before Tax	269	437	466	512	559
Income tax	7	35	37	41	45
Net profit	262	402	429	471	515
S/O (m)	178	255	258	265	271
Diluted EPS	**1.47**	**1.58**	**1.67**	**1.78**	**1.90**
DPS	**0.91**	**0.97**	**1.04**	**1.11**	**1.20**
Cash	1,869	5	5	5	5
Receivables	108	110	113	121	126
Inventory	18	30	30	30	31
Other short-term assets	18	18	18	18	18
Other-long term assets	1,003	3,810	3,810	3,810	3,811
Property, plant, and equipment	6,346	9,081	9,659	9,929	10,181
Total assets	**9,362**	**13,054**	**13,635**	**13,913**	**14,172**
Financial liabilities	117	496	496	496	496
Operating liabilities	67	109	108	108	111
Other liabilities	108	220	220	220	220
Deferred credits	2,057	2,758	2,757	2,757	2,756
Long-term debt	2,943	4,750	5,619	5,769	5,932
Shareholders' equity	4,070	4,721	4,434	4,563	4,656
Total liabilities and equity	**9,362**	**13,054**	**13,635**	**13,913**	**14,172**
Net income	262	402	429	471	515
D&A, goodwill amortisation	156	264	281	305	323
Other non cash elements	-40	-6	-6	-6	-4
Funds from operations	379	660	704	769	833
Non-cash working capital	-40	43	-1	0	3
CFO	**339**	**703**	**703**	**769**	**836**
Net investments in fixed assets	-610	-6,675	-1,309	-925	-975
Net investments in financial assets	6	0	0	0	0
Free cash flow before dividends	**-266**	**-5,972**	**-606**	**-156**	**-139**
Dividends paid	-161	-242	-266	-293	-323
Free cash flow after dividends	-427	-6,214	-872	-449	-461
Changes in equity	1,935	302	2	298	298
Changes in financial debt	386	4,047	869	150	163
Adjustment for minorities / miscellaneous	-28	1	1	1	1
Increase in cash	1,866	-1,864	0	0	0

Essential Utilities, Inc. (WTRG) Disclosures

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Risks & Considerations for Essential Utilities, Inc. (WTRG)

Allowed ROEs for WTRG's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. WTRG's only pending rate case (in NC) is very small.

Lower sales volumes could weigh on WTRG's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, it's up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. WTRG's regulatory calendar is quiet in 2020, with a pending small rate case in NC, and a likely filing for a catch-up repair tax adjustment for Peoples in PA.

Gas utilities have a higher operating risk than water utilities: Over-pressurized gas systems seem to happen more frequently among gas utilities in the US. While we recognize that Peoples Gas is a well-managed system, WTRG's risk profile could further deteriorate with any gas-related operational issues. Additionally, investors increasingly scrutinize the carbon footprint of gas LDCs which in turn weighs on their market valuations.

Risks & Considerations for Atmos Energy Corp. Atmos Energy Corp. (ATO)

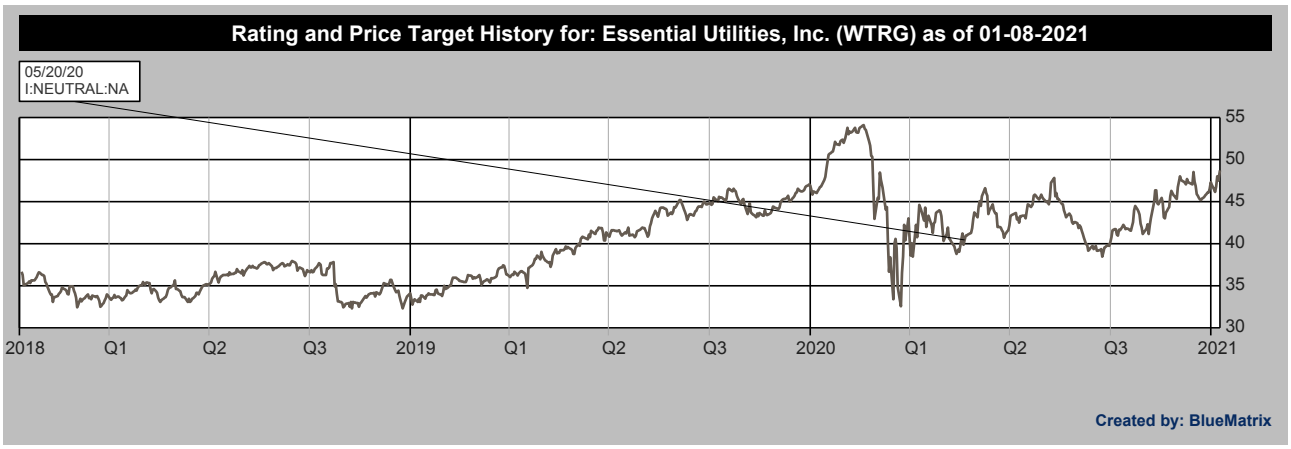
Allowed ROEs for ATO's gas LDCs and pipeline could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. ATO's gas LDCs and its pipeline have above-average allowed ROEs and equity ratios especially when compared to regulated electric utilities in TX. Future rate reviews could lead to lower allowed ROEs though cheap natural gas prices are supportive of premium returns for ATO's assets.

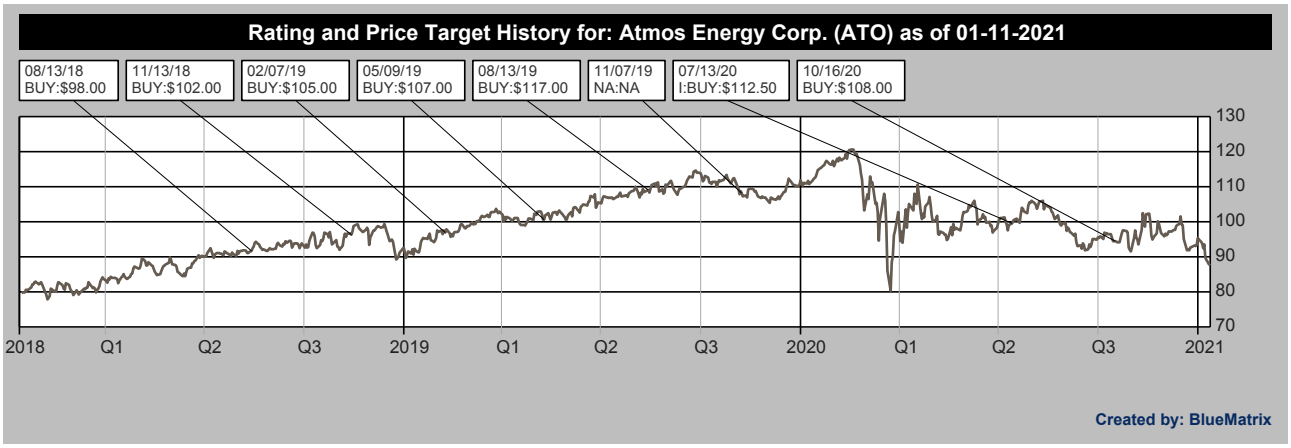
Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, it's up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings.

Gas distribution and transmission systems have a higher operating risk than electric systems: Overpressurized gas distribution pipes have led to explosions and severe regulatory repercussions especially in California and the Northeast. While ATO was not involved in any of these accidents and the company operates in very constructive regulatory regimes, we still see some elevated operating risk vs. an average regulatory utility we cover.

Other Companies Mentioned in This Report

- Atmos Energy Corp. (ATO: $87.67, Buy)
- New Jersey Resources Corp. (NJR: $35.78)
- ONE Gas Inc. (OGS: $71.92)
- South Jersey Industries Inc. (SJI: $21.86)





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NA - A rating is not assigned.

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Reduce - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.

Sell - The investment outlook and risk/reward over the following 12 months are very unfavorable on an absolute basis and relative to the peer group.

NA - A rating is not assigned.

Ratings Distribution

	Research Coverage		Investment Banking Clients*		
Rating	Count	% of Total	Count	% of Total	% of Rating Category
Buy	124	63.9%	2	100.0%	1.6%
Neutral	68	35.1%	0	0.0%	0.0%
Sell	2	1.0%	0	0.0%	0.0%
Total	194	100.0%	2	100.0%	1.0%

*Investment banking clients are companies for whom Seaport Global Securities has provided investment banking services in the previous 12 months.

Note: Ratings Distribution as of December 31, 2020

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May 20, 2020
Initiating Coverage
Utilities/Power

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Utilities/Power

Water Utilities: For growth and safety; Initiating coverage of AWK, AWR, CWT, SJW, and WTRG

Summary:
We are initiating coverage of water utilities with a bullish outlook, and **AWK** and **AWR** as our top picks, while we're Neutral on **CWT**, **SJW**, and **WTRG**.
To us, there is no better utility than a water utility:

- The water/wastewater industry remains highly fragmented with ~90% of the US population getting water/wastewater services from municipally-owned systems.
- Water/wastewater systems, especially those owned by municipalities, are heavily under-invested and often non-compliant with EPA regulations. While munis resist water/wastewater M&A, growing budget pressures coupled with fair value laws should facilitate privatizations.
- Outside of CA/HI, water/wastewater bills remain low. The current work-from-home arrangements inflate higher-margin residential water volumes, and we'd expect at least some of this volume uptick to persist beyond 2020, benefiting AWK and WTRG in particular.
- Water/wastewater capex is non-cyclical and highly fragmented.
- Water utilities have high ESG/sustainability ratings. Those translate into rich valuations and a very low cost of financing.

The debate about the right multiple for water vs. electric utilities continues. An average water utility under our coverage grows EPS/DPS at a ~9%/~8% rate or ~300 bps/~300 bps faster than an average regulated electric utility. However, the water EPS growth rates are inflated by recent M&A deals and/or non-water earnings. Based on our 2022 EPS estimates, water utilities under our coverage trade at a ~45% P/E premium to an average regulated electric utility (24.6x vs. 16.9x respectively) which is in line with the historical average. The average 2019 EV/Rate base multiple of 1.78x also seems average.

Highlights

Water utilities: Trading multiples

	Rating	Market Cap ($B)	2019 EV/Rate Base	2022 P/E	2019-2022 EPS CAGR	2019-2022 DPS CAGR
AWK	Buy	22.2	1.74x	26.2x	8.3%	10.0%
AWR	Buy	2.9	1.77x	29.2x	4.9%	7.6%
CWT	Neutral	2.2	1.76x	23.9x	11.5%	7.4%
SJW	Neutral	1.6	1.68x	21.0x	14.0%	6.9%
WTRG	Neutral	10.1	1.94x	22.7x	6.3%	7.0%
Average water			**1.78x**	**24.6x**	**9.0%**	**7.8%**

Source: FactSet, Seaport Global Securities

Water utilities: EPS/DPS CAGRs

	2019-2022 EPS CAGR	2019-2022 DPS CAGR
AWK	8.3%	10.0%
AWR	4.9%	7.6%
CWT	11.5%	7.4%
SJW	14.0%	6.9%
WTRG	6.3%	7.0%
Average	**9.0%**	**7.8%**

Source: Seaport Global Securities

AWK (Buy): AWK's scale and strong operational execution position it well to benefit from ongoing privatization of municipal water/wastewater systems. We acknowledge AWK's 60%+ debt/cap and pending/upcoming rate cases in three of its largest jurisdictions happening during the COVID-19 pandemic. Yet, the strain on municipal budgets on the back of this pandemic could further accelerate muni water deals, with AWK best positioned to consolidate the industry.

AWR (Buy): The company keeps surprising to the upside on its regulated water/electric earnings thanks to strong regulatory and operational execution in CA. Though AWR trades at the highest PE multiple among water names under our coverage, it's largely a function of its military water/wastewater contracts, we believe. When we adjust AWR's EV for those contracts, the stock trades in line with peers on 2019 EV/Rate base.

CWT (Neutral): With its rate base/customer more than a third lower than that of its public peers, CWT offers unmatched long-term EPS growth prospects. Yet, a pending decision by CA regulators in CWT's general rate case could meaningfully increase the volatility in its earnings by removing revenue decoupling and/or balancing accounts for pension/medical expenses. The latter seems likely to us.

SJW (Neutral): The recent cancelation of SJW's temporary revenue decoupling mechanism in CA and a lack of a balancing account for purchase water costs in the state have more severe earnings implications than we once expected. Through the merger with CTWS, SJW reduced its concentration on CA, but the volatility in SJW's earnings is still pretty severe. The stock trades at a large 15% P/E discount to an average water utility on our 2022 EPS though just a 5% discount based on the 2019 EV/Rate base multiples. The volatility in SJW's earnings should persist through at least 2021 because SJW's San Jose Water plans to ask for a purchased water tracker in its next general rate case in CA covering 2022-2024.

WTRG (Neutral): To us, WTRG's recent purchase of a gas utility (Peoples Gas) muddled the original water growth story in exchange for a ~150+ bps pick-up in WTRG's EPS CAGR. Management should pursue a catch-up repair tax deduction for Peoples Gas in PA, but we'd expect most of the earnings benefit to be shared with ratepayers. Given its higher operating risk profile, WTRG's gas earnings are unlikely to ever trade at a water P/E. Given the earnings mix, WTRG seems therefore fairly valued to us.

Seaport Global

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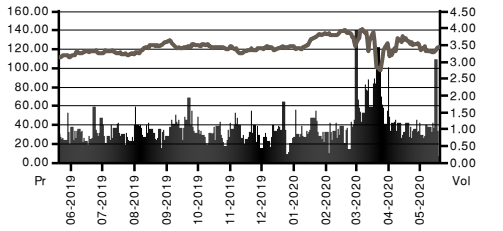
Rating:	**Buy**
Price Target:	**$130.00**

Price Target Metrics:
2022 SOTP valuation implying 28.4x 2022 EPS

Current Price:	**$120.17**
Float:	180.5MM
Diluted Shares:	181.0MM
Short Interest:	2.0MM
Average Daily Volume:	1,097k
52 Week Range:	$92.00 - $141.70
Market Cap:	**$21,751MM**
Cash and Investments:	$1MM
Debt:	$10,315MM
Enterprise Value:	$32,065MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Adjusted)				
FY	$3.61A	$3.84E	$4.23E	$4.59E
P/E	**33.3x**	**31.3x**	**28.4x**	**26.2x**
Dividends Per Share				
FY	$1.955A	$2.150E	$2.365E	$2.600E
Dividend Yield	**1.6%**	**1.8%**	**2.0%**	**2.2%**

American Water Works Company, Inc.

(NYSE: AWK)

Best-in-class water growth story

Summary:
We are initiating coverage of AWK with a Buy rating and a $130 price target based on our 2022 SOTP valuation implying 28.4x our 2022 EPS. We see the rich valuation as warranted by AWK's multi-decade investment needs, its low risk profile and growth in ESG-related investing. AWK's above-average 8.3%/10% EPS/DPS CAGR between 2019-2022 should be achievable largely regardless of future economic cycles, driven by organic capex and acquisitions of municipal water systems (~7% EPS growth), with contracted services adding an additional ~1-1.5% to the growth. Assuming no federal infrastructure bill, the current COVID-19 pandemic could, over time, boost muni water/wastewater M&A for large water operators such as AWK. We admit that it's not ideal, however, that AWK will be asking for meaningfully higher rates in three of its largest regulatory jurisdictions (NJ, PA and MO) during the COVID-19 pandemic, or that AWK's net debt/cap should exceed 60% through 2021/2022.

Highlights

Regulated utilities (~88% of 2022 EPS): AWK's 7-8% rate base CAGR between 2019 and 2024 is supported by organic water main replacement capex and acquisitions of municipal water/wastewater systems. While AWK's existing systems offer decades of growth, the customer bill affordability is the key limiting factor for the organic growth. AWK's muni M&A is focused on rural systems with 30,000-60,000 existing customer accounts in states which adopted fair value legislation or similar laws. Assuming no federal infrastructure bill, the muni M&A in the water sector could further accelerate benefiting large water utilities such as AWK in particular, we believe.

Contract-based operations (~12% of 2022 EPS): AWK provides water/wastewater services to 16 military, with pending solicitations for five more contracts, three of which to be awarded still this year. Given the 50-year duration, inflation indexation, premium returns, and the exclusive nature of these contracts we see them as even more valuable than the regulated water business. AWK won more than 50% of all new military water/wastewater service contracts offered to private contractors over the last couple of years, with AWR as the only real competitor in this field. AWK's Homeowner Services business offers warranties mainly for wastewater sewer lines not covered by homeowner's insurance. The business EPS should grow at a ~9% CAGR between 2019 and 2022. We recognize a higher risk profile of this business, reflected in a lower P/E multiple in our 2022 SOTP, but also its strong cash flow generation.

2020 earnings: Management reiterated its 2020 EPS guidance despite the COVID-19 pandemic as higher residential water consumption (~70% of total regulated sales volumes) should more than offset lower C&I volumes, and any meaningful COVID-related expenses, if material, should be deferred. Admittedly, AWK's 2020 earnings guidance always seemed conservative to us though we recognize that it's a particularly busy year on the regulatory front with AWK seeking large revenue increases (US $224MM annualized) in four states, including NJ and PA, AWK's largest jurisdictions, with a likely MO rate case coming later this year.

Company Description:
AWK is the largest publicly-traded regulated water and wastewater utility in the US with operations in 16 states, primarily in the Northeast and the Midwest, serving 3.4 million customer accounts. AWK also engages in unregulated contract-based water/wastewater services for military bases (16 bases) and provides water/wastewater line warranty services (homeowner services) to ~1.5 million residential accounts

AWK: EPS breakdown by segment ($)

AWK	2018A	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated utilities	3.32	3.60	3.80	4.16	4.50	7.7%
Unregulated ops	0.33	0.45	0.48	0.51	0.56	7.6%
Parent	-0.35	-0.44	-0.44	-0.44	-0.47	2.5%
Total EPS	**3.30**	**3.61**	**3.84**	**4.23**	**4.59**	**8.3%**
DPS	**1.78**	**1.96**	**2.15**	**2.37**	**2.60**	**10.0%**
Dividend payout	54%	54%	56%	56%	57%	

Source: Company data for 2018-2019; Seaport Global Securities

AWK - 2022 SOTP valuation

AWK - 2022 SOTP	EPS	Multiple	Value per share
Regulated utilities less parent	4.03	27.9x	112.32
Military contracts	0.19	41.9x	7.95
Homeowner services	0.37	25.0x	9.25
Total per share			**129.52**

Source: Seaport Global Securities

Risks

Allowed ROEs for AWK's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings.

Lower sales volumes could weigh on AWK's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWK has a particularly busy regulatory calendar in 2020, with rate cases in three of its largest jurisdictions – NJ, PA and MO.

Potentially higher equity needs due to weakening operating cash flows and underfunded pension funds: Lower customer collections (due to lower sales or non-payment) coupled with growing federal cash taxes and underperforming pension funds should be weighing on operating cash flows of regulated utilities especially during/following the COVID-19 pandemic. That in turn could require some deleveraging of balance sheets of regulated utilities thus more equity. AWK already announced ~$500m in new equity as soon as 2022, but the issuances could be enlarged and accelerated to protect AWK's credit ratings.

AWK	2018A	2019A	2020E	2021E	2022E
Sales	3,440	3,610	3,775	4,008	4,220
Operating expenses	1,773	1,824	1,871	1,919	1,969
EBITDA	1,667	1,786	1,904	2,089	2,251
Depreciation	545	582	626	670	714
EBIT	1,122	1,204	1,278	1,419	1,538
Net interest expense	350	382	402	442	460
Ordinary Profit Before Tax	809	872	926	1,027	1,127
Income tax	216	218	232	257	282
Net profit	593	654	695	770	845
S/O (m)	180	181	181	182	184
Diluted EPS	**3.30**	**3.61**	**3.84**	**4.23**	**4.59**
DPS	**1.78**	**1.96**	**2.15**	**2.37**	**2.60**
Cash	158	90	45	45	45
Financial and Operating Receivables	301	294	311	330	348
Inventory	41	44	44	45	46
Other short-term assets	281	857	292	292	292
Goodwill	1,575	1,501	1,501	1,501	1,501
Other-long term assets	1,458	1,664	1,664	1,664	1,664
Property, plant, and equipment	17,409	18,232	19,475	20,675	21,832
Total assets	**21,223**	**22,682**	**23,332**	**24,552**	**25,727**
Financial liabilities	1,035	814	936	936	936
Operating liabilities	175	203	194	199	204
Other liabilities	884	1,028	851	851	851
Deferred credits and other regulatory liabiliti	5,689	5,872	6,053	6,253	6,396
Long-term debt	7,576	8,639	9,472	9,896	10,408
Shareholders' equity	5,864	6,126	5,827	6,418	6,933
Total liabilities and equity	**21,223**	**22,682**	**23,332**	**24,552**	**25,727**
Net income	565	654	695	770	845
D&A, goodwill amortisation	545	582	626	670	714
Other non cash elements	308	214	181	200	220
Funds from operations	1,418	1,450	1,501	1,640	1,779
Decrease (increase) in non-cash working ca	-32	-67	-26	-15	-91
CFO	**1,386**	**1,383**	**1,475**	**1,625**	**1,688**
Net investments in fixed assets	-1,949	-1,841	-1,865	-1,865	-1,865
Net investments in financial assets	-87	-104	-104	-104	-104
Free cash flow before dividends	**-650**	**-562**	**-494**	**-344**	**-281**
Dividends paid (group + minorities)	-319	-354	-389	-431	-479
Free cash flow after dividends	-969	-916	-883	-775	-760
Increase or (repayment) of capital and subsi	892	857	883	474	562
Increase or (repayment) of financial debt	138	-36	-45	301	198
Adjustment for minorities / miscellaneous	14	27	0	0	0
Increase in cash	75	-68	-45	0	0

Seaport Global

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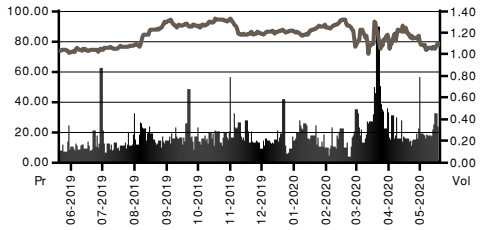
Rating:	**Buy**
Price Target:	**$84.00**

Price Target Metrics:
2022 SOTP valuation which implies 32.6x '22 EPS

Current Price:	**$75.62**
Float:	36.4MM
Diluted Shares:	37.0MM
Short Interest:	1.0MM
Average Daily Volume:	286k
52 Week Range:	$65.11 - $96.64
Market Cap:	**$2,796MM**
Cash and Investments:	$6MM
Debt:	$339MM
Enterprise Value:	$3,129MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Diluted)				
FY	$2.24A	$2.31E	$2.45E	$2.58E
P/E	**33.8x**	**32.8x**	**30.9x**	**29.3x**
Dividends Per Share				
FY	$1.160A	$1.263E	$1.351E	$1.446E
Dividend Yield	**1.5%**	**1.7%**	**1.8%**	**1.9%**

American States Water Company
(NYSE: AWR)

Pricey water utility, but with best-in-class execution

Summary:
We are initiating coverage of AWR with a Buy rating and an US$84 price target based on our 2022 SOTP valuation which implies 32.6x our 2022 EPS. Trading at 29.2x our '22 EPS, AWR is the most expensive utility under our coverage despite a peer-average EPS/DPS annual growth of ~4.9%/~7.6%. Yet, this is the only CA-based water utility which has always earned at least its allowed ROE and the Street (us included) has historically underestimated AWR's earnings power. While losses in a pension account incurred in March pose some EPS headwind for 2020, we still expect the company to beat its 2020 consensus EPS through higher regulated electric and contract-based earnings. A new general rate case and a cost of capital proceeding will determine AWR's 2022 EPS on the water side, but we still expect our/consensus estimates to turn out low.

Highlights

Regulated water/wastewater utilities (~70% of 2022 EPS): Golden States Water Company (GSWC) has been uniquely successful at earning its allowed ROE and getting regulatory approvals for higher water capex through general rate cases and separate advisory letters. The next general rate case (to be filed in July) and the cost of capital proceeding (to be filed in May 2021) should determine GSWC's earnings power for 2022-2024, and we are hoping for meaningful upside to our 2022 EPS due to higher capex though the allowed ROE (to be determined in a separate proceeding) remains uncertain.

Military contracts/ASUS (~21% of 2022 EPS): Through its unregulated American States Utility Services (ASUS) business, AWR provides water/wastewater services to 11 military bases under 50-year inflation-indexed contracts. The contracts offer periodic openers to account for incremental scope of work thus higher expenses or incremental infrastructure upgrades. Given the duration, premium returns, and the exclusive nature of these contracts we see them as even more valuable than the regulated water business. Hence, in our SOTP, we value the contracts at a 50% P/E premium to water utilities. We see at least three pending RFPs for new water/wastewater contracts for military bases, and while the contract awards may get delayed due to COVID-19, we'd expect at least one of these contracts to be awarded to AWR.

2020 earnings: Thanks to revenue decoupling on both the water and electric side, balancing accounts for both purchased water and power costs, and a catastrophic event memorandum account tracking COVID-related expenses, AWR should not see much of a COVID-19 impact on its regulated earnings if not for losses in one of its pension account, an US$0.08 YoY EPS hit in 1Q20. However, it has yet again become apparent to us that we were underestimating AWR's earnings power on the electric/water side. Management expects to fully execute its water/electric capex plan during 2020. The military contracts division saw some cost overruns during 1Q20, but that's just a timing issue.

Company Description:
AWR is the parent of Golden States Water Co. (GSWC), a regulated water (261,000 water connections in 37 systems) and electric utility (24,400 electric connections in one system) in CA, and American States Utility Services (ASUS), which engages in contract-based water and wastewater services primarily for military bases, currently 11 bases.

AWR: EPS breakdown by segment ($)

AWR	2019A	2020E	2021E	2022E	2019-2022 CAGR
Regulated water	1.62	1.64	1.73	1.82	4.1%
Regulated electric	0.15	0.18	0.20	0.21	11.9%
Military contracts/ASUS	0.47	0.49	0.52	0.55	5.4%
Total EPS	**2.24**	**2.31**	**2.45**	**2.58**	**4.9%**
DPS	**1.16**	**1.26**	**1.35**	**1.45**	**7.6%**
Dividend payout	52%	55%	55%	56%	

Source: Company data for 2019; Seaport Global Securities

AWR: 2020 Sum-Of-The-Parts valuation ($)

AWR - SOTP	Metric	Multiple	Price	Anchor PE	PE premium
2022 Regulated Water EPS	1.82	30.7x	$55.91	27.9x	10%
2022 Regulated Electric EPS	0.21	20.7x	$4.35	18.0x	15%
2022 ASUS EPS	0.55	43.2x	$23.78	27.9x	55%
Total equity value/sh			**$84.04**		

Source: Seaport Global Securities

Risks

Allowed ROEs for AWR's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. AWR's allowed ROE for its water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWR should be filing a new water rate case by July 2020 with new rates in effect in January 2021.

Returns in pension accounts impact AWR's earnings in between rate cases in CA: AWR has no balancing account tracking changes in returns in its pension accounts. Those changes can be trued up/reflected in AWR's rates during rate cases, but those take place every three years.

Military contracts are highly competitive: Through its unregulated ASUS subsidiary, AWR provides water and wastewater services to 11 military bases. The company awaits awards of up to three more of these contracts in 2020. We assume that AWR secures at least one new military contract per year in 2020-2022 though AWK, AWR's largest competitor, has been winning most of the contract awards as of late.

AWR	2018A	2019A	2020E	2021E	2022E
Total Revenues	437	474	490	504	525
Total Operating Expenses	336	347	360	369	382
Operating income	101	127	130	136	144
EBT	82	107	109	115	122
Income tax expense	18	25	24	25	27
Net income	$ 64	$ 83	$ 85	$ 90	$ 95
S/O	37	37	37	37	37
Diluted EPS	**$1.72**	**$2.24**	**$2.31**	**$2.45**	**$2.58**
DPS	**$1.06**	**$1.16**	**$1.26**	**$1.35**	**$1.45**
Net income	64	83	85	90	95
Adjustments to reconcile non-cash charges	40	42	46	48	51
Changes in assets and liabilities	33	(8)	(12)	(12)	(12)
CFO	137	117	119	126	134
Capital expenditures	(127)	(152)	(125)	(135)	(135)
Other	(1)	(1)	-	-	-
CFI	(128)	(153)	(125)	(135)	(135)
Issuance/repurchase of common stock	1	1	1	1	1
Long-term debt issued/repaid	(0)	(40)	30	45	45
Short-term debt issued/repaid	37	110	20	15	15
Dividends paid	(39)	(43)	(47)	(50)	(53)
Other	0	4	4	4	4
CFF	(2)	31	7	14	11
Net change in cash and cash equivalents	2	(6)	2	5	10
Cash and cash equivalents, end of period	7	1	3	8	18
Current assets	$ 131	$ 122	$ 125	$ 132	$ 144
PP&E	1,323	1,447	1,526	1,621	1,715
Regulatory and other assets	47	72	72	72	72
Total assets	1,501	1,641	1,723	1,825	1,931
Current liabilities	147	116	157	157	157
Long-term debt	281	281	311	356	401
Other liabilities (including construction)	516	643	643	643	643
Total liabilities	943	1,040	1,111	1,156	1,201
Total Shareholders' Equity	558	601	612	668	730
Liabilities and Shareholders' Equity	$ 1,501	$ 1,641	$ 1,723	$ 1,825	$ 1,931

Seaport Global

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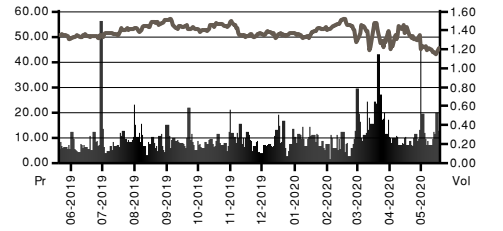
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$43.58**
Float:	48.3MM
Diluted Shares:	48.6MM
Short Interest:	1.0MM
Average Daily Volume:	335k
52 Week Range:	$39.74 - $57.48
Market Cap:	**$2,117MM**
Cash and Investments:	$141MM
Debt:	$1,143MM
Enterprise Value:	$3,120MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Diluted)				
FY	$1.31A	$1.40E	$1.70E	$1.82E
P/E	**33.2x**	**31.1x**	**25.7x**	**23.9x**
Dividends Per Share				
FY	$0.790A	$0.850E	$0.909E	$0.978E
Dividend Yield	**1.8%**	**2.0%**	**2.1%**	**2.2%**

California Water Services Group

(NYSE: CWT)

Potential earnings volatility overshadows strong rate base growth

Summary:

Thanks to its highly underinvested water systems, CWT offers the fastest earnings growth in regulated water earnings among publicly-traded companies – we project an 11.5% EPS CAGR between 2019 and 2022. However, depending on the outcome of a pending rate case in CA and given conservatism of CWT's management, we could see meaningful volatility in CWT's earnings driven by changes in sales volumes as well higher operating expenses related to pensions, medical insurance and COVID-19. Therefore, we are initiating coverage with a Neutral rating as we await the outcome of CWT's general rate case in CA by July.

Highlights

Regulated water (98% of 2022 EPS): Based on the 2019 rate base per customer connection, CWT's water systems are more than a third less invested than those of its public water peers, even despite sharp capex increases in the last two of CWT's rate cases in CA. CWT's earnings largely followed higher capex and we now project an 11% EPS CAGR between 2019 and 2022. However, CWT awaits a proposed decision in its latest general rate case in CA, and while the utility settled with the consumer advocate on key issues back in October 2019, the revenue decoupling and recovery of pension/ medical costs through balancing accounts remain disputed. We don't expect CWT to lose its revenue decoupling though balancing accounts for pension/medical costs might not get renewed, and that could add some volatility in CWT's earnings.

2020 earnings: CWT is tracking COVID-related expenses in a catastrophic memorandum account, but unlike other CA utilities, it plans to expense the costs until they are recovered in the next rate case. Also, depending on the outcome of the pending general rate case, CWT could be exposed to higher pension and medical costs given a potential removal of balancing accounts for these costs. It helps that CWT never provides earnings guidance, but we see downside to our/consensus estimates for 2020-2022 depending on the outcome of the CA rate case.

CWT: EPS/DPS projections

CWT	2018A	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.36**	**1.31**	**1.40**	**1.70**	**1.82**	**11.5%**
DPS	**0.75**	**0.79**	**0.85**	**0.91**	**0.98**	**7.4%**
Dividend payout	55%	60%	61%	54%	54%	

Source: Company data for 2018-2019; Seaport Global Securities

Company Description:

CWT operates regulated water and wastewater utilities in CA, WA, HI and NM, with 490,000 connections in CA (90%), 36,000 connections in WA (recently doubled through an acquisition), 5,000 in HI, and 8,300 connections in NM.

Risks

Allowed ROEs for CWT's regulated water utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. CWT's allowed ROE for its water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. CWT awaits a proposed decision in its 2018 general rate case in CA with rates retroactive to January 1, 2021. Though the utility reached a partial settlement with the consumer advocate late in 2019, outstanding issues involve the continuation of the revenue decoupling and balancing accounts for pension and medical expenses. Without those, CWT could see a meaningful spike in its earnings volatility.

CWT	2018A	2019A	2020E	2021E	2022E
EBIT	132	117	126	149	160
EBITDA	218	209	225	255	274
Net interest expense	38	41	44	45	47
Net income	66	63	69	87	96
EPS	**$1.36**	**$1.31**	**$1.40**	**$1.70**	**$1.82**
DPS	**$0.75**	**$0.79**	**$0.85**	**$0.91**	**$0.98**

CFO	**$ 179**	**$ 169**	**$ 189**	**$ 214**	**$ 231**
Utility plant expenditures	(272)	(274)	(275)	(285)	(285)
Other	(1)	(2)	(2)	(2)	(2)
CFI	**(273)**	**(276)**	**(277)**	**(287)**	**(287)**
Issuance of common stock	(2)	18	96	80	86
Issuance of debt	73	103	28	32	32
Dividends	(36)	(38)	(41)	(44)	(47)
Other	11	20	20	20	20
CFF	**47**	**103**	**103**	**88**	**91**
Change in cash and cash equivalents	(48)	(4)	14	15	35

Net utility plant	2,233	2,406	2,583	2,761	2,932
Cash and cash equivalents	47	43	63	78	112
Other current assets	142	142	142	142	142
Total current assets	189	184	204	219	254
Regulatory assets	354	433	433	433	433
Goodwill	3	3	3	3	3
Other assets	60	85	85	85	85
Total assets	**$ 2,838**	**$ 3,111**	**$ 3,308**	**$ 3,502**	**$ 3,707**
Total common stockholders' equity	$ 730	$ 780	$ 808	$ 851	$ 900
Long-term debt, less current maturities	710	787	814	847	879
Total capitalization	**1,440**	**1,567**	**1,622**	**1,698**	**1,778**
Total current liabilities	321	359	479	578	682
Deferred income taxes	213	223	223	223	223
Pension and postretirement benefits ot	194	259	259	259	259
Other long-term liabilities	257	270	270	270	270
Advances for construction	186	191	191	191	191
Contributions in aid of construction	225	242	262	282	302
Total capitalization and liabilities	**$ 2,838**	**$ 3,111**	**$ 3,308**	**$ 3,502**	**$ 3,707**

Seaport Global

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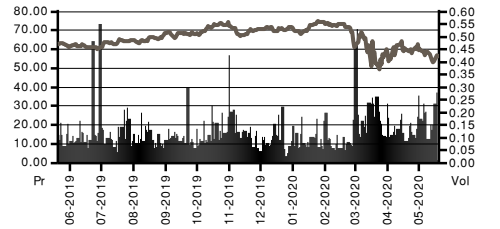
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$55.44**
Float:	26.0MM
Diluted Shares:	28.7MM
Short Interest:	0.3MM
Average Daily Volume:	160k
52 Week Range:	$45.60 - $74.99
Market Cap:	**$1,590MM**
Cash and Investments:	$28MM
Debt:	$1,471MM
Enterprise Value:	$3,032MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Diluted)				
FY	$1.78A	$1.97E	$2.42E	$2.64E
P/E	**31.1x**	**28.2x**	**22.9x**	**21.0x**
Dividends Per Share				
FY	$1.200A	$1.280E	$1.370E	$1.465E
Dividend Yield	**2.2%**	**2.3%**	**2.5%**	**2.6%**

SJW Group

(NYSE: SJW)

Earnings volatility too high to handle

Summary:

We are initiating coverage of SJW with a Neutral rating as volatility in SJW's CA earnings (~60% of our 2022 EPS) meaningfully limits the investment appeal of this pure-play regulated water utility. While last year's merger with Connecticut Water Service reduced SJW's exposure to CA and San Jose Water is likely to request a purchased water cost tracker in its next general rate case, we are at least two years away from clarity on this issue. Additionally, SJW's earnings for 2021/2022 should be highly impacted by its upcoming rate cases in CT and CA with some risks of regulatory clawbacks of any merger-related savings, especially in CA.

Highlights

Regulated water/wastewater utilities (95% of 2022 EPS): SJW operates in states with relatively constructive regulatory regimes for water utilities. CT and ME, the jurisdictions of the recently acquired Connecticut Water Service, offer revenue decoupling mechanisms and capex riders thus ensuring that the utilities fully earn their allowed ROEs. In CA, the state offers three-year visibility into capex and separates rate cases from the ROE/equity ratio proceedings, but consumer advocates have been pushing back against revenue decoupling, and San Jose Water has recently lost its temporary decoupling retroactive to 2018. Worse yet, the utility does not currently have a purchased water tracker which should cost SJW even US$0.30 in EPS this year. In TX, SJW sees meaningful growth opportunities supported by a recently adopted fair value legislation, though admittedly starting from a very low customer count. The state has recently adopted a capex recovery rider (DSIC).

2020 earnings: Management issued its first ever earnings guidance in February, but had to lower it by 13% just two months later due to sharply higher purchased water costs due to the lower surface water availability of just ~1.1B vs. 3.5B gallons typically. Additionally, while SJW can track (and eventually recover) COVID-related expenses (including bad debts) in CA through a catastrophic event memorandum account, the utility could see lower capex deployed in the state during 2020, with a catch up in 2021. While SJW no longer has even a temporary revenue decoupling in CA, the COVID pandemic should result in a net increase in water sales volumes as SJW's customer base is predominantly residential (60% of revenues) and apartment buildings dominate among commercial accounts. Those higher volumes could offer some earnings benefit in 2020.

SJW: EPS/DPS growth prospects

SJW	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.78**	**1.97**	**2.42**	**2.64**	**14.0%**
DPS	**1.20**	**1.28**	**1.37**	**1.47**	**6.9%**
Dividend payout	67%	65%	57%	55%	

Source: Company data for 2019; Seaport Global Securities

Company Description:

SJW Group is a regulated water and wastewater utility serving ~390,000 accounts across CA, CT, TX and ME. SJW merged with Connecticut Water Service in October 2019.

Risks

Allowed ROEs for SJW's regulated water utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. SJW's allowed ROE for its CA water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. SJW should file a rate case for its new CT business in 2021. Also, the CA utility of SJW should go through a general rate case in the state in 2021 and state regulators could attempt to claw-back some synergies related to the recent merger with CTWS.

SJW's CA earnings are highly volatile: Now that SJW no longer has even a temporary decoupling mechanism in CA, it's CA earnings change along with changes in volumes and changes in purchased water costs. SJW plans to ask for a purchased water cost balancing account in the next rate case in CA, but that means that 2021 could be another weak earnings year before the regulatory fix arrives for 2022, if at all.

SJW	2019A	2020E	2021E	2022E
EBITDA	157	210	231	242
Net income	51	56	69	76
EPS diluted	**$1.78**	**$1.97**	**$2.42**	**$2.64**
DPS	**$1.20**	**$1.28**	**$1.37**	**$1.47**
CFO	**$ 130**	**$ 139**	**$ 158**	**$ 167**
CFI	**(1,018)**	**(216)**	**(277)**	**(257)**
Issuance of common stock	0.0	0.0	0.0	0.0
Issuance of debt	502	113	113	113
Dividends	-34	-36	-39	-40
CFF	**485**	**101**	**99**	**99**
Change in cash and cash equivalents	-403	24	-21	9
Net utility plant	2,206	2,323	2,495	2,644
Cash and cash equivalents	18	42	21	30
Other current assets	109	112	115	117
Total current assets	127	154	136	148
Regulatory assets	114	114	114	114
Goodwill	628	628	628	628
Other assets	57	57	57	57
Total assets	**3,132**	**3,276**	**3,430**	**3,591**
Total common stockholders' equity	$ 890	$ 974	$ 990	$ 1,009
Long-term debt, less current	1,261	1,187	1,195	1,203
Total capitalization	**2,151**	**2,161**	**2,185**	**2,212**
Total current liabilities	235	349	460	574
Deferred income taxes	196	193	190	188
Pension and postretirement benefits oth	108	108	108	107
Other long-term liabilities	45	45	45	45
Advances for construction	112	135	157	180
Contributions in aid of construction	286	286	286	286
Total capitalization and liabilities	**3,132**	**3,276**	**3,430**	**3,591**

Seaport Global

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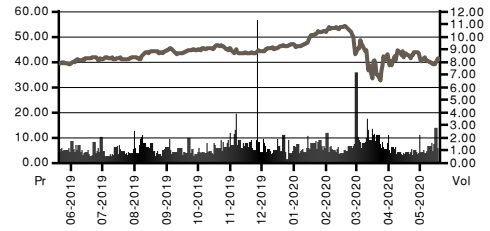
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$39.90**
Float:	244.3MM
Diluted Shares:	255.1MM
Short Interest:	5.3MM
Average Daily Volume:	1,130k
52 Week Range:	$30.40 - $54.52
Market Cap:	**$10,177MM**
Cash and Investments:	$5MM
Debt:	$4,754MM
Enterprise Value:	$14,925MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Diluted)				
FY	$1.47A	$1.55E	$1.66E	$1.76E
P/E	**27.1x**	**25.7x**	**24.1x**	**22.7x**
Dividends Per Share				
FY	$0.907A	$0.970E	$1.038E	$1.111E
Dividend Yield	**2.3%**	**2.4%**	**2.6%**	**2.8%**

Essential Utilities, Inc.

(NYSE: WTRG)

Gas deal muddled the water

Summary:

We are initiating coverage of WTRG with a Neutral rating as we see the stock as close to fairly valued given its water/gas utility mix. WTRG's ~6.3%/7% EPS/DPS CAGR between 2019-2022 should be driven by a 6-7% water and 8-10% rate base growth as well as merger-related synergies related to Peoples Gas. To us, the recent addition of the gas utility to WTRG's core water utility business has diminished the scarcity value of the pure-play water utility in exchange for just a ~150 bps pick-up up in WTRG's consolidated EPS growth. WTRG should try to get some incremental gas utility earnings in PA through a catch-up repair tax deduction, though we'd expect the earnings benefit to be largely clawed back by the state. Assuming no federal infrastructure bill, WTRG could see some incremental municipal water/wastewater M&A on the back of the COVID-19 pandemic, but we prefer to play this benefit through AWK.

Highlights

Regulated water (~67% of 2022 EPS): WTRG's 6-7% water rate base CAGR through 2022 does not incorporate growth through muni acquisitions of water/wastewater systems though WTRG has been very successful at those, especially in PA, its key jurisdiction (68% of 2019 water rate base). All in, we expect WTRG to deliver a ~7% rate base CAGR through 2022, off of 2019 of $5B. Without a federal infrastructure bill supporting upgrades of municipal water/wastewater system, they are likely to be sold to private operators, such as WTRG, at an accelerated pace, following the COVID-19 outbreak, we believe. The growth in WTRG's water rate base should outpace the growth in its water net income through 2022, however, as the Aqua PA pulled forward its earnings through a repair tax election in 2012.

Regulated gas (~33% of 2022 EPS): The 8-10% rate base CAGR on the gas side, together with a recently completed gas rate case in PA and some cost efficiencies related to the merger with WTRG should deliver a 17% net income CAGR for Peoples between 2019 and 2022. That in turn should drive a 6.3% consolidated EPS CAGR for WTRG. That's 100-150 bps higher than our net income growth expectations for WTRG's standalone water business, and admittedly, there could be some further upside to the gas capex and PA could allow WTRG to retain a portion of a catch-up repair tax adjustment. We remain skeptical, however, about the strategic rationale of the gas acquisition as to us it has diminished the scarcity value of WTRG's water utility.

2020 earnings: With higher residential water volumes offsetting lower C&I consumption (~20% of total volumes) and regulators likely allowing for deferrals of COVID costs, WTRG doesn't see risks related to its pro forma 2020 EPS guidance of $1.53-1.58, especially with additional cost levers on the back of the Peoples merger. This should be a quiet year on the regulatory front except for a pending small rate case in NC and a likely filing for a catch-up repair tax deduction in PA, though the timing of the latter is uncertain given the pandemic.

WTRG: EPS breakdown by segment ($)

WTRG	2018A	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated water utilities	1.41	1.47	1.09	1.16	1.22	
Regulated gas utilities	0.00	0.00	0.57	0.67	0.70	
Parent	0.00	0.00	-0.10	-0.17	-0.16	
Total EPS	**1.41**	**1.47**	**1.55**	**1.66**	**1.76**	**6.3%**
DPS	**0.85**	**0.91**	**0.97**	**1.04**	**1.11**	**7.0%**
Dividend payout	60%	62%	62%	63%	63%	

Source: Company data for 2018-2019; Seaport Global Securities

Company Description:

WTRG owns and operates water utilities (1 million accounts) and gas utilities (0.74 million accounts) in 10 states though mainly PA.

Risks

Allowed ROEs for WTRG's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. WTRG's only pending rate case (in NC) is very small.

Lower sales volumes could weigh on WTRG's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. WTRG's regulatory calendar is quiet in 2020, with a pending small rate case in NC, and a likely filing for a catch-up repair tax adjustment for Peoples in PA.

Gas utilities have a higher operating risk than water utilities: Overpressurized gas systems seem to happen more frequently among gas utilities in the US. While we recognize that Peoples Gas is a well-managed system, WTRG's risk profile could further deteriorate with any gas-related operational issues.

WTRG	2018A	2019A	2020E	2021E	2022E
Operational EBITDA	470	505	868	920	984
Operational EBIT	323	349	604	641	690
Net interest expense	99	100	201	209	227
Ordinary Profit Before Tax	252	269	431	459	490
Income tax	1	7	34	37	39
Net profit	251	262	396	422	451
S/O (m)	178	178	255	255	256
Diluted EPS	**1.41**	**1.47**	**1.55**	**1.66**	**1.76**
DPS	**0.85**	**0.91**	**0.97**	**1.04**	**1.11**
Cash	4	1,869	5	5	5
Receivables	101	108	109	113	118
Inventory	16	18	30	30	30
Other short-term assets	26	18	18	18	18
Other-long term assets	887	1,003	3,810	3,810	3,810
Property, plant, and equipment	5,930	6,346	8,962	9,113	9,249
Total assets	**6,965**	**9,362**	**12,934**	**13,089**	**13,230**
Financial liabilities	117	117	496	496	496
Operating liabilities	63	67	109	109	109
Other liabilities	108	108	220	220	220
Deferred credits	2,068	2,057	2,758	2,757	2,757
Long-term debt	2,398	2,943	4,750	5,063	5,384
Shareholders' equity	2,210	4,070	4,601	4,444	4,264
Total liabilities and equity	**6,965**	**9,362**	**12,934**	**13,089**	**13,230**
Net income	251	262	396	422	451
D&A, goodwill amortisation	147	156	264	279	294
Other non cash elements	-54	-40	-6	-6	-6
Funds from operations	344	379	654	695	738
Non-cash working capital	25	-40	43	0	-1
CFO	**369**	**339**	**697**	**694**	**738**
Net investments in fixed assets	-641	-610	-6,555	-765	-780
Net investments in financial assets	2	6	0	0	0
Free cash flow before dividends	**-271**	**-266**	**-5,858**	**-71**	**-42**
Dividends paid	-151	-161	-229	-245	-284
Free cash flow after dividends	-422	-427	-6,087	-316	-327
Changes in capital	2	1,935	2	2	3
Changes in financial debt	421	386	4,220	313	323
Adjustment for minorities / miscellaneous	-2	-28	1	1	1
Increase in cash	-1	1,866	-1,864	0	0

Utilities/Power Disclosures

I, Angie Storozynski, hereby certify: (1) that all of the views expressed in this report accurately reflect my personal views about any and all of the subject securities or issuers; and (2) that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

As with all employees of Seaport Global Securities LLC, a portion of our analysts' compensation is paid from the total collection of revenues from all areas of the firm including but not limited to Investment Banking and Sales and Trading departments. In no instance are research analysts' compensation directly derived from Investment Banking revenues.

Risks & Considerations for American Water Works Company, Inc. American Water Works Company, Inc. (AWK)

Allowed ROEs for AWK's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings.

Lower sales volumes could weigh on AWK's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWK has a particularly busy regulatory calendar in 2020, with rate cases in three of its largest jurisdictions – NJ, PA and MO.

Potentially higher equity needs due to weakening operating cash flows and underfunded pension funds: Lower customer collections (due to lower sales or non-payment) coupled with growing federal cash taxes and underperforming pension funds should be weighing on operating cash flows of regulated utilities especially during/following the COVID-19 pandemic. That in turn could require some deleveraging of balance sheets of regulated utilities thus more equity. AWK already announced ~$500m in new equity as soon as 2022, but the issuances could be enlarged and accelerated to protect AWK's credit ratings.

Other Companies Mentioned in This Report

- American Water Works Company, Inc. (AWK: $120.17, Buy)
- California Water Services Group (CWT: $43.58)
- Essential Utilities, Inc. (WTRG: $39.90)
- American States Water Company (AWR: $75.62)
- SJW Group (SJW: $55.44)

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Buy - The investment outlook and risk/reward over the following 12 months are favorable on an absolute basis and relative to the peer group.

Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.

Sell - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.

NA - A rating is not assigned.

Prior to Feb 1., 2017, Seaport Global Securities analyst ratings included:

Buy - The investment outlook and risk/reward over the following 12 months are very favorable on an absolute basis and relative to the peer group.

Speculative Buy - The investment outlook over the following 12 months is very favorable on an absolute basis and relative to the peer group, however, there is higher than average risk associated with the investment that could result in material loss.

Accumulate - The investment outlook and risk/reward over the following 12 months are favorable on an absolute basis and relative to the peer group.

Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.

Reduce - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.

Sell - The investment outlook and risk/reward over the following 12 months are very unfavorable on an absolute basis and relative to the peer group.

NA - A rating is not assigned.

Ratings Distribution

	Research Coverage		Investment Banking Clients*		
Rating	Count	% of Total	Count	% of Total	% of Rating Category
Buy	49	55.1%	3	75.0%	6.1%
Neutral	36	40.4%	0	0.0%	0.0%
Sell	4	4.5%	1	25.0%	25.0%
Total	89	100.0%	4	100.0%	4.5%

*Investment banking clients are companies for whom Seaport Global Securities has provided investment banking services in the previous 12 months.

Note: Ratings Distribution as of March 31, 2020

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May 28, 2020
Flash Note
Utilities/Power
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Utilities/Power

Investor feedback on utilities/power stocks - Part 2

Summary:
Since our initiation of coverage of the Utilities sector last week, we've collected various feedback from clients. As a follow-up to part 1 (click here), we offer additional perspectives on our coverage universe.

- **DTE**'s midstream business continues to weigh on the stock's valuation though investors recognize DTE's exceptional financial track record plus some potential upside to the midstream earnings.
- Investors recognize that **EXC** and **PEG** do not currently reflect any value for their merchant power businesses, with little differentiation between both stocks, but see little incentive to support the names ahead of FRR decisions in IL/NJ and an update on a federal investigation of EXC's lobbying practices in IL.
- The recent short squeeze and upcoming regulatory updates are likely behind a strong outperformance of **AGR** and **PPL** vs. the XLU since our launch (+7.8% for AGR and +9.3% for PPL vs. +5% for XLU). The stories continue to face challenges, but AGR's NY rate case settlement should be filed any day now and the BOEM should update its review of the Vineyard Wind project in mid-June. Ofgem, the UK electric/gas utility regulator, should update its thoughts on allowed returns for electric transmission and gas distribution networks in late June, and that could be neutral to marginally positive for PPL, we believe.
- The recent rally among smid-cap stocks seems to have supported smaller water utilities, with **AWK**, our top pick for water names, trailing smaller names, **SJW** in particular, despite no fundamental updates. Among water names, AWK continues to attract most investor support, especially from those with an ESG mandate. Hedge funds remain attracted to **WTRG** given potential upside to gas earnings in PA and some expecting WTRG's gas earnings to gradually gain a water P/E multiple vs. the current 30% discount, we estimate. Investors recognize AWR's strong operational and financial track record despite a pension-related earnings hit in 1Q20.

Highlights

Regulated/diversified electric/gas utilities:

AGR (Neutral): The updated rate case settlement for AGR's NY utilities (NYSEG & RG&E) should be out any day and that, together with management's outreach has triggered a debate on AGR's bear investment thesis. In ME, AGR has filed a court challenge to the inclusion of the NECEC electric transmission project on the November ballot – a court decision would need to come out before September 11 when the ballots should be printed. Last week's FERC decision on the MISO electric transmission ROE and the methodology to set it has been widely seen as constructive by investors though more for AEP/FE rather than New England transmission operators (AGR/ES). The new methodology when updated for a 100 bps RTO adder would imply a wider range of reasonableness, with the high end 10.6-10.7%, we estimate. Challenges to FERC transmission ROEs for New England operators are still pending, they cover a different/earlier period (thus a higher interest rate environment) and FERC has not yet opined on additional non-RTO ROE adders and thus a cap on the all-in transmission ROEs for new projects. AGR currently earns ~11.3% in all-in transmission ROEs in CT and ME (vs. ~11.5% for ES), so we/investors don't see much (if any) downside to AGR's transmission earnings assuming higher incentive caps. Management still expects the BOEM to comment on the Vineyard Wind (VW) offshore wind project (a supplement to VW's Environmental Impact Statement) on June 12 and the Bureau to issue the final permit for the project in December 2020. Assuming no additional delays, we hope for some positive implications for AGR and ES.

DTE (Buy): Among all of our Buy-rated names, we had expected most constructive investor feedback on DTE given that the stock seemed to be trading even below the fair value of its regulated utilities (assuming a CMS-like P/E). The feedback has been mixed with the stock just marginally outperforming the XLU since our launch though gaining some strength this week. In general, investors recognize DTE's strong execution track record and its premium regulated utilities in MI. They admit that DTE's midstream business is less commodity-price sensitive than average, that it could benefit from higher gathering demand in the Northeast in 2021 and that NEXUS could see some longer-term contracts if/when ACP/MVP pipelines get delayed. Yet, an average investor would rather create a "synthetic DTE" by buying shares of CMS and a midstream business, though the latter would have to come at a negative equity value to truly reflect DTE's current valuation. We hope that with strong operational execution, no negative updates from Antero/Southwestern, and further construction delays for MVP/ACP the DTE stock should continue to re-rate through the end of 2020.

EXC (Buy)/PEG (Neutral): Investors don't see much difference between the two stocks or the reason to support either one any time soon. Neither implies any value for their respective merchant power businesses even though both should see some upside to their nuclear power earnings from IL and NJ eventually pursuing the FRR option outside of the PJM capacity market. For EXC, investors seem reluctant to support the stock ahead of an update on a pending federal investigation of Exelon's/ComEd's lobbying practices in IL or the November legislative session in the state where the FRR future could be decided. For PEG, though the company thinks no

legislation is needed for NJ to pursue an FRR option, the NJ BPU (state's utility regulator) is unlikely to opine on the FRR until early/mid-2021, we believe. In the meantime, PEG's electric transmission ROE should drop and the company is likely to pursue an equity stake in Orsted's Ocean Wind offshore wind project off the coast in NJ, likely intensifying the debate about the future of margins of PEG's gas plants in NJ/MD/CT.

PPL (Neutral): Investors seem unanimously surprised by our Neutral stance on the name despite ongoing FX pressures and the lack of growth prospects for PPL's US utilities until 2025 or beyond. Our Neutral rating was based a combination of somewhat fair valuation and our expectations that Ofgem's pending review of allowed equity returns for electric transmission and gas distribution won't result in an incremental reduction in the equity return (RORE) on the back of lower interest rates. The returns are still coming down however – starting April 2023, we'd expect the realized RORE for WPD to not exceed 9% vs. ~13-13.5% currently. Since our launch, PPL has outperformed the XLU by 420 bps and now the stock seems to imply a 37% premium to the 2022 EV/RAB for WPD assuming just a 5% discount to PPL's slow growing US utilities. The valuation yet again looks rich to us though PPL's 6% 2020 dividend yield does provide some support, and we believe the company could maintain the current level of dividends given lower regulated utility capex.

Water utilities:

AWK (Buy): Investors continue to like the story and, for once, few questioned AWK's current valuation premium vs. an average electric utility (~52% on our 2022 estimates). Investors appreciate how resilient the stock has been YTD (+0.7% vs. -8.7% for XLU and -5.4% for S&P 500). The heavy regulatory calendar for 2020 doesn't seem to worry investors.

AWR (Buy): Dedicated water utility investors recognize AWR's strong earnings/operational track record despite a large pension-related earnings hit in 1Q20. The high valuation premium we assign to AWR's (and AWK's) military contracts has received some debate, but overall we've heard little to no pushback to our bullish stance on AWR especially given growing volatility in earnings of AWR's peers in CA, CWT and SJW.

WTRG (Neutral): Hedge funds and some long-onlys remain attracted to WTRG given potential upside to gas earnings in PA and some expecting WTRG's gas earnings to gradually gain a water P/E multiple vs. the current 30% discount, we estimate. We recognize incremental cost levers on the back of the Peoples merger and that the look back repair tax application to be filed for the business in PA could deliver incremental earnings though it's tough for us to say how meaningful the EPS benefit would be after sharing with ratepayers. We do admit, however, that the stock does not currently discount any incremental earnings upside in PA.

Utilities/Power Disclosures

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Other Companies Mentioned in This Report

- Avangrid, Inc. (AGR: $43.50, Neutral)
- American States Water Company (AWR: $81.73, Buy)
- PPL Corporation (PPL: $27.60, Neutral)
- Essential Utilities, Inc. (WTRG: $42.87, Neutral)
- Exelon Corporation (EXC: $38.38, Buy)
- SJW Group (SJW: $61.38, Neutral)
- American Electric Power Company, Inc. (AEP: $84.69, Buy)
- American Water Works Company, Inc. (AWK: $123.72, Buy)
- DTE Energy Company (DTE: $108.27, Buy)
- Public Service Enterprise Group Inc. (PEG: $50.56, Neutral)
- Eversource Energy (ES: $80.51, Buy)
- Utilities Select Sector SPDR Fund ETF (XLU: $58.97)
- FirstEnergy Corp. (FE: $42.26, Buy)
- CMS Energy Corporation (CMS: $57.51, Buy)

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Explanation of Ratings

Seaport Global Securities analyst ratings include (effective Feb. 1, 2017):

Buy - The investment outlook and risk/reward over the following 12 months are favorable on an absolute basis and relative to the peer group.
Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.
Sell - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.
NA - A rating is not assigned.

Prior to Feb 1., 2017, Seaport Global Securities analyst ratings included:

Buy - The investment outlook and risk/reward over the following 12 months are very favorable on an absolute basis and relative to the peer group.
Speculative Buy - The investment outlook over the following 12 months is very favorable on an absolute basis and relative to the peer group, however, there is higher than average risk associated with the investment that could result in material loss.
Accumulate - The investment outlook and risk/reward over the following 12 months are favorable on an absolute basis and relative to the peer group.
Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.
Reduce - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.
Sell - The investment outlook and risk/reward over the following 12 months are very unfavorable on an absolute basis and relative to the peer group.
NA - A rating is not assigned.

Ratings Distribution

	Research Coverage		Investment Banking Clients*		
Rating	Count	% of Total	Count	% of Total	% of Rating Category
Buy	49	55.1%	3	75.0%	6.1%
Neutral	36	40.4%	0	0.0%	0.0%
Sell	4	4.5%	1	25.0%	25.0%
Total	89	100.0%	4	100.0%	4.5%

*Investment banking clients are companies for whom Seaport Global Securities has provided investment banking services in the previous 12 months.

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Utilities

2Q20 Earnings Preview (Correction*)

Summary:
We expect strong 2Q20 earnings prints for electric utilities thanks to strong residential electric sales, sooner-than expected recovery in C&I loads, and aggressive cost-cutting. Consensus estimates look stale to us, but we expect the strongest positive surprises from MI utilities, **CMS** and **DTE**, though no increase in the 2020 EPS guidance for **DTE** at this point, **SRE**, thanks to tax benefits and cost efficiencies at SDG&E/SoCalGas, and **AEP**, thanks to aggressive cost-cutting which started before COVID. We struggle to call **ETR** results.

There should be plenty of volatility in earnings of water stocks, **CWT** and **AWR** in particular, and that's even before CA makes changes to the revenue decoupling mechanism (WRAM). There should be few surprises from **AWK** and **WTRG**. We chase **AWK** and raise our price target to $145.50 from $130.

Power/retail stocks in TX, **NRG** and **VST**, should report very strong results even though we have yet to see scarcity in spot power prices in ERCOT. Thanks to solid 1H20 results both **NRG** and **VST** should be tracking ahead of the midpoint of their 2020 EBITDA guidance ranges, but we don't expect them to narrow/raise the guidance just yet. We raised our 2021/2022 EBITDA estimates for **VST** to reflect additional hedges.

We updated 2Q20 earnings estimates for: **AEP, AES, AGR, ATO, AWK, AWR, CMS, CWT, D, DTE, DUK, EIX, ES, ETR, EXC, FE, NRG, PCG, PEG, PPL, SJW, SO, SRE, VST and WTRG**. We also increased our price target for **AWK**.
*(*Correction made to the original version of this note: Our 2Q20 estimate for PEG displayed on page 3 has been corrected.)*

Highlights

Electric/gas utilities

An earlier than expected recovery in C&I loads coupled with cost-cutting and some YoY weather benefit should deliver strong earnings beats for MI utilities, **CMS** and **DTE**, in our view. **AEP's** aggressive cost-cutting started pre-COVID should support 2Q20 results while the load weakness should be largely in-line with management's forecasts from the 1Q20 call. The company plans to provide an updated capex and cash flow schedule through 2023 which should incorporate lower capex in 2020 and the $2B North Central Wind project (and its financing). **D** and **SO** should have some weather-related headwinds in 2Q20, but updates on the Vogtle cost schedule (Unit 3 % completion in May and June) and cost contingency being utilized should dominate **SO**'s earnings call. **SO** kept its May 2021 in-service date for Vogtle unit 3 to help with managing the scheduling of the construction work on the site, but the decision has not been well-received by investors. **DUK** plans to provide an update on its capex replacement for the cancelled ACP pipeline only on the 4Q20 earnings call, but we'd expect the replacement for the $2B capex reduction to start only in 2022.

Water utilities

AWK and **WTRG** should have relatively easy YoY comps in the Northeast/Mid-Atlantic as 2Q19 was very rainy, and **WTRG** now has additional cost levers thanks to the Peoples Gas merger. We don't expect any meaningful COVID impacts on their 2Q20 or annual 2020 earnings. Intervener testimonies in **AWK's** NJ rate case should be made public any day now – this rate case together with similar proceedings in PA and MO should dominate **AWK's** earnings call. We are chasing **AWK's** stock by raising our price target to $145.50 from $130 previously.

WTRG's pending acquisition of the Delcora wastewater system in PA has run into legal issues, making investors concerned about the future of municipal water/wastewater M&A.

In CA, Commissioner Guzman Aceves has yet again proposed to do away with the current full revenue decoupling mechanism (WRAM) for investor-owned water utilities, calling it ineffective at promoting water conservation. The CPUC should consider/vote on the proposed decision as soon as August 6. **AWR's** GSWC will have filed its new General Rate Case (GRC) by then while **CWT's** and **AWK's** GRCs in CA are already pending. We therefore assume that any changes to the WRAM, if any, would apply to these companies only in the next GRC, starting in 2024.

CWT keeps waiting for an approval of its GRC to record a revenue increase. In the meantime, **CWT's** quarterly results should continue to come well below expectations. We expect **AWR** to fully recoup the $0.08 EPS hit recorded in 1Q20 related to the underperformance of its pension funds.

Power/retail

The TX load has recovered to pre-COVID levels and while we have seen no real scarcity in power prices so far this summer, strong retail results supported by lower than expected bad debt and optimization of generation hedges should support 2020 EBITDA for **VST** and **NRG** at least at the midpoint of their annual guidance. We don't expect them to narrow the guidance yet, however, as August tends to be a crucial earnings month for both companies.

NRG should provide an update on its 2020 capital allocation strategy which might include another retail acquisition. **VST** hasn't given up on some uplift to forward power curves in TX happening in late August/early September, like we saw last year. Yet, even without the recovery and thanks to additional power hedges, the downside to 2021 EBITDA seems now lower than the $200-250MM below the midpoint of the 2020 guidance range that VST used to quote as a COVID-related downside scenario. Therefore, we raised our 2021/2022 EBITDA expectations for VST to $3,135MM/3,044MM up from $3,034MM/3,009MM, respectively.

We expect **AES** to keep its new/lowered EPS guidance range for 2020 though 2Q20 should be weak on a combination of the DPL/ Argentina/IPL hits, with the earnings uplift from cost-cutting and Southland's PPA should kick in only in 3Q20. The OH and IN load seem to be performing ahead of management's expectations from the 1Q20 earnings call. We await an update on another divestiture of coal-fired plant, potentially Maritza in Bulgaria, we believe.

2Q20 EPS/EBITDA Estimates for Utilities and Power Stocks

Regulated electric/gas utilities	Seaport 2Q20 EPS ($)	Consensus 2Q20 EPS ($)	Seaport/Consensus
AEP	**1.09**	0.99	10%
AGR	0.36	0.33	9%
ATO	0.80	0.76	5%
CMS	**0.46**	0.36	28%
D	0.81	**N/A**	N/A
DTE	**1.35**	1.14	18%
DUK	1.05	1.02	3%
EIX	1.20	1.16	3%
ES	0.76	0.79	-4%
ETR	**1.10**	1.25	-12%
EXC	**0.42**	0.45	-7%
FE	0.56	0.55	2%
PCG	1.00	0.94	6%
PEG	**0.57**	0.62	-8%
PPL	0.55	0.56	-2%
SO	0.66	0.69	-4%
SRE	**1.82**	1.19	53%

Regulated water utilities	Seaport 2Q20 EPS ($)	Consensus 2Q20 EPS ($)	Seaport/Consensus
AWK	0.98	0.95	3%
AWR	**0.70**	0.63	11%
CWT	**0.25**	0.64	-61%
SJW	0.70	0.66	6%
WTRG	0.23	0.24	-4%

Power/retail	Seaport 2Q20 EPS/EBITDA $/$MM	Consensus 2Q20 EPS/EBITDA $/$MM	Seaport/Consensus
AES	**0.22**	0.28	-21%
NRG	550	521	6%
VST	**840**	729	15%

Source: FactSet for consensus, Seaport Global Securities

Comp Sheet: Utilities & Power

Regulated electric utilities	Share price ($) 7/15/2020	Rating	Price target ($)	2022 PE	Premium/Discount to Avg 2022 P/E ex
AEP	84.68	Buy	91.00	**16.8x**	-5%
AGR	45.20	Neutral	N/A	**17.3x**	-2%
CMS	59.74	Buy	65.00	**19.6x**	11%
D	75.45	Buy	91.00	**18.2x**	3%
DTE	109.20	Buy	133.50	**14.7x**	-17%
DUK	80.43	Neutral	N/A	**15.8x**	-11%
EIX	55.28	Buy	70.00	**10.2x**	-42%
ES	85.00	Buy	93.00	**20.6x**	17%
ETR	96.24	Buy	114.00	**15.2x**	-14%
EXC	38.05	Buy	44.00	**14.0x**	-21%
FE	40.82	Buy	50.00	**14.8x**	-16%
PCG	9.20	Neutral	50.00	**8.5x**	-52%
PEG	52.40	Neutral	N/A	**15.4x**	-13%
PPL	25.69	Sell	25.00	**14.3x**	-19%
SO	53.02	Buy	63.00	**14.9x**	-16%
SRE	123.15	Buy	142.00	**15.0x**	-15%
Average P/E for regulated electrics with exclusions				**17.7x**	

Regulated water utilities	Share price ($) 7/15/2020	Rating	Price target ($)	2022 PE	Premium/Discount to Avg 2022 P/E ex
AWK	134.06	Buy	145.50	**29.2x**	9%
AWR	77.21	Buy	84.00	**29.9x**	12%
CWT	48.00	Neutral	N/A	**26.4x**	-1%
SJW	62.63	Neutral	N/A	**23.7x**	-11%
WTRG	43.04	Neutral	N/A	**24.4x**	-9%
Average P/E for regulated water utilities				**26.7x**	**51%**

Power/retail	Share price ($) 7/15/2020	Rating	Price target ($)	2022 PE/FCF yield	Premium/Discount to Avg 2022 P/E ex
AES	15.07	Buy	17.00	**9.1x**	N/A
NRG	34.02	Buy	42.50	**16.7%**	N/A
VST	19.30	Buy	24.00	**20.0%**	N/A

Source: FactSet, Seaport Global Securities

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- Sempra Energy (SRE: $123.15, Buy)
- NRG Energy, Inc. (NRG: $34.02, Buy)
- Entergy Corporation (ETR: $96.24, Buy)
- Vistra Energy Corp. (VST: $19.30, Buy)
- American States Water Company (AWR: $77.21, Buy)
- Essential Utilities, Inc. (WTRG: $43.04, Neutral)
- Duke Energy Corp. (DUK: $80.43, Neutral)
- Atmos Energy Corp. (ATO: $100.64, Buy)
- Eversource Energy (ES: $85.00, Buy)
- FirstEnergy Corp. (FE: $40.82, Buy)
- Public Service Enterprise Group Inc. (PEG: $52.40, Neutral)
- SJW Group (SJW: $62.63, Neutral)
- DTE Energy Company (DTE: $109.20, Buy)
- Southern Co. (SO: $53.02, Buy)
- American Electric Power Company, Inc. (AEP: $84.68, Buy)
- California Water Services Group (CWT: $48.00, Neutral)
- American Water Works Company, Inc. (AWK: $134.06, Buy)
- AES Corporation (AES: $15.07, Buy)
- Dominion Energy, Inc. (D: $75.45, Buy)
- Avangrid, Inc. (AGR: $45.20, Neutral)
- Edison International (EIX: $55.28, Buy)
- Exelon Corporation (EXC: $38.05, Buy)
- PG&E Corporation (PCG: $9.20, Neutral)
- PPL Corporation (PPL: $25.69, Sell)

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Neutral	42	34.1%	0	0.0%	0.0%
Sell	5	4.1%	1	33.3%	20.0%
Total	123	100.0%	3	100.0%	2.4%

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August 11, 2020
Industry Update
Utilities

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Utilities

Water utilities – Updated thoughts following 2Q20 earnings season

Summary:
There is no better utility than a water utility, but even they have regulatory issues like potential changes to the revenue decoupling in CA or regulatory/legal delays to asset acquisitions/sales like with **AWK** in NY or **WTRG** in PA. **AWK** and **AWR** remain our favorite water utilities, and we are impressed with **WTRG**'s strong growth prospects on the gas side, especially if the catch-up repair tax deduction in PA is approved. We updated our thoughts on **AWK, CWT, SJW,** and **WTRG**. We are raising our PT for **AWK**. Also note that we published an update on **AWR** last week (link).
Managements of **AWK** and **AWR** will be attending Seaport's Virtual Summer Conference on August 26. Please use the link to register for the event (registration link).

Highlights

AWK – Teflon stock: The COVID-related drop in C&I sales volumes more than offset higher residential sales, leading to a $0.04 EPS hit to AWK's regulated earnings in 2Q20. Management chose not to offset it with cost-cutting though the hot and dry summer in the Mid-Atlantic and the Midwest should do the trick. We have very limited visibility into AWK's large pending rate cases (requesting $294MM in annualized revenue increases) and the sale of the NY system is getting delayed. Yet, those are still not enough to diminish AWK's investment appeal to us. Therefore, we reiterate our Buy rating and raise our PT to $152 from $145.50.

AWR – Appealing EPS/DPS growth despite decoupling uncertainty: Potential changes to AWR's water revenue decoupling caught us by surprise, but we'd still expect the company to earn its allowed ROEs on the water and electric side, and the military contract business to deliver incremental growth. We raise our 2020/2022 EPS and 2020-2022 DPS estimates. We recently trimmed our PT to $83 from $84 to reflect the risk to the water decoupling and reiterated our Buy rating.

CWT – Waiting continues: Last week, the CPUC delayed its decision on changes to the full decoupling mechanism for water utilities (WRAM). Yet, depending on the outcome of a pending rate case in CA (GRC) and given conservatism of CWT's management, we could see meaningful volatility in CWT's earnings driven by changes in sales volumes as well higher operating expenses related to pensions, medical insurance and COVID-19. The stock trades at a 7% 2022 P/E discount to an average water utility which seems fair to us.

SJW – Delivering against lowered guidance: SJW maintained its lowered 2020 EPS guidance range as the $0.30/share EPS hit for higher purchased water costs remained unchanged, water sales were not materially impacted by COVID, and the accounts collections, though slowing, remained strong. The stock trades at an 8% 2022 P/E discount to an average water utility which seems a bit rich to us given the higher-than-average volatility in SJW's sales volumes and thus realized ROEs. We maintain our Neutral rating.

WTRG – Catch-up repair tax deduction in PA: WTRG sees no negative earnings impact from COVID as stronger residential sales offset lower C&I volumes, and the recent merger with Peoples Gas adds cost levers. The catch-up repair tax deduction in PA would extend the strong mid-teen annual EPS growth rate for gas through even 2026. The future of the DELCORA wastewater acquisition remains uncertain, but WTRG already issued equity to finance it. We maintain our Neutral rating.

Comp sheet - water utilities

Regulated water utilities	Share price ($) 8/10/2020	Rating	Price target ($)	Market cap ($B)	2020 Div Yield	2022 EPS ($)	2022 PE
AWK	149.11	Buy	152.00	27.0	1.4%	4.59	**32.5x**
AWR	79.85	Buy	83.00	3.0	1.6%	2.61	**30.6x**
CWT	48.98	Neutral	N/A	2.4	1.7%	1.82	**26.9x**
SJW	71.06	Neutral	N/A	2.0	1.8%	2.64	**26.9x**
WTRG	47.81	Neutral	N/A	11.7	2.0%	1.77	**27.0x**
Average P/E for regulated water utilities					**1.7%**		**28.8x**

Source: FactSet, Seaport Global Securities

Seaport Global

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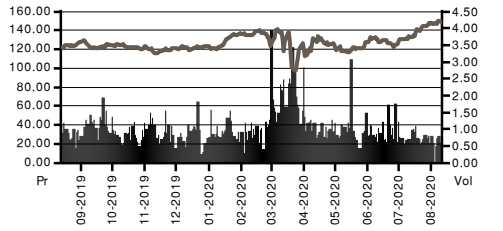
Rating:	**Buy**
Price Target:	**$152.00**

Price Target Metrics:
2022 SOTP valuation implying 33.2x 2022 EPS

Current Price:	**$149.11**
Float:	180.7MM
Diluted Shares:	181.0MM
Short Interest:	2.5MM
Average Daily Volume:	763k
52 Week Range:	$92.00 - $150.47
Market Cap:	**$26,989MM**
Cash and Investments:	$569MM
Debt:	$9,593MM
Enterprise Value:	$36,013MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Adjusted)							
FY	$3.61A	$3.84	$3.85E	$4.23	$4.23E	$4.59	$4.59E
P/E	**41.3x**		**38.8x**		**35.2x**		**32.5x**
Dividends Per Share							
FY	$1.955A	$2.150	$2.150E	$2.365	$2.365E	$2.600	$2.600E
Dividend Yield	**1.3%**		**1.4%**		**1.6%**		**1.7%**

American Water Works Company, Inc.

(NYSE: AWK)

Teflon stock; raising PT

Summary:
The COVID-related drop in C&I sales volumes more than offset higher residential sales, leading to a $0.04 EPS hit to AWK's regulated earnings in 2Q20. Management chose not to offset it with cost-cutting though the hot and dry summer in the Mid-Atlantic and the Midwest should do the trick. We have very limited visibility into AWK's large pending rate cases (requesting $294MM in revenue increases) and the sale of the NY system is getting delayed. Yet, those are still not enough to diminish AWK's investment appeal to us. Therefore, we reiterate our Buy rating and raise our PT to $152 from $145.50.

Highlights

COVID hit to earnings: In 1H20, the COVID-related pick up in residential sales volumes was not enough to offset lower C&I sales, leading to a $0.04 EPS hit to regulated earnings. Management doesn't want to make arbitrary cost reductions to offset this (hopefully) one-time earnings hit. Given the hot and dry summer in the Mid-Atlantic and the Midwest, the weather-driven spike in usage should offset the COVID expenses, especially as AWK's water demand should have become more sensitive to CDDs and changes in precipitation levels, we believe.

Rate cases: 2020 is a very busy regulatory year for AWK, and we have little clarity on its pending rate cases, in particular in NJ and CA. The interveners in the NJ case filed their testimonies, but those haven't been made public by the regulator/BPU. In CA, the regulator/CPUC proposed to remove full revenue decoupling for water utilities (WRAM) given that it has not resulted in water conservation. The vote of the Commission on this issue has been delayed, and for now, we assume that AWK's pending general rate case in the state should not be affected thus providing visibility into realized ROEs in CA through 2023.

NY asset sale: In November 2019, AWK announced the sale of its NY operations to Liberty Utilities for $608MM and hoped to finalize the transaction in 2H20. The regulatory review of the deal got originally delayed due to COVID, and the NY PSC recently extended from August 3 to October 15 the deadline for munis to submit municipalization proposals for their systems within AWK's NY service territory. Long Island, NY is a challenging jurisdiction for AWK, so we remain hopeful the sale transaction should eventually close, and the ~$400MM in net proceeds should offset AWK's future equity needs.

Estimates and valuation: Our 2021/2022 EPS estimates remain unchanged as we await outcomes of AWK's numerous rate cases. We raised our 2020 EPS estimate to $3.85 from $3.84 based on YTD results and as we expect the summer weather to offset the COVID impact. We raised our PT to $152 from $145.50 as we continue to chase the stock. Our new PT is based on our 2022 SOTP valuation and implies a 33.2x 2022 EPS up from 32x previously.

Company Description:
AWK is the largest publicly-traded regulated water and wastewater utility in the US with operations in 16 states, primarily in the Northeast and the Midwest, serving 3.4 million customer accounts. AWK also engages in unregulated contract-based water/wastewater services for military bases (16 bases) and provides water/wastewater line warranty services (homeowner services) to ~1.5 million residential accounts

AWK: EPS breakdown by segment ($)

AWK	2018A	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated utilities	3.32	3.60	3.92	4.32	4.67	9.1%
Unregulated ops	0.33	0.45	0.49	0.52	0.56	7.6%
Parent	-0.35	-0.44	-0.56	-0.61	-0.64	13.3%
Total EPS	**3.30**	**3.61**	**3.85**	**4.23**	**4.59**	**8.3%**
DPS	**1.78**	**1.96**	**2.15**	**2.37**	**2.60**	**10.0%**
Dividend payout	54%	54%	56%	56%	57%	

Source: Company data for 2018-2019; Seaport Global Securities

AWK: 2020 SOTP valuation ($)

AWK - 2022 SOTP	EPS	Multiple	Value per share
Regulated utilities less parent	4.03	32.3x	130.17
Military contracts	0.19	50.0x	9.50
Homeowner services	0.37	32.3x	11.95
Total per share			**151.62**

AWK	2018A	2019A	2020E	2021E	2022E
Sales	3,440	3,610	3,777	4,010	4,221
Operating expenses	1,773	1,824	1,871	1,919	1,969
EBITDA	1,667	1,786	1,906	2,091	2,253
Depreciation	545	582	626	670	714
EBIT	1,122	1,204	1,280	1,421	1,539
Net interest expense	350	382	402	442	460
Ordinary Profit Before Tax	809	872	928	1,029	1,129
Income tax	216	218	232	257	282
Net profit	593	654	696	771	847
S/O (m)	180	181	181	182	184
Diluted EPS	**3.30**	**3.61**	**3.85**	**4.23**	**4.59**
DPS	**1.78**	**1.96**	**2.15**	**2.37**	**2.60**
Cash	158	90	45	45	45
Financial and Operating Receivables	301	294	311	330	348
Inventory	41	44	44	45	46
Other short-term assets	281	857	292	292	292
Goodwill	1,575	1,501	1,501	1,501	1,501
Other-long term assets	1,458	1,664	1,664	1,664	1,664
Property, plant, and equipment	17,409	18,232	19,475	20,675	21,832
Total assets	**21,223**	**22,682**	**23,332**	**24,552**	**25,727**
Financial liabilities	1,035	814	936	936	936
Operating liabilities	175	203	194	199	204
Other liabilities	884	1,028	851	851	851
Deferred credits and other regulatory liabiliti	5,689	5,872	6,053	6,254	6,397
Long-term debt	7,576	8,639	9,470	9,893	10,403
Shareholders' equity	5,864	6,126	5,828	6,420	6,937
Total liabilities and equity	**21,223**	**22,682**	**23,332**	**24,552**	**25,727**
Net income	565	654	696	771	847
D&A, goodwill amortisation	545	582	626	670	714
Other non cash elements	308	214	181	201	220
Funds from operations	1,418	1,450	1,503	1,642	1,780
Decrease (increase) in non-cash working ca	-32	-67	-26	-15	-91
CFO	**1,386**	**1,383**	**1,477**	**1,626**	**1,690**
Net investments in fixed assets	-1,949	-1,841	-1,865	-1,865	-1,865
Net investments in financial assets	-87	-104	-104	-104	-104
Free cash flow before dividends	**-650**	**-562**	**-492**	**-343**	**-279**
Dividends paid (group + minorities)	-319	-354	-389	-431	-479
Free cash flow after dividends	-969	-916	-881	-774	-758
Increase or (repayment) of capital and subsi	892	857	881	473	560
Increase or (repayment) of financial debt	138	-36	-45	301	198
Adjustment for minorities / miscellaneous	14	27	0	0	0
Increase in cash	75	-68	-45	0	0

Seaport Global

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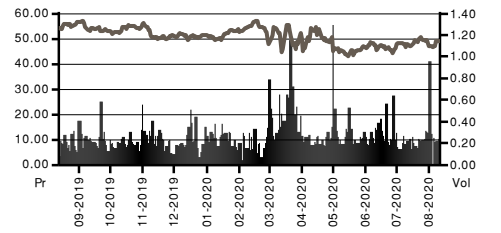
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$48.98**
Float:	48.9MM
Diluted Shares:	48.9MM
Short Interest:	0.8MM
Average Daily Volume:	263k
52 Week Range:	$39.74 - $57.48
Market Cap:	**$2,397MM**
Cash and Investments:	$114MM
Debt:	$1,182MM
Enterprise Value:	$3,465MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
FY	$1.31A	$1.40	$1.39E	$1.70	$1.70E	$1.82	$1.82E
P/E	**37.3x**		**35.2x**		**28.8x**		**26.9x**
Dividends Per Share							
FY	$0.790A	$0.850	$0.850E	$0.909	$0.909E	$0.978	$0.978E
Dividend Yield	**1.6%**		**1.7%**		**1.9%**		**2.0%**

California Water Services Group

(NYSE: CWT)

Waiting continues

Summary:

Last week, the CPUC delayed its decision on changes to the full decoupling mechanism for water utilities (WRAM). Yet, depending on the outcome of a pending rate case in CA (GRC) and given conservatism of CWT's management, we could see meaningful volatility in CWT's earnings driven by changes in sales volumes as well higher operating expenses related to pensions, medical insurance and COVID-19. The stock trades at a 7% 2022 P/E discount to an average water utility which seems fair to us.

Highlights

Potential changes to revenue decoupling: One of CPUC Commissioner has renewed her previous proposal to do away with WRAM for CA water utilities as, according to her, it has failed to result in water conservation. The proposed decision related to this issue has been held by the Commission at least until the August 27 meeting of the CPUC. The Commissioner proposed to adopt WRAM changes only in the next rate following the CPUC approval which, if adopted as currently proposed, would mean CWT should retain the full decoupling until the end of 2022, our current assumption.

Awaiting proposed decision in 2020 GRC: The CPUC should issue a proposed decision in this case by late August. While most of the issues in the rate case were settled, the revenue decoupling mechanism and balancing accounts for pension and healthcare expenses were not a part of the settlement.

Estimates and valuation: We lowered our 2020 EPS estimate by $0.01 to $1.38 to reflect COVID-related expenses which are being expensed despite a catastrophic memorandum account which other CA utilities use to defer these costs. CWT trades at a 7% 2022 P/E discount to an average water utility in the US despite premium EPS growth prospects. Yet, the discount seems fair to us given the ongoing uncertainty regarding CWT's general rate case and the potential volatility in CWT's future earnings power.

Company Description:

CWT operates regulated water and wastewater utilities in CA, WA, HI and NM, with 490,000 connections in CA (90%), 36,000 connections in WA (recently doubled through an acquisition), 5,000 in HI, and 8,300 connections in NM.

CWT: EPS breakdown by segment ($)

CWT	2018A	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.36**	**1.31**	**1.39**	**1.70**	**1.82**	**11.5%**
DPS	**0.75**	**0.79**	**0.85**	**0.91**	**0.98**	**7.4%**
Dividend payout	55%	60%	61%	54%	54%	

Source: Company data for 2018-2019; Seaport Global Securities

CWT	2018A	2019A	2020E	2021E	2022E
EBIT	132	117	125	149	160
EBITDA	218	209	224	255	274
Net interest expense	38	41	44	45	47
Net income	66	63	68	87	96
EPS	**$1.36**	**$1.31**	**$1.39**	**$1.70**	**$1.82**
DPS	**$0.75**	**$0.79**	**$0.85**	**$0.91**	**$0.98**

CFO	**$ 179**	**$ 169**	**$ 188**	**$ 214**	**$ 231**
Utility plant expenditures	(272)	(274)	(275)	(285)	(285)
Other	(1)	(2)	(2)	(2)	(2)
CFI	**(273)**	**(276)**	**(277)**	**(287)**	**(287)**
Issuance of common stock	(2)	18	96	80	86
Issuance of debt	73	103	28	32	32
Dividends	(36)	(38)	(41)	(44)	(47)
Other	11	20	20	20	20
CFF	**47**	**103**	**103**	**88**	**91**
Change in cash and cash equivalents	(48)	(4)	13	15	35

Net utility plant	2,233	2,406	2,583	2,761	2,932
Cash and cash equivalents	47	43	62	77	112
Other current assets	142	142	142	142	142
Total current assets	189	184	204	219	253
Regulatory assets	354	433	433	433	433
Goodwill	3	3	3	3	3
Other assets	60	85	85	85	85
Total assets	**$ 2,838**	**$ 3,111**	**$ 3,307**	**$ 3,501**	**$ 3,707**
Total common stockholders' equity	$ 730	$ 780	$ 807	$ 850	$ 899
Long-term debt, less current maturities	710	787	814	847	879
Total capitalization	**1,440**	**1,567**	**1,622**	**1,697**	**1,778**
Total current liabilities	321	359	479	578	682
Deferred income taxes	213	223	223	223	223
Pension and postretirement benefits ot	194	259	259	259	259
Other long-term liabilities	257	270	270	270	270
Advances for construction	186	191	191	191	191
Contributions in aid of construction	225	242	262	282	302
Total capitalization and liabilities	**$ 2,838**	**$ 3,111**	**$ 3,307**	**$ 3,501**	**$ 3,707**

Seaport Global

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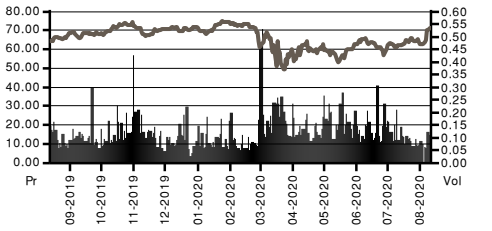
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$71.06**
Float:	26.0MM
Diluted Shares:	28.7MM
Short Interest:	0.5MM
Average Daily Volume:	94k
52 Week Range:	$45.60 - $74.99
Market Cap:	**$2,038MM**
Cash and Investments:	$23MM
Debt:	$1,508MM
Enterprise Value:	$3,523MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
FY	$1.78A	$1.97	$2.00E	$2.42	$2.43E	$2.64	$2.64E
P/E	**39.8x**		**35.5x**		**29.3x**		**26.9x**
Dividends Per Share							
FY	$1.200A	$1.280	$1.280E	$1.370	$1.370E	$1.465	$1.465E
Dividend Yield	**1.7%**		**1.8%**		**1.9%**		**2.1%**

SJW Group

(NYSE: SJW)

Delivering against lowered guidance

Summary:

SJW maintained its lowered 2020 EPS guidance range as the $0.30/share EPS hit for higher purchased water costs remained unchanged, water sales were not materially impacted by COVID, and the accounts collections, though slowing, remained strong. The stock trades at an 8% 2022 P/E discount to an average water utility which seems a bit rich to us given the higher-than-average volatility in SJW's sales volumes and thus realized ROEs. We maintain our Neutral rating.

Highlights

CA: The water usage volumes tracked authorized sales levels with higher residential sales offsetting lower C&I volumes. San Jose Water had adequate water supplies and continues to expect a ~$0.30 EPS hit in 2020 from the lower availability of surface water. The utility's three-year capex in CA of $320MM remains achievable.

CT: The recent Isaiah storm caused widespread power outages in the state, forcing ~100 facilities of CT Water to run on back-up generators, but the water service continued uninterrupted. We assume that Connecticut Water should be able to defer and subsequently recover incremental costs related to the storm.

Estimates and valuation: SJW reaffirmed its previously lowered 2020 EPS guidance range of $1.95-2.05. In 1H20, SJW recorded $0.12/share in merger-related cost benefits in $0.12/share in other benefits, ahead of our prior expectations. We raised our 2020/2021 EPS estimates to $2.00/2.43 from $1.97/2.42 to reflect stronger-than-expected sales volumes in CA during 2020 and some incremental cost efficiencies in both 2020 and 2021. SJW trades at an 8% 2022 P/E discount to an average water utility while offering a stronger-than-average EPS growth (though with an above-average volatility) and an average DPS growth. To us, SJW deserves a 10%+ discount to an average utility and that's why we stick to our Neutral rating.

Company Description:

SJW Group is a regulated water and wastewater utility serving ~390,000 accounts across CA, CT, TX and ME. SJW merged with Connecticut Water Service in October 2019.

SJW: EPS breakdown by segment ($)

SJW	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.78**	**2.00**	**2.43**	**2.64**	**14.1%**
DPS	**1.20**	**1.28**	**1.37**	**1.47**	**6.9%**
Dividend payout	67%	64%	56%	55%	

Source: Company data for 2019; Seaport Global Securities

SJW	2019A	2020E	2021E	2022E
EBITDA	157	213	242	253
Net income	51	57	70	76
EPS diluted	**$1.78**	**$2.00**	**$2.43**	**$2.64**
DPS	**$1.20**	**$1.28**	**$1.37**	**$1.47**
CFO	**$ 130**	**$ 151**	**$ 169**	**$ 178**
CFI	**(1,018)**	**(216)**	**(277)**	**(257)**
Issuance of common stock	0.0	0.0	0.0	0.0
Issuance of debt	502	113	113	113
Dividends	-34	-36	-39	-40
CFF	**485**	**101**	**99**	**99**
Change in cash and cash equivalents	-403	36	-9	20
Net utility plant	2,206	2,312	2,473	2,611
Cash and cash equivalents	18	54	45	65
Other current assets	109	112	115	117
Total current assets	127	166	159	182
Regulatory assets	114	114	114	114
Goodwill	628	628	628	628
Other assets	57	57	57	57
Total assets	**3,132**	**3,277**	**3,431**	**3,593**
Total common stockholders' equity	$ 890	$ 967	$ 984	$ 1,003
Long-term debt, less current	1,261	1,187	1,195	1,203
Total capitalization	**2,151**	**2,154**	**2,179**	**2,206**
Total current liabilities	235	357	467	581
Deferred income taxes	196	193	190	188
Pension and postretirement benefits oth	108	108	108	107
Other long-term liabilities	45	45	45	45
Advances for construction	112	135	157	180
Contributions in aid of construction	286	286	286	286
Total capitalization and liabilities	**3,132**	**3,277**	**3,431**	**3,593**

Seaport Global

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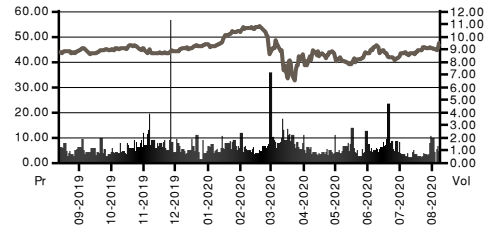
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$47.81**
Float:	244.6MM
Diluted Shares:	254.4MM
Short Interest:	6.4MM
Average Daily Volume:	865k
52 Week Range:	$30.40 - $54.52
Market Cap:	**$12,164MM**
Cash and Investments:	$5MM
Debt:	$5MM
Enterprise Value:	$12,165MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
FY	$1.47A	$1.55	$1.56E	$1.66	$1.66E	$1.76	$1.77E
P/E	**32.5x**		**30.7x**		**28.9x**		**27.0x**
Dividends Per Share							
FY	$0.907A	$0.970	$0.970E	$1.038	$1.038E	$1.111	$1.111E
Dividend Yield	**1.9%**		**2.0%**		**2.2%**		**2.3%**

Essential Utilities, Inc.

(NYSE: WTRG)

Catch-up repair tax deduction in PA

Summary:
WTRG sees no negative earnings impact from COVID as stronger residential sales offset lower C&I volumes, and the recent merger with Peoples Gas adds cost levers. The catch-up repair tax deduction in PA would extend the strong mid-teen annual EPS growth rate at Peoples through even 2026. The future of the DELCORA wastewater acquisition remains uncertain, but WTRG already issued equity to finance it. We maintain our Neutral rating.

Highlights

No COVID impact on earnings: With stronger residential sales volumes offsetting lower C&I sales and regulatory deferrals of bad debts and other COVID-related expenses, WTRG saw no earnings impact from the pandemic in 1H20. We could see some positive earnings impact if the current heat continues in PA – dry lawns should be eyesores to residential customers working from home during COVID.

Catch-up repair tax deduction for Peoples Gas in PA: Last week, following consultations with the regulator (PA PUC), Peoples Gas field its long-awaited application in this case. The additional tax deduction of $380.7MM (~$141MM tax benefit) is related to federal and state taxes for tax years 2012-2019 and through March 2020. The company proposed a $14MM annual customer credit for four years (2021-2024) which would represent less than a 2% reduction in a residential monthly bill. It seems very low to us, but is constrained by Peoples' limited tax capacity as the utility uses forward-looking repair tax deductions especially in 2021 and 2022. The remaining $85MM in tax deductions would be used by Peoples in 2023-2026 to boost realized ROEs by reducing the tax expense. It's an interesting proposal as it extends the current strong earnings growth at Peoples through 2026, but doesn't change the growth trajectory through 2022 thus avoiding a likely fierce regulatory battle in PA.

DELCORA wastewater acquisition: Aqua PA believes it has a legally-binding purchase agreement for the wastewater system from last November and the regulatory approval process of the transaction at the PA PUC should conclude in early 2021, assuming no delays. The Delaware County sued to stop the sale and by mid-September a judge in the case should rule if the County has a right to stop the sale transaction. The issue seems to be who gets the net proceeds from the sale transaction (~$200MM) – the County or a trust which would offset future ratepayer bill increases as Aqua plans to invest $700MM in the system over the next couple of years. Last night, WTRG priced a 6.7MM share equity forward which should finance the DELCORA deal, we believe, even though the future of the transaction seems uncertain to us.

Estimates and valuation: We raised our 2020 EPS estimate by $0.01 to $1.56 to reflect favorable weather and no COVID-related EPS drag. We raised our 2022 EPS by $0.01 to $1.77 to reflect marginally higher merger-related cost efficiencies. WTRG trades in line with CWT and slightly higher than SJW based on our 2022 EPS estimates which seems fair to us given that ~30% of WTRG's EPS should come from a gas LDC rather than a water utility.

Company Description:
WTRG owns and operates water utilities (1 million accounts) and gas utilities (0.74 million accounts) in 10 states though mainly PA.

WTRG: EPS breakdown by segment ($)

WTRG	2018A	2019A	2020E	2021E	2022E	19-'22 CAGR
Regulated water utilities	1.41	1.47	1.09	1.16	1.23	
Regulated gas utilities	0.00	0.00	0.53	0.62	0.70	
Parent	0.00	0.00	-0.06	-0.12	-0.16	
Total EPS	**1.41**	**1.47**	**1.56**	**1.66**	**1.77**	**6.4%**
DPS	**0.85**	**0.91**	**0.97**	**1.04**	**1.11**	**7.0%**
Dividend payout	60%	62%	62%	63%	63%	

Source: Company data for 2018-2019, Seaport Global Securities

WTRG	2018A	2019A	2020E	2021E	2022E
Operational EBITDA	470	505	868	920	986
Operational EBIT	323	349	604	641	692
Net interest expense	99	100	201	209	227
Ordinary Profit Before Tax	252	269	431	459	492
Income tax	1	7	34	37	39
Net profit	251	262	396	422	453
S/O (m)	178	178	254	255	256
Diluted EPS	**1.41**	**1.47**	**1.56**	**1.66**	**1.77**
DPS	**0.85**	**0.91**	**0.97**	**1.04**	**1.11**
Cash	4	1,869	5	5	5
Receivables	101	108	109	113	118
Inventory	16	18	30	30	30
Other short-term assets	26	18	18	18	18
Other-long term assets	887	1,003	3,810	3,810	3,810
Property, plant, and equipment	5,930	6,346	8,962	9,113	9,249
Total assets	**6,965**	**9,362**	**12,934**	**13,089**	**13,230**
Financial liabilities	117	117	496	496	496
Operating liabilities	63	67	109	109	109
Other liabilities	108	108	220	220	220
Deferred credits	2,068	2,057	2,758	2,757	2,757
Long-term debt	2,398	2,943	4,750	5,081	5,401
Shareholders' equity	2,210	4,070	4,601	4,425	4,247
Total liabilities and equity	**6,965**	**9,362**	**12,934**	**13,089**	**13,230**
Net income	251	262	396	422	453
D&A, goodwill amortisation	147	156	264	279	294
Other non cash elements	-54	-40	-6	-6	-6
Funds from operations	344	379	654	695	740
Non-cash working capital	25	-40	43	0	-1
CFO	**369**	**339**	**697**	**694**	**740**
Net investments in fixed assets	-641	-610	-6,555	-765	-780
Net investments in financial assets	2	6	0	0	0
Free cash flow before dividends	**-271**	**-266**	**-5,858**	**-71**	**-40**
Dividends paid	-151	-161	-247	-264	-284
Free cash flow after dividends	-422	-427	-6,105	-334	-325
Changes in capital	2	1,935	2	2	3
Changes in financial debt	421	386	4,238	331	321
Adjustment for minorities / miscellaneous	-2	-28	1	1	1
Increase in cash	-1	1,866	-1,864	0	0

Utilities Disclosures

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Risks & Considerations for American Water Works Company, Inc. American Water Works Company, Inc. (AWK)

Allowed ROEs for AWK's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings.

Lower sales volumes could weigh on AWK's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWK has a particularly busy regulatory calendar in 2020, with rate cases in three of its largest jurisdictions – NJ, PA and MO.

Potentially higher equity needs due to weakening operating cash flows and underfunded pension funds: Lower customer collections (due to lower sales or non-payment) coupled with growing federal cash taxes and underperforming pension funds should be weighing on operating cash flows of regulated utilities especially during/following the COVID-19 pandemic. That in turn could require some deleveraging of balance sheets of regulated utilities thus more equity. AWK already announced ~$500m in new equity as soon as 2022, but the issuances could be enlarged and accelerated to protect AWK's credit ratings.

Risks & Considerations for American States Water Company American States Water Company (AWR)

AWR's water utility (GSWC) could see volatility in earnings due to usage: The CPUC considers changes to the current water revenue decoupling mechanism (WRAM). While it should not impact GSWC until the next rate case, covering 2024-2026, CA utility consumer advocates push for an immediate change to the decoupling mechanism. GSWC has always excelled at earning at least its allowed ROE in CA, but it could prove challenging with WRAM.

Allowed ROEs for AWR's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. AWR's allowed ROE for its water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWR should be filing a new water rate case by July 2020 with new rates in effect in January 2021.

Returns in pension accounts impact AWR's earnings in between rate cases in CA: AWR has no balancing account tracking changes in returns in its pension accounts. Those changes can be trued up/reflected in AWR's rates during rate cases, but those take place every three years.

Military contracts are highly competitive: Through its unregulated ASUS subsidiary, AWR provides water and wastewater services to 11 military bases. The company awaits awards of up to three more of these contracts in 2020. We assume that AWR secures at least one new military contract per year in 2020-2022 though AWK, AWR's largest competitor, has been winning most of the contract awards as of late.

Risks & Considerations for California Water Services Group California Water Services Group (CWT)

Allowed ROEs for CWT's regulated water utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. CWT's allowed ROE for its water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. CWT awaits a proposed decision in its 2018 general rate case in CA with rates retroactive to January 1, 2021. Though the utility reached a partial settlement with the consumer advocate late in 2019, outstanding issues involve the continuation of the revenue decoupling and balancing accounts for pension and medical expenses. Without those, CWT could see a meaningful spike in its earnings volatility.

Risks & Considerations for SJW Group SJW Group (SJW)

Allowed ROEs for SJW's regulated water utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. SJW's allowed ROE for its CA water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. SJW should file a rate case for its new CT business in 2021. Also, the CA utility of SJW should go through a general rate case in the state in 2021 and state regulators could attempt to claw-back some synergies related to the recent merger with CTWS.

SJW's CA earnings are highly volatile: Now that SJW no longer has even a temporary decoupling mechanism in CA, it's CA earnings change along with changes in volumes and changes in purchased water costs. SJW plans to ask for a purchased water cost balancing account in the next rate case in CA, but that means that 2021 could be another weak earnings year before the regulatory fix arrives for 2022, if at all.

Risks & Considerations for Essential Utilities, Inc. Essential Utilities, Inc. (WTRG)

Allowed ROEs for WTRG's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average

10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. WTRG's only pending rate case (in NC) is very small.

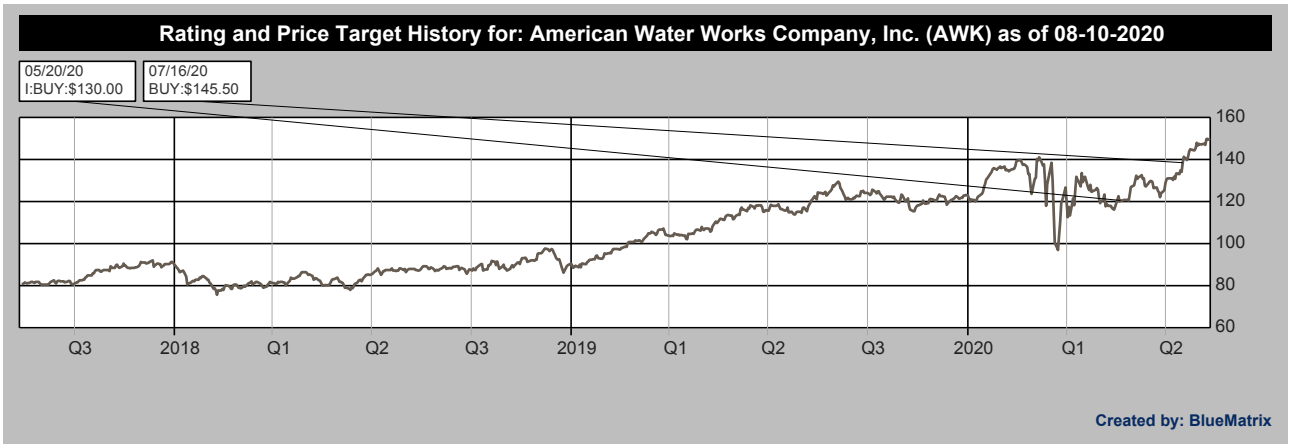
Lower sales volumes could weigh on WTRG's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

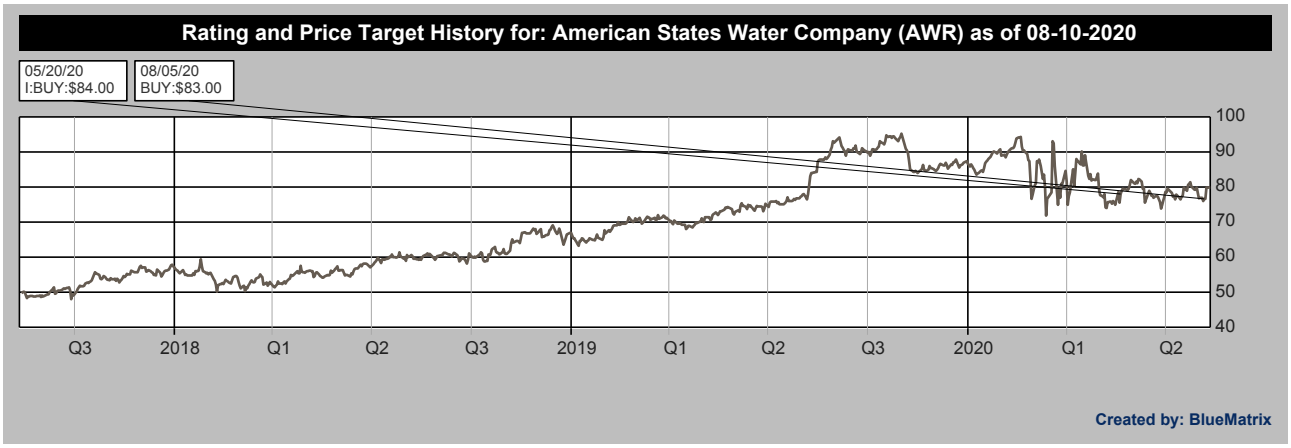
Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. WTRG's regulatory calendar is quiet in 2020, with a pending small rate case in NC, and a likely filing for a catch-up repair tax adjustment for Peoples in PA.

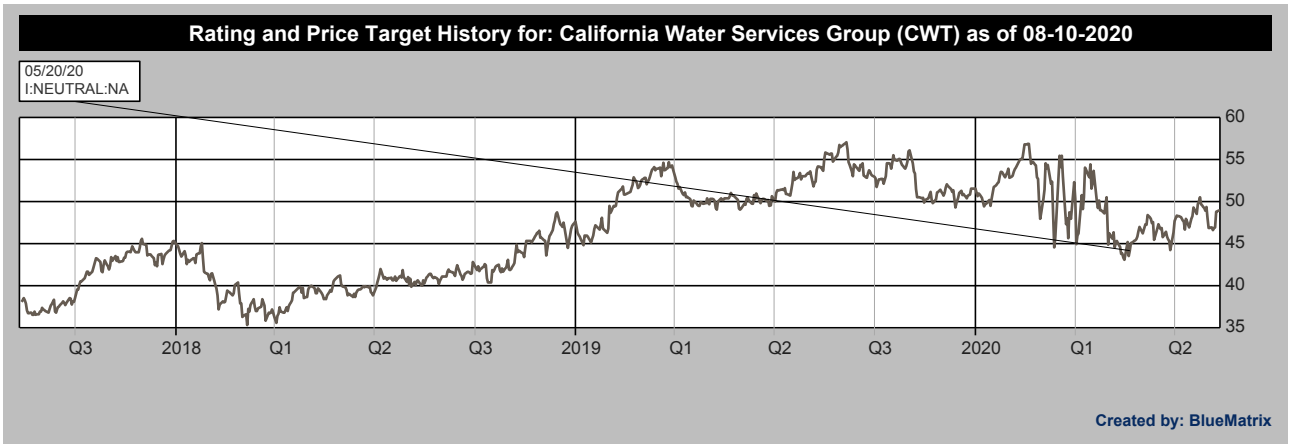
Gas utilities have a higher operating risk than water utilities: Overpressurized gas systems seem to happen more frequently among gas utilities in the US. While we recognize that Peoples Gas is a well-managed system, WTRG's risk profile could further deteriorate with any gas-related operational issues.

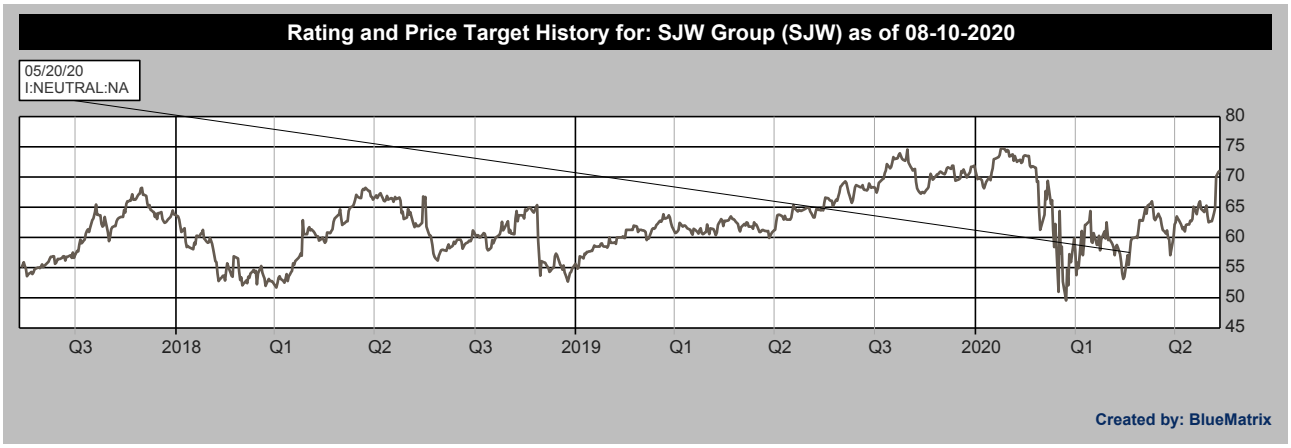
Other Companies Mentioned in This Report

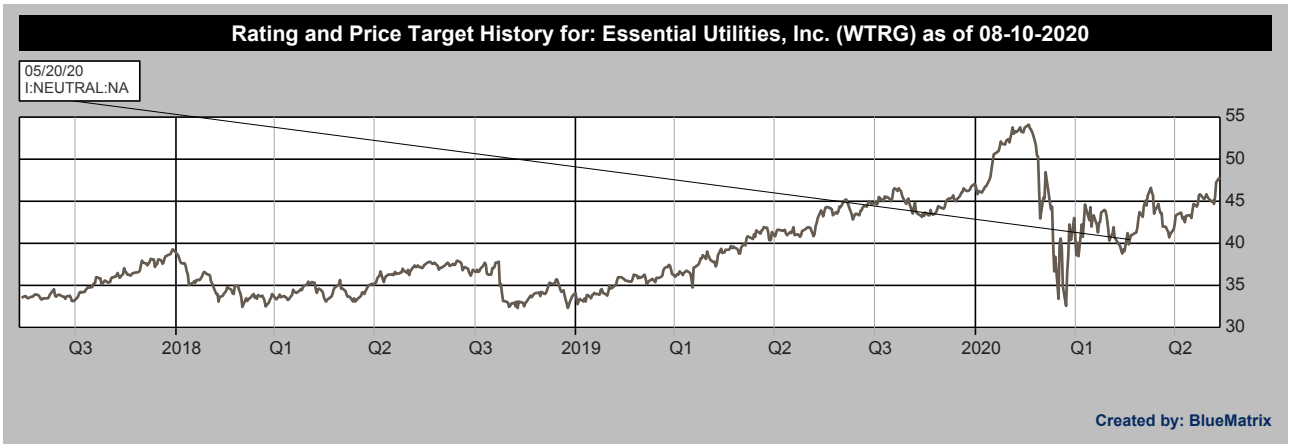
- American Water Works Company, Inc. (AWK: $149.11, Buy)
- California Water Services Group (CWT: $48.98, Neutral)
- Essential Utilities, Inc. (WTRG: $47.81, Neutral)
- American States Water Company (AWR: $79.85, Buy)
- SJW Group (SJW: $71.06, Neutral)











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Sell - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.
NA - A rating is not assigned.

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Accumulate - The investment outlook and risk/reward over the following 12 months are favorable on an absolute basis and relative to the peer group.
Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.
Reduce - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.
Sell - The investment outlook and risk/reward over the following 12 months are very unfavorable on an absolute basis and relative to the peer group.
NA - A rating is not assigned.

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	Research Coverage		Investment Banking Clients*		
Rating	Count	% of Total	Count	% of Total	% of Rating Category
Buy	76	61.8%	2	66.7%	2.6%
Neutral	42	34.1%	0	0.0%	0.0%
Sell	5	4.1%	1	33.3%	20.0%
Total	123	100.0%	3	100.0%	2.4%

*Investment banking clients are companies for whom Seaport Global Securities has provided investment banking services in the previous 12 months.

Note: Ratings Distribution as of June 30, 2020

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October 01, 2020
Industry Update
Utilities

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Utilities

Water Utilities: Updated thoughts ahead of 3Q20 earnings season

Summary:
The bifurcation in market valuations of US utility stocks stretches to water utilities though it's less pronounced than that among electric utilities. AWK, the top YTD performer among all utilities in the US, beating even NEE, trades at an 19% 2022 P/E premium to all water utilities in the US. The premium grew from just ~1% when we launched coverage in mid-May as investors increasingly flock to (almost) pure-play water utilities with strong ESG growth stories. While gas utilities should contribute only a third of WTRG's earnings and PA is highly supportive of natural gas, WTRG continues to derate on the back of its recent gas LDC acquisition. The stock once trading in line with AWK on FY3, currently trades at a 29% discount to AWK on our 2022 EPS estimates, even though WTRG's muni wastewater M&A pipeline has never been this impressive. Yet, the muni project pipeline is highly dependent on a November court ruling on the DELCORA wastewater system acquisition in PA ($276.5MM) and that uncertainty holds us back. The change to full water revenue decoupling (WRAM) and ongoing delays to CWT's general rate case decision in CA continue to weigh on CWT and AWR, with yet another ugly earnings print likely for CWT. We are increasingly comfortable with the strong earnings trajectory for the two CA water utilities, but remain on the sidelines on CWT as we brace another knee-jerk reaction on a likely big earnings miss in 3Q20.

Highlights

AWK – Strongest utility stock performer and counting: AWK is up ~21% YTD vs. XLU down ~8% and the second best performing water utility, MSEX, down ~2%. Since we launched coverage of AWK in mid-March, AWK's valuation premium to an average water utility grew from less than 1% to 19% currently on 2022 P/Es along with the bifurcation of electric/gas/water utility multiples driven by ESG investors. Though AWK trades at 32.4x our 2022 EPS, we cannot find a better regulated utility growth story in the US even during a year filled with important rate cases. Therefore, we reiterate our Buy rating.

AWR – We can live with WRAM changes, if any, but we'd like to see more military contract awards: We are increasingly comfortable with AWR's ability to earn at least its allowed ROE on the water and electric side, and grow its dividends at a ~9% CAGR through 2022, regardless of future changes to the full water decoupling mechanism (WRAM) which should kick in in 2025, if at all. We'd like to see at least one more military contract award, with at least one more pending solicitation to be resolved in October/ November, we believe. We reiterate our Buy rating.

CWT – Another ugly quarterly print ahead of us, but rate case outcome should be fine, eventually: This should be yet another ugly earnings season for CWT as CA regulators yet again delayed a decision in CWT's never-ending general rate case (GRC), this time until early November. Based on our expectations for the GRC outcome, CWT trades at a 16% 2022 P/E discount to AWR and just a 5% premium to SJW despite heavily under-invested assets of CWT likely driving a premium 11% EPS CAGR through 2022, with little volatility given that the full WRAM modification seems unlikely to impact CWT until 2023. We are concerned of another a knee-jerk pullback in CWT's stock on the back of the upcoming 3Q20 print and that's why we remain on the sidelines.

WTRG – Gas-related discount seemed likely, but it came sooner and larger than expected: We were always skeptical about WTRG's pursuit of a gas LDC, even a fast-growing one, as we worried it would diminish the scarcity value of WTRG's water utility business. Yet, we didn't anticipate the sharp de-rating of gas LDC stocks we saw YTD on concerns over their carbon footprint and electrification of house heating. We don't expect WTRG's ~9% annual gas rate base growth in PA to moderate any time soon, and WTRG's water muni deal pipeline is the strongest in the company's history. We remain on the sidelines as we await a court ruling of the DELCORA acquisition in early November, but find WTRG's value proposition compelling.

Water Utilities: Comp Sheet

Regulated water utilities	Share price ($) 10/01/2020	Rating	Price target ($)	Market cap ($B)	2020 Div Yield	2022 EPS ($)	2022 PE
AWK	148.57	Buy	152.00	26.9	1.4%	4.59	**32.4x**
AWR	76.12	Buy	83.00	2.8	2.8%	2.61	**29.2x**
CWT	44.61	Neutral	N/A	2.2	1.9%	1.82	**24.5x**
SJW	61.57	Neutral	N/A	1.8	2.1%	2.64	**23.3x**
WTRG	40.78	Neutral	N/A	10.0	2.4%	1.78	**22.9x**
Average P/E for regulated water utilities					**2.1%**		**26.5x**

Source: FactSet, Seaport Global Securities

Seaport Global

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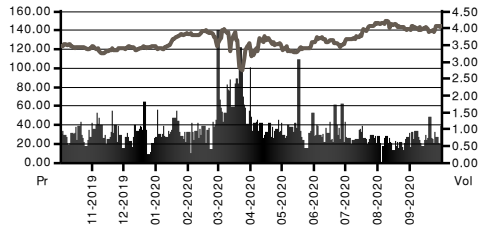
Rating:	**Buy**
Price Target:	**$152.00**

Price Target Metrics:
2022 SOTP valuation implying 33.2x 2022 EPS

Current Price:	**$148.57**
Float:	180.7MM
Diluted Shares:	181.0MM
Short Interest:	2.2MM
Average Daily Volume:	753k
52 Week Range:	$92.00 - $150.47
Market Cap:	**$26,891MM**
Cash and Investments:	$569MM
Debt:	$9,593MM
Enterprise Value:	$35,915MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Adjusted)				
FY	$3.61A	$3.85E	$4.23E	$4.59E
P/E	**41.1x**	**38.6x**	**35.1x**	**32.3x**
Dividends Per Share				
FY	$1.955A	$2.150E	$2.365E	$2.600E
Dividend Yield	**1.3%**	**1.4%**	**1.6%**	**1.8%**

American Water Works Company, Inc.

(NYSE: AWK)

Strongest utility stock performer YTD and counting

Summary:

AWK is up ~21% YTD vs. XLU down ~8% and the second best performing water utility, MSEX, down ~2%. Since we launched coverage of AWK in mid-March, AWK's valuation premium to an average water utility grew from less than 1% to 19% currently on 2022 P/Es along with the bifurcation of electric/gas/water utility multiples driven by ESG investors. Though AWK trades at 32.4x our 2022 EPS, we cannot find a better regulated utility growth story in the US even during a year filled with important rate cases. Therefore, we reiterate our Buy rating.

Highlights

COVID and hot/dry summer: According to NOAA, cooling degree days in NJ/PA/IL were up 24%/27%/39% vs. normal and while the precipitation levels were just slightly below normal, we'd expect AWK's residential sales to be sharply up, especially given COVID-related work from home arrangements. C&I sales in the Mid-Atlantic could serve as a drag, but then again some of AWK's service territories fully resumed C&I operations during 3Q20.

Rate cases: We await hearings in AWK's NJ rate case during October. In CA, the regulator/CPUC recently removed the full revenue decoupling for water utilities (WRAM), but AWK's current general rate case should not be impacted. We hope changes among CPUC commissioners could eventually lead to a new/modified WRAM by the time AWK's new rates will be due in 2024.

NY asset sale: In November 2019, AWK announced the sale of its NY operations to Liberty Utilities for $608MM. Long Island munis have until October 15 to submit municipalization proposals for their water systems within AWK's NY service territory. The Massapequa Water District already submitted their proposal to the NY PSC while Sea Cliff and Hempstead continue to consider a municipalization route. AWK remains optimistic about the closing of the NY sale transaction even if small parts of the system were to be excluded due to municipalization.

Military contracts: AWK was recently awarded its 17th water and wastewater service contract for military bases. This time it is a 50-year $771MM contract for the Joint Base Lewis-McChord in WA. This contract is more than 50% larger than AWK's past military contracts, and the company expects another contract award this year, potentially this month. Given the duration, annual indexation and likely expansion of scope of these contracts, we continue to value them at a sharp premium to even regulated water operations.

Homeowner services: AWK entered into a partnership with Iberdrola TX to offer residential customers in the state an optional cooling repair and maintenance plan as well as a surge protection plan. We assume that is the deal which was previously delayed due to COVID. The services covered by this partnership seem unrelated to water which is nothing new for AWK's Homeowner Services business, but it's not ideal for water purists. Then again if we can live with NEE's gas E&P, we can live with AWK's air conditioner service contract.

Company Description:

AWK is the largest publicly-traded regulated water and wastewater utility in the US with operations in 16 states, primarily in the Northeast and the Midwest, serving 3.4 million customer accounts. AWK also engages in unregulated contract-based water/wastewater services for military bases (17 bases) and provides water/wastewater line warranty services (homeowner services) to ~1.5 million residential accounts.

AWK: EPS breakdown by segment ($)

AWK	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated utilities	3.60	3.92	4.32	4.67	9.1%
Unregulated ops	0.45	0.49	0.52	0.56	7.6%
Parent	-0.44	-0.56	-0.61	-0.64	13.3%
Total EPS	**3.61**	**3.85**	**4.23**	**4.59**	**8.3%**
DPS	**1.96**	**2.15**	**2.37**	**2.60**	**10.0%**
Dividend payout	54%	56%	56%	57%	

Source: Company data for 2019; Seaport Global Securities

Seaport Global

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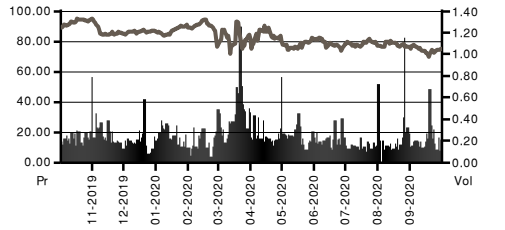
Rating:	**Buy**
Price Target:	**$83.00**

Price Target Metrics:
2022 SOTP valuation which implies 31.8x '22 EPS

Current Price:	**$76.10**
Float:	36.4MM
Diluted Shares:	37.0MM
Short Interest:	0.9MM
Average Daily Volume:	227k
52 Week Range:	$65.11 - $96.64
Market Cap:	**$2,816MM**
Cash and Investments:	$6MM
Debt:	$330MM
Enterprise Value:	$3,139MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020	2021	2022
EPS (Diluted)				
Q1 (Mar)	$0.35A	$0.38A	$0.50E	$0.54E
Q2 (Jun)	$0.64A	$0.69A	$0.64E	$0.68E
Q3 (Sep)	$0.69A	$0.77E	$0.79E	$0.84E
Q4 (Dec)	$0.55A	$0.48E	$0.51E	$0.54E
FY	$2.24A	$2.33E	$2.45E	$2.61E
P/E	**34.0x**	**32.7x**	**31.1x**	**29.2x**
Dividends Per Share				
FY	$1.160A	$1.280E	$1.390E	$1.495E
Dividend Yield	**1.5%**	**1.7%**	**1.8%**	**2.0%**

American States Water Company
(NYSE: AWR)

We can live with WRAM changes, but we'd like to see more military contract wins

Summary:
We are increasingly comfortable with AWR's ability to earn at least its allowed ROE on the water and electric side, and grow its dividends at a ~9% CAGR through 2022, regardless of future changes to the full water decoupling mechanism (WRAM) which should kick in in 2025, if at all. We'd like to see at least one more military contract award, with at least one more pending solicitation to be resolved in October/November, we believe. We reiterate our Buy rating.

Highlights

Modifications to full water decoupling and GSWC's pending rate case: In late August, the CPUC removed the full water revenue decoupling (WRAM) for all four investor-owned water utilities in CA which currently use the mechanism, including AWR's GSWC. The Commission ruled that the WRAM removal should impact "any future general rate case applications filed after the effective date of this decision" so we assume that GSWC's current rate case/GRC (filed on July 15) should not be impacted. Comm. Ranldoph who dissented the WRAM change is assigned to GSWC's rate case which, to us, bodes well for the company given that the Commissioner should not be open to the suggestions from the consumer advocate (ORA) to include the WRAM change in the pending proceeding. Assuming a statutory 18-month review period of the rate case, GSWC's new rates should be decided by the end of 2021 and remain in effect through the end of 2024. Therefore, we'd expect the WRAM changes to affect GSWC's earnings only in 2025, if at all. Management insists the company should do just fine even under the new Monterey-style WRAM, and GSWC has a history of earning at least its allowed ROE on the water side. We are still hopeful the Commission could change its mind on the full WRAM, especially given that the current term of Comm. Guzman-Aceves, the author of the WRAM change, should expire by the end of 2022, i.e. before the filing of GSWC's next general rate case.

ASUS: AWK rather than AWR was recently awarded a particularly large $771MM military water/wasterwater service contract in WA, but we expect at least one (if not two) more military contract awards in October/early November. We still hope AWR's ASUS can get at least one more contract though for now, our 2021-2022 estimates assume ASUS growth driven by existing contracts and changes in the scope of work under them.

Company Description:
AWR is the parent of Golden States Water Co. (GSWC), a regulated water (261,000 water connections in 37 systems), Beaver Valley Electric Service (BVESI), an electric utility (24,400 electric connections in one system) in CA, and American States Utility Services (ASUS), which engages in contract-based water and wastewater services primarily for military bases, currently 11 bases.

AWR: EPS breakdown by segment ($)

AWR	2019A	2020E	2021E	2022E	2019-2022 CAGR
Regulated water	1.62	1.66	1.73	1.85	4.6%
Regulated electric	0.15	0.18	0.20	0.21	11.9%
Military contracts/ASUS	0.47	0.49	0.52	0.55	5.4%
Total EPS	**2.24**	**2.33**	**2.45**	**2.61**	**5.3%**
DPS	**1.16**	**1.28**	**1.39**	**1.49**	**8.8%**
Dividend payout	52%	55%	57%	57%	

Source: Company data for 2019; Seaport Global Securities

Seaport Global

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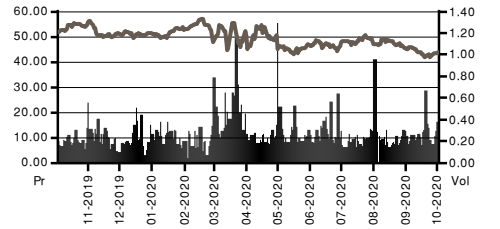
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$44.64**
Float:	49.0MM
Diluted Shares:	49.4MM
Short Interest:	0.9MM
Average Daily Volume:	271k
52 Week Range:	$39.74 - $57.36
Market Cap:	**$2,205MM**
Cash and Investments:	$114MM
Debt:	$1,182MM
Enterprise Value:	$3,273MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
FY	$1.31A	$1.39	$1.39E	$1.70	$1.70E	$1.82	$1.82E
P/E	**34.0x**		**32.0x**		**26.3x**		**24.5x**
Dividends Per Share							
FY	$0.790A	$0.850	$0.850E	$0.909	$0.909E	$0.978	$0.978E
Dividend Yield	**1.8%**		**1.9%**		**2.0%**		**2.2%**

California Water Services Group

(NYSE: CWT)

Another ugly quarterly print ahead of us, but rate case outcome should be fine

Summary:
This should be yet another ugly earnings season for CWT as CA regulators yet again delayed a decision in CWT's never-ending general rate case (GRC), this time until early November. Based on our expectations for the GRC outcome, CWT trades at a 16% 2022 P/E discount to AWR and just a 5% premium to SJW despite heavily under-invested assets of CWT likely driving a premium 11% EPS CAGR through 2022, with little volatility given that the full WRAM modification seems unlikely to impact CWT until 2023. We are concerned of another a knee-jerk pullback in CWT's stock on the back of the upcoming 3Q20 print and that's why we remain on the sidelines.

Highlights

Change to full revenue decoupling and CWT's pending general rate case in CA: In late August, the CPUC removed the full water revenue decoupling (WRAM) for all four investor-owned water utilities in CA which currently use the mechanism, including CWT. The Commission ruled that the WRAM removal should impact "any future general rate case applications filed after the effective date of this decision". CWT's management believes that it means its current never-ending rate case, covering 2020-2022, won't be impacted, though WRAM remains one of several contested items in the proceeding which was partially settled in October 2019. We assume the WRAM change, if any, won't impact CWT's earnings until 2023.

Another ugly quarterly print ahead of us: The CPUC yet again extended the statutory decline to resolve CWT's general rate case (GRC), this time until early November. We remain optimistic that new/higher rates should kick in still this calendar year, and will be retroactive to 1/1/20, making 4Q20 a big earnings quarter. Yet, in the meantime, we'd expect a ~45% EPS miss vs. adjusted consensus for 3Q20. Yes, it will be just due to timing, but that explanation didn't help the stock following the 1Q20 and 2Q20 earnings misses.

Estimates and valuation: Our 2020-2022 annual estimates remain unchanged as we await the final GRC decision. We changed the quarterly distribution of earnings in 2020 to sharply lower 3Q20 results. Based on our expectations for the GRC outcome, CWT trades at a 16% 2022 P/E discount to AWR and just a 5% premium to SJW despite heavily underinvested assets of CWT likely driving a premium 11% EPS CAGR through 2022 with little volatility given that the full WRAM modification seems unlikely to impact CWT until 2023. We are concerned of another knee-jerk pullback in CWT's stock on the back of the upcoming 3Q20 print and that's why we remain on the sidelines.

Company Description:
CWT operates regulated water and wastewater utilities in CA, WA, HI and NM, with 490,000 connections in CA (90%), 36,000 connections in WA (recently doubled through an acquisition), 5,000 in HI, and 8,300 connections in NM.

CWT: EPS breakdown by segment ($)

CWT	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.31**	**1.39**	**1.70**	**1.82**	**11.5%**
DPS	**0.79**	**0.85**	**0.91**	**0.98**	**7.4%**
Dividend payout	60%	61%	54%	54%	

Source: Company data for 2019; Seaport Global Securities

CWT	2018A	2019A	2020E	2021E	2022E
EBIT	132	117	125	149	160
EBITDA	218	209	224	255	274
Net interest expense	38	41	44	45	47
Net income	66	63	68	87	96
EPS	**$1.36**	**$1.31**	**$1.39**	**$1.70**	**$1.82**
DPS	**$0.75**	**$0.79**	**$0.85**	**$0.91**	**$0.98**

CFO	**$ 179**	**$ 169**	**$ 188**	**$ 214**	**$ 231**
Utility plant expenditures	(272)	(274)	(275)	(285)	(285)
Other	(1)	(2)	(2)	(2)	(2)
CFI	**(273)**	**(276)**	**(277)**	**(287)**	**(287)**
Issuance of common stock	(2)	18	96	80	86
Issuance of debt	73	103	28	32	32
Dividends	(36)	(38)	(41)	(44)	(47)
Other	11	20	20	20	20
CFF	**47**	**103**	**103**	**88**	**91**
Change in cash and cash equivalents	(48)	(4)	13	15	35

Net utility plant	2,233	2,406	2,583	2,761	2,932
Cash and cash equivalents	47	43	62	77	112
Other current assets	142	142	142	142	142
Total current assets	189	184	204	219	253
Regulatory assets	354	433	433	433	433
Goodwill	3	3	3	3	3
Other assets	60	85	85	85	85
Total assets	**$ 2,838**	**$ 3,111**	**$ 3,307**	**$ 3,501**	**$ 3,707**
Total common stockholders' equity	$ 730	$ 780	$ 807	$ 850	$ 899
Long-term debt, less current maturities	710	787	814	847	879
Total capitalization	**1,440**	**1,567**	**1,622**	**1,697**	**1,778**
Total current liabilities	321	359	479	578	682
Deferred income taxes	213	223	223	223	223
Pension and postretirement benefits ot	194	259	259	259	259
Other long-term liabilities	257	270	270	270	270
Advances for construction	186	191	191	191	191
Contributions in aid of construction	225	242	262	282	302
Total capitalization and liabilities	**$ 2,838**	**$ 3,111**	**$ 3,307**	**$ 3,501**	**$ 3,707**

Seaport Global

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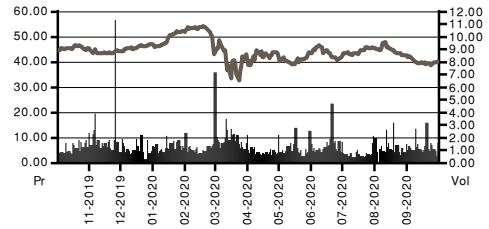
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$40.83**
Float:	244.6MM
Diluted Shares:	254.4MM
Short Interest:	13.1MM
Average Daily Volume:	1,290k
52 Week Range:	$30.40 - $54.52
Market Cap:	**$10,389MM**
Cash and Investments:	$5MM
Debt:	$5MM
Enterprise Value:	$10,389MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
FY	$1.47A	$1.56	$1.58E	$1.66	$1.66E	$1.77	$1.78E
P/E	**27.7x**		**25.9x**		**24.6x**		**22.9x**
Dividends Per Share							
FY	$0.907A	$0.970	$0.970E	$1.038	$1.038E	$1.111	$1.111E
Dividend Yield	**2.2%**		**2.4%**		**2.5%**		**2.7%**

Essential Utilities, Inc.

(NYSE: WTRG)

Gas-related discount seemed likely, but it came sooner and larger than expected

Summary:

We were always skeptical about WTRG's pursuit of a gas LDC, even a fast-growing one, as we worried it would diminish the scarcity value of WTRG's water utility business. Yet, we didn't anticipate the sharp de-rating of gas LDC stocks we saw YTD on concerns over their carbon footprint and electrification of house heating. We don't expect WTRG's ~9% annual gas rate base growth in PA to moderate any time soon, and WTRG's water muni deal pipeline is the strongest in the company's history. We remain on the sidelines as we await a court ruling of the DELCORA acquisition in early November, but find WTRG's value proposition compelling.

Highlights

COVID and hot/dry summer: According to NOAA, cooling degree days in Philly were up 27% vs. normal and while the precipitation levels were just slightly below normal, those drying lawns were likely an eyesore for Aqua PA's residential customers working from home. Therefore, we'd expect residential sales volumes to be up sharply vs. management's assumptions. Granted that lower C&I volumes should moderate the earnings impact, but we'd expect very strong prints from WTRG (and AWK) in 3Q20, even with changes in the quarterly distribution in gas earnings, especially with incremental regulatory deferrals of COVID-related expenses.

De-rating of gas LDCs: To us, the March 2020 addition of Peoples Gas LDC to WTRG's core water utility business diminished the scarcity value of the pure-play water utility which used to trade on par with AWK on FY3 EPS. Following the acquisition, WTRG's annual EPS growth picked up by 150-200 bps vs. our prior water-only expectations, but the stock now trades at a 29% 2022 P/E discount to AWK. In 3Q20, WTRG's stock closely tracked that of ATO, a fast-growing gas LDC from the South, with both stocks sharply underperforming XLU by 900 bps and 850 bps, respectively. We continue to project a ~9% annual rate base growth for WTRG's Peoples in PA and ATO in TX, but investors increasingly question the longevity of this infrastructure replacement cycle given the growing push to decarbonize house heating in Europe. Ongoing gas pipe replacement should continue to reduce methane leaks and blending of RNG should lower the carbon footprint of gas LDCs without any detriment to their earnings growth over the next decade if not longer, we believe, as electric heat pumps gain on popularity. Even if hydrogen becomes a commercially viable option in 2030+, gas distribution systems will likely be retrofitted to accommodate this highly flammable, low density gas. In other words, we don't expect the rate base growth of gas LDCs to slow down any time soon.

Municipal wastewater M&A and equity funding: With the recent wastewater system acquisition in Makefield, PA, WTRG has $359MM in pending muni deals in the state, the largest backlog we can recall in Aqua's/WTRG's history. The backlog includes the DELCORA wastewater acquisition ($276.5MM) which continues to face legal challenges, but WTRG's management feels comfortable with its ability to close the transaction in late March/April 2021, following a delayed PA PUC review, and even issued ~$300MM in equity forwards, half of which should finance the DELCORA transaction. WTRG/Aqua PA insists that they have a legally binding asset purchase agreement (APA) for the wastewater system, but courts should rule on the APA validity only November 4-5. The DELCORA transaction should be additive to WTRG's water earnings only in 2022 following Aqua PA's rate case to be filed next year.

Estimates and valuation: We raised our 2020 EPS estimate by $0.02 to $1.58 to reflect very favorable weather in PA during 3Q20 and no COVID-related EPS drag. We raised our 2022 EPS by another $0.01 to $1.78 to reflect a partial earnings impact related to the DELCORA acquisition diluted by a higher share count. WTRG is now the cheapest water utility under our coverage though not if we account for ongoing de-rating of gas LDCs, even those with premium rate base growth such as ATO. We are admittedly attracted to WTRG at this level, but stay on the sidelines as we await court's decision on the DELCORA APA in early November.

Company Description:
WTRG owns and operates water utilities (1 million accounts) and gas utilities (0.74 million accounts) in 10 states though mainly PA.

WTRG: EPS breakdown by segment ($)

WTRG	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated water utilities	1.47	1.10	1.17	1.26	
Regulated gas utilities	0.00	0.54	0.61	0.69	
Parent	0.00	-0.06	-0.13	-0.16	
Total EPS	**1.47**	**1.58**	**1.66**	**1.78**	**6.7%**
DPS	**0.91**	**0.97**	**1.04**	**1.11**	**7.0%**
Dividend payout	62%	62%	63%	62%	

Source: Company data for 2019; Seaport Global Securities

WTRG	2018A	2019A	2020E	2021E	2022E
Operational EBITDA	470	505	874	923	1,000
Operational EBIT	323	349	610	645	706
Net interest expense	99	100	201	209	227
Ordinary Profit Before Tax	252	269	436	463	506
Income tax	1	7	35	37	40
Net profit	251	262	402	426	466
S/O (m)	178	178	255	257	261
Diluted EPS	**1.41**	**1.47**	**1.58**	**1.66**	**1.78**
DPS	**0.85**	**0.91**	**0.97**	**1.04**	**1.11**
Cash	4	1,869	5	5	5
Receivables	101	108	110	113	120
Inventory	16	18	30	30	30
Other short-term assets	26	18	18	18	18
Other-long term assets	887	1,003	3,810	3,810	3,810
Property, plant, and equipment	5,930	6,346	8,962	9,113	9,249
Total assets	**6,965**	**9,362**	**12,935**	**13,090**	**13,232**
Financial liabilities	117	117	496	496	496
Operating liabilities	63	67	109	109	109
Other liabilities	108	108	220	220	220
Deferred credits	2,068	2,057	2,758	2,757	2,757
Long-term debt	2,398	2,943	4,750	5,347	5,659
Shareholders' equity	2,210	4,070	4,602	4,160	3,991
Total liabilities and equity	**6,965**	**9,362**	**12,935**	**13,090**	**13,232**
Net income	251	262	402	426	466
D&A, goodwill amortisation	147	156	264	279	294
Other non cash elements	-54	-40	-6	-6	-6
Funds from operations	344	379	659	698	753
Non-cash working capital	25	-40	43	0	-1
CFO	**369**	**339**	**702**	**698**	**752**
Net investments in fixed assets	-641	-610	-6,555	-1,032	-780
Net investments in financial assets	2	6	0	0	0
Free cash flow before dividends	**-271**	**-266**	**-5,853**	**-334**	**-28**
Dividends paid	-151	-161	-242	-266	-290
Free cash flow after dividends	-422	-427	-6,095	-600	-317
Changes in equity	2	1,935	302	2	3
Changes in financial debt	421	386	3,928	597	313
Adjustment for minorities / miscellaneous	-2	-28	1	1	1
Increase in cash	-1	1,866	-1,864	0	0

Utilities Disclosures

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Other Companies Mentioned in This Report

- American Water Works Company, Inc. (AWK: $148.57, Buy)
- California Water Services Group (CWT: $44.64, Neutral)
- NextEra Energy, Inc. (NEE: $282.76, Buy)
- SJW Group (SJW: $61.60, Neutral)
- American States Water Company (AWR: $76.10, Buy)
- Essential Utilities, Inc. (WTRG: $40.83, Neutral)
- Middlesex Water Co. (MSEX: $63.42)
- Atmos Energy Corp. (ATO: $95.47, Buy)

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Sell - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.
NA - A rating is not assigned.

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Accumulate - The investment outlook and risk/reward over the following 12 months are favorable on an absolute basis and relative to the peer group.
Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.
Reduce - The investment outlook and risk/reward over the following 12 months are unfavorable on an absolute basis and relative to the peer group.
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NA - A rating is not assigned.

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	Research Coverage		Investment Banking Clients*		
Rating	Count	% of Total	Count	% of Total	% of Rating Category
Buy	76	61.8%	2	66.7%	2.6%
Neutral	42	34.1%	0	0.0%	0.0%
Sell	5	4.1%	1	33.3%	20.0%
Total	123	100.0%	3	100.0%	2.4%

*Investment banking clients are companies for whom Seaport Global Securities has provided investment banking services in the previous 12 months.

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October 21, 2020
Industry Update
Utilities
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Utilities

Utilities/Power: Investor sentiment

Summary:
We summarized key investor arguments for electric/gas utility and power stocks with the most positive (AES, ES, ETR, EXC, FE, NEE, NRG), most negative (AGR, ATO, SRE, WTRG) and the tug-of-war sentiment (DTE, DUK, EIX, PPL, SO and VST) ahead of the 3Q20 earnings season and the annual EEI financial conference.

Highlights

Names with most positive investors' sentiment (in alphabetical order):

AES (AES, Buy, PT $21):
- Green wave - more renewable power/storage PPAs + incremental coal plant retirements/divestitures;
- Growth in regulated utility capex/earnings in IN/OH;
- IG rating from S&P as soon as early November.

Entergy (ETR, Buy, PT $113):
- Visible/above-average rate base growth;
- Improving capex execution and regulatory relationships;
- Truly discounted valuation and low customer bills even after securitization of growing storm costs.

Eversource (ES, Buy, PT $99):
- 3Q20 miss + likely delay of the South Fork offshore wind project + likely regulatory fine in CT following storm Isaias.
- Yet, annual EPS growth should rise to 7% for 2021-2023 thanks to Columbia Gas.
- ~10% annual EPS growth in 2024/2025 thanks to offshore wind.

Exelon (EXC, Buy, PT $45):
- Spin-off of ExGen/Constellation seems unlikely any time soon.
- Yet, Biden's wind/Blue sweap could lead to carbon pricing which would be highly beneficial for merchant nuclear plants;
- Current valuation doesn't reflect much value for ExGen.

FirstEnergy (FE, Buy, PT $42):
- Update on the DOJ investigation of lobbying practices surrounding the HB 6 in OH - a potential settlement without admission of any wrongdoing? The first update from CEO since 2Q20 call.
- Continued strong operational performance;
- Current valuation reflects unraveling of regulatory setup in OH (ESP settlement and changes to overearning/SEED test) which are seen as increasingly unlikely;
- A likely M&A target once the DOJ risk is addressed.

NextEra Energy (NEE, Buy, PT $324):
- Accelerating renewable power spending seems largely independent of November election results;
- Marginal investor in US utilities has an ESG mandate so NEE should continue to outperform XLU;
- Biden's win/Blue sweep would be additive to growth of NEER;
- NEE needs to watch its earnings mix for credit reasons - a large regulated utility acquisition could grow in importance after the Democratic sweep.

NRG Energy (NRG, Buy, PT $48):
- Proposed sale of PJM plants and incremental cost efficiencies at NRG could eliminate $750MM in converts to finance Direct Energy;
- PJM coal plant divestitures should boost NRG's ESG profile;
- 20%+ 2022 FCF yield with fewer questions about the longevity of cash flows.

Names with most negative investors' sentiment (in alphabetical order):

Atmos Energy (ATO, Buy, PT $108):
- Marginal equity investor for US utilities is an ESG investor, and he's not interested in gas LDCs, even those in gas supportive states (like TX or PA);
- ATO's P/E premium is measured vs. P/Es of other gas LDCs and not all electric/gas utilities; as other gas LDCs derate so does ATO.

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- ATO's upcoming addition to the DJUA could boost the stock.

Avangrid (AGR, Neutral, PT N/A):
- Stock sharply re-rated thanks to renewable power halo effect even though AGR's Renewables business struggles;
- Analyst day (Nov 5) should (yet again) re-set earnings expectations:
  - Whisper buy-side expectations for 2022 EPS of $2.45 are already meaningfully below sell-side consensus expectations, however, though the $1.95 midpoint of the new 2020 EPS guidance was lower than the $2.10 whisper number.
- Potential combination with PPL/WPD could still be possible, and could be decided by Iberdrola, AGR's majority owner, in December/ January.

Essential Utilities (WTRG, Neutral, PT N/A):
- Peoples Gas should increasingly suppress WTRG's P/E multiple as ESG investors stay away from gas LDCs;
- WTRG may need to spin off the gas LDC to rebuild its water P/E, or be taken over by an electric/gas utility.

Sempra Energy (SRE, Buy, PT $144):
- Expansion of Cameron or construction of ECA/Port Arthur LNG facilities now very unlikely;
- Monetization of a portion of Cameron LNG terminal should be difficult following lengthy storm-related outages (no backup power);
- Lack of extension of franchise agreement with San Diego would be a major negative leaving SRE with a gas LDC in CA, with limited long-term growth prospects;
- Share buyback is not being executed, and it's announcement on the 2Q20 earnings call is seen by many as an attempt to boost the stock price ahead of a potential regulated utility acquisition in TX. Yet, the company could still reiterate their willingness to support the stock with buybacks.

Tug of war names (in alphabetical order):

DTE Energy (DTE, Buy, PT $133.50):
- Management seems focused on correcting its stock's valuation discount.
- Yet, a spin-off of midstream assets might not create much (if any) shareholder value: a smid-cap midstream stock (~$3-3.5B in market cap) with a major technical overhang (as utility investors will want out) should not trade well.
- Instead, DTE could try to dilutive its midstream exposure through an acquisition of a regulated utility, preferably an electric utility with a contiguous service territory. CMS seems like an unlikely seller so it would have to be outside of MI.

Duke Energy (DUK, Neutral, PT N/A):
- NEE-DUK combination could create very meaningful shareholder value for both companies, and many LO investors continue to expect the combination to eventually happen; A lot depends on the outcome of the November elections.
- A blue sweep in D.C. could make the combination even more likely as NEE should need to address its earnings mix with a likely re-acceleration of its renewable power growth.
- A blue sweep in NC could boost DUK's standalone value and its appeal to NEE.
- The regulatory approval of the combination should be challenging. Investors believe the transaction is being blocked by DUK's Board/management only partly due to regulatory concerns.

Edison International (EIX, Buy, PT $62) and PG&E (PCG, Neutral, PT N/A):
- Recent rebound in stocks of EIX/PCG is seen as driven by a value trade rather than any fundamental reasons,
- Yet, we are getting close to the beginning of a seasonal trade in CA electric utilities.
- The Victims Trust doesn't seem to be shedding PCG's stock. And EIX could be announcing additional settlements of 20172018 wildfires.
- Yet, both stocks need to issue equity as soon as December/January.

PPL (PPL, Neutral, PT N/A):
- The sale of WPD is still months away and 2020 results from the business should disappoint due to COVID.
- Recent CMA rulings on ROEs/capex of UK water utilities are seen as positive for WPD's future earnings power and thus its sale price.
- Yet, WPD's sale would create meaningful shareholder value only if it's sold at north of 1.45x 2021 EV/RAB and PPL manages to eliminate practically all tax leakage.
- It's still possible, especially if Iberdrola were to agree to a swap between WPD and a majority stake in AGR. Yet, it remains unclear if Iberdrola is open to it, and the outcome of the US elections could determine the value of AGR.

Southern Company (SO, Buy, PT $66):
- Cold hydro testing is done and hot functional testing could start as soon as mid/late-November.
- Yet, the duration of the HFT is unknown and no one knows what SO's Georgia Power should uncover once the reactor (Vogtle Unit 3) is pressurized and the stream generator is turned on.

Vistra Energy (VST, Buy, PT $24):

- The stock looks cheap on practically every metric and buybacks should start in early 2021.
- Yet, VST's merchant renewable power/storage investments in TX conflict with VST's bullish views on fwd power prices in the state.
- Investors would prefer more buybacks or an investment in a renewable power developer (like AES's acquisition of sPower). Otherwise, terminal value questions should continue to weigh on the stock.

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Other Companies Mentioned in This Report

- AES Corporation (AES: $20.00, Buy)
- Atmos Energy Corp. (ATO: $94.28, Buy)
- Duke Energy Corp. (DUK: $92.06, Neutral)
- Eversource Energy (ES: $92.24, Buy)
- FirstEnergy Corp. (FE: $31.83, Buy)
- NRG Energy, Inc. (NRG: $33.18, Buy)
- PPL Corporation (PPL: $28.07, Neutral)
- Sempra Energy (SRE: $129.68, Buy)
- Essential Utilities, Inc. (WTRG: $42.10, Neutral)
- Avangrid, Inc. (AGR: $54.06, Neutral)
- DTE Energy Company (DTE: $121.34, Buy)
- Edison International (EIX: $59.75, Buy)
- Exelon Corporation (EXC: $42.40, Buy)
- NextEra Energy, Inc. (NEE: $300.99, Buy)
- PG&E Corporation (PCG: $10.92, Neutral)
- Southern Co. (SO: $58.60, Buy)
- Vistra Energy Corp. (VST: $18.95, Buy)
- Entergy Corporation (ETR: $106.22, Buy)

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Buy	102	61.1%	1	100.0%	1.0%
Neutral	62	37.1%	0	0.0%	0.0%
Sell	3	1.8%	0	0.0%	0.0%
Total	167	100.0%	1	100.0%	0.6%

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October 23, 2020
Industry Update
Utilities
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Utilities

Utilities/Power/Yieldcos/Water - What we've learned this week

Summary:
AEP's results and comments on the OH political risk bode well for FE. We'd expect solid EEI updates from both, and we're raising our PT for AEP ahead of them. AES's settlement in OH is more impressive than the grid modernization capex would indicate. AGR's proposed acquisition of PNM caught us by surprise, and why the EPS accretion math should work, the addition of NM to AGR's already challenging regulatory jurisdictions surprised us. The deal coupled with commentary from IBE's holders do not bode well for PPL's pending sale of WPD (RAB multiples and a tax shield) though the stock seems to already reflect that. NEE's renewable power growth keeps accelerating and with that the company's need to add regulated utilities. The NEE-DUK deal could look even better after the elections so it's too early to give up on it. SO's updated schedule for its new Vogtle nuke is a bit longer than we had hoped for, but way better than the bear case. And lastly, smid-cap water utilities are getting a technical boost (i.e., AWR, CWT, SJW, WTRG). They do seem undervalued based on fundamentals, but the recent/ongoing move is more about quant screens. Also note that we've updated our models for AEP, NEE, and NEP with this update.

Highlights

AEP (Buy, PT $99 up from $96) and FE (Buy, PT $42) – More regulated renewables at EEI + shedding of OH overhang which bodes well for FE

- There were few surprises from AEP's 3Q20 print, but management plans to comment on AEP's rate based renewable power investments (incremental to the $2B North Central Wind) during the upcoming EEI conference. It sounds like the company plans to pursue renewable power capex in VA and IN, and besides ESG benefits, it should get AEP's EPS CAGR closer to 7% from the current 6.5%, we estimate.
- AEP seems to have shed most of the overhang related to the HB 6 in OH, and investors seem increasingly hopeful that FE will act the same way. FE delayed its 3Q20 print until Nov 2, the day before the elections with the latter being increasingly seen as a particularly sensitive event in OH.
- We updated our model and our annual estimates for AEP remain unchanged, but we raised our PT to $99 from $96 on lower risks in OH. No changes to our estimates/PT for FE as we await management's EEI update.

AES (Buy, PT $21) – Capex boost in OH is small, but lots of positives from PUCO settlement; regulated capex updates from IPL on 3Q20 call

- DP&L, AES's OH regulated utility, just settled with state utility regulators (PUCO) on grid modernization capex, among others. The utility can now invest $249MM over the next four years which is small, but that's just a part of DP&L capex program which includes FERC transmission investments. Also, through the settlement DP&L confirmed its ability to continue to collect $80MM annually under the rate stabilization charge (RSC) and resolved three overearning (SEET) tests. The utility also plans to file another rate case. We expect an update on AES's regulated generation capex in IN (for IPL) on the 3Q20 call.
- No changes to estimates or PT for AES.

AGR (Neutral, PT N/A) and PPL (Neutral, PT N/A) – PNM merger and WPD's valuation

- The PNM acquisition came as a surprise to investors even though everybody seemed aware of IBE's (and thus AGR's) plans to grow its regulated utility presence in the US. A change to the NM utility commission is on the ballot on November 3 – if approved, PNM/AGR could be regulated by three new Commissioners appointed by the Legislature instead of the current five elected Commissioners. That could be an improvement starting Jan 1, 2023, yet the question remains how this potential change should impact the conduct of the current Commissioners over the next 26 months. They will be reviewing the AGR-PNM merger while trying to secure a job on the new downsized Commission. That could mean a longer-than-expected approval process for the deal, investors believe.
- We had openly hoped for a combination of AGR and PPL given IBE's past interest in WPD, PPL's UK distribution networks. Yet, we are hearing from IBE shareholders that the Spanish renewable power major thought the WPD deal would have been too big for them and would have detracted from IBE's renewable power focus. That's bad news for WPD's likely valuation, we believe, as consortiums of financial investors (infra funds) now seem like the most likely buyers of PPL's UK business, and the 1.5x+ EV/RAB seems increasingly unlikely. Then there is the potential Biden win in November and a likely change in the federal tax law which would follow. That in turn could impact the tax leakage associated with the WPD sale. Investors believe that WPD needs to sell above 1.35x 2021 EV/RAB and eliminate practically any tax leakage to create any meaningful shareholder value for PPL at the stock's current share price. And that still seems realistic to us.
- No changes to our recently-updated estimates for AGR. No changes to PPL.

NEE (Buy, PT $324) – 15GW renewable backlog, but regulated utility M&A dominates investor minds

- NEER keeps adding new storage/wind/solar contracts, and the accelerating growth in those unregulated contract-based operations continue to fuel questions on regulated utility M&A. Stand-alone ITCs for storage projects on the back of Biden's wind could lead to retrofits of NEER's existing wind farms thus further boosting the NEER growth. Management emphasizes no pre-set earnings mix or credit concerns, but depending on the outcome of November elections (both federal and state), the NEE-DUK merger rationale could get another boost. As we mentioned in our recent note, investors are increasingly optimistic on this eventual combination.
- We updated our model for NEE and our annual estimates and PT for NEE (and DUK) remain unchanged as we await the eventual outcome of November elections.

NEP (Buy, PT $70) – 15% YoY growth in 4Q20 distributions/share

- The 3Q20 wind (96% of normal) and solar power generation dropped YoY which was in line with our below-consensus expectations for NEP and other yieldcos. Yet, NEP delivered on a 15% YoY growth in unit distributions per share and its ~70% payout ratio leaves plenty of room to continue the ~15% annual growth in distributions through 2022 without any additional outside project acquisitions. It also helps that NEP pursues organic growth through the repowering a of a 125MW wind project in CO or an addition of backup compression capacity at the Agua Dulce gas compressor station, both just completed ahead of schedule and on budget. The repowering of the 100MW Baldwin wind farm in ND should be complete by the year-end.
- We marginally increased our 2020/2021 EBITDA estimates for NEP following the 3Q20 print to $1,263M/$1,291MM up from $1,260MM/$1,289MM, respectively. Our PT remains unchanged.

SO (Buy, PT $66) – Pressurization of Vogtle Unit 3 and operations of its steam generator will start only in January 2021, a month later than hoped

- SO provided a construction update on Vogtle Unit 3. The cold hydro testing (CHT) is done, but hot functional testing (HFT) which involves the pressurization of the nuclear reactor and first-time operations of the steam generator won't start until January 2021. That's later than we had hoped for – we had expected a 1-2 month gap between the end of CHT and the beginning of HFT thus implying a start of HFT by mid-December at the latest. The duration of HFT testing remains unclear though, for now, SO/Georgia Power expect the nuclear fuel load in April 2021. The end of HFT is widely seen as the main de-risking event for the Vogtle nuclear project so the wait continues.
- No changes to our estimates or PT for SO.

Water utilities (AWR/CWT/SJW/WTRG) - Technical trade boosting the group, especially smid caps

- We keep hearing from generalist investors that their equity strategists/internal quant screens predict a rally in stocks of US water utilities. We rarely pay attention to those comments unless they come from a couple unrelated sources and we see the recent consistent outperformance of these names which doesn't seem driven by fundamentals. We like the group based on fundamentals, even with the recent change to water revenue decoupling in CA.
- No changes in estimates or PTs for the water utilities under our coverage.

Utilities Disclosures

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Other Companies Mentioned in This Report

- American Electric Power Company, Inc. (AEP: $91.95, Buy)
- NextEra Energy, Inc. (NEE: $303.35, Buy)
- PPL Corporation (PPL: $28.51, Neutral)
- Duke Energy Corp. (DUK: $93.07, Neutral)
- PNM Resources, Inc. (PNM: $49.97)
- American States Water Company (AWR: $79.27, Buy)
- SJW Group (SJW: $64.50, Neutral)
- Avangrid, Inc. (AGR: $49.84, Neutral)
- NextEra Energy Partners LP (NEP: $64.86, Buy)
- Southern Co. (SO: $61.08, Buy)
- FirstEnergy Corp. (FE: $33.08, Buy)
- AES Corporation (AES: $20.49, Buy)
- California Water Services Group (CWT: $47.96, Neutral)
- Essential Utilities, Inc. (WTRG: $44.29, Neutral)

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Neutral	62	37.1%	0	0.0%	0.0%
Sell	3	1.8%	0	0.0%	0.0%
Total	167	100.0%	1	100.0%	0.6%

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November 16, 2020
Industry Update
Utilities
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Utilities

Water Utilities: Updated thoughts following 3Q20 prints/EEI meetings

Summary:
We continue to like water utilities in the US, especially given the recently gained earnings visibility for Buy-rated AWK in NJ and CWT in CA. AWK's large balance sheet makes it best-positioned to benefit from acquisitions of municipally- and privately-owned water and wastewater systems while the company keeps collecting additional water/wastewater service contracts for military bases. Buy-rated AWR has been less lucky in those military contract solicitations though two more of the contracts should be awarded still this year. Worse yet, the work under AWR's existing military contracts has been delayed due to COVID. The re-rating of CWT's stock on the back of its general rate case decision in CA came earlier than we hoped and the stock now looks (almost) fairly valued to us. SJW's 2021 guidance, if any, could disappoint due to the potential impact of La Nina on SJW's surface water production volumes in CA and some uncertainty related to the upcoming rate case in CT. WTRG pushes back against the discounted valuation of its gas LDC given its strong growth prospects, which we don't dispute, though we look toward the proposed DELCORA wastewater system acquisition in PA to change WTRG's earnings mix more toward water.
We continue to chase AWK hence we increased our PT to $175 from $152. We tweaked earnings estimates for AWK/AWR/CWT/SJW.

Highlights

AWK (Buy, PT $175 up from $152): A large balance sheet and a strong ESG profile increasingly matter among regulated water utilities in the US especially as acquisitions of municipally- and privately-owned water and wastewater systems continue to gain momentum. We reiterate our Buy rating on AWK, marginally raise estimates, and (again) increase our PT to $175 from $152 as we continue to chase the stock.

AWR (Buy, PT $83 unchanged): We were surprised by ongoing COVID-related delays of work under AWR's military water/wastewater contracts. Worse yet, AWK rather than AWR has been awarded the latest (and the largest) military contract though we await updates on two more contract awards over the next 45 days. We can live with eventual changes to AWR's full water revenue decoupling in CA as long as the company secures additional military contracts. We stick to our Buy rating and $83 PT.

CWT (Neutral, PT N/A): We delayed any rating changes on CWT until after its 3Q20 earnings print, in anticipation of yet another big earnings miss vs. consensus given the lack of a final decision in CWT's general rate case in CA. Yet, management decided to book an earnings catch up related to the rate case already in 3Q20 based on a Proposed Decision and comments on it from the CPUC consumer advocate. The stock jumped ~14% during a week following its earnings print vs. ~4% for XLU and ~5% for smid cap water names. Now, CWT trades at just a 4% 2022 P/E discount to an average regulated water utility in the US which seems almost fair to us. Therefore, we stick to our Neutral rating.

SJW (Neutral, PT N/A): San Jose Water's Monterey-style WRAM benefited SJW's earnings thanks to favorable weather and a COVID-related uptick in residential sales, though the earnings uplift was a bit lower than we had hoped. We remain concerned about the potential impact of the ongoing La Nina and the uncertainty surrounding the upcoming rate case in CT on SJW's 2021 guidance, if the company even decides to issue one in early 2021. Therefore, we remain on the sidelines on SJW even though the stock trades at a 15% 2022 P/E to an average regulated water utility.

WTRG (Neutral, PT N/A): While we share WTRG's rate base/earnings growth expectations for its gas LDC, we look to the pending acquisition of the DELCORA wastewater system in PA as a way to boost WTRG's earnings mix more towards water. We remain on the sidelines until we get more legal/regulatory clarity on this large wastewater system acquisition.

Seaport Global

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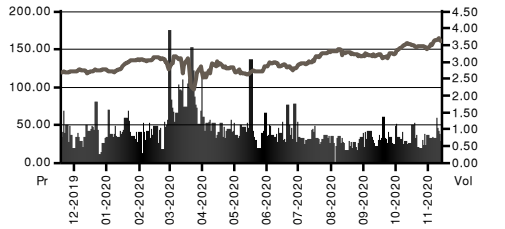
Rating:	**Buy**
Price Target:	**$175.00**

Price Target Metrics:
2022 SOTP valuation implying 38x 2022 EPS

Current Price:	**$161.31**
Float:	180.7MM
Diluted Shares:	181.0MM
Short Interest:	1.5MM
Average Daily Volume:	768k
52 Week Range:	$92.00 - $172.56
Market Cap:	**$29,197MM**
Cash and Investments:	$569MM
Debt:	$9,593MM
Enterprise Value:	$38,221MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Adjusted)							
FY	$3.61A	$3.85	$3.87E	$4.23	$4.25E	$4.59	$4.60E
P/E	**44.6x**		**41.7x**		**37.9x**		**35.1x**
Dividends Per Share							
FY	$1.955A	$2.150	$2.150E	$2.365	$2.365E	$2.600	$2.600E
Dividend Yield	**1.2%**		**1.3%**		**1.5%**		**1.6%**

American Water Works Company, Inc.

(NYSE: AWK)

Size & pure-play profile increasingly matter in US water sector; raising PT

Summary:
A large balance sheet and a strong ESG profile increasingly matter among regulated water utilities in the US especially as acquisitions of municipally- and privately-owned water and wastewater systems continue to gain momentum. We reiterate our Buy rating on AWK, marginally raise estimates, and (again) increase our PT to $175 from $152 as we continue to chase the stock.
We met with AWK's management during the annual EEI conference.

Highlights

NJ rate case: The NJ BPU approved AWK's general rate case settlement in the state and in general, the order seemed constructive. AWK received a $39MM increase in annual revenues (vs. $87.7MM requested) starting Nov 1, 2020, based on a rate base of $3.57B (down $69MM from the requested level), an allowed ROE of 9.6% (vs. 10.5% requested, but flat vs. the previous ROE) and an equity ratio of 54.6% (marginally up from 54% previously). The settlement and thus the final order didn't include acquisition adjustments related to the goodwill paid in Shorelands/Haddonfield/ Roxbury transactions or a revenue stabilization mechanism (aka revenue decoupling). We expect NJ AWK to ask for decoupling in the next rate case, while the acquisition adjustments for avoided capex related to privately-owned water/wastewater systems should be decided by the BPU within the next 2-3 months. The Board previously found that an acquisition adjustment is appropriate only when a utility can demonstrate specific benefits to its incumbent customers (rather than just for the system being acquired) stemming from the proposed acquisition or when the system being acquired is distressed. AWK believes the acquisition premium should be recoverable because the three transactions should result in avoided capital spending over the next 5-10 which should be in excess of that the premium over the book value that AWK paid. For now, the $31MM is not included in AWK's rate base and while it's very small vs. AWK's $14.6B total rate base, the BPU ruling in these acquisition adjustment cases could have very meaningful implications for any future larger acquisitions of investor-owned water utilities in NJ, we believe.

NY asset sale: Management still hopes to close its pending sale of NY operations to Liberty Utilities in early 2021 despite delays from the NY PSC to allow for municipalization plans being filed in Long Island and now proposed legislative initiatives. Gov. Cuomo recently proposed a new bill which, among others, would "expedite and clarify the process of utility franchise revocation for recurring failures" and require the NY PSC to study "whether private water suppliers like American Water on Long Island should come under municipal control". The new legislation would require the NY PSC to issue a report on the potential municipalization of the Long Island water utilities by April 2021, but AWK hopeful the regulatory review of the Liberty Utilities deal could be concurrent with PSC's work on this report.

Military contracts: AWK awaits two more military water/wastewater contracts awards this year – the last three contracts were awarded exclusively to AWK though for now we assume the next two contracts should be split between AWK and AWR. Management reminded us that back in 2000, AWK faced 10 competitors in military water/wastewater contract solicitations, but AWR is now the only credible competitor. AWK won't provide any disclosures on the profitability of this segment of its market-based businesses, partly because that would allow us to back into profit margins for the highly competitive

homeowners' services business, but we see these 50-year inflation-adjusted contracts as even more lucrative than any of AWK's regulated utility franchises.

Changes to estimates and PT: AWK raised its 2020 GAAP EPS guidance to $3.87-3.93 up from $3.79-3.89. The guidance includes a $0.05 EPS net hit related to COVID and a summer weather benefit ($0.10) as well as a $0.06 lower depreciation expense related to the NY system held for sale. The $0.06 benefit was not included in the original adjusted EPS guidance range and is excluded from our estimates. Still, given the strong 3Q20 print, we raised our 2020 adjusted EPS estimate to $3.87 up from $3.85. We marginally increased our 2021/2022 EPS estimates to reflect the recently awarded military contract which was much larger than expected. Our new 2021/2022 EPS estimates are $4.25/4.60 up from $4.23/4.59. We continue to chase the stock even though the P/E multiple is increasingly hard for us to defend. Our new PT of $175 (up from $152) implies a 38x 2022 P/E multiple.

Company Description:
AWK is the largest publicly-traded regulated water and wastewater utility in the US with operations in 16 states, primarily in the Northeast and the Midwest, serving 3.4 million customer accounts. AWK also engages in unregulated contract-based water/wastewater services for military bases (17 bases) and provides water/wastewater line warranty services (homeowner services) to ~1.5 million residential accounts.

AWK: EPS estimates by segment ($)

AWK	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated utilities	3.60	3.94	4.34	4.68	9.1%
Unregulated ops	0.45	0.49	0.52	0.56	7.6%
Parent	-0.44	-0.56	-0.61	-0.64	13.3%
Total EPS	**3.61**	**3.87**	**4.25**	**4.60**	**8.4%**
DPS	**1.96**	**2.15**	**2.37**	**2.60**	**10.0%**
Dividend payout	54%	56%	56%	57%	

Source: Company data for 2019; Seaport Global Securities

AWK: 2022 SOTP valuation ($)

AWK - 2022 SOTP	EPS	Multiple	Value per share
Regulated utilities less parent	4.04	39.0x	157.56
Military contracts	0.19	50.0x	9.50
Homeowner services	0.37	23.0x	8.51
Total per share			**175.57**

Source: Seaport Global Securities

AWK	2019A	2020E	2021E	2022E
Sales	3,610	3,780	4,025	4,233
Operating expenses	1,824	1,881	1,927	1,977
EBITDA	1,786	1,899	2,098	2,257
Depreciation	582	615	670	714
EBIT	1,204	1,284	1,428	1,543
Net interest expense	382	399	442	460
Ordinary Profit Before Tax	872	935	1,036	1,133
Income tax	218	234	259	283
Net profit	654	701	777	850
S/O (m)	181	181	183	185
Diluted EPS	**3.61**	**3.87**	**4.25**	**4.60**
DPS	**1.96**	**2.15**	**2.37**	**2.60**
Cash	90	45	45	45
Financial and Operating Receivables	294	311	332	349
Inventory	44	44	45	46
Other short-term assets	857	292	292	292
Goodwill	1,501	1,501	1,501	1,501
Other-long term assets	1,664	1,664	1,664	1,664
Property, plant, and equipment	18,232	19,486	20,686	21,843
Total assets	**22,682**	**23,343**	**24,564**	**25,739**
Financial liabilities	814	936	936	936
Operating liabilities	203	194	198	203
Other liabilities	1,028	851	851	851
Deferred credits and other regulatory liabiliti	5,872	6,054	6,256	6,400
Long-term debt	8,639	9,475	9,893	10,400
Shareholders' equity	6,126	5,833	6,430	6,949
Total liabilities and equity	**22,682**	**23,343**	**24,564**	**25,739**
Net income	654	701	777	850
D&A, goodwill amortisation	582	615	670	714
Other non cash elements	214	182	202	221
Funds from operations	1,450	1,499	1,648	1,784
Decrease (increase) in non-cash working ca	-67	-26	-17	-90
CFO	**1,383**	**1,472**	**1,632**	**1,694**
Net investments in fixed assets	-1,841	-1,865	-1,865	-1,865
Net investments in financial assets	-104	-104	-104	-104
Free cash flow before dividends	**-562**	**-497**	**-337**	**-275**
Dividends paid (group + minorities)	-354	-389	-432	-480
Free cash flow after dividends	-916	-886	-769	-755
Increase or (repayment) of capital and subsi	857	886	468	557
Increase or (repayment) of financial debt	-36	-45	301	198
Adjustment for minorities / miscellaneous	27	0	0	0
Increase in cash	-68	-45	0	0

Seaport Global

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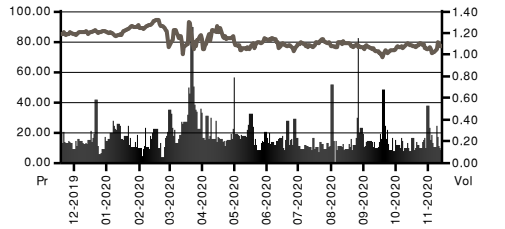
Rating:	**Buy**
Price Target:	**$83.00**

Price Target Metrics:
2022 SOTP valuation which implies 33x '22 EPS

Current Price:	**$77.20**
Float:	36.4MM
Diluted Shares:	37.0MM
Short Interest:	0.9MM
Average Daily Volume:	201k
52 Week Range:	$65.11 - $96.64
Market Cap:	**$2,857MM**
Cash and Investments:	$8MM
Debt:	$440MM
Enterprise Value:	$3,289MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
Q1 (Mar)	$0.35A	$0.38	$0.38A	$0.50	$0.49E	$0.54	$0.53E
Q2 (Jun)	$0.64A	$0.69	$0.68A	$0.64	$0.63E	$0.68	$0.67E
Q3 (Sep)	$0.69A	$0.77	$0.72A	$0.79	$0.77E	$0.84	$0.83E
Q4 (Dec)	$0.55A	$0.48	$0.52E	$0.51	$0.50E	$0.54	$0.53E
FY	$2.24A	$2.33	$2.30E	$2.45	$2.39E	$2.61	$2.56E
P/E	**34.5x**		**33.6x**		**32.3x**		**30.2x**
Dividends Per Share							
FY	$1.160A	$1.280	$1.280E	$1.390	$1.390E	$1.495	$1.495E
Dividend Yield	**1.5%**		**1.7%**		**1.8%**		**1.9%**

American States Water Company
(NYSE: AWR)

COVID continues to impact execution of military contracts; still awaiting new contract awards

Summary:
We were surprised by ongoing COVID-related delays of work under AWR's military water/wastewater contracts. Worse yet, AWK rather than AWR has been awarded the latest (and the largest) military contract though we await updates on two more contract awards over the next 45 days. We can live with eventual changes to AWR's full water revenue decoupling in CA as long as the company secures additional military contracts. We stick to our Buy rating and $83 PT.

Highlights

Military contracts: AWR awaits awards of two military water/wastewater contracts awards over the next 45 days – the last three contracts were awarded exclusively to AWK though for now we assume the next two contracts should be split between AWR and AWK. COVID continues to delay some current work and expansions of scope of some of AWR's current military contracts. As a result, management now expects to earn only $0.46 in 2020 EPS for this segment (ASUS) and for the earnings to stay largely flat YoY in 2021 assuming the COVID pandemic continues.

Modifications to full water decoupling (WRAM) and GSWC's pending rate case: We continue to expect the recent full WRAM changes to affect AWR's/GSWC's earnings only in 2025, if at all. Management insists the company should do just fine even under the new Monterey-style WRAM, and GSWC has a history of earning at least its allowed ROE on the water side. We are still hopeful the Commission could change its mind on the full WRAM, especially that all investor-owned water utilities in CA with the full WRAM have asked for the rehearing of the CPUC decision and, if unsuccessful, seem willing to challenge the decision in courts. The current term of Comm. Guzman-Aceves, the author of the WRAM change, should expire by the end of 2022, i.e. before the filing of GSWC's next general rate case.

Changes to estimates: We lowered our estimates to reflect the weaker earnings for existing military contracts (ASUS) and some uncertainty around new contract awards given that AWK (rather than AWR) has been winning all of the recent awards. Our new 2020/2021/2022 EPS estimates are $2.29/2.39/2.56 down from $2.33/2.45/2.61, respectively.

Company Description:
AWR is the parent of Golden States Water Co. (GSWC), a regulated water (261,000 water connections in 37 systems), Beaver Valley Electric Service (BVESI), an electric utility (24,400 electric connections in one system) in CA, and American States Utility Services (ASUS), which engages in contract-based water and wastewater services primarily for military bases, currently 11 bases.

AWR: EPS breakdown by segment ($)

AWR	2019A	2020E	2021E	2022E	2019-2022 CAGR
Regulated water	1.62	1.65	1.72	1.83	4.2%
Regulated electric	0.15	0.18	0.20	0.21	11.9%
Military contracts/ASUS	0.47	0.46	0.47	0.52	3.4%
Total EPS	**2.24**	**2.29**	**2.39**	**2.56**	**4.6%**
DPS	**1.16**	**1.28**	**1.39**	**1.49**	**8.8%**
Dividend payout	52%	56%	58%	58%	

Source: Company data for 2019; Seaport Global Securities

AWR	2018A	2019A	2020E	2021E	2022E
Total Revenues	437	474	481	497	518
Total Operating Expenses	336	347	351	362	374
EBIT	101	127	130	135	144
Net income	$ 64	$ 83	$ 85	$ 88	$ 95
S/O	37	37	37	37	37
Diluted EPS	**$1.72**	**$2.24**	**$2.29**	**$2.39**	**$2.56**
DPS	**$1.06**	**$1.16**	**$1.28**	**$1.39**	**$1.49**
Net income	64	83	85	88	95
Adjustments to reconcile non-cash charges	40	42	46	48	51
Changes in assets and liabilities	33	(8)	(12)	(12)	(12)
CFO	137	117	119	125	134
Capital expenditures	(127)	(152)	(115)	(145)	(155)
Other	(1)	(1)	-	-	-
CFI	(128)	(153)	(115)	(145)	(155)
Issuance/repurchase of common stock	1	1	1	1	1
Long-term debt issued/repaid	(0)	(40)	30	45	45
Short-term debt issued/repaid	37	110	20	15	20
Dividends paid	(39)	(43)	(47)	(51)	(55)
Other	0	4	4	4	4
CFF	(2)	31	7	13	14
Net change in cash and cash equivalents	2	(6)	11	(8)	(7)
Cash and cash equivalents, end of period	7	1	12	4	(3)
Current assets	$ 131	$ 122	$ 135	$ 129	$ 124
PP&E	1,323	1,447	1,519	1,621	1,729
Regulatory and other assets	47	72	72	72	72
Total assets	1,501	1,641	1,726	1,821	1,925
Current liabilities	147	116	157	157	157
Long-term debt	281	281	311	356	401
Other liabilities (including construction)	516	643	643	643	643
Total liabilities	943	1,040	1,111	1,156	1,201
Total Shareholders' Equity	558	601	614	665	723
Liabilities and Shareholders' Equity	$ 1,501	$ 1,641	$ 1,726	$ 1,821	$ 1,925

Seaport Global

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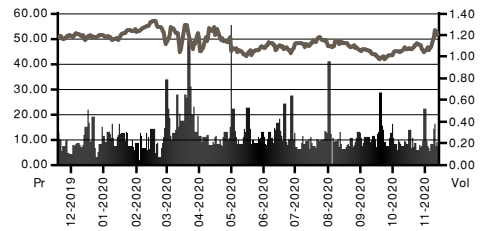
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$52.38**
Float:	49.4MM
Diluted Shares:	49.4MM
Short Interest:	0.8MM
Average Daily Volume:	221k
52 Week Range:	$39.74 - $57.36
Market Cap:	**$2,588MM**
Cash and Investments:	$114MM
Debt:	$1,182MM
Enterprise Value:	$3,655MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
Q1 (Mar)	$(0.16)A	$(0.42)	$(0.42)A	$(0.12)	$(0.12)E	$(0.08)	$(0.08)E
Q2 (Jun)	$0.35A	$0.11	$0.11A	$0.43	$0.42E	$0.53	$0.53E
Q3 (Sep)	$0.88A	$0.78	$1.94A	$0.85	$0.85E	$0.95	$0.95E
Q4 (Dec)	$0.24A	$1.03	$0.24E	$0.54	$0.54E	$0.43	$0.43E
FY	$1.31A	$1.49	$1.87E	$1.70	$1.70E	$1.83	$1.83E
P/E	**39.8x**		**27.9x**		**30.9x**		**28.6x**
Dividends Per Share							
FY	$0.790A	$0.850	$0.850E	$0.909	$0.909E	$0.978	$0.978E
Dividend Yield	**1.5%**		**1.6%**		**1.7%**		**1.9%**

California Water Services Group

(NYSE: CWT)

Re-rating came faster than we expected

Summary:

We delayed any rating changes on CWT until after its 3Q20 earnings print, in anticipation of yet another big earnings miss vs. consensus given the lack of a final decision in CWT's general rate case in CA. Yet, management decided to book an earnings catch up related to the rate case already in 3Q20 based on a Proposed Decision and comments on its from the CPUC consumer advocate. The stock jumped ~14% during a week following its earnings print vs. ~4% for XLU and ~5% for smid cap water names. Now, CWT trades at just a 4% 2022 P/E discount to an average regulated water utility in the US which seems almost fair to us. Therefore, we stick to our Neutral rating.

Highlights

2020 earnings catch up came earlier and was bigger than we expected: CWT booked YTD adjustments to its CA earnings in 3Q20 based on a Proposed Decision (PD) in its pending general rate case (GRC) and comments from the consumer advocate on the PD. We were clearly surprised by this move as CWT's management tends to be very conservative on any regulatory adjustments. The earnings adjustments were meaningfully higher than we had anticipated, even adjusting for the accelerated true up in YTD earnings, and seemed driven by one-time adjustments for the 2017 TCJA-related tax customer refund. This is why our 2021/2022 estimates, which drive our rating, remained unchanged while our 2020 estimates went up sharply.

Change to CWT's full revenue decoupling (WRAM) only in 2023, if at all: In late August, the CPUC removed the full water revenue decoupling (WRAM) for all four investor-owned water utilities in CA which currently use the mechanism, including CWT. The Commission ruled that the WRAM removal should impact "any future general rate case applications filed after the effective date of this decision". The PD agreed with CWT's stance and as a result, CWT's earnings in CA should be impacted only starting 2023 if at all. CWT along with the remaining three investor-owned water utilities in CA have asked for rehearing of the CPUC decision, and if unsuccessful, the utilities seem ready to challenge the decision in courts.

Estimates and valuation: We raised our 2020 estimates (to $1.87 from $1.49) to reflect YTD results and cost deferrals which meaningfully exceeded our expectations. Our 2021-2022 estimates remain unchanged. Following a recent rally, CWT not trades at just a 4% discount to an average regulated water utility which seems almost fair to us. The company has highly underinvested utility assets in CA, but management's conservatism results in volatility in earnings which in effect reduce the rate base growth appeal of CWT. Therefore, we remain on the sidelines.

Company Description:

CWT operates regulated water and wastewater utilities in CA, WA, HI and NM, with 490,000 connections in CA (90%), 36,000 connections in WA (recently doubled through an acquisition), 5,000 in HI, and 8,300 connections in NM.

CWT: EPS breakdown by segment ($)

CWT	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.31**	**1.87**	**1.70**	**1.83**	**11.7%**
DPS	**0.79**	**0.85**	**0.91**	**0.98**	**7.4%**
Dividend payout	60%	45%	54%	53%	

Source: Company data for 2019; Seaport Global Securities

CWT	2019A	2020E	2021E	2022E
EBIT	117	149	148	163
EBITDA	209	248	255	277
Net interest expense	41	44	45	47
Net income	63	92	87	96
EPS	**$1.31**	**$1.87**	**$1.70**	**$1.83**
DPS	**$0.79**	**$0.85**	**$0.91**	**$0.98**

CFO	**$ 169**	**$ 211**	**$ 214**	**$ 231**
Utility plant expenditures	(274)	(275)	(285)	(285)
Other	(2)	(2)	(2)	(2)
CFI	**(276)**	**(277)**	**(287)**	**(287)**
Issuance of common stock	18	96	80	86
Issuance of debt	103	28	32	32
Dividends	(38)	(41)	(44)	(47)
Other	20	20	20	20
CFF	**103**	**103**	**88**	**91**
Change in cash and cash equivalents	(4)	37	15	35

Net utility plant	2,406	2,583	2,761	2,932
Cash and cash equivalents	43	86	100	136
Other current assets	142	142	142	142
Total current assets	184	227	242	277
Regulatory assets	433	433	433	433
Goodwill	3	3	3	3
Other assets	85	85	85	85
Total assets	**$ 3,111**	**$ 3,331**	**$ 3,524**	**$ 3,731**
Total common stockholders' equity	$ 780	$ 831	$ 874	$ 923
Long-term debt, less current maturities	787	814	847	879
Total capitalization	**1,567**	**1,645**	**1,720**	**1,802**
Total current liabilities	359	479	578	682
Deferred income taxes	223	223	223	223
Pension and postretirement benefits ot	259	259	259	259
Other long-term liabilities	270	270	270	270
Advances for construction	191	191	191	191
Contributions in aid of construction	242	262	282	302
Total capitalization and liabilities	**$ 3,111**	**$ 3,331**	**$ 3,524**	**$ 3,731**

Seaport Global

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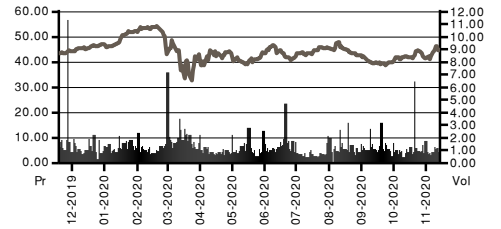
Rating:	**Neutral**
Price Target:	**N/A**
Price Target Metrics: ***N/A***	
Current Price:	**$44.71**
Float:	244.8MM
Diluted Shares:	254.4MM
Short Interest:	11.0MM
Average Daily Volume:	1,188k
52 Week Range:	$30.40 - $54.52
Market Cap:	**$11,376MM**
Cash and Investments:	$5MM
Debt:	$5MM
Enterprise Value:	$11,376MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
FY	$1.47A	$1.58	$1.58E	$1.66	$1.66E	$1.78	$1.78E
P/E	**30.4x**		**28.3x**		**27.0x**		**25.2x**
Dividends Per Share							
FY	$0.907A	$0.970	$0.970E	$1.038	$1.038E	$1.111	$1.111E
Dividend Yield	**2.0%**		**2.2%**		**2.3%**		**2.5%**

Essential Utilities, Inc.

(NYSE: WTRG)

DELCORA deal is increasingly important as it should dilute gas LDC exposure

Summary:
While we share WTRG's rate base/earnings growth expectations for its gas LDC, we look to the pending acquisition of the DELCORA wastewater system in PA as a way to boost WTRG's earnings mix more towards water. We remain on the sidelines until we get more legal/regulatory clarity on this large wastewater system acquisition.

Highlights

Gas LDCs and ESG investing: We continue to project a ~9% annual rate base growth for WTRG's Peoples in PA, but investors increasingly question the longevity of this infrastructure replacement cycle given the growing push to decarbonize house heating in Europe. Ongoing gas pipe replacement should continue to reduce methane leaks and blending of RNG should lower the carbon footprint of gas LDCs without any detriment to their earnings growth over the next decade if not longer, we believe, as electric heat pumps gain on popularity. In other words, we don't expect the rate base growth of gas LDCs especially those in gas-supportive states like PA to slow down any time soon. However, the marginal US water utility investor seems to have a strict ESG mandate and WTRG's 30% of earnings coming from gas LDCs seems to diminish the investment appeal of WTRG's stock. The DELCORA acquisition, if successful, should reduce the gas LDC earnings contributions hence the transaction is increasingly important for the stock.

DELCORA acquisition: WTRG has $363MM in pending muni water/wastewater deals in PA (and TX), the largest backlog we can recall in Aqua's/WTRG's history. The backlog includes the DELCORA wastewater acquisition ($276.5MM) which continues to face legal challenges, but WTRG's management feels comfortable with its ability to close the transaction in late March/April 2021, following a delayed PA PUC review. WTRG/ Aqua PA insists that they have a legally binding asset purchase agreement (APA) for the wastewater system, but courts should rule on the APA validity only within the next 60 days. The DELCORA transaction should be additive to WTRG's water earnings only in 2022 following Aqua PA's rate case to be filed next year.

Estimates and valuation: WTRG's 3Q20 earnings and management's guidance toward the high-end of its 2020 EPS target range came in line with our expectations. Our 2020-2022 EPS estimates remain unchanged. We recognize that WTRG's gas utility is in good regulatory jurisdictions and has strong rate base/earnings growth prospects, similar to those of ATO. WTRG's water utility is an average grower unless the company should be successful with the DELCORA acquisition, we believe. Excluding the DELCORA deal, WTRG's stock now adequately reflects its current earnings mix and growth prospects, we believe. Therefore, we remain on the sidelines until we grow more comfortable with the DELCORA deal actually closing.

Company Description:
WTRG owns and operates water utilities (1 million accounts) and gas utilities (0.74 million accounts) in 10 states though mainly PA.

WTRG: EPS estimates per segment ($)

WTRG	2019A	2020E	2021E	2022E	'19-'22 CAGR
Regulated water utilities	1.47	1.10	1.17	1.25	
Regulated gas utilities	0.00	0.54	0.61	0.69	
Parent	0.00	-0.06	-0.13	-0.16	
Total EPS	**1.47**	**1.58**	**1.66**	**1.78**	**6.7%**
DPS	**0.91**	**0.97**	**1.04**	**1.11**	**7.0%**
Dividend payout	62%	61%	63%	62%	

Source: Company data for 2019, Seaport Global Securities

WTRG	2019A	2020E	2021E	2022E
Operational EBITDA	505	874	923	1,000
Operational EBIT	349	610	645	706
Net interest expense	100	202	210	228
Ordinary Profit Before Tax	269	437	464	507
Income tax	7	35	37	41
Net profit	262	402	427	466
S/O (m)	178	255	258	262
Diluted EPS	**1.47**	**1.58**	**1.66**	**1.78**
DPS	**0.91**	**0.97**	**1.04**	**1.11**
Cash	1,869	5	5	5
Receivables	108	110	113	120
Inventory	18	30	30	30
Other short-term assets	18	18	18	18
Other-long term assets	1,003	3,810	3,810	3,810
Property, plant, and equipment	6,346	8,962	9,113	9,249
Total assets	**9,362**	**12,935**	**13,090**	**13,232**
Financial liabilities	117	496	496	496
Operating liabilities	67	109	109	109
Other liabilities	108	220	220	220
Deferred credits	2,057	2,758	2,757	2,757
Long-term debt	2,943	4,750	5,346	5,658
Shareholders' equity	4,070	4,602	4,161	3,992
Total liabilities and equity	**9,362**	**12,935**	**13,090**	**13,232**
Net income	262	402	427	466
D&A, goodwill amortisation	156	264	279	294
Other non cash elements	-40	-6	-6	-6
Funds from operations	379	660	699	754
Non-cash working capital	-40	43	0	-1
CFO	**339**	**703**	**699**	**753**
Net investments in fixed assets	-610	-6,555	-1,032	-780
Net investments in financial assets	6	0	0	0
Free cash flow before dividends	**-266**	**-5,852**	**-333**	**-27**
Dividends paid	-161	-242	-266	-290
Free cash flow after dividends	-427	-6,095	-599	-316
Changes in equity	1,935	302	2	3
Changes in financial debt	386	3,927	596	313
Adjustment for minorities / miscellaneous	-28	1	1	1
Increase in cash	1,866	-1,864	0	0

Seaport Global

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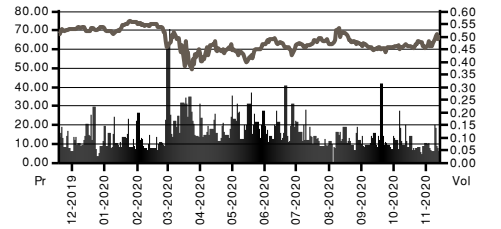
Rating:	**Neutral**
Price Target:	**N/A**

Price Target Metrics:
N/A

Current Price:	**$66.17**
Float:	26.0MM
Diluted Shares:	28.7MM
Short Interest:	0.3MM
Average Daily Volume:	73k
52 Week Range:	$45.60 - $74.99
Market Cap:	**$1,899MM**
Cash and Investments:	$20MM
Debt:	$1,505MM
Enterprise Value:	$3,384MM

PRICE & VOLUME CHART



ESTIMATES $ (MMs except multiples & EPS)

	2019	2020 Prior	2020 New	2021 Prior	2021 New	2022 Prior	2022 New
EPS (Diluted)							
Q1 (Mar)	$0.21A	$0.08	$0.08A	$0.23	$0.23E	$0.26	$0.26E
Q2 (Jun)	$0.48A	$0.69	$0.69A	$0.70	$0.70E	$0.79	$0.79E
Q3 (Sep)	$0.68A	$0.95	$0.91A	$0.82	$0.82E	$0.92	$0.92E
Q4 (Dec)	$0.42A	$0.33	$0.36E	$0.59	$0.59E	$0.65	$0.65E
FY	$1.78A	$2.05	$2.04E	$2.35	$2.35E	$2.62	$2.62E
P/E	**37.1x**		**32.5x**		**28.2x**		**25.3x**
Dividends Per Share							
FY	$1.200A	$1.280	$1.280E	$1.370	$1.370E	$1.465	$1.465E
Dividend Yield	**1.8%**		**1.9%**		**2.1%**		**2.2%**

SJW Group
(NYSE: SJW)

2021 guidance, if any, could disappoint

Summary:
San Jose Water's Monterey-style WRAM benefited SJW's earnings thanks to favorable weather and a COVID-related uptick in residential sales, though the earnings uplift was a bit lower than we had hoped. We remain concerned about the potential impact of the ongoing La Nina and the uncertainty surrounding the upcoming rate case in CT on SJW's 2021 guidance, if the company even decides to issue one in early 2021. Therefore, we remain on the sidelines on SJW even though the stock trades at a 15% 2022 P/E to an average regulated water utility.

Highlights

Tweaking estimates: We trimmed our recently increased 2020 EPS estimate to $2.04 from 2.05 based on SJW's 3Q20 earnings print. Our 2021/2022 EPS estimates remain unchanged. We continue to be concerned about SJW's 2021 EPS guidance range given the likely La Nina impact on its surface water production levels as well as an uncertain outcome of its CT rate case. We wouldn't be surprised if management decided not to provide 2021 EPS guidance in early 2021 which would not be well-received, we believe. Please see our most recent note on SJW for our latest thoughts on the name.

Company Description:
SJW Group is a regulated water and wastewater utility serving ~390,000 accounts across CA, CT, TX and ME. SJW merged with Connecticut Water Service in October 2019.

SJW: EPS breakdown by segment ($)

SJW	2019A	2020E	2021E	2022E	2019-2022 CAGR
Total EPS	**1.78**	**2.04**	**2.35**	**2.62**	**13.7%**
DPS	**1.20**	**1.28**	**1.37**	**1.47**	**6.9%**
Dividend payout	67%	63%	58%	56%	

Source: Company data for 2019; Seaport Global Securities

SJW	2019A	2020E	2021E	2022E
EBITDA	157	211	236	248
Net income	51	58	67	75
EPS diluted	**$1.78**	**$2.04**	**$2.35**	**$2.62**
DPS	**$1.20**	**$1.28**	**$1.37**	**$1.47**
CFO	**$ 130**	**$ 151**	**$ 167**	**$ 177**
CFI	**(1,018)**	**(216)**	**(277)**	**(257)**
Issuance of common stock	0.0	0.0	0.0	0.0
Issuance of debt	502	113	113	113
Dividends	-34	-36	-39	-40
CFF	**485**	**101**	**99**	**99**
Change in cash and cash equivalents	-403	36	-12	19
Net utility plant	2,206	2,313	2,474	2,612
Cash and cash equivalents	18	54	42	62
Other current assets	109	112	115	117
Total current assets	127	166	157	179
Regulatory assets	114	114	114	114
Goodwill	628	628	628	628
Other assets	57	57	57	57
Total assets	**3,132**	**3,278**	**3,430**	**3,591**
Total common stockholders' equity	$ 890	$ 966	$ 980	$ 999
Long-term debt, less current	1,261	1,187	1,195	1,203
Total capitalization	**2,151**	**2,153**	**2,175**	**2,202**
Total current liabilities	235	359	470	583
Deferred income taxes	196	193	190	188
Pension and postretirement benefits oth	108	108	108	107
Other long-term liabilities	45	45	45	45
Advances for construction	112	135	157	180
Contributions in aid of construction	286	286	286	286
Total capitalization and liabilities	**3,132**	**3,278**	**3,430**	**3,591**

Utilities Disclosures

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Risks & Considerations for American Water Works Company, Inc. American Water Works Company, Inc. (AWK)

Allowed ROEs for AWK's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings.

Lower sales volumes could weigh on AWK's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWK has a particularly busy regulatory calendar in 2020, with rate cases in three of its largest jurisdictions – NJ, PA and MO.

Potentially higher equity needs due to weakening operating cash flows and underfunded pension funds: Lower customer collections (due to lower sales or non-payment) coupled with growing federal cash taxes and underperforming pension funds should be weighing on operating cash flows of regulated utilities especially during/following the COVID-19 pandemic. That in turn could require some deleveraging of balance sheets of regulated utilities thus more equity. AWK already announced ~$500m in new equity as soon as 2022, but the issuances could be enlarged and accelerated to protect AWK's credit ratings.

Risks & Considerations for American States Water Company American States Water Company (AWR)

AWR's water utility (GSWC) could see volatility in earnings due to usage: The CPUC recently modified the full water decoupling mechanism (WRAM). While it should not impact GSWC until the next rate case, covering 2025-2027, CA utility consumer advocates push for an immediate change to the decoupling mechanism. GSWC has always excelled at earning at least its allowed ROE in CA, but it could prove challenging with WRAM.

Allowed ROEs for AWR's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. AWR's allowed ROE for its water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. AWR should be filing a new water rate case by July 2020 with new rates in effect in January 2021.

Returns in pension accounts impact AWR's earnings in between rate cases in CA: AWR has no balancing account tracking changes in returns in its pension accounts. Those changes can be trued up/reflected in AWR's rates during rate cases, but those take place every three years.

Military contracts are highly competitive: Through its unregulated ASUS subsidiary, AWR provides water and wastewater services to 11 military bases. The company awaits awards of up to three more of these contracts in 2020. We assume that AWR secures at least one new military contract per year in 2020-2022 though AWK, AWR's largest competitor, has been winning most of the contract awards as of late.

Risks & Considerations for California Water Services Group California Water Services Group (CWT)

Allowed ROEs for CWT's regulated water utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. CWT's allowed ROE for its water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. CWT awaits a proposed decision in its 2018 general rate case in CA with rates retroactive to January 1, 2021. Though the utility reached a partial settlement with the consumer advocate late in 2019, outstanding issues involve the continuation of the revenue decoupling and balancing accounts for pension and medical expenses. Without those, CWT could see a meaningful spike in its earnings volatility.

Risks & Considerations for SJW Group SJW Group (SJW)

Allowed ROEs for SJW's regulated water utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average 10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. SJW's allowed ROE for its CA water utility for 2022-2024 should be set by late 2021 in a cost of capital proceeding.

Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, its up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. SJW should file a rate case for its new CT business in 2021. Also, the CA utility of SJW should go through a general rate case in the state in 2021 and state regulators could attempt to claw-back some synergies related to the recent merger with CTWS.

SJW's CA earnings are highly volatile: Now that SJW no longer has even a temporary decoupling mechanism in CA, it's CA earnings change along with changes in volumes and changes in purchased water costs. SJW plans to ask for a purchased water cost balancing account in the next rate case in CA, but that means that 2021 could be another weak earnings year before the regulatory fix arrives for 2022, if at all.

Risks & Considerations for Essential Utilities, Inc. Essential Utilities, Inc. (WTRG)

Allowed ROEs for WTRG's regulated utilities could fall due to lower market interest rates: Equity returns/ROE of regulated electric/gas/water utilities are indirectly linked to the 10-year Treasury yield. The average allowed ROE of a regulated utility in the US dropped just 25 bps since 2008 despite a 152 bps drop in the average

10-year T yield over this period. However, state utility regulators could sharply reduce allowed ROEs of regulated utilities going forward which currently average 9.75% average. The allowed ROE together with an equity ratio are the key drivers of regulated utility earnings. WTRG's only pending rate case (in NC) is very small.

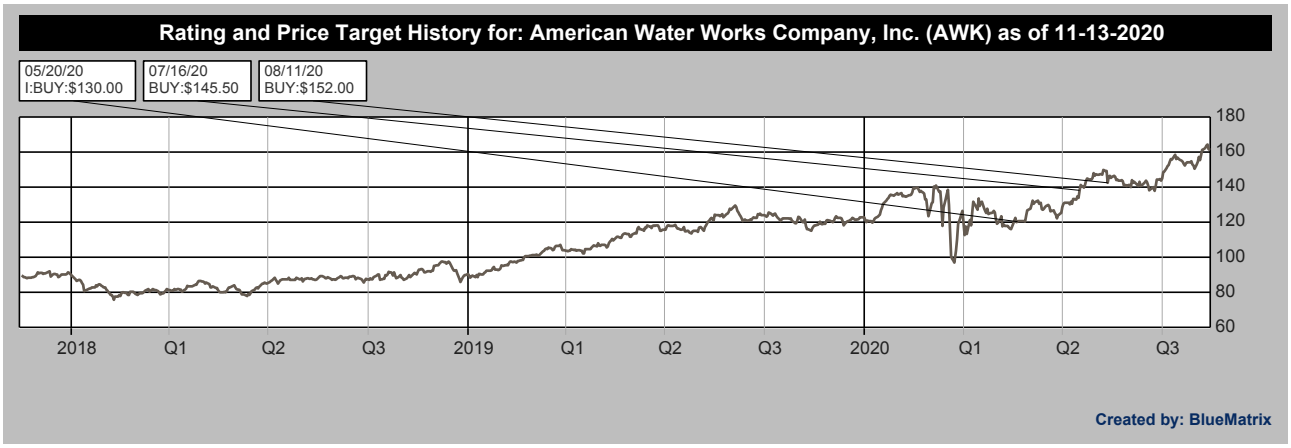
Lower sales volumes could weigh on WTRG's realized ROEs and thus earnings: A utility can see a meaningful deficiency between its realized and allowed ROE depending on the level of sales volumes and operating expenses. While the latter can be controlled, sharp reductions in sales volumes due to energy efficiency (residential and commercial sales) or closure of industrial facilities. The latter is particularly pronounced during the COVID pandemic. The sharply lower C&I sales volumes could weigh on utility earnings beyond 2020. While rate cases could true up sales volume assumptions, utilities could delay rate filings because their ROE could be reduced during those proceedings on the back of sharply lower interest rates.

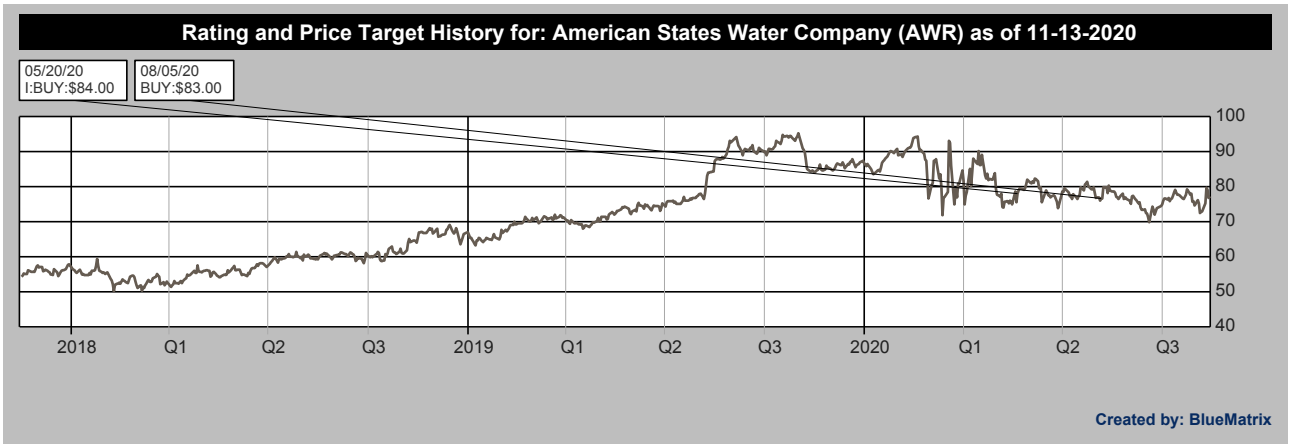
Rate case outcomes are hard to predict: While regulated utilities are allowed to recover prudently incurred costs, it's up to state utility regulators to determine which costs are in fact recoverable and the return on regulated assets. Some rate case requesting higher revenues may end with a reduction in authorized rates thus revenues and thus earnings. WTRG's regulatory calendar is quiet in 2020, with a pending small rate case in NC, and a likely filing for a catch-up repair tax adjustment for Peoples in PA.

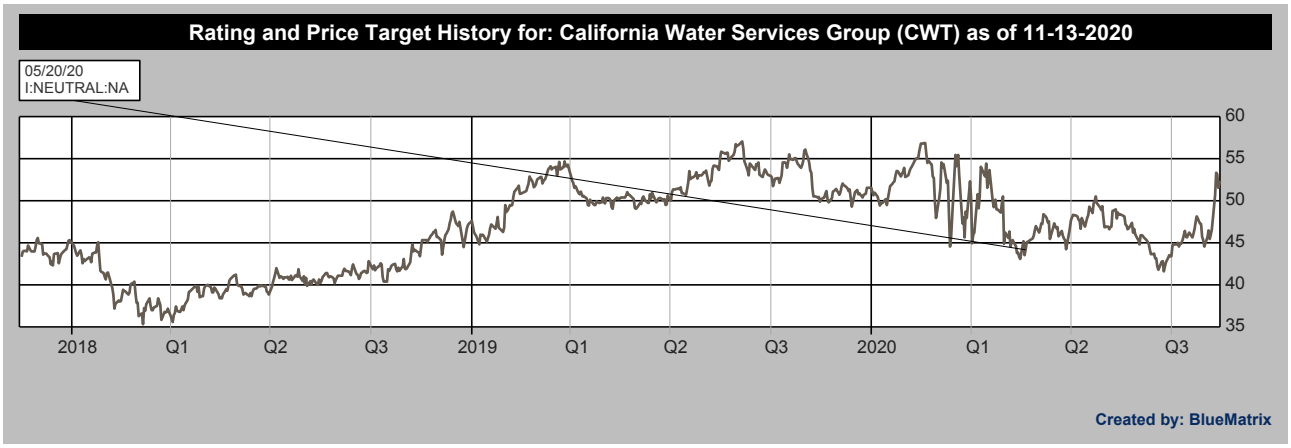
Gas utilities have a higher operating risk than water utilities: Over-pressurized gas systems seem to happen more frequently among gas utilities in the US. While we recognize that Peoples Gas is a well-managed system, WTRG's risk profile could further deteriorate with any gas-related operational issues. Additionally, investors increasingly scrutinize the carbon footprint of gas LDCs which in turn weighs on their market valuations.

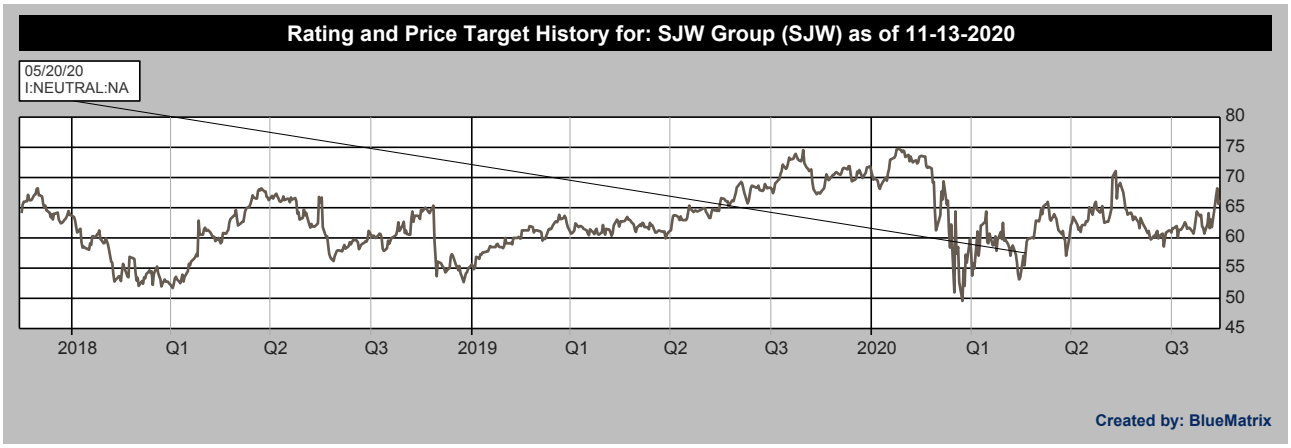
Other Companies Mentioned in This Report

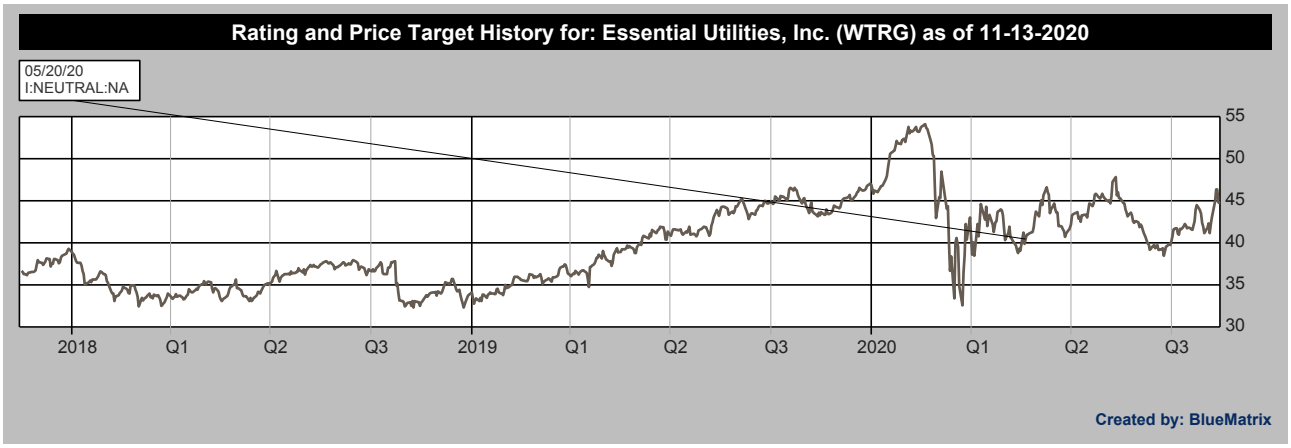
- American Water Works Company, Inc. (AWK: $161.31, Buy)
- California Water Services Group (CWT: $52.38, Neutral)
- Essential Utilities, Inc. (WTRG: $44.71, Neutral)
- American States Water Company (AWR: $77.20, Buy)
- SJW Group (SJW: $66.17, Neutral)











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NA - A rating is not assigned.

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Neutral - The investment outlook and risk/reward over the following 12 months are neutral on an absolute basis and relative to the peer group.

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Sell - The investment outlook and risk/reward over the following 12 months are very unfavorable on an absolute basis and relative to the peer group.

NA - A rating is not assigned.

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Buy	102	61.1%	1	100.0%	1.0%
Neutral	62	37.1%	0	0.0%	0.0%
Sell	3	1.8%	0	0.0%	0.0%
Total	167	100.0%	1	100.0%	0.6%

*Investment banking clients are companies for whom Seaport Global Securities has provided investment banking services in the previous 12 months.

Note: Ratings Distribution as of September 30, 2020

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This report is intended exclusively for:
bcobrien@ aquaamerica.com

First Read

Aqua America Inc

Line of Sight to Merger Close Not as Clear as Expected

Equities

Americas
Water Utilities

12-month rating	**Buy**
12m price target	**US$42.00**
Price	**US$41.12**

RIC: WTR.N **BBG:** WTR US

Trading data and key metrics

52-wk range	US$41.12-32.37
Market cap.	US$7.34bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	461
Avg. daily value (m)	US$17.4
Common s/h equity (12/19E)	US$2.15bn
P/BV (12/19E)	3.4x
Net debt / EBITDA (12/19E)	5.1x

EPS (UBS, diluted) (US$)

	12/19E	
	UBS	Cons.
Q1E	0.30	0.28
Q2E	0.39	0.40
Q3E	0.47	0.41
Q4E	0.32	0.36
12/19E	1.48	1.46
12/20E	1.58	1.56
12/21E	1.68	1.66

Two Intervenor Holdouts Take the Merger down a Litigated Path

During the hearing yesterday at the PA Public Utilities Commission for the merger between WTR and Peoples, it was disclosed that WTR reached a settlement with most intervenors in the case, with the exception of two parties to the docket: the Bureau of Investigation and Enforcement (BIE) and the Office of Small Business Advocate (OSBA). WTR filed an 8K today with little detail regarding the sticking points for the two intervenors; however, as we understand it, BIE (which is effectively the PUC Staff) disagrees with an aspect of the settlement reached with the other parties related to a small gas system (Goodwin Tombaugh ~1,600 customers) within Peoples. As a result of failing to reach an all-party settlement, the merger case will have to proceed through a litigated process to address the outstanding issues. Although at this stage we don't believe the issues put the transaction in jeopardy, this development is disappointing. We had anticipated that WTR would be successful in reaching settlement with all parties based on the confidence that management portrayed earlier in the process, as well as indications that transaction financing would only be issued when there was "line of sight" to merger close. In April, WTR issued $900MM debt, $650MM convertible equity units, and ~$1.3B in common equity, in addition to another $750MM that will be placed privately upon merger close.

Peoples Rate Case

The Peoples rate case is proceeding on a parallel path at the PA commission. Settlement discussions are expected to begin ~early-July and WTR expects to be more active in Peoples' rate case once settlement discussions begin. Rate case proceedings in PA have a history of settlement. It remains unclear if/how the intervenor issues in the merger docket would weave into the rate case.

Next Steps

Briefs in the merger docket are due July 10 and reply briefs are due July 25. WTR now expects the merger to close fall 2019, as opposed to its original projection for a close in mid-2019.

Valuation: $42 Price Target

We value WTR at a 25.2x P/E on 2021e EPS of $1.68.

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Highlights (US$m)	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
Revenues	820	810	838	881	921	956	995	1,033
EBIT (UBS)	326	329	337	370	399	425	454	482
Net earnings (UBS)	234	240	251	265	281	299	319	342
EPS (UBS, diluted) (US$)	1.32	1.35	1.41	1.48	1.58	1.68	1.79	1.92
DPS (US$)	0.74	0.79	0.88	0.94	1.00	1.07	1.15	1.23
Net (debt) / cash	(1,891)	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)

Profitability/valuation	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
EBIT margin %	39.7	40.6	40.3	42.0	43.3	44.5	45.6	46.7
ROIC (EBIT) %	9.0	8.4	7.9	8.0	8.0	8.1	8.3	8.4
EV/EBITDA (core) x	16.2	17.0	17.6	18.9	18.1	17.4	16.7	15.8
P/E (UBS, diluted) x	23.9	24.8	25.0	27.7	26.1	24.5	23.0	21.5
Equity FCF (UBS) yield %	0.2	(1.6)	(1.6)	(1.8)	0.2	0.5	0.9	1.2
Net dividend yield %	2.3	2.4	2.5	2.3	2.4	2.6	2.8	3.0

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$41.12 on 12 Jun 2019 18:43 EDT

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Forecast returns

Forecast price appreciation	+2.1%
Forecast dividend yield	2.3%
Forecast stock return	+4.4%
Market return assumption	6.9%
Forecast excess return	-2.5%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 1% discount to the 2021 average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 7% discount to reflect impact of lower P/E associated with gas earnings.

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	47%	25%
Neutral	FSR is between -6% and 6% of the MRA.	39%	22%
Sell	FSR is > 6% below the MRA.	14%	19%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 31 March 2019.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

KEY DEFINITIONS:Forecast Stock Return (FSR) is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months. In some cases, this yield may be based on accrued dividends. **Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium). **Under Review (UR)** Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation. **Short-Term Ratings** reflect the expected near-term (up to three months) performance of the stock and do not reflect any change in the fundamental view or investment case. **Equity Price Targets** have an investment horizon of 12 months.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Aqua America Inc[16]	WTR.N	Buy	N/A	US$41.12	12 Jun 2019

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date
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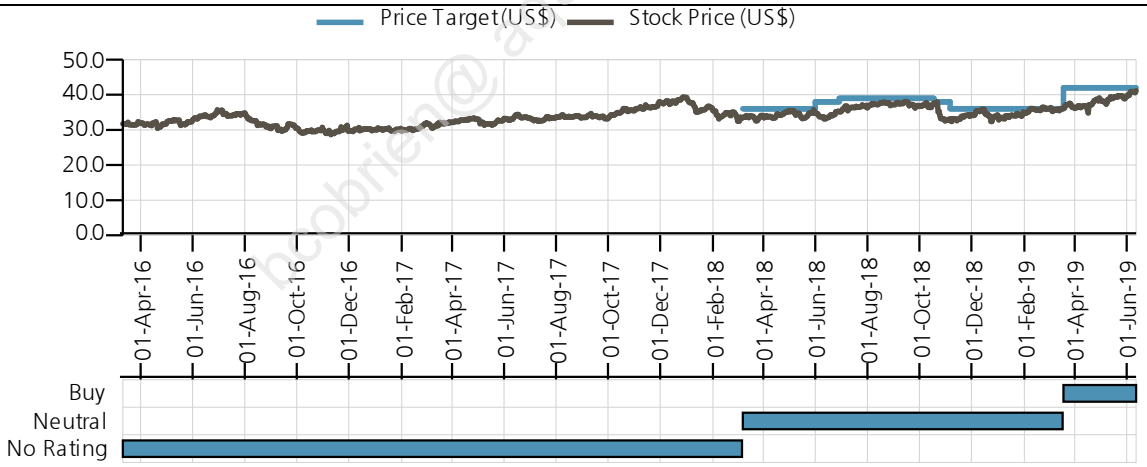
Aqua America Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2016-03-11	31.72	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy

Source: UBS; as of 12 Jun 2019

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Q2 2020 Earnings Preview

North America Power & Utilities, Alternative Energy, and Environmental Services

Equities

North America
Utilities

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Regulated Utilities: Strong Weather Comparison

We expect favorable weather conditions helped offset the impact of the pandemic on demand. 2Q'20 degree days rose 12% above last year and 9% above normal with the biggest impacts in the Midwest and Northeast. Our forecasts average 5% above consensus and 2% above 2Q'19. Consensus may still be developing but we see few if any shortfalls versus consensus. Names that will likely create the most interest for investors are Buy-rated DTE, DUK, PCG, PEG and SRE and Neutral-rated EVRG, PNW and SO. Our water utility forecasts are in line with consensus with positive quarters for Neutral-rated AWK and AWR. We expect to hold a conference call on Monday, July 20 at 10 AM with a dial in number of 800-950-3502 and a code 21966464.

Power: 2Q Beats on Weather and Retail Acquisitions; Updating UBSe EBITDA

Our 2Q'20 Adjusted EBITDA estimates are above consensus for both NRG and VST at $543mln and $819mln respectively. We expect bad debts and volume dislocations from COVID-19 were not as bad as anticipated in 2Q and weather provided a positive volume offset. VST results will be driven by OPI cost savings offsetting lower capacity payments, the retail acquisitions of Crius and Ambit and better pricing in ERCOT due to the commercial impact noted on the 1Q '20 call. NRG results will be driven by the Stream retail acquisition, better weather, and margin enhancement at retail. VST and NRG were both significantly hedged for the balance of 2020 at the time of the 1Q'20 earnings calls. We are updating our UBSe Adj. EBITDA. NRG to $1,986 /$1,840/$1,737mln and VST to $3,444/$3,087/$3,076mln for '20/21/22 respectively.

Alternative Energy

We expect 2Q20 calls to focus on 2H20 demand given the on-going recovery from COVID-19 troughs in April; the potential for further policy support after the 2020 election; and impacts of corporate actions (RUN/VSLR merger, Maxeon spin from SPWR); as well as GNRC's storage product update (initiation).

Environmental Services

The MSW names operationally weathered the COVID-19 economic downturn (top pick WCN). We continue to see value in the more depressed share prices of CVA and ECOL. As the election approaches we expect increased focus on potential for higher tax rates.

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Figure 1: Electric Utilities Universe

Rating	Ticker	Company	7/16/2020 Price	Price Target	Total Return inc. Div. Yld	UBS 2019A EPS	UBS 2020A EPS	UBS 2021E EPS	UBS 2022E EPS	2021 P/E Ratio	2021 Prem/ Disc	2022 P/E Ratio	2022 Prem/ Disc	Current Dividend Yield	5 Yr EPS Growth	5 Yr DPS Growth	Regulatory Quartile
Buy (CBE)	PCG	PG&E Corp	$9.02	$15	66%	$3.93	$1.41	$0.98	$1.11	9.2x	(49%)	8.1x	(53%)	0.0%	N/A	N/A	3rd
Buy	SRE	Sempra Energy	$122.63	$172	43%	$6.78	$7.45	$7.84	$8.33	15.6x	(14%)	14.7x	(14%)	3.2%	6.2%	8.1%	3rd
Buy	EIX	Edison International	$56.09	$75	38%	$4.70	$4.45	$4.67	$4.80	12.0x	(34%)	11.7x	(32%)	4.5%	1.2%	4.0%	3rd
Buy	DUK	Duke Energy	$81.07	$102	30%	$5.05	$5.07	$5.27	$5.50	15.4x	(15%)	14.7x	(14%)	4.7%	3.7%	2.0%	1st
Buy	EXC	Exelon	$38.06	$48	30%	$3.22	$2.98	$2.99	$3.10	12.7x	(30%)	12.3x	(28%)	4.0%	0.1%	5.3%	3rd
Buy	ETR	Entergy Corp	$98.33	$121	27%	$5.33	$5.62	$5.90	$6.30	16.7x	(8%)	15.6x	(9%)	3.8%	6.0%	2.3%	2nd
Buy	FE	FirstEnergy Corp	$41.29	$50	25%	$2.58	$2.50	$2.62	$2.74	15.7x	(13%)	15.1x	(12%)	3.8%	3.8%	4.5%	2nd
Buy	PNM	PNM Resources	$39.13	$47	23%	$2.16	$2.16	$2.38	$2.50	16.4x	4%	15.6x	6%	3.1%	5.9%	5.5%	4th
Buy	PPL	PPL Corporation	$25.85	$30	22%	$2.92	$2.40	$2.40	$2.45	10.8x	(41%)	10.6x	(38%)	6.4%	-3.7%	0.0%	1st
Buy	DTE	DTE Energy	$109.70	$130	22%	$6.30	$6.61	$7.21	$7.58	15.2x	(16%)	14.5x	(15%)	3.7%	6.8%	6.0%	1st
Buy	PEG	Public Service Ent Group	$52.91	$62	21%	$3.28	$3.31	$3.41	$3.58	15.5x	(15%)	14.8x	(13%)	3.7%	5.0%	4.8%	2nd
Buy	EMA	Emera Inc (C$)	$55.94	$65	20%	$2.60	$2.76	$3.07	$3.28	18.2x	15%	17.1x	15%	4.3%	5.3%	4.5%	1st
Buy	AES	AES Corp.	$14.88	$17	18%	$1.36	$1.38	$1.55	$1.67	9.6x	(47%)	8.9x	(48%)	3.8%	6.9%	4.8%	1st
Buy	FTS	Fortis Inc (C$)	$54.10	$62	18%	$2.55	$2.66	$2.93	$3.12	18.5x	2%	17.3x	2%	3.4%	7.3%	6.0%	3rd
Buy	NEE	NextEra Energy	$268.38	$305	16%	$8.37	$9.08	$9.84	$10.55	27.3x	50%	25.4x	49%	1.9%	7.9%	10.0%	1st
Buy	ACO	ATCO Ltd. (C$)	$42.31	$47	15%	$3.18	$2.91	$3.25	$3.41	13.0x	(17%)	12.4x	(16%)	4.1%	3.6%	7.1%	4th
Buy	OGE	OGE Energy Corp	$31.90	$35	15%	$2.16	$2.17	$2.21	$2.31	14.5x	(20%)	13.8x	(19%)	4.9%	3.5%	5.0%	3rd
Buy	AEP	American Electric Power	$85.09	$94	14%	$4.24	$4.30	$4.65	$4.93	18.3x	1%	17.3x	1%	3.3%	5.5%	5.7%	2nd
Buy	D	Dominion Energy	$76.95	$81	10%	$4.13	$3.50	$3.87	$4.12	19.9x	9%	18.7x	9%	4.9%	2.5%	-4.1%	2nd
Neutral	ED	Consolidated Edison	$71.84	$76	10%	$4.38	$4.25	$4.58	$4.76	15.7x	(14%)	15.1x	(12%)	4.3%	3.2%	3.5%	4th
Neutral	CU	Canadian Utilities Ltd (C$)	$34.41	$36	9%	$2.23	$2.04	$2.25	$2.37	15.3x	(3%)	14.5x	(2%)	4.8%	3.2%	4.8%	4th
Neutral	CMS	CMS Energy	$60.33	$64	9%	$2.49	$2.68	$2.87	$3.05	21.0x	16%	19.8x	16%	2.7%	7.0%	7.0%	1st
Neutral	LNT	Alliant Energy	$49.73	$52	8%	$2.33	$2.45	$2.60	$2.72	19.1x	5%	18.3x	7%	3.1%	5.5%	6.2%	1st
Neutral	POR	Portland General	$42.32	$44	8%	$2.39	$2.44	$2.60	$2.64	16.3x	(10%)	16.0x	(6%)	3.6%	3.8%	6.0%	3rd
Neutral	SO	Southern Company	$53.74	$55	7%	$3.11	$3.20	$3.31	$3.56	16.2x	(11%)	15.1x	(12%)	4.6%	6.0%	3.9%	1st
Buy	AEE	Ameren Corp	$76.79	$80	7%	$3.35	$3.47	$3.76	$4.04	20.4x	12%	19.0x	11%	2.6%	6.6%	6.0%	2nd
Neutral	EVRG	Evergy	$61.41	$62	4%	$2.89	$3.06	$3.24	$3.46	19.0x	4%	17.8x	4%	3.3%	5.1%	5.3%	3rd
Neutral	WEC	WEC Energy Group	$87.76	$88	3%	$3.58	$3.75	$3.98	$4.23	22.0x	21%	20.8x	22%	2.9%	6.2%	6.7%	1st
Neutral	PNW	Pinnacle West Capital Corp	$80.56	$79	2%	$4.77	$4.85	$4.90	$5.14	16.4x	(10%)	15.7x	(8%)	3.9%	3.5%	6.0%	4th
Neutral	ES	Eversource Energy	$85.81	$85	2%	$3.46	$3.67	$3.87	$4.08	22.2x	22%	21.0x	23%	2.6%	6.0%	5.9%	2nd
Sell	CUP	Caribbean Utilities Corp Ltd	$15.49	$15	1%	$0.84	$0.69	$0.79	$0.89	19.7x	25%	17.5x	18%	4.5%	6.6%	7.1%	4th
Neutral	XEL	Xcel Energy	$64.99	$64	1%	$2.64	$2.77	$3.02	$3.20	21.5x	18%	20.3x	19%	2.5%	5.7%	6.0%	2nd
Sell	H	Hydro One Ltd (C$)	$27.26	$24	(8%)	$1.41	$1.37	$1.42	$1.49	19.1x	5%	18.3x	7%	3.6%	3.8%	4.7%	4th
Sell	HE	Hawaiian Electric Industries	$37.00	$32	(10%)	$1.88	$1.99	$1.82	$2.20	20.3x	12%	16.8x	(2%)	3.6%	3.1%	3.2%	4th
Overall Average (unnormalized, inc. Gas Midstream)										**16.7x**		**15.7x**					
Electric Utility Normalized (including Gas Midstream)										**18.2x**		**17.1x**					

Source: FactSet, UBS Equity Research

Figure 2: Water Utilities Universe

Rating	Ticker	Company	7/16/2020 Price	UBS Price Target	Total Return inc. Div. Yld	UBS 2018A EPS	UBS 2019A EPS	UBS 2020E EPS	UBS 2021E EPS	2021E P/E Ratio	2021E Prem/ Disc	Current Dividend Yield	5 Yr EPS Growth	5 Yr DPS Growth
Neutral	WTRG	Essential Utilities	$43.88	$45	5%	$1.41	$1.48	$1.58	$1.68	26.2x	(15%)	2.0%	6.6%	7.0%
Neutral	AWK	American Water	$138.32	$139	2%	$3.30	$3.63	$3.85	$4.17	33.1x	8%	1.3%	6.9%	10.0%
Neutral	SJW	SJW Group	$63.02	$62	0%	$2.51	$2.03	$2.34	$2.49	25.3x	(18%)	1.9%	8.3%	7.0%
Sell	AWR	American States Water	$77.59	$70	(8%)	$1.73	$2.03	$2.25	$2.36	32.9x	7%	1.4%	7.3%	6.0%
Sell	CWT	California Water Service	$48.28	$43	(9%)	$1.44	$1.31	$1.55	$1.69	28.6x	(7%)	1.6%	9.0%	5.0%
AVERAGE										**30.8x**				

Source: FactSet, UBS Equity Research

Figure 3: Independent Power Producers

Rating	Ticker	Company	7/16/2020 Price	Price Target	Total Return inc. Div. Yld	UBS 2018A EBITDA	UBS 2019A EBITDA	UBS 2020E EBITDA	UBS 2021E EBITDA	2020 EV/ EBITDA Ratio	2020 Prem/ Disc	2021 EV/ EBITDA Ratio	2021 Prem/ Disc	2019E Net Debt/ EBITDA
Buy	VST	Vistra Energy Corp	$19.40	$31	62%	$2,899	$3,393	$3,287	$3,195	5.7x	(21%)	5.6x	(18%)	3.2x
Buy	NRG	NRG Energy	$33.84	$41	22%	$2,001	$1,977	$1,914	$1,813	4.1x	(43%)	4.0x	(41%)	2.2x
MID-CYCLE MEDIAN										**7.2x**		**6.8x**		

Source: FactSet, UBS Equity Research

Figure 4: Regulated Utilities & Power 1Q20 Earnings Summary

U.S. companies in US$ Cdn companies in C$ CUP in US$		Quarterly					Annual					
Company	Ticker	Scheduled Reporting Date	2Q20E UBS	2Q20E Consensus	UBS Vs. Consensus	UBS Confidence Indicator[1]	2Q19A Adjusted	2020E UBS	2020E Consensus	UBS Vs. Consensus	Trailing 12 Month	2019A UBS	2020E Guidance
ELECTRIC UTILITIES													
AES Corp	AES	6-Aug	$0.21	$0.26	($0.05)		$0.26	$1.38	$1.42	($0.04)	$1.33	$1.36	$1.32-$1.42
ATCO Ltd (C$)	ACO.x-TSE	30-Jul	$0.55	$0.55	$0.00		$0.68	$2.91	$2.92	($0.01)	$2.85	$3.18	N/A
Alliant Energy	LNT	7-Aug	$0.57	$0.40	$0.17		$0.40	$2.45	$2.44	$0.01	$2.69	$2.33	$2.34-$2.48
Ameren Corp	AEE	7-Aug	$0.85	$0.84	$0.01		$0.72	$3.47	$3.45	$0.02	$3.29	$3.35	$3.40-$3.60
American Electric Power	AEP	6-Aug	$1.08	$0.99	$0.09		$1.00	$4.30	$4.31	($0.01)	$4.16	$4.24	$4.25-$4.45
Canadian Utilities Ltd (C$)	CU-TSE	30-Jul	$0.35	$0.38	($0.03)		$0.46	$2.04	$2.02	$0.02	$2.05	$2.23	N/A
Caribbean Utilities Corporation Ltd	CUP.USD-TSE	31-Jul	$0.19	$0.18	$0.01		$0.24	$0.69	$0.74	($0.04)	$0.77	$0.84	N/A
CMS Energy	CMS	3-Aug	$0.48	$0.36	$0.12		$0.33	$2.68	$2.62	$0.06	$2.57	$2.49	$2.64-$2.68
Consolidated Edison	ED	6-Aug	$0.52	$0.54	($0.02)		$0.58	$4.25	$4.40	($0.15)	$4.28	$4.38	$4.15-$4.35
Dominion Energy	D	31-Jul	$0.78	$0.73	$0.05		$0.77	$3.50	$4.38	($0.88)	$4.22	$4.13	$4.25-$4.60
DTE Energy	DTE	28-Jul	$1.51	$1.16	$0.35		$0.99	$6.61	$6.57	$0.05	$6.35	$6.30	$6.47-$6.75
Duke Energy	DUK	10-Aug	$1.00	$1.02	($0.02)		$1.12	$5.07	$5.14	($0.07)	$4.83	$5.05	$5.05-$5.45
Edison International	EIX	28-Jul	$1.16	$1.16	($0.00)		$1.58	$4.45	$4.46	($0.01)	$4.28	$4.70	$4.32-$4.62
Emera Inc (C$)	EMA-TSE	12-Aug	$0.52	$0.58	($0.06)		$0.54	$2.76	$2.80	($0.04)	$2.43	$2.60	N/A
Entergy Corp	ETR	29-Jul	$1.30	$1.24	$0.06		$1.22	$5.62	$5.56	$0.06	$5.75	$5.33	$5.45-$5.75
Evergy, Inc (2)	EVRG	w/o 8/3 Est	$0.63	$0.67	($0.04)		$0.57	$3.06	$3.09	($0.03)	$2.94	$2.89	N/A
Eversource Energy	ES	31-Jul	$0.75	$0.78	($0.03)		$0.72	$3.67	$3.65	$0.02	$3.52	$3.46	$3.60-$3.70
Exelon Corp	EXC	4-Aug	$0.45	$0.45	$0.00		$0.60	$2.98	$3.06	($0.08)	$3.07	$3.22	$2.80-$3.10
FirstEnergy Corp	FE	24-Jul	$0.53	$0.55	($0.02)		$0.61	$2.50	$2.49	$0.01	$2.50	$2.58	$2.40-$2.60
Fortis Inc (C$)	FTS-TSE	30-Jul	$0.57	$0.58	($0.01)		$0.54	$2.66	$2.65	$0.01	$2.54	$2.55	N/A
Hawaiian Electric Industries	HE	30-Jul	$0.40	$0.38	$0.02		$0.39	$1.61	$1.95	($0.34)	$1.90	$1.99	$1.90-$2.10
Hydro One Ltd (C$)	H-TSE	11-Aug	$0.32	$0.27	$0.05		$0.26	$1.37	$1.39	($0.02)	$1.33	$1.41	N/A
NextEra Energy	NEE	24-Jul	$2.49	$2.49	$0.00		$2.35	$9.08	$9.08	$0.00	$8.69	$8.37	$8.70-$9.20
OGE Energy Corp	OGE	6-Aug	$0.50	$0.50	$0.00		$0.50	$2.17	$2.19	($0.02)	$2.16	$2.16	$2.08-$2.18
PG&E Corp	PCG		$0.84	$0.94	($0.10)		$1.10	$1.41	$1.45	($0.04)	$3.52	$3.93	N/A
Pinnacle West Capital Corporation	PNW	w/o 8/3 Est	$1.55	$1.36	$0.19		$1.28	$4.85	$4.83	$0.02	$5.16	$4.77	$4.75-$4.95
PNM Resources	PNM	31-Jul	$0.50	$0.40	$0.10		$0.35	$2.16	$2.19	($0.03)	$2.34	$2.16	$2.16-$2.26
Portland General	POR	31-Jul	$0.34	$0.25	$0.09		$0.28	$2.44	$2.39	$0.04	$2.54	$2.39	$2.20-$2.50
PPL Corporation	PPL	8/7 Est	$0.57	$0.56	$0.01		$0.58	$2.40	$2.46	($0.05)	$2.41	$2.37	$2.40-$2.60
Public Service Enterprise Group	PEG	31-Jul	$0.59	$0.62	($0.03)		$0.58	$3.31	$3.37	($0.06)	$3.25	$3.28	$3.30-$3.50
Sempra Energy	SRE	5-Aug	$1.65	$1.19	$0.46		$1.38	$7.45	$7.15	$0.30	$7.78	$6.78	$7.20-$7.80
Southern Company	SO	30-Jul	$0.64	$0.69	($0.05)		$0.79	$3.20	$3.15	$0.05	$3.03	$3.11	$3.10-$3.22
WEC Energy Group	WEC	4-Aug	$0.67	$0.67	($0.00)		$0.74	$3.75	$3.74	$0.01	$3.61	$3.58	$3.71-$3.75
Xcel Energy	XEL	30-Jul	$0.49	$0.48	$0.01		$0.46	$2.77	$2.76	$0.01	$2.62	$2.64	$2.73-$2.83
Average			**$0.75**	**$0.71**	**$0.04**		**$0.73**	**$3.38**	**$3.42**	**($0.04)**	**$3.43**		
WATER UTILITIES													
American States Water Company	AWR		$0.70	$0.63	$0.07		$0.59	$2.25	$2.27	($0.02)	$2.75	$2.03	N/A
American Water Works Company	AWK	6-Aug	$0.99	$0.95	$0.04		$0.94	$3.85	$3.85	$0.00	$4.25	$3.63	$3.79-$3.89
Essential Utilities	WTRG	6-Aug	$0.26	$0.24	$0.02		$0.37	$1.58	N/A	N/A	$1.27	$1.48	$1.53-$1.58
California Water Service Group	CWT	30-Jul	$0.51	$0.64	($0.13)		$0.37	$1.55	$1.51	$0.03	$2.27	$1.31	N/A
SJW Group	SJW		$0.70	$0.70	$0.00		$0.50	$2.34		$2.34	$2.65	$2.03	N/A
Average			**$0.63**	**$0.62**	**($0.01)**		**$0.57**	**$2.31**	**$2.54**	**$0.01**	**$2.64**		
IPPS - Adjusted EBITDA not EPS	**US$mlns**												
NRG Energy	NRG	TBA	$543	$528	$15		$469	$1,986	$1,967	$19	N/A		$1,900-$2,100
Vistra Energy	VST	5-Aug	$819	$749	$70		$707	$3,444	$3,409	$35	N/A		$3,285-$3,585

1. UBS Confidence Indicator: Green = high confidence in estimate vs. consensus; Red = low confidence in estimate vs. consensus; Yellow = mid confidence in estimate vs. consensus
2. UBS estimates exclude corporate owned life insurance.
3. UBS estimates reflected above remove the estimated NRG Yield assets results from prior and current quarter and consensus for comparison purposes as they were sold on 8/31/18

Source: FactSet, company filings, UBS Equity Research

Regulated Utilities 2Q20 preview

Focus Stocks this Quarter

DTE Energy. Management will likely provide an update on the electric rate freeze until 2022 and the LEAP expansion which we expect is on track to go into service his quarter.

Duke Energy. In the investor call following Q2 earnings, DUK will have an opportunity to update investors on the financial impact of the ACP abandonment decision; highlighting the potential for higher spending at the Piedmont subsidiary to source replacement capacity. Also, we expect a regulatory update, both on the recent GRC decision in Indiana and the ongoing GRC in North Carolina. With an number of parties signing on to settlements that stipulate an ROE and equity layer in North Carolina, we see most contentious element of this case being the potential to earn a return on the deferred balance of coal ash remediation expenses. Should the PSC ultimately decide not to allow a return on that balance, we estimate ongoing EPS will be impacted by $0.10/share.

Evergy Inc. The Strategic Operations Committee recommendations to the Board are due July 30 and the Board decision August 17 so the timing will be interesting. We expect EVRG to continue delivering cost cuts at the higher end of the 6-9% reduction range.

PG&E Corp. With the company's first quarterly call out of bankruptcy we look for a calendar update and additional financial guidance. We also expect a discussion on preparations for fire season which has so far started without much impact.

Pinnacle West Capital. We expect an update on the general rate case following Staff testimony August 3 and the results of the August 4 primary as 3 seats on the Arizona Corporation Commission are up this year (Chairman Burns who is term-limited, Commissioner Dunn who is not running and Commissioner Marquez-Peterson).

Public Service Enterprise Group. We expect PEG to provide updates on cost cutting efforts embedded in their reiteration of annual guidance on the 1Q 2020 conference call and the COVID-19 impacts on volumes seen in 2Q 2020. We believe investors will be focused on management's updates around the energy efficiency spending program in New Jersey, and any prospects for settlement on the Transmission ROE at FERC.

Sempra Energy. We expect Sempra to report $1.65/share for 2Q 2020, well ahead of consensus estimates of $1.19. We also expect management to reiterate the 2020 eps guidance range of $7.20 - $7.80, which was recently increased from $6.70-$7.50 after closing the sales of the South American businesses. On the call management could also update 2021 guidance. Current 2021 guidance (on a GAAP basis) was provided during the March 2020 Analyst Day at $7.50-$8.10 commensurate with the original Adjusted EPS guidance for 2020 of $6.70-$7.50. Other items of interest will be an update on COVID impacts, particularly at IEnova, and the status of the last remaining permit for ECA LNG Phase 1.

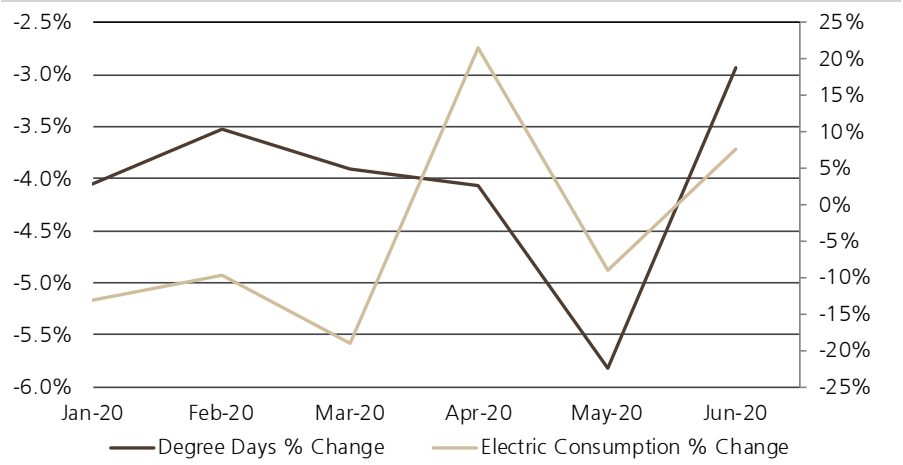
Southern Company. We expect the market to be focused on an update on the Vogtle new nuclear construction project for schedule and budget and any COVID-19 impacts to productivity.

Weather

Weather was positive in 2Q'20 as degree days rose 9% above normal and 12% above Q2'19. Weather was most favorable in the Midwest and Northeast versus Q2'19 and all regions experienced an increase in degree days.

From an electric consumption standpoint electric sales declined 4.1% in April, 5.8% in May and 2.9% in June versus 2019 including weather. We believe this was in line or better than expectations in company guidance.

Figure 5: 2Q Change in Weather versus Electric Consumption



Source: NOAA, EIA, UBS

Figure 6: Q2'20 Weather and Sales Comparisons

		Retail Sales Growth YoY										
		YTD			Deg Days vs '19		2Q'20		Deg Days vs Normal		2Q'20	
State	Decoupled?	April	April	March	May	June	VS. 2Q'19	Rank	May	June	VS. 2Q'19	Rank
Connecticut	Yes	-6.0%	-7.0%	-9.6%	12.2%	17.6%	21.1%	16	17.6%	52.2%	18.7%	2
Maine	No	-7.1%	-3.7%	-9.0%	-13.8%	10.3%	-2.3%	42	4.6%	5.3%	4.6%	42
Massachusetts	Yes	-3.5%	-5.4%	-6.0%	2.7%	71.0%	24.2%	11	7.0%	36.6%	12.9%	19
New Hampshire	No	-4.7%	-3.1%	-3.5%	-3.2%	45.9%	9.9%	27	10.1%	33.8%	10.6%	27
Rhode Island	Yes	-7.6%	-1.1%	-3.2%	0.7%	8.8%	16.1%	19	9.4%	50.0%	14.7%	14
Vermont	Yes	-4.7%	-7.6%	-4.0%	7.6%	27.0%	13.8%	21	21.2%	59.0%	18.5%	4
New Jersey	No	-5.6%	-3.8%	-8.8%	44.8%	19.6%	41.5%	2	16.7%	29.7%	15.6%	11
New York	Yes	-4.1%	-3.6%	-4.5%	22.5%	60.3%	28.7%	7	12.5%	27.6%	12.6%	21
Pennsylvania	No	-7.3%	-5.4%	-12.4%	50.0%	7.9%	36.8%	3	19.0%	23.5%	13.0%	18
Illinois	Yes	-5.0%	-7.1%	-7.8%	19.0%	37.2%	21.0%	18	5.6%	23.5%	10.2%	30
Indiana	Yes	-6.1%	-12.8%	-7.4%	23.1%	21.0%	23.5%	13	8.5%	15.5%	11.3%	26
Michigan	No	-6.8%	-15.9%	-8.3%	27.2%	43.4%	21.7%	15	15.3%	-3.3%	10.3%	28
Ohio	Partial	-5.1%	-6.1%	-9.6%	47.7%	13.4%	34.6%	4	16.0%	21.2%	13.6%	17
Wisconsin	No	-4.0%	-7.0%	-4.8%	1.4%	15.3%	7.5%	30	9.7%	-1.1%	6.5%	35
Iowa	No	-2.3%	-2.8%	-6.8%	-3.7%	14.9%	8.9%	28	9.8%	21.6%	12.9%	20
Kansas	No	-5.8%	-6.8%	-7.3%	-3.0%	42.9%	22.9%	14	0.5%	30.0%	14.2%	15
Minnesota	Yes	-3.9%	-7.3%	-6.2%	-13.7%	11.6%	0.6%	37	5.6%	-6.2%	6.7%	34
Missouri	No	-5.4%	-4.6%	-8.2%	2.2%	27.3%	23.7%	12	1.7%	17.7%	12.5%	23
Nebraska	No	-2.5%	-2.6%	-5.3%	-13.3%	32.4%	13.5%	23	9.1%	32.4%	16.3%	8
North Dakota	No	2.6%	5.7%	2.7%	-12.6%	4.4%	3.9%	34	14.7%	-2.7%	12.1%	24
South Dakota	No	-3.9%	-4.3%	-7.0%	-16.5%	14.7%	2.2%	35	6.8%	7.1%	9.2%	31
Delaware	Yes	-5.1%	-0.3%	-7.8%	19.7%	3.3%	29.8%	6	38.6%	32.6%	19.2%	1
District of Columbia	Yes	-7.9%	-8.0%	-16.8%	-9.3%	5.5%	14.5%	20	24.4%	18.1%	13.8%	16
Florida	No	1.4%	3.4%	3.3%	-16.0%	-6.2%	-3.8%	43	4.2%	7.8%	16.6%	7
Georgia	No	-3.0%	-8.5%	-2.6%	-23.0%	-3.7%	-10.2%	47	19.0%	4.0%	6.3%	36
Maryland	No	-7.7%	-1.9%	-13.1%	22.6%	-3.8%	31.6%	5	24.5%	19.4%	15.3%	13
North Carolina	Yes	-3.4%	-8.1%	-4.7%	-10.8%	3.0%	1.8%	36	41.4%	11.5%	18.3%	5
South Carolina	No	-2.9%	-10.4%	-0.2%	-26.3%	-0.8%	-12.2%	50	22.9%	4.1%	10.2%	29
Virginia	No	-5.9%	-1.5%	-6.1%	12.0%	6.0%	26.5%	9	37.9%	20.1%	17.7%	6
West Virginia	No	-4.6%	0.1%	-10.6%	61.2%	3.7%	46.2%	1	30.6%	4.9%	16.0%	9
Alabama	No	-3.1%	-8.5%	-2.7%	-20.4%	-6.5%	-10.5%	48	16.5%	7.5%	6.0%	37
Kentucky	No	-4.7%	-7.1%	-7.7%	15.2%	0.8%	26.7%	8	19.3%	4.1%	12.1%	25
Mississippi	No	-1.7%	-2.9%	0.5%	-15.6%	-1.7%	-7.8%	45	16.9%	4.1%	5.3%	40
Tennessee	No	-4.0%	-6.6%	-3.4%	4.0%	3.7%	13.7%	22	28.6%	4.0%	15.5%	12
Arkansas	No	-3.9%	-5.9%	-5.4%	-19.9%	6.0%	0.1%	38	-2.0%	3.8%	4.7%	41
Louisiana	No	-0.5%	1.2%	1.1%	-16.4%	-7.4%	-8.5%	46	3.8%	-1.6%	6.0%	38
Oklahoma	No	-3.1%	-5.1%	-1.6%	-6.1%	22.1%	21.1%	17	0.5%	14.1%	15.9%	10
Texas	Partial	1.0%	3.1%	3.0%	0.0%	3.5%	4.1%	33	14.3%	5.5%	12.6%	21
Arizona	No	-1.5%	-1.1%	-3.4%	100.0%	-1.0%	25.8%	10	5.7%	-7.7%	-4.5%	46
Colorado	No	-0.3%	-4.0%	-1.8%	-39.9%	-10.9%	-10.8%	49	-24.1%	-18.9%	-11.8%	47
Idaho	Yes	0.1%	2.6%	-3.2%	4.9%	23.5%	10.6%	26	3.4%	8.5%	5.5%	39
Montana	No	-4.3%	3.4%	-8.8%	-7.8%	17.3%	7.7%	29	3.7%	-0.4%	8.1%	33
Nevada	Yes	0.6%	-6.8%	2.1%	-0.5%	-13.3%	12.2%	24	-35.4%	-24.8%	-20.0%	49
New Mexico	No	2.5%	-4.0%	3.9%	-32.1%	12.8%	-1.7%	39	-32.1%	-8.6%	-16.4%	48
Utah	No	-0.3%	-4.3%	1.6%	-27.3%	24.6%	-2.1%	41	-11.3%	-3.6%	-3.1%	45
Wyoming	No	-4.8%	-11.0%	-6.5%	-26.7%	-21.9%	-6.4%	44	-4.8%	-27.0%	-1.0%	44
California	Yes	-3.5%	-4.4%	-2.3%	-37.8%	6.6%	5.7%	32	-41.2%	-29.1%	-21.5%	50
Oregon	Partial	-2.1%	-2.0%	-0.7%	14.2%	14.3%	6.0%	31	9.0%	29.0%	8.8%	32
Washington	Yes	-4.2%	-3.2%	-6.1%	21.5%	18.5%	11.4%	25	-3.5%	15.3%	2.7%	43
Hawaii	No	-0.3%	-13.7%	4.3%	-3.1%	-2.0%	-2.0%	40	20.4%	17.0%	18.6%	3

Source: EIA, NOAA, UBS

Electric Utilities

AES Corp

We estimate Q2'20 EPS of $0.21 versus $0.26 last year. We assume a -$0.04/share impact from COVID globally of the $0.06-$0.07/share the company identified on the Q1 call. We do not see a material impact from sensitivities. A knowable driver is the absence of the Ohio rider which we estimate is -$0.01/share. We look forward to an update on where AES stands with S&P, renewable PPA origination and the company's progress to reduce coal generation to 30% of total by year-end.

Alliant Energy

We estimate an increase in LNT's EPS to $0.57 versus $0.40 last year. We estimate a strong comparison due to rate relief at IP&L and WP&L (+$0.16/share) and the first half of 2020 tax timing from wind production credits. We estimate this added $0.06/share in Q2'20 versus the $0.08/share in Q1'20. We estimate a small net negative impact from the combination of weather normalized sales and cost cuts. We expect LNT to discuss progress on the Wisconsin rate freeze proposal and solar filing.

Figure 7: LNT Q2'20 EPS Drivers

Q2'19	$0.40
Weather to Normal	$0.02
Weather Below Normal	$0.01
IP&L & WP&L Rates	$0.16
Tax timing - PTCs	$0.06
O&M	$0.03
Interest Expense	-$0.01
Dilution	-$0.02
Depreciation/other	-$0.03
Weather Normalized Demand	-$0.05
Q2'20 Estimate	$0.57

Source: Company reports, FactSet, UBS Equity Research

Ameren Corp

We forecast EPS for AEE of $0.85 versus $0.72 last year. Weather likely helped offset the impact of lower demand. Ameren assumes a -$0.10/share impact from lower Ameren Missouri sales in 2020 (-7%: +2.5% Residential, -15% Commercial and -10% Industrial). The absence of a Callaway outage likely added $0.08/share. We estimate a mark-to-market of the Illinois formula distribution ROE is a -$0.03/share impact versus 2019.

Figure 8: AEE Q2'20 EPS Drivers

Q2'19	$0.72
Weather to Normal	$0.06
Weather versus Normal	$0.05
Callaway Outage	$0.08
Missouri Rates	$0.02
IL Rate base Growth	$0.01
Interest Expense	-$0.01
IL Electric Distribution ROE (7.3% vs. 8.8%)	-$0.03
Demand	-$0.05
Q2'20 Estimate	$0.85

Source: Company reports, FactSet, UBS Equity Research

American Electric Power

We forecast AEP EPS of $1.08 versus $1.00 last year. The absence of a transmission true-up at AEP Transco is a -$0.08/share impact absent a similar development. At the 2019 EEI conference AEP identified $0.19/share of cost cuts at the Vertically Integrated Utilities and $0.14/share at the T&D Utilities which will help offset a demand reduction. Overall we expect T&D utility rates will be slightly higher net of the absence of the legacy rider in Ohio.

Figure 9: AEP Q2'20 Earnings Drivers by Segment

Q2'19	$1.00
Vertically Integrated ($0.50 v. $0.38)	
Weather to Normal	$0.01
Weather vs Normal	$0.02
Operations and Maintenance	$0.07
Transmission	$0.05
Rates	$0.03
Other	-$0.01
Load	-$0.02
Depreciation	-$0.03
T&D Utilities ($0.31 v. $0.27)	
Transmission	$0.04
Operations and Maintenance	$0.03
Rates	$0.02
Depreciation	-$0.02
Tax Carrying Charge	-$0.03
AEP Transmission ($0.25 v. $0.31)	-$0.06
Generation & Marketing ($0.07 v. $0.06)	$0.01
Corp and Other (-$0.05 v. -$0.02)	-$0.03
Q2'20 Estimate	$1.08

Source: Company reports, FactSet, UBS Equity Research

ATCO Ltd

We expect ATCO Ltd to report 2Q 2020 adjusted eps of C$0.55 vs. C$0.55 consensus estimates and C$0.68 last year. The largest negative drivers in the quarter are the asset divestitures of the Alberta Power Line and the Canadian competitive generation assets. Further, we expect lower earnings contributions from Neltume Ports on economically driven lower trade volumes, slightly higher corporate expenses, and lower earnings year on year at the Australian gas distribution utility on lower ROE and flat CPI adjustor. Partially offsetting these negative drivers will be higher earnings at the Structures business driven by LNG Canada completing the manufacturing phase and rate base growth at the electric distribution and Canadian gas utilities.

Figure 10: ATCO Ltd. 2Q 2020 Drivers

2Q 2019 EPS	**$ 0.68**
2Q 2019 Cons. Adj. Earnings	78
Naltume Ports	(2)
Corporate Drag	(2)
Canadian Utilities	(3)
S&L	4
Sale of Power & Alberta Power Line	(8)
Australia lower RB growh/ROE/CPI	(4)
2Q 2020 Cons. Adj. Earnings	**63**
Shares	114.3
2Q 2020 EPS	**$ 0.55**

Source: UBS Equity Research Estimates

Canadian Utilities

We expect Canadian Utilities to report 2Q 2020 adjusted eps of C$0.35 vs. consensus estimates of C$0.35 and C$0.38 last year. Results will be driven by the sale of the Alberta Power Line and the Canadian generation assets, higher corporate expenses year on year, and lower earnings at the Australian gas utility business on lower rate base growth, lower allowed ROE, and a lower CPI adjustor year on year. This will be mostly offset by rate base growth at the electric distribution and Canadian gas utilities.

Caribbean Utilities

We expect Caribbean Utilities to report 2Q 2020 eps of $0.19 vs. consensus estimates of $0.18, and $0.24 last year. The biggest driver of year on year results will be lower electric volumes due to a significant decline in by air and by sea tourism visits to Grand Cayman. This will be partially offset by lower O&M as a result of lower volumes as well as cost discipline.

CMS Energy

We expect an increase for CMS' EPS to $0.48 versus $0.33 last year. Weather and cost cuts likely helped offset the impact of lower demand due to COVID. NOAA data shows a 24% increase in degree days from last year and 11% above normal. Michigan manufacturing returned in May and retail in June at or ahead of the company's plan. MISO load was -15% in April and gradually recovered to flat in July including weather. Cost cuts included the company's CE Way, employee benefits and COVID-related impacts like mileage reimbursement.

Figure 11: CMS Q2 EPS Drivers

Q2'19	$0.33
Weather to Normal	$0.06
Weather	$0.10
O&M reinvestment	$0.06
Gas Rates	$0.06
Pension	$0.02
Enterprises and Enerbank	$0.01
Debt and Dilution	-$0.02
Demand	-$0.07
Depreciation, Interest and Other	-$0.07
Q2'20 Estimate	$0.48

Source: Company reports, FactSet, UBS Equity Research

Consolidated Edison

We forecast ED EPS of $0.52 versus $0.58 last year. We do not expect ED to move off its 2020 EPS guidance reduction of $0.15/share to $4.15-$4.35. We assume lower results at Consolidated Edison Company of New York ($0.41 versus $0.46) which is decoupled but the lower EPS reflects the costs of doing work with social distancing which raised costs. CECONY and other New York investor owned utilities filed comments with the New York Public Service Commission to: 1) Allow for deferral of net costs of COVID-19; 2) Establish mechanisms to mitigate cash flow stress like riders and 3) Declare COVID-19 a pandemic crisis that justifies excusing a utility from meeting a rate plan performance metric.

Dominion Energy

We expect Dominion Energy to report adjusted 2Q EPS of $0.78/share; this is modestly below the mid-point of the original guidance for the quarter of $0.75-$0.85/share and includes earnings from both the company's midstream and ACP assets. We expect that in conjunction with its Q3 earnings release (later in the year), Dominion will restate earnings from the first and second quarter to reflect the discontinued nature of those midstream and pipeline operations, consistent with its restated guidance for 2020 of $3.37-$3.63 and 2021 of $3.85-$3.90.

Year/Year second quarter earnings will benefit from continued investment in Dominions regulated business lines, higher capacity revenues in PJM, lower depreciation expense due to the early retirement of coal plants and life extension of nuclear plants, and very modestly lower interest expenses. These benefits will be offset by lower earnings from Cove Point, lower capacity earnings at the Millstone nuclear plant and equity dilution. Our earnings forecast assumes that any negative impact from the Covid-19 economic slowdown will be offset by lower O&M expenses, and that below normal weather in the quarter will have a negative earnings impact..

We expect Dominion's second quarter investor call will focus on the future goals of the company; its increasing focus on regulated earnings, an improving balance sheet, renewable generation development and zero carbon and methane emissions by 2050. In this context we expect the refreshed EPS and dividend growth target of 6.5% and 6% respectively, to be reiterated.

Figure 12: Dominion Energy Q2'20 EPS Drivers

Q2'19	$0.75
Weather - Weaker vs. normal	-$0.02
Regulated Investment Growth	$0.07
Capacity - New Gen	$0.04
Nuclear & Asset life Extension	$0.02
Interest Expense	$0.00
Cove Point - Lower Ownership	-$0.03
Millstone - Lower capacity revenues	-$0.01
Equity Dilution	-$0.04
Covid-19 - Demand Shift/O&M Savings	$0.00
Q2'20 Estimate	$0.78

Source: UBS Equity Research, Company Reports, FactSet

DTE Energy

We forecast lower EPS of $1.51 versus $0.99. Overall, DTE seems on track for the year. We expect favourable weather versus last year (+$0.05/share) and normal (+$0.16/share) benefitted the second quarter result. The company likely saw a higher mix of residential sales which provides for a greater impact from a rise in degree days. DTE Electric recovered the impacts of 2 rate cases. Share based incentive comp was a -$0.18/share impact in Q1 due to a lower stock price but recovered in Q2. DTE is progressing with the LEAP expansion to the Blue Union expansion which they expect to complete in Q3. Lower demand from DTE Electric from waste coal REF sales could impact the Power & Industrials business.

Figure 13: DTE Q2'20 EPS Drivers

Q2'19	$0.99
DTE Electric weather	$0.18
DTE Electric sales	-$0.17
DTE Electric rate case recovery	$0.20
DTE Electric Share based incentive comp	$0.11
DTE Electric O&M	$0.08
DTE Gas weather	$0.03
DTE Gas rate base	$0.03
GS&P - similar to 1Q'20	$0.12
Power & Industrials - lower utility waste coal to DTE Electric	-$0.01
DTE Energy Trading	$0.02
Corp & Other	$0.01
Dilution (192M versus 182M)	-$0.08
Q2'20 Estimate	$1.51

Source: Company reports, FactSet, UBS Equity Research

Duke Energy

We expect Duke Energy to report adjusted 2Q'20 EPS of $1.00 vs. a weather adjusted Q2'19 result of $1.04. The most significant variable (and source of uncertainty) in Q2'20 earnings will be the impact of the Covid-19 related economic shutdown and the related O&M savings the company can realize as an offset. Our estimate assumes a negative EPS impact of $0.19 (reflects residential demand +5%, commercial demand -15%, industrial demand -20%) offset by O&M savings of $0.12. Beyond the impact of lower demand in the quarter, higher rates, investment in renewables and the gas LDC business will be offset by higher depreciation, interest and equity dilution.

We expect DUK's investor call will focus on the company's regulatory calendar (Indiana & North Carolina), potential need for additional capital spending at its gas LDC (following the cancelation of ACP) and the potential outcome of the Governors upcoming clean energy plan.

Figure 14: Duke Energy Q2'20 EPS Summary

Q2'19	$1.04
Weather impact	$0.01
Demand Impact of Covid-19 Shut down	-$0.19
O&M Savings to Offset Covid-19 Impact	$0.12
FL/NC/SC rates & riders	$0.05
Gas LDC & Pipeline (net)	$0.01
Wholesale Contracts & Renewables	$0.02
Depreciation & Interest Expense	-$0.05
Equity Dilution	-$0.01
Q2'20 Estimate	$1.00

Source: UBS Equity Research, Company Reports, FactSet

Edison International

We forecast EPS of $1.16 versus $1.58 last year. Our EIX jurisdictional revenue impact includes the absence of a $0.20/share benefit from a revenue true-up from the rate case along with an attrition year impact. EIX also likely experienced higher costs related to insurance and its wildfire plan and we do not expect a similar year-on-year impact to O&M (-$0.30/share) as we are looking for in this quarter.

Figure 15: Edison International Q2'20 EPS Summary

Q2'19	$1.58
California Jurisdictional Revenue	$0.06
FERC Transmission Revenue	$0.04
Depreciation	-$0.02
Financing	-$0.03
O&M	-$0.30
Corporate Expenses	-$0.01
Dilution (378M vs. 331M avg shrs)	-$0.16
Q2'20 Estimate	$1.16

Source: Company reports, FactSet, UBS Equity Research

Emera Inc

We expect Emera Inc. to report 2Q 2020 adjusted eps of C$0.52 vs. C$0.58 consensus estimates and C$0.54 last year. Normalizing the C$0.54 in 2Q 2019 for the Emera Maine asset sale yields C$0.49. Drivers off of this normalized level last year will by rate base growth in Florida, slightly better results in Nova Scotia, and positive impacts from FX due to a stronger USD/CAD year over year. Mostly offsetting these positive drivers will be lower results at Emera Energy due to lower natural gas price volatility, the $12mln one time regulatory decision impact at New Mexico Gas in 2Q 2019, and slightly higher corporate expenses and share dilution.

Figure 16: Emera Inc. 2Q 2020 Drivers

2Q 2019	**$**	**0.54**
Maine Asset Sale	$	(0.05)
2Q'19 Normalized	**$**	**0.49**
FL Electric	$	0.03
Emera Energy	$	(0.02)
Gas Utes & Infra	$	0.04
Canadian	$	0.01
One-Time NM Reg. Dec.	$	(0.04)
FX	$	0.03
Other/Parent	$	(0.02)
4Q 2019	**$**	**0.52**

Source: UBS Equity Research Estimates

Entergy Corp

We expect Entergy Corp. to report adjusted 2Q'20 EPS of $1.30 vs. a weather adjusted Q2'19 result of $1.29. Second quarter earnings will benefit from a step up in regulated earning related the company's formulaic rate plans and tracking mechanisms, offset by higher depreciation, interest and tax expense and equity

dilution. We estimate that slowdown associated with the Covid-19 pandemic could impact earnings by up to $0.15 in the quarter (retail +4%, commercial -15%, industrial -10%) but that some portion of that will be offset by O&M cost reductions (we assume $0.11).

We expect ETR will affirm its 2020 full year earnings guidance of $5.45-$5.75, its EPS CAGR through '22 of 5-7% and its plans for a fall investor day when it will expand the current three year forward look that includes both EPS and capital spending plans to a five year look forward.

Figure 17: Entergy Q2'20 EPS Summary

ETR - Earnings Walk Q2'19-Q2'20				Q2'19
EPS as reported Q2'19				$1.35
Adjustments (weather benefit)				($0.06)
Q2'19 Operating EPS				$1.29
	Annual Impact (mm)	After Tax Q2 (mm)	Per Share	
E - LA Saint Charles SCPS	$110.0	$13.75	$0.07	
E - MS FRP ($33/$18 net of D&A)	$18.0	$3.38	$0.02	
E - LA FRP	$25.0	$4.69	$0.02	
E - MS Chowtaw	$59.0	$11.06	$0.06	
E - NO Rate Case	(15.00)	(2.81)	(0.01)	
E - AR FRP	$57.0	$10.69	$0.05	
AMI Annual Rider	$20.0	$3.75	$0.02	
E - TX TCRF	$17.0	$2.13	$0.01	
E-LA Lake Charles Power Station	$108.0	$13.50	$0.07	
E-MS FRP	$23.8	$2.98	$0.01	$0.31
	Annual Impact			
Annual Guidance from ETR:	(EPS)		Qtrly Impact	
Regulated Utility:				
O&M	$0.05		($0.01)	
Nuclear Refuel Expense	$0.05		$0.02	
Depreciation Expense	($0.70)		($0.18)	
Net Interest Expense (wgted in 2H)	($0.40)		($0.08)	
Effective Income Tax	($0.15)		($0.05)	
Share Count	($0.14)		($0.04)	($0.33)
Parent & Other:				
Effective Tax Rate	$0.07		$0.02	
Share Count	$0.03		$0.01	$0.03
Covid-19 Related Damand Loss			($0.15)	
O&M Savings			$0.11	($0.04)
Projected Weather Benefit				$0.04
Q2 2020 EPS Estimate				$1.30

Source: UBS Equity Research, Company Reports, FactSet

Eversource Energy

We expect Eversource Energy to report 2Q'20 EPS of $0.75 vs $0.70 in the prior year quarter (adjusted for a $0.04 gain on landfill gas investments). Q2'20 EPS will benefit from continuing investment in the regulated utility business, the transmission system and the gas LDC business (through pipeline replacement). Higher depreciation, property tax and interest will be a modest drag on earnings for the quarter. We expect ES will reiterate its full year earnings guidance $3.60-$3.70, EPS growth rate of 5-7% and capital spending plans.

On the investor call following the earnings release we expect ES to update investors on ongoing regulatory proceedings including its New Hampshire general rate case, the approval of its Columbia Gas acquisition and the RFP process addressing grid modernization in Connecticut.

Figure 18: Eversource Energy Q2'20 EPS Drivers

Q2'19	$0.70
Regulatory actions (Nstar/CL&P/PSNH)	$0.06
Transmission investment	$0.03
Gas pipe trackers	$0.01
O&M/Depreciation/Tax	-$0.02
Weather (NH)	$0.01
Equity Dilution	-$0.04
Q1'20 Estimate	$0.75

Source: UBS Equity Research, Company Reports, FactSet

Evergy Inc.

We forecast EPS of $0.63 versus $0.57 last year excluding the impact of income from corporate owned life insurance. Above normal weather and cost cuts will offset the impact of lower weather normalized sales. EVRG's guidance for O&M cuts is 6-9% from $1.187B and we assume the higher end of the range. On the financing side we see an impact from the issuance of $1.6B of parent debt.

Figure 19: EVRG Q2'20 EPS Drivers

Q2'19 Estimate	$0.57
Weather to Normal	$0.04
Weather	$0.04
Weather Normal Sales	-$0.08
O&M	$0.09
KCP&L refinancing and term loan	$0.01
Other	-$0.01
Depreciation	-$0.02
Interest on $1.6B parent debt	-$0.02
Share buyback	$0.01
Q2'20 Estimate	$0.63

Source: NOAA, Company reports, FactSet, UBS Equity Research

Exelon Corp

We expect Exelon to report 2Q 2020 adjusted EPS of $0.45 vs. $0.45 consensus and $0.60 last year. Drivers at ExGen are expected to be poorer market and portfolio conditions, volume degradation from COVID-19 dislocations particularly at the Constellation C&I retail segment, higher nuclear refueling outages year on year, and lower capacity prices for two of the three months of the quarter. These negative drivers will be partially offset by incrementally higher ZEC revenues and lower O&M. At the utilities we expect a drag from the distribution ROE formula in Illinois and volumes at PECO, which will be more than offset collectively by weather at PECO, distribution investment at ComEd, the distribution rate increase at BGE and rate increases at PHI.

Figure 20: Exelon 2Q 2020 Drivers

2Q 2019	**$**	**0.60**
ExGen		
Lower O&M	$	0.06
NDT Fund Losses	$	(0.02)
ZEC Revenues	$	0.02
Market & Portfolio Conditions	$	(0.10)
Nuclear Outages	$	(0.02)
Capacity Revenue	$	(0.11)
ComEd		
Distribution Formula Rate Timing	$	(0.02)
Distribtution Investment	$	0.02
PECO		
Volumes/Weather	$	(0.03)
BGE		
Distribution Rate Increases	$	0.03
PHI		
Rate Increases	$	0.02
Corporate		
Other	$	0.01
1Q 2020	**$**	**0.45**

Source: UBS Equity Research Estimates

FirstEnergy Corp.

We forecast $0.53 of EPS versus $0.61 last year. FE previously provided a guidance range of $0.48-$0.58/share. We do not expect weather had a significant impact across FE's service territory and the final quarter of the expiration of the Ohio distribution modernization rider is -$0.06/share. We estimate that other riders contributed from Ohio and Pennsylvania $0.02/share. The company incurred interest expense for the Energy Harbor payment but is now a fully regulated utility.

Figure 21: FE Q2'20 EPS

Q2'19	$0.61
Normal Weather	$0.01
Weather Normalized Distribution Deliveries	-$0.02
Ohio Distribution Modernization Rider	-$0.06
Other Rider Recovery	$0.02
O&M Reduction	$0.01
Other Financing	-$0.01
Depreciation	-$0.01
General Taxes	-$0.01
Transmission Growth	$0.02
Transmission O&M	-$0.01
Parent and Transmisison Financing	-$0.02
Q2'20 Estimate	$0.53

Source: Company reports, FactSet, UBS Equity Research

Fortis Inc.

We expect Fortis Inc. to report 2Q 2020 adjusted eps of C$0.57 vs. C$0.58 consensus estimates and C$0.54 last year. Drivers year on year will be rate base growth at the western Canadian utilities, rate base growth at ITC, rate design timing and rate base growth at Central Hudson and slightly better results at energy infrastructure with better rainfall in Belize and slightly better margins at Aitken Creek storage. Offsetting these positive drivers are higher weighted average shares from the C$1.2Bln equity issuance completed in late 2019, and slightly lower results at UNS. Results at UNS will be driven by higher costs year on year on yet in rate base given the ongoing rate case in Arizona, and lower volumes related to coronavirus dislocations. These negative drivers are mostly offset by warmer weather and the partial reversal of the pension loss recorded in 1Q 2020.

Figure 22: Fortis Inc. 2Q 2020 Drivers

2Q 2019	**$**	**0.54**
Western CA Elec & Gas	$	0.03
US Transmission - ITC	$	0.03
Central Hudson	$	0.02
Energy Infrastructure	$	0.02
Corp & Other	$	-
UNS Energy	$	(0.01)
Wtd. Avg. Shares	$	(0.06)
2Q 2020	**$**	**0.57**

Source: UBS Equity Research Estimates

Hawaiian Electric

We expect HE to report adjusted 2Q'20 EPS of $0.40 vs. $0.39 in the prior year quarter. Earnings in the quarter will be driven by the regulated utility, with growth through the tracking and recovery mechanisms and O&M efficiency, offset only

modestly by higher depreciation expense. We expect HE's American Savings Bank subsidiary will report lower earnings than in the prior quarter ($0.10 vs. 0.14) due to the challenged economic environment in the state of Hawaii (closed to tourists till September). American Savings bank will report earnings on the evening of July 30.

We expect HE will reiterate its full year utility earning guidance of $1.46-$1.54, but will not reinstate earnings guidance for American Savings Bank given the continued economic uncertainty in the state. Further, we expect an update on the ongoing regulatory proceedings (PBR), cost saving initiatives and capital spending plans.

Figure 23: Hawaiian Electric Q2'20 earnings summary

Q2'19 - Utility	$0.30
Regulatory actions (RAM/MPIR etc.)	$0.06
O&M efficiency	$0.01
Depreciation	-$0.01
Q2'20 Estimate	$0.36
Earnings Composition	
Utility	$0.36
Bank	$0.10
Hold Co. & Other	-$0.06
Q2'20 Estimate	$0.40

Source: UBS Equity Research, Company Reports, FactSet

Hydro One

We expect Hydro One to report 2Q 2020 adjusted eps of C$0.32 vs. C$0.27 consensus and C$0.26 last year. Results will be mainly driven by strong weather in May and June driving peak demand load higher which impacts transmission segment earnings. OM&A expenses are also likely to be lower given higher vegetation management and storm cost expenses in 2Q 2019 as well as stand down of work crews in part of April 2020. Some of those lower cost drivers will be partially offset by higher COVID-19 related mitigation costs. Revenues will also be up year on year related to the transmission rate order from the Ontario Energy Board, and the one-time regulatory dispositions and catch up items to be booked this quarter as a result.

Figure 24: Hydro One Estimates and Actual Results 2Q 2020 vs. 2Q 2019

C$mlns	2Q 2019A	2Q 2020E
Revenue Net of Purch. Power	760	814
OM&A Costs	267	259
D&A	221	221
Finance Charges	117	119
Income Taxes	(6)	15
Other/NonCont/Pref. Divs	6	7
Net Income to Common	155	193
Shares Outstanding	595	595
Reported EPS	$ 0.26	$ 0.32
Items	-	-
Adj. NI	155	193
Shares Outstanding	595	595
Adjusted EPS	**$ 0.26**	**$ 0.32**

Source: UBS Equity Research Estimates

NextEra Energy

We expect NextEra Energy to report 2Q 2020 adjusted eps of $2.49 vs. $2.49 consensus and $2.35 last year. Given the move of transmission from the corporate segment to the Energy Resource segment the comparable segment break-out for 2Q 2020 is $0.97 at Energy Resources and $0.01 at Corporate & Other. Drivers in the quarter will be rate base investments at FPL and at Gulf Power. From a retail sales perspective vs. the prior two year average was +5.4% in April and (2.4%) in May as coronavirus dislocations on volumes were not as large as expected and significantly warmer weather (particularly in April) offset some of the negative volume impacts. At the end of last quarter FPL had a reserve balance of $744mln. At Energy Resources the drivers will be new investment and better results at existing resources given the 92/93% wind resource in 2Q 2019. Offsetting these positive impacts will be a drag from customer supply and trading and an outage at Seabrook. At Gulf we expect largely flat year on year results and at Corporate & Other we expect increased interest expense given debt issuance at the parent of $1.25Bln in April at 2.75%, and $2Bln in May at 2.25%. There will also be some share dilution year on year given equity unit share issuances in September 2019 and February 2020.

OGE Energy

We forecast EPS of $0.50 versus $0.50 last year. From a GAAP basis OGE's remaining 2020 results will include an offsetting $0.26/share consolidating tax adjustment benefit for the remainder of the year related to the Enable write-down. We do not include that in our EPS estimates. Below normal weather and lower demand likely kept results similar to Q2'19. Rate case recovery and cost cuts likely helped OGE.

Figure 25: OGE Q2'20 EPS Summary

Q2'19	$0.50
Weather to Normal	$0.07
Weather	-$0.03
Rates	$0.09
O&M	$0.02
Interest Expense	-$0.01
Depreciation	-$0.05
Sales	-$0.08
ENBL	-$0.01
Q2'20 Estimate	$0.50

Source: Company reports, FactSet, UBS Equity Research

PG&E Corp.

We estimate Q2'20 EPS forecast of $0.84 versus $1.10 last year. The company will report earnings and should provide 1 or more years of annual EPS and potentially net income guidance. We estimate 695M shares outstanding using an average method and reflecting 2 trading days post close of the block equity (97% at 647M and the remaining 3% at the 2153M maximum) versus 529M last year. Other drivers are rate base (+$0.02/share and energy efficiency (+$0.01/share) as positives. We estimate negative drivers of unrecoverable interest and legacy O&M.

Figure 26: PCG Q2'20 EPS Summary

Q2'19	$1.10
Rate base Growth	$0.02
Energy Efficiency	$0.01
Timing of Taxes	-$0.01
Unrecoverable interest/other	-$0.02
Shares outstanding (695M vs. 529M)	-$0.26
Q2'20 Estimate	$0.84

Source: Company reports, FactSet, UBS Equity Research

Pinnacle West Capital

We forecast $1.55 of EPS versus $1.28 last year. Weather which impacted residential demand and cost cuts led the quarter. The impact of May weather (194 versus 107 degree days) is an important driver. PNW disclosed that the impact from March 13 to May 26 was -$0.14/share versus the company's initial expectation and that a 1% change in sales is $0.16-$0.20/share on an annual basis. PNW disclosed that residential sales rose 4% and commercial and industrial sales fell 4% versus 2019 from May 13 to June 16. There was 1 fewer planned outage and we expect PNW worked to offset the impact of lower demand through cost cuts.

Figure 27: PNW Q2'20 EPS Summary

Q2'19	$1.28
Weather to Normal	$0.22
Weather versus Normal	$0.05
O&M	$0.13
Pension and Other	$0.06
Other	$0.01
Sales	$0.01
LFCR	-$0.01
Interest	-$0.01
Depreciation and Taxes	-$0.03
Demand	-$0.16
Q2'20 Estimate	$1.55

Source: Company reports, FactSet, UBS Equity Research

PNM Resources

We expect PNM Resources to report Q2'20 EPS of $0.50 vs. $0.44 in the prior year quarter. Better weather in 2Q'20 is expected to offset the negative impact of the Covid-19 related shift in demand (-$0.02 in both April & May), along with rate base growth and the absence of a San Juan maintenance outage. Interest expense, depreciation and property have a modestly negative impact on the quarter. In conjunction with the disclosure of its earnings release date (July 31), PNM affirmed its annual EPS guidance of $2.16-$2.26 (targeting the mid-point).

On its investor call we expect PNM will update investors on its ongoing proceeding in New Mexico to replace the power provided by the San Juan coal plant (decision deadline is October 1), the potential to retire the Four Corners generation station and any possible updates to the capital spending plan.

Figure 28: PNM Resources Q2'20 EPS Sumary

Q2'19	$0.44
Retail rate phase in (PNM & TNMP)	$0.05
Retail load growth (PNM & TNMP)	$0.00
Weather improvement	$0.00
O&M improvement	$0.00
Depreciation & property tax	-$0.05
Interest Expense	$0.00
San Juan Outage Costs	$0.04
Transmission/Renewables/AFUDC	$0.02
Q2'20 Estimate	$0.50

Source: UBS Equity Research, Company Reports, FactSet

Portland General Electric

We forecast $0.34 of EPS versus $0.28 last year. Weather conditions were slightly below normal in POR's region with heating degree days down 13% and cooling degree days up 11%. POR's 1-2% sales baseline would imply a $0.15/share reduction for the balance of the year. The company's guidance on non-fuel O&M

would imply a $0.10-$0.15/share reduction per quarter. Depreciation could fall in the $104-$106M range per quarter using the $410-$430M guidance and $108M in Q1'20. We also expect an impact related to the non-qualified benefit program. POR had no portfolio changes but the recovery in the markets should help reverse some of the -$0.06/share impact in 1Q'20. We expect an update on regulation in Oregon on the investor call although no resolution on the COVID-19 docket until 2022.

Figure 29: POR Q2'20 EPS Summary

Q2'19	$0.28
Weather to Normal	$0.04
Weather Normalized Demand	-$0.07
Non-Fuel Operations and Maintenance	$0.13
Employee Benefits	$0.03
Depreciation	-$0.02
PCAM to the Baseline	-$0.05
Q2'20 Estimate	$0.34

Source: Company reports, FactSet, UBS Equity Research

PPL Corporation

We expect lower EPS of $0.57 versus $0.58 last year. In general F/X hedges (86% hedged at 1.55x) and small benefits from weather in Kentucky and the U.K. helped to offset the pandemic impacts and dilution. PPL continues to benefit from returns on transmission investment Pennsylvania.

Figure 30: PPL Q2'20 EPS Summary

Q2'19	$0.58
Kentucky weather versus normal	$0.01
Weather normalzized KY sales	-$0.03
F/X 1.51x '20 vs 1.36x '19 Pound/US$	$0.03
Kentucky Rate Case	$0.02
Other Expenses	-$0.01
Transmission	$0.01
U.K. weather	$0.01
Other U.K.	-$0.02
Dilution (770M versus 730M shares)	-$0.02
Q2'20 Estimate	$0.57

Source: Company reports, FactSet, UBS Equity Research

Public Service Enterprise Group

We expect Public Service Enterprise Group to report adjusted eps of $0.59 vs. $0.62 consensus and $0.58 last year. At PSE&G we expect positive drivers of continued rate base growth, better weather year on year, lower distribution O&M, and better pension and OPEB. Partially offsetting these positive drivers are lower volumes as a result of coronavirus dislocations, and higher D&A, interest expense, and taxes. At PEG Power we expect positive drivers related to NJ ZECs for a full quarter in 2020 vs. 2019, lower O&M on cost controls, and lower D&A as a result of the extension of the Peach Bottom operating license to 80 years and the sale of

the Hudson and Mercer retired coal generation stations in January to Hilco Redevelopment Partners. Bridgeport Harbor 5 also went into service year on year increasing volumes at PEG Power all else equal. More than offsetting these positive drivers will be volume declines related to coronavirus dislocations and lower capacity prices in April and May, while price for the new capacity year took effect in June. At corporate and other we expect slightly higher taxes and slightly higher interest expense relate the $800mln in term loans in March and April.

Figure 31: PEG 2Q 2020 Drivers

PEG Consolidated	2Q 2019A	2Q 2020E
	$ 0.58	**$ 0.59**
PSE&G		
2Q 2019	**$ 0.45**	
Transmission	$ 0.06	
Weather/Load	$ (0.02)	
Gas Margin	$ 0.01	
Distribution O&M	$ 0.02	
D&A, Int.	$ (0.02)	
Pension, OPEB	$ 0.02	
Taxes & Other	$ (0.02)	
2Q 2020	**$ 0.50**	
PSEG Power		
2Q 2019	**$ 0.13**	
ZECs	$ 0.02	
Capacity Prices	$ (0.05)	
Re-Contracting Mkt	$ (0.01)	
Volume	$ (0.02)	
O&M	$ 0.06	
Int. Exp.	$ (0.01)	
Lower Gas Sendout	$ (0.01)	
1Q 2020	**$ 0.11**	
Enterprise/Corporate		
2Q 2019	**$ -**	
Int. Exp/Taxes	$ (0.02)	
2Q 2020	**$ (0.02)**	

Source: UBS Equity Research Estimates

Sempra Energy

We expect Sempra Energy to beat the quarter and report ongoing adjusted eps of $1.65 vs. $1.19 consensus and $1.10 last year. The big beat will be driven by a shift in seasonality of the utility earnings given the delayed CPUC rate order last year which will impact both SDG&E, and SoCalGas. Further SDG&E will also have rate base growth at transmission and one-time benefits of ~$60mln from the

CPUC tax memo account decision (as disclosed on page 48 in 1Q'20 10-Q). One slight offset at SDG&E will be wildfire related amortization. At SoCalGas, in addition to the impacts of the CPUC rate order we expect a one- time benefit of ~$60mln similar to SDG&E also related to the CPUC tax memo account decision. In Texas we expect year on year rate base growth driving results higher by ~$40mln, with minimal coronavirus disruption in the 2Q in Texas. For South America, the assets were divested in the quarter, however, Peru will have a one-month contribution to results and Chile will have a 3 month contribution to results, leaving overall results down ~$30mln year over year. In Mexico results will be lower given Peso appreciation vs. the USD and a drag to capex deployment and volumes related to COVID-19. We see higher results at Sempra LNG & Midstream by ~$30mln related to an additional 2 months of Cameron Train 2 in service offset by higher liquefaction project development costs. At Parent & Other we expect a reversal of the year over year pension and OPEB loss recorded in 1Q 2020 and slightly lower interest expense as Peru sale proceeds began to pay down debt in the quarter.

Southern Company

We expect Southern Company to report adjusted eps of $0.64 vs. $0.69 consensus, their $0.65 guidance and $0.80 last year. Drivers in the quarter will be coronavirus volume impacts only partially offset by O&M cost controls as those programs got started in the quarter and will have more impact in the second half of the year. The southeast also did not have the positive weather of most of the rest of the country so we expect a negative weather drag vs. the warmer than normal weather in 2Q 2019. There will also be a slight drag at Southern Power related to the divestiture of the Nacogdoches and Mankato power plants. At corporate & other we expect higher interest expense and share dilution. These negative drivers will be offset by some cost control impact on non-fuel O&M and the year on year retail revenue impacts from the Georgia rate case decisions in December 2019.

Figure 32: Southern Company 2Q 2020 Drivers

2Q 2019	$	0.80
Retail Sales	$	(0.06)
Retail Rev. Impacts	$	0.05
Weather	$	(0.08)
Wholesale Operations	$	-
Other Op. Revenues	$	-
Non-Fuel O&M	$	0.04
Int. Exp. D&A, Other	$	(0.07)
Income Taxes	$	-
SO Power	$	(0.02)
SO Company Gas	$	-
Parent & Other	$	(0.01)
Increase in Shares	$	(0.01)
2Q 2020	$	0.64

Source: UBS Equity Research Estimates

WEC Energy Group

We expect WEC to report adjusted eps of $0.67 vs. $0.67 consensus estimates and $0.74 last year. We see drivers year on year of lower volumes due to coronavirus economic disruptions and higher interest expense, D&A and lack of fuel band earnings in 2Q 2020 vs. 2Q 2019. These negative drivers will be mostly offset by efficiencies in O&M year on year, slightly better results at energy infrastructure from Coyote Ridge and the incremental 10% ownership stake in Upstream Wind, and slightly better results at ATC transmission due to the FERC ROE decision and rate base growth. Weather was also better year over year.

Xcel Energy

We expect Xcel Energy to report adjusted 2Q'20 earnings of $0.49 vs. $0.47 in the prior year quarter. Our estimate assumes load loss associated with the Covid-19 related economic shut down reduce earnings by $0.11 in the quarter, offset by $0.05 of lower O&M. This assumption is consistent the with company's 'base case' scenario which assumes a total annual EPS impact of $0.17, and we spread the offsetting projected O&M savings assumption (4-5% of prior year) over the three remaining three quarters of the year as an offset. Q2 EPS benefit from higher regulated rates and AFUDC earnings which offset higher depreciation, property tax and interest expense. We expect XEL will maintain its 5-7% EPS growth target, and 2020 EPS guidance of $2.73-$2.83.

On the investor call following the earnings release we expect XEL to provide some additional colour around its Minnesota filing to both pull forward capital spending plans and extend its current rate case stay out agreement. Hearings in this process are scheduled for July 29 to discuss the process and procedure. To date, none of the company's other jurisdictions have followed Minnesota in exploring a potential acceleration of capital spending in order to drive additional economic growth and employment.

Figure 33: Xcel Energy Q2'20 EPS Summary

Q2'19			$0.47
	Base Case Annual	Quarterly Impact	
Load Loss - 6%	($0.17)	($0.11)	
O&M Savings - 4.5% (After Tax)	$0.15	$0.05	
Est. Qtrly Impact of Covid-19 Shutdown			($0.06)
MN/ND/SD/NM revenue step-up			$0.04
Property tax up/AfUDC down			$0.04
Q2'20 Estimate			$0.49

Source: UBS Equity Research, Company Reports, FactSet

Water Utilities

American Water Works.

We expect American Water Works to report adjusted 2Q'20 EPS of $0.99 vs. $0.94 in the prior year quarter (which included both a negative $0.05 weather impact and $0.03 benefit from the sale of a legacy investment). Quarterly earnings should benefit from higher rates (achieved through regulatory proceedings and formulaic step increases), infrastructure charges and favorable spring weather.

These benefits will likely be offset by higher depreciation and interest expenses. On its investor call, we expect AWK will reiterate it 7-10% EPS CAGR guidance, capital spending plans ($8.8-$9.4 billion through '24), full year earnings guidance (GAAP $3.85-$3.95/operating $3.79-$3.89) and developments in both its regulated and market based businesses.

American States Water

We expect AWR to report adjusted 2Q'20 EPS of $0.70 vs. $0.64 in the prior year quarter (after adjusting for the retroactive impact of a CPUC decision: $0.08). Year over year earnings growth is attributable to rate base investment (second step increase in CA rates effective 1/1/20), demand growth and modestly lower depreciation expense (offset by higher administrative & general expense). In conjunction with its quarterly earnings release, we expect AWR will update investors on the impact of the Covid-19 pandemic (memorandum account), its contracted services business and regulatory schedule in California (a GRC may be filed by the time of the earnings release).

California Water

We expect CWT to report adjusted 2Q'20 EPS of $0.51 vs the prior year quarter of $0.35. Without a final general rate case decision (PD may come by the end of July), we expect there will be no year over year revenue increase. Our projected step up in earnings is derived from a reversal of the Q1 charges associated with the loss on benefits adjustment and the pension expense that we attribute to the recovery of the broader market. These benefits may be offset by higher depreciation and operating expense. Absent a decision in the pending general rate case around the contested revenue adjustment mechanisms, we believe this quarter results will be similar in character to those of the first quarter, that is somewhat distorted vs. normal. That said it is possible that we will see a proposed decision in the general rate case prior to the earnings release.

SJW Group

We expect SJW to report adjusted ongoing 2Q'20 EPS of $0.70 vs $0.58 from the prior year quarter. Q2'20 earnings will benefit from the rate base growth and investment, and the close of the Connecticut Water acquisition (October '19). In conjunction with its earnings release we expect SJW will update investors on its water production costs, ongoing regulatory calendar and the memorandum account it has established to manage costs associated with the ongoing Covid-19 pandemic. SJW updated in annual guidance on its first quarter call to a range of $1.95-$2.05, we do not expect any change or adjustment to this guidance after what is largely considered a shoulder quarter for California water utilities.

Essential Utilities

We expect Essential Utilities to report adjusted 2Q'20 EPS of $0.26 vs. the prior year quarter (pre Peoples Gas acquisition and excluding acquisition related costs) of $0.37. This estimate is consistent with the company's annual guidance of $1.53-$1.58 and its expectations for earnings dispersion across the year (35-45% in Q1/10-20% in Q2/10-20% in Q3/25-35% in Q4). While annual guidance is largely theoretical given the timing of the Peoples Gas deal close and its inclusion in earnings at a assumed level, Q2 will be the first full quarter for the whole entity and should provide investors will useful insight (albeit in a slow quarter for a gas LDC) of the company's earnings power. Earnings drivers for the quarter include positive weather (warm & dry spring season), rate increases across the company's

operating jurisdictions, somewhat lower expenses associated with 'work from home' environment.

In conjunction with its earnings release, we expect WTRG will update investors on the integration of its Peoples Gas acquisition, its pending acquisition of DELCORA (and the timing of the associated equity) and other potential M&A activity (Chester Water Authority, Norristown etc.). We also expect an update on the company's 'catch-up' repairs tax adjustment filing in Pennsylvania and pending federal infrastructure legislation.

Independent Power Producers

NRG Energy

We expect NRG Energy to report ongoing Adjusted EBITDA of $533mln vs. $528mln consensus estimates and $469mln last year. We expect drivers you over year to be incremental EBITDA from the Stream retail acquisition, continued margin enhancement at the retail business and warmer weather year on year. This warmer weather is likely to offset any coronavirus bad debt or volume related impacts in the quarter, which we expect to be less impactful overall than originally estimated in March.

On the 1Q 2020 earnings call update, NRG indicated that they were 98% hedged in the East/West segment for the balance of 2020 and had the integrated hedge in ERCOT through retail. For 2022, hedging levels were 22% in the East/West segment at the time of the 1Q 2020 earnings call.

We are also updating our annual Adjusted EBITDA estimates on a mark to market basis to $1,986/$1,840/$1,737mln from $1,914/$1,813/$1,773mln for '20/21/22 respectively.

Vistra Energy

We expect Vistra Energy to report ongoing Adjusted EBITDA of $819mln vs. $749mln consensus estimates, and $707mln last year. We expect operational performance improvement cost cutting initiatives (OPIs) to begin to show impact in the quarter and to largely if not completely offset the impact of lower capacity revenues for the non-ERCOT generation businesses. We expect ERCOT results will be higher by ~$50mln year-year as that segment also captures OPIs and we do not expect bad debts to be a high as anticipated by management on the 1Q call, at least in 2Q 2020 given that Texas did not significantly lock down. Further the capture of ~$60mln in the guidance walk on the 1Q conference call discussed by management was largely in 1Q but there will be some residual impact carried into the 2Q period. At retail we expect that results will be higher year over year related to the acquisitions of both the Crius and Ambit retail businesses. This will not be damped by mild weather as in 1Q and will somewhat shift the seasonality of results for Vistra more toward 1Q, 2Q, and 4Q and away from 3Q.

On the 1Q 2020 earnings call update, VST indicated that they were 100% hedged across the non-natural gas generation fleet and 97% hedged at the gas fleet for the balance of 2020. In 2020 hedging levels were 72% at the non-natural gas fleet an 36% at the natural gas fleet for 2021, with the largest open position at the natural gas fleet in ERCOT and PJM.

We are also updating our annual Adjusted EBITDA estimates on a mark to market basis to $3,444/$3,087 /$3,076mln from $3,287/$3,195/$3,074mln for '20/21/22 respectively.

Figure 34: Vistra Energy Adj. EBITDA – 2Q 2019A vs. 2Q 2020E

US$mlns	2Q 2019A	2Q 2020E	Variance
Retail	293	355	62
ERCOT	156	206	50
PJM	167	167	-
NY/NE	91	91	-
MISO	1	1	-
Non-Seg Ops	(1)	(1)	-
Asset Closure	-	-	-
Total	**707**	**819**	**112**

Source: UBS Equity Research Estimates

Figure 35: Actual Power Price Comparisons ($/MWh)

ISO	Hub	2Q '20	2Q '19	Change
ISO NE	Internal Hub	19.07	24.02	(4.96)
NYISO	Zone G	15.54	20.98	(5.44)
PJM	AEP-Dayton	18.60	24.38	(5.78)
PJM	Eastern	15.89	22.48	(6.58)
PJM	N Illinois	15.90	22.19	(6.29)
PJM	PSEG	16.12	21.54	(5.41)
PJM	Western	18.01	24.07	(6.06)
MISO	Indiana	20.24	25.23	(4.99)
MISO	Michigan	21.00	25.67	(4.67)
ERCOT	North	16.45	25.09	(8.64)
ERCOT	Houston	18.66	26.28	(7.62)
ERCOT	West	15.04	23.34	(8.30)
CAISO	NP15	21.15	21.18	(0.04)
CAISO	SP15	19.31	21.64	(2.33)

Source: S&P Global Market Intelligence, UBS Equity Research Estimates

Figure 36: Power Price Comparisons & Spark Spread Trends ($/MWh)

Period	ISO	Hub	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7
Q220	ISO NE	Internal Hub	$ 9.93	$ 10.85	$ 10.88	$ 11.47	$ 13.18	$ 12.02	$ 12.46
Q219	ISO NE	Internal Hub	$ 10.92	$ 12.49	$ 11.90	$ 8.72	$ 5.71	$ 6.54	$ 6.20
		Change	$ (0.99)	$ (1.64)	$ (1.02)	$ 2.75	$ 7.47	$ 5.48	$ 6.25
Q220	PJM	Eastern	$ 12.27	$ 13.50	$ 13.86	$ 14.32	$ 15.04	$ 15.52	$ 15.56
Q219	PJM	Eastern	$ 13.60	$ 12.36	$ 11.82	$ 11.69	$ 11.24	$ 11.12	$ 11.54
		Change	$ (1.33)	$ 1.14	$ 2.05	$ 2.63	$ 3.80	$ 4.40	$ 4.01
Q220	PJM	Western	$ 14.35	$ 15.87	$ 15.92	$ 16.16	$ 16.56	$ 16.69	$ 16.91
Q219	PJM	Western	$ 14.47	$ 15.50	$ 14.61	$ 14.53	$ 14.28	$ 13.66	$ 14.08
		Change	$ (0.12)	$ 0.37	$ 1.32	$ 1.63	$ 2.28	$ 3.03	$ 2.83
Q220	ERCOT	Houston	$ 33.20	$ 22.13	$ 20.05	$ 19.38	$ 18.82	$ 17.92	$ 16.11
Q219	ERCOT	Houston	$ 22.74	$ 22.67	$ 20.44	$ 17.41	$ 15.01	$ 12.05	$ 9.39
		Change	$ 10.46	$ (0.54)	$ (0.39)	$ 1.97	$ 3.81	$ 5.87	$ 6.72

Source: S&P Global Market Intelligence, UBS Equity Research Estimates

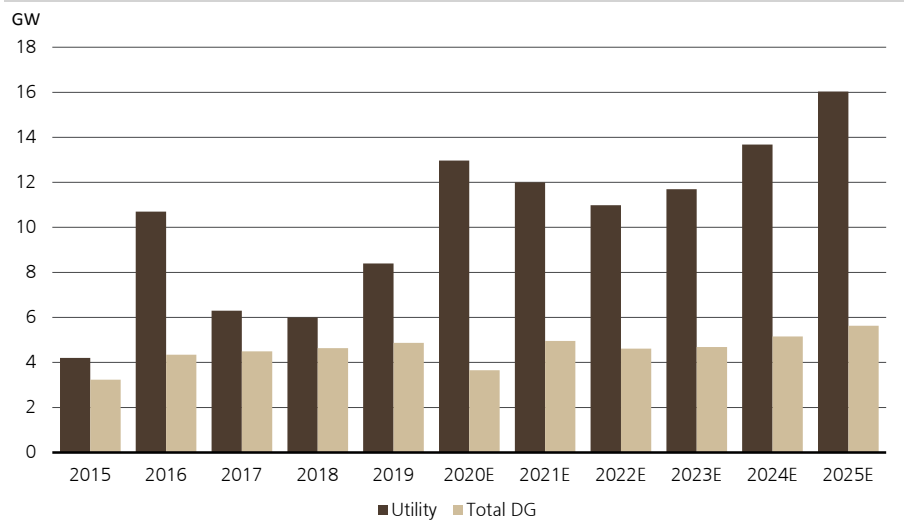
Alternative Energy 2Q20 preview

Key issues for the quarter

We expect 2Q20 results calls to focus on 1) Strength of the post-COVID recovery in distributed solar demand 2) potential policy support following the election and 3) RUN/VSLR deal impact on supply chains and potential to drive adoption of residential storage. We expect the market to look past trough 2Q actuals which are likely to be noisy; FSLR consensus revenue estimate dispersion is at the widest since 3Q17.

Our top pick in our Alternative Energy coverage is Generac (GNRC, Buy, PT $145) with exposure to accelerating residential solar + storage demand. See our GNRC initiation here.

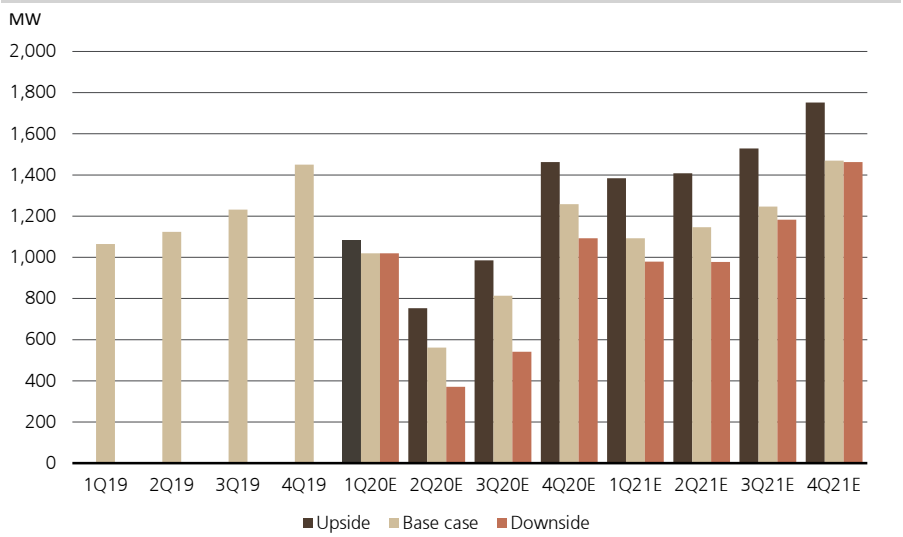
Figure 37: U.S. new solar installations (GW)



Source: EIA, IRENA, SEIA, Wood Mackenzie, UBS estimates

Recent comments from RUN indicate demand potentially tracking closer to our upside case for a 33% y/y 2Q decline in distributed solar demand.

Figure 38: U.S. distributed solar demand – quarterly forecast



Source: EIA, SEIA, Wood Mackenzie, UBS estimates

Company specific focus areas

- **FSLR**: We expect a 2Q20 loss per share of $0.04 driven by lower systems segment contribution from project sale timing delays. Consensus 2Q20 adj. EPS is currently $0.30. FSLR previously pulled 2020 financial guidance but maintained module production guidance of 5.9GW indicating confidence in manufacturing execution. Uncertainty of systems sales remains driven by timing rather than quantity. Management flagged a sequential quarterly decline in module ASP with 1Q20 having benefitted from safe harbor demand. UBSe 2Q20 module ASP is $0.36/watt.

- **SPWR**: 2Q20 revenue guide of $290-330mn implies down 27-36% q/q & down 32-40% y/y. Adj. EBITDA guidance is negative $40-20mn. We expect a sequential recovery in earnings after 2Q but note SPWR has over 50% market share in the new home solar market which could be a drag in 2H20. On the 16 July Maxeon analyst day management highlighted the Maxeon spin remains on track to close in 3Q20. Preliminary Maxeon results were provided for 2Q20 revenue of $160-170mn, down 40% y/y at the midpoint driven by 8 week production shut downs. We expect Maxeon to continue to focus on deploying a base of premium-quality modules while driving faster growth through expanding sales of lower-cost modules produced by the TZS JV in China. Maxeon currently arranged financings provide enough liquidity to cover the expected $385mn investment in capacity expansion through 2022.

- **CSIQ**: 2Q20 guidance is 2.5-2.7GW module shipments, $630-680mn revenue, and gross margin 18.5-20.5%. 2020 shipment guidance 10-12GW. We see risk of industry overcapacity potentially dragging on profit margins into 2H20. Key uncertainty for utility scale solar exposure remains project sale timing and price. Project revenue has comprised 24% of total net sales over the last 5 years. We look for an updated on CSIQ's prior suspension of its share repurchase program.

- **JKS**: 2Q20 guidance is 4.2-4.5GW shipments, $1.1-1.18bn revenue, and 16-18% gross margin. 2020 shipment guidance is 18-20GW. We forecast module ASP declining ~10% 2Q20 q/q with margin pressure persisting through 2020.

JKS management is targeting cost reductions to offset ASP pressure and maintain ~flat margin to 2Q20.

- **RUN**: RUN's latest commentary implies 2Q20 deployments better than the previous 30% y/y decline expectation. Our 2Q20 deployment estimate is 77MW, -25% y/y. We expect focus on the conference call around potential impacts on the inverter supply chain following RUN's acquisition of VSLR. Based on our analysis of California distributed solar data, RUN installs have historically use a ~50/50 mix of SEDG and ENPH inverters with VSLR primarily using ENPH equipment.

- **SEDG**: 2Q20 revenue guidance of $305-335mn implies a decline of 22-29% q/q. The 2Q guidance is well ahead of ENPH's 2Q revenue guide for a 37-44% q/q decline. SEDG noted a 33% y/y decline in U.S. installations in April and we see likely sequential improvement in May-June. 2Q20 gross margin guidance of 30-32% reflects margin pressure driven by higher European sales mix, with a U.S./Europe margin differential of 450bps, partially offset by 200bps margin improvement on reduced air shipments.

- **GNRC**: We forecast 2Q20 adj. EPS of $0.68, reflecting -43% y/y growth driven by a 40% y/y 2Q decline in C&I segment sales. GNRC provided only directional 2Q guidance for a modest sequential decline in net sales (UBSe $449mn) and adj. EBITDA margin (UBSe 15.7%). Our focus will be on customer adoption of Clean Energy products and GNRC's progress in shifting its manufacturing to Vietnam (which we expect to have largely been completed in June). See our recent initiation here.

- **HASI**: Long-term core EPS growth guidance of 2-6% off a 2017 baseline remains intact implying core EPS of $1.43 in 2020 at the midpoint. We model 2Q20 core EPS of $0.33.

- **ORA**: We forecast 2Q20 adj. EPS of $0.39 and adj. EBITDA of $98mn reflecting typical seasonality of electricity generation. ORA 2020 guidance is revenue $710-740mn and adj. EBITDA $400-415mn. The Puna plant re-start previously pushed to 4Q20 and we look for an update on progress toward completing permitting & necessary transmission upgrades. The emerging market assets continue to be a source of concern. Trade receivables reached $169mn, and DSO is at 93 days, up from 73 days in 1Q19. See our read-throughs from California Public Utility Commission's latest Integrated Resource Plan here.

- **TPIC**: We expect 2Q20 line utilization of 70% driven by Juarez & Matamoros COVID-19 related shutdowns. 2Q20 UBSe adj. EBITDA is $22mn. We expect cumulative 2020-2021 wind demand to remain intact with the impact to TPIC earnings being one of timing. In addition, customer pushout of blade transitions could help mitigate the COVID related earnings impact to 2020 by reducing TPIC's blade transition costs.

Figure 39: Alternative Energy key estimates

		Quarterly				Annual		
Company	Ticker	Scheduled Reporting Date	2Q20E UBS	2Q20E Consensus	UBS Vs. Consensus	2020E UBS	2020E Consensus	UBS Vs. Consensus
ALTERNATIVE ENERGY								
Hannon Armstrong	HASI	29-Jul est.	$0.33	$0.32	$0.01	$1.50	$1.47	$0.04
Generac	GNRC	30-Jul	$0.68	$0.88	($0.20)	$4.18	$4.38	($0.20)
First Solar	FSLR	30-Jul est.	($0.04)	$0.32	($0.36)	$3.39	$2.82	$0.58
Ormat Technologies	ORA	4-Aug	$0.39	$0.39	($0.00)	$1.74	$1.77	($0.04)
Sunpower	SPWR	4-Aug est.	($0.30)	($0.38)	$0.08	($0.27)	($0.44)	$0.17
SolarEdge	SEDG	5-Aug est.	$0.74	$0.53	$0.21	$4.22	$3.06	$1.16
TPI Composites	TPIC	5-Aug est.	$0.04	($0.23)	$0.27	$0.35	$0.41	($0.05)
SunRun	RUN	6-Aug est.	($0.01)	$0.07	($0.08)	($0.23)	$0.15	($0.37)
Canadian Solar	CSIQ	13-Aug est.	($0.13)	($0.06)	($0.07)	$2.47	$2.91	($0.44)
Jinko Solar Holding Company	JKS	20-Aug est.	$0.98	$0.66	$0.32	$3.77	$3.61	$0.16

Source: Company reports, FactSet, UBS research estimates.

Environmental Services 2Q20 preview

Progress on recovery in waste volumes

We expect relatively upbeat 2Q20 conference call as the recovery in municipal solid waste appears to be firmly underway. At the UBS Industrial and Transportation conference in early June, Management's noted continued w/w improvements in commercial waste volumes & landfill tons following the bottom in April. In addition, WCN pre-announced high-level results on 9 July driving a 4% increase in our 2Q20 revenue estimate.

As we approach the election we expect increased focus on potential for higher corporate tax rates. Broadly, every 1% increase in the corporate tax rates (from 21% to 22%) drives a 0.6% decrease in MSW FCF.

Re-issuing 2020 guidance

We expect most of the waste names will re-issue 2020 guidance with 2Q20 results. In our view, names best positioned to exceed expectations are nationally diversified players (WM, RSG, WCN) that were likely able to mitigate the impact of the relatively more restrictive COVID-19 shutdowns in the U.S. Northeast. For CVA, CLH, and ECOL waste volumes expected to recover sequentially after 2Q20 but likely to ramp more slowly than for the MSW haulers.

Figure 40: Environmental Services business exposures

Metric 2020E	WM	RSG	WCN	ADSW	CWST	CVA
2020 revenue ($bn)	14.9	9.6	5.3	1.5	0.7	1.9
N. American market share	24%	16%	9%	2%	1%	3%
Geographic						
U.S. Northeast	22%	18%	22%	26%	100%	47%
U.S. South	24%	34%	17%	36%	0%	33%
U.S. Midwest	23%	20%	12%	38%	0%	7%
U.S. West	24%	28%	33%	0%	0%	10%
Canada/other	7%	0%	16%	0%	0%	3%
Total	100%	100%	100%	100%	100%	100%
Revenue composition						
Residential collection	17%	19%	21%	25%	17%	0%
Commercial collection	22%	25%	26%	23%	18%	0%
Industrial collection	15%	18%	14%	15%	17%	0%
Total collection	54%	62%	61%	63%	52%	0%
Other operations						
Transfer	9%	11%	12%	10%	9%	10%
Disposal	19%	20%	20%	21%	18%	56%
Recycling	7%	3%	1%	1%	5%	5%
E&P	1%	2%	4%	1%	2%	0%
Other operations	10%	2%	2%	4%	14%	29%
Total	100%	100%	100%	100%	100%	100%
Cost composition						
SGA as % of revenue	10.4%	10.3%	10.0%	11.6%	11.9%	5.1%
Opex as % of revenue	62%	62%	-85%	64%	70%	75%

Source: Company reports, UBS Research estimates

Figure 41: UBSe, Consensus, prior guidance table

		Original 2020 guidance				
Ticker	Metric	Low	Mid	High	UBSe	Consensus
WM						
	Price		2.5%		1.1%	
	Volume		1.5%		-7.4%	
	Adj. EBITDA ($bn)	4.56	4.61	4.66	4.14	4.05
	FCF ($bn)	2.15	2.20	2.25	2.82	1.81
	Capex ($bn)	1.70	1.75	1.80	1.65	1.59
RSG						
	Price		3.0%		1.1%	
	Volume	0.8%	0.9%	1.0%	-7.0%	
	Sales growth	4.3%	4.6%	5.0%	-6.4%	-3.4%
	Adj. EBITDA ($bn)	3.05	3.08	3.10	2.65	2.73
	Adj. EPS	3.48	3.51	3.53	2.51	2.79
	Adj. EBITDA ($bn)	3.05	3.08	3.10	2.65	2.73
	FCF ($bn)	1.18	1.20	1.23	1.01	1.03
	Capex ($bn)		1.20		1.16	1.13
WCN						
	Sales ($bn)	5.73	5.75	5.78	5.35	5.34
	Adj. EBITDA ($bn)	1.76	1.77	1.79	1.61	1.58
	Net income ($mn)	653	661	668	522	630
	FCF ($bn)	975	988	1000	899	850
CWST						
	Price	3.5%	4.0%	4.5%	3.0%	
	Volume	-0.5%	0.0%	0.5%	-8.2%	
	Sales ($mn)	800	808	815	735	757
	Adj. EBITDA ($mn)	170	172	174	151	152
	Net income ($mn)	35	37	39	18	24
	FCF ($mn)	60	62	64	46	51
	Capex ($mn)		113		101	102
CVA						
	Adj. EBITDA ($mn)	415	430	445	390	402
	FCF ($mn)	100	120	140	16	74
CLH						
	Adj. EBITDA ($mn)	545	565	585	466	449
	FCF ($mn)	210	225	240	207	175
ECOL						
	Adj. EBITDA ($mn)	230	240	250	198	184
	Adj. EPS	1.65	1.89	2.12	0.91	0.70
	FCF ($mn)	81	94	106	72	50
	Capex ($mn)	90	93	95	79	68

Source: FactSet, company reports, UBS research estimates. Note: UBSe for WM reflects partial year contribution from ADSW acquisition. All companies have withdrawn original 2020 guidance in light of COVID-19 pandemic.

Company specific focus areas

- **WM**: WM's well-diversified national exposure should help mitigate the most severe of the shutdown impacts on the U.S. Northeast (22% of revenue) and Canada (7% of revenue). WM's acquisition of ADSW is now expected to close 3Q20. WM expects to redeem ~$3bn of outstanding senior notes issued in May 2019 under the redemption provision that the deal be closed by 14 July 2020. Assuming refinancing at current rates we see a potential ~$27mn annual interest savings and $1.20/sh share price accretion at a 5% FCF yield.

- **RSG**: We forecast 2Q20 volumes down 14% y/y and adj. EBITDA of $596mn. RSG had previously disclosed 40% decremental EBITDA margin on the entire company driven by declines in high margin small container and landfill volumes. At our UBS Industrials & Transportation conference in early June, management highlighted continued improvement in volumes through May and expectations for a good June result. In addition, the company has seen no material change in DSO to-date.

- **WCN**: WCN pre-announced high level 2Q results. See our note here. 2Q revenue declined 4.7% y/y ($1.3bn; +1.5% to consensus) with adj. EBITDA margin down 90-100bps y/y ($392-394mn; +6.8% to consensus at mid-point). WCN highlighted same store solid waste revenue down 5.3% y/y and down 1.3% y/y excluding Canada and the U.S. Northeast. In addition WCN closed $50mn in new annualized revenue of new tuck-ins. We had previously expected a pause on acquisition spending in 2Q-3Q20. We expect WCN to re-issue formal 2020 guidance with the 2Q20 results and see FY2020 revenue tracking above the $5.25bn baseline provided previously.

- **ADSW**: ADSW will not be hosting an earnings conference call given the announced acquisition by WM. We do not expect the stock to trade on results given expected near-term acquisition closure.

- **CWST**: CWST's Northeast footprint suggests a more muted recovery than that experienced by WCN (and likely other nationally diversified players). We forecast 2Q20 volumes to decline 15% y/y. Our 2Q20 adj. EBITDA is $35mn, down 13% y/y. As of the 1Q results call, CWST expected a 150-200bps negative headwind to adj. EBITDA margin from COVID-19. Excluding M&A, the April y/y revenue impacts by product line were: Residential: 0%, Commercial -9.3%, Roll-off -26%, Disposal -14.4%, Resource Solution +1%. CWST noted a sequential up-tick from trough demand in late-April and May.

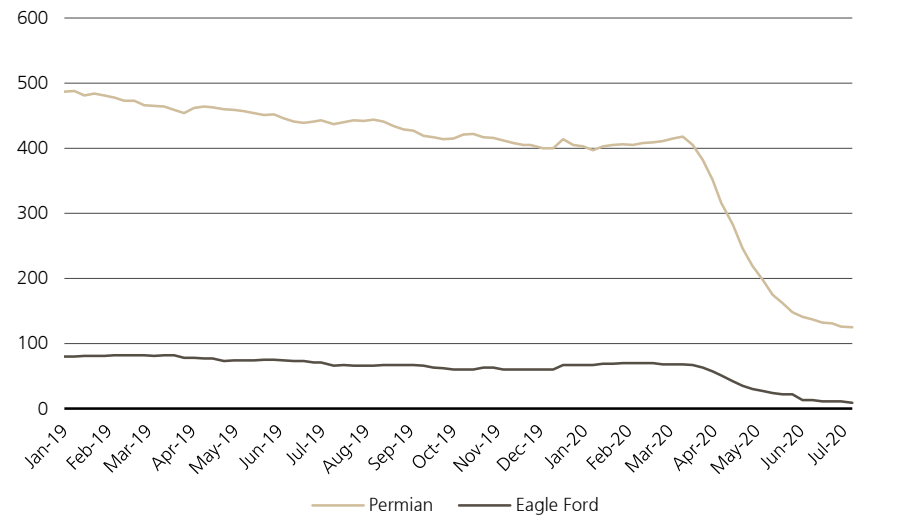
- **CVA**: Given CVA's Northeast concentration we expect a relatively slower recovery ramp than for the large national solid waste names, however we expect waste volumes for CVA have continued to improve off of April lows. Our 2Q20 adj. EBITDA is $68mn, down 28% y/y. Management previously highlighted April tip fee pricing down $4-6 per blended tip fee ton, or approximately 7-10% vs. 2Q19 averages and ~$5mn per month impact. See our recent upgrade of CVA to Buy here.

- **CLH**: We forecast 2Q20 adj. EBITDA of $92mn, -39% y/y. We see CLH's Safety Kleen segment taking the brunt of COVID related impacts, with segment revenue down 30% y/y in April but improving sequentially through June. CLH has completed ~$50mn of decontamination work related to COVID-19. As of 1Q20 CLH had closed half of its refinery capacity to reduce fixed costs and we

look for an update on potentially restarting these assets. Expect management to issue revised guidance with the 2Q results.

- **ECOL:** We forecast 2Q20 adj. EBITDA $39mn, ~flat y/y despite contribution from the NRCG acquisition. April & May likely reflecting trough months with the recovery in earnings underway in June. For the ES segment, management had previously flagged base business declines (~30% of revenue) of 10-15% y/y in April and likely similar May impact. Rig count has yet to find a bottom indicating pressure on ECOL's E&P waste revenues continuing to worsen in 3Q. ECOL has energy waste landfill exposures in the Permain (avg. 2Q rig count down 55% y/y) and Eagle Ford (avg. 2Q rig count down 63%) basins.

Figure 42: North America rig count



Source: Baker Hughes, UBS Research

Figure 43: Environmental Services EPS estimates

		Quarterly				Annual		
Company	Ticker	Scheduled Reporting Date	2Q20E UBS	2Q20E Consensus	UBS Vs. Consensus	2020E UBS	2020E Consensus	UBS Vs. Consensus
ENVIRONMENTAL SERVICES								
Clean Harbors	CLH	29-Jul est.	$0.07	($0.00)	$0.07	$0.99	$0.85	$0.14
Advanced Disposal Services	ADSW	30-Jul	($0.02)	($0.01)	($0.01)	$0.02	$0.14	($0.12)
Covanta Holding Corp	CVA	30-Jul	($0.24)	($0.19)	($0.05)	($0.34)	($0.29)	($0.05)
Waste Management	WM	30-Jul	$0.74	$0.77	($0.04)	$3.49	$3.68	($0.19)
Casella Waste System	CWST	3-Aug	$0.05	$0.05	($0.00)	$0.44	$0.52	($0.08)
US Ecology	ECOL	5-Aug est.	$0.22	($0.02)	$0.24	$1.24	$1.12	$0.12
Republic Services	RSG	6-Aug	$0.47	$0.56	($0.09)	$2.51	$2.79	($0.28)
Waste Connections	WCN	6-Aug	$0.49	$0.54	($0.06)	$2.36	$2.38	($0.02)

Source: Company reports, FactSet, UBS research estimates.

Figure 44: Environmental Services EBITDA estimates ($mn)

		Quarterly				Annual		
Company	Ticker	Scheduled Reporting Date	2Q20E UBS	2Q20E Consensus	UBS Vs. Consensus	2020E UBS	2020E Consensus	UBS Vs. Consensus
ENVIRONMENTAL SERVICES								
Clean Harbors	CLH	29-Jul est.	106	93	14.2%	474	447	6.0%
Covanta Holding Corp	CVA	30-Jul	68	77	-11.5%	381	403	-5.5%
Advanced Disposal Services	ADSW	30-Jul	93	87	7.2%	374	390	-4.2%
Waste Management	WM	30-Jul	908	922	-1.5%	4,141	4,067	1.8%
Casella Waste System	CWST	3-Aug	35	33	5.5%	151	153	-1.3%
US Ecology	ECOL	5-Aug est.	49	39	24.4%	211	184	14.4%
Republic Services	RSG	6-Aug	596	608	-2.0%	2,652	2,729	-2.8%
Waste Connections	WCN	6-Aug	393	376	4.6%	1,609	1,576	2.1%

Source: Company reports, FactSet, UBS research estimates.

Valuation Method and Risk Statement

Our valuation methodology for North American utilities is price to earnings based. The adjustments applied fall into 6 categories. These are as follows: 1) Group Valuation Bias: Flowing from our valuation work comparing Baa corporate yields to group dividend yields and RU price to earnings ratios to those for the S&P 500, we incorporate a positive or negative adjustment to our group multiple representing the gap we calculate to the nearest 5%; 2) Growth Adjustment: We adjust our valuations based on the growth quartile each utility occupies. First quartile receives a 5% premium, second quartile a 2% premium, third quartile a 2% discount and fourth quartile a 5% discount; 3) Regulatory Adjustment: Our valuation adjustments for regulation are based on our proprietary Regulatory Rankings. First quartile jurisdictions receive 5%, second quartile 2%, third quartile -2% and fourth quartile -5%; 4) Earnings Consistency Adjustment: For companies that fall in the top quartile of % Time Beat/Meet, we include +5%; 5) Multi Utility Diversified Valuation: For multi utilities (those with more than 15% diversified or foreign earnings), we perform a sum-of-parts analysis applying business/region appropriate valuations to those diversified businesses; 6) One-off Adjustments: In special situations, we value risk on an issue specific basis. Common areas where we apply such an adjustment include: ESG advantage, large project construction risk, legal risk, and announced M&A completion risk. We identify the following risk factors for the sector overall: rising interest rates; regulatory and policy risks; operational risks; construction risks; cybersecurity risk to the transmission grid and/or customer data, and extreme weather events.

Our valuation methodology for the IPPs is based on mid-cycle EV/EBITDA multiples of 7.2x on UBSe 2020 EBITDA, UBSe 2020 Net Debt, the NPV of hedges and any NOLs discounted to the current year at 8%, and UBSe 2020 share count.

Our valuation methodology for the Alternative Energy space is based on a variety of metrics including P/BV, EV/EBITDA, P/E, and retained equity value per share. Our target multiples are derived from historical group averages with adjustments for expected growth rates, leverage, and earnings growth confidence. We identify the following risks for the sector: Demand for new renewable installations has historically been volatile around changes in state and federal policy, and we expect this volatility to continue. In addition, margins for product manufacturers can be impacted by swings in raw materials pricing and the overall level of energy prices.

Our valuation methodology for the Environmental Services space is based on EV/EBITDA with adjustments made to the target EV/EBITDA multiple based on relative growth rates, Free Cash Flow (FCF) conversion, expected earnings stability, and the general level of risk and our confidence in future earnings estimates. We identify the following risks for the sector: Housing remains a key driver of incremental municipal solid waste volume growth, and a slowdown in new housing starts could put downward pressure on sales growth. In addition, pricing tends to follow GDP growth, and a slowdown in economic growth could drive lower ability to raise pricing driving potential contraction in margins. For more industrial-exposed names, swings in commodity prices can impact the overall level of waste-generating activity, contributing to earnings volatility.

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Buy	FSR is > 6% above the MRA.	49%	32%
Neutral	FSR is between -6% and 6% of the MRA.	39%	30%
Sell	FSR is > 6% below the MRA.	13%	20%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 June 2020.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Advanced Disposal Services Inc[3, 5, 13, 16, 19]	ADSW.N	Neutral (CBE)	N/A	US$30.16	16 Jul 2020
AES Corp[16]	AES.N	Buy	N/A	US$14.88	16 Jul 2020
Alliant Energy Corp[16]	LNT.O	Neutral	N/A	US$49.73	16 Jul 2020
Ameren Corp[16]	AEE.N	Buy	N/A	US$76.79	16 Jul 2020
American Electric Power Inc[7, 16]	AEP.N	Buy	N/A	US$85.09	16 Jul 2020
American States Water Co[16]	AWR.N	Sell	N/A	US$77.59	16 Jul 2020
American Water Works Co[16]	AWK.N	Neutral	N/A	US$138.32	16 Jul 2020
ATCO Ltd	ACOx.TO	Buy	N/A	C$42.31	16 Jul 2020
California Water Service Group[16]	CWT.N	Sell	N/A	US$48.28	16 Jul 2020
Canadian Solar Inc[6c, 7, 13, 16, 20a]	CSIQ.O	Neutral (CBE)	N/A	US$22.80	16 Jul 2020
Canadian Utilities Ltd	CU.TO	Neutral	N/A	C$34.41	16 Jul 2020
Caribbean Utilities Corp	CUPu.TO	Sell	N/A	US$15.49	16 Jul 2020
Casella Waste Systems Inc[16]	CWST.O	Neutral	N/A	US$53.39	16 Jul 2020
Clean Harbors Inc[16, 20b]	CLH.N	Neutral (CBE)	N/A	US$60.25	16 Jul 2020
CMS Energy Corp[4, 5, 6a, 16]	CMS.N	Neutral	N/A	US$60.33	16 Jul 2020
Consolidated Edison Inc[16]	ED.N	Neutral	N/A	US$71.84	16 Jul 2020
Covanta Holding Corp[4, 16]	CVA.N	Buy	N/A	US$9.69	16 Jul 2020
Dominion Energy Inc[7, 16]	D.N	Buy	N/A	US$76.95	16 Jul 2020
DTE Energy Co[16]	DTE.N	Buy	N/A	US$109.70	16 Jul 2020
Duke Energy Corp[7, 16]	DUK.N	Buy	N/A	US$81.07	16 Jul 2020
Edison International[7, 16]	EIX.N	Buy	N/A	US$56.09	16 Jul 2020
Emera Inc	EMA.TO	Buy	N/A	C$55.94	16 Jul 2020
Entergy Corp[7, 16]	ETR.N	Buy	N/A	US$98.33	16 Jul 2020
Essential Utilities Inc[16]	WTRG.N	Neutral	N/A	US$43.88	16 Jul 2020
Evergy, Inc[16]	EVRG.N	Neutral	N/A	US$61.41	16 Jul 2020
Eversource Energy[7, 16]	ES.N	Neutral	N/A	US$85.81	16 Jul 2020
Exelon Corp[7, 16]	EXC.O	Buy	N/A	US$38.06	16 Jul 2020
First Solar Inc[16]	FSLR.O	Buy	N/A	US$59.03	16 Jul 2020
FirstEnergy Corp[16]	FE.N	Buy	N/A	US$41.29	16 Jul 2020
Fortis Inc[16]	FTS.TO	Buy	N/A	C$54.10	16 Jul 2020
Generac Holdings Inc[16]	GNRC.N	Buy	N/A	US$132.54	16 Jul 2020
Hannon Armstrong Sustainable Infra[16]	HASI.N	Neutral	N/A	US$32.37	16 Jul 2020
Hawaiian Electric Industries Inc[16]	HE.N	Sell	N/A	US$37.00	16 Jul 2020
Hydro One	H.TO	Sell	N/A	C$27.26	16 Jul 2020
JinkoSolar Holding Co Ltd[13, 16, 20a]	JKS.N	Neutral (CBE)	N/A	US$19.86	16 Jul 2020
NextEra Energy Inc[4, 6a, 7, 16]	NEE.N	Buy	N/A	US$268.38	16 Jul 2020
NRG Energy Inc[7, 16]	NRG.N	Buy	N/A	US$33.84	16 Jul 2020
OGE Energy Corp[16]	OGE.N	Buy	N/A	US$31.90	16 Jul 2020
Ormat Technologies Inc[16]	ORA.N	Neutral	N/A	US$61.53	16 Jul 2020
PG&E Corp[7, 16, 20b]	PCG.N	Buy (CBE)	N/A	US$9.02	16 Jul 2020
Pinnacle West Capital Corp[7, 16]	PNW.N	Neutral	N/A	US$80.56	16 Jul 2020

Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
PNM Resources Inc[7, 16]	PNM.N	Buy	N/A	US$39.13	16 Jul 2020
Portland General Electric Co[16]	POR.N	Neutral	N/A	US$42.32	16 Jul 2020
PPL Corp[16]	PPL.N	Buy	N/A	US$25.85	16 Jul 2020
Public Service Enterprise Group[7, 16]	PEG.N	Buy	N/A	US$52.91	16 Jul 2020
Republic Services Inc[13, 16]	RSG.N	Buy	N/A	US$84.60	16 Jul 2020
Sempra Energy[7, 16]	SRE.N	Buy	N/A	US$122.63	16 Jul 2020
SJW Group[4, 16]	SJW.N	Neutral	N/A	US$63.02	16 Jul 2020
SolarEdge Technologies Inc[16, 20a]	SEDG.O	Neutral (CBE)	N/A	US$164.75	16 Jul 2020
Southern Co[6b, 7, 13, 16]	SO.N	Neutral	N/A	US$53.74	16 Jul 2020
SunPower Corp[16, 20a]	SPWR.O	Neutral (CBE)	N/A	US$9.79	16 Jul 2020
Sunrun Inc[16, 20a]	RUN.O	Neutral (CBE)	N/A	US$36.65	16 Jul 2020
TPI Composites Inc[16]	TPIC.O	Buy	N/A	US$26.25	16 Jul 2020
US Ecology Inc[16]	ECOL.O	Buy	N/A	US$32.89	16 Jul 2020
Vistra Energy Corp[2, 4, 6a, 16]	VST.N	Buy	N/A	US$19.40	16 Jul 2020
Waste Connections Inc[16]	WCN.N	Buy	N/A	US$100.04	16 Jul 2020
Waste Management Inc[3, 16]	WM.N	Buy	N/A	US$107.46	16 Jul 2020
WEC Energy Group Inc[16]	WEC.N	Neutral	N/A	US$87.76	16 Jul 2020
Xcel Energy Inc[16]	XEL.O	Neutral	N/A	US$64.99	16 Jul 2020

Source: UBS. All prices as of local market close.
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Q2 2019 Earnings Preview

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Regulated Utilities:
Our Q2'19 EPS estimates are 3% below consensus and 3% below Q2'18. Weather conditions were below normal in every region of the country with the upper Midwest and West most impacted (CMS, EVRG, PNM, PNW) although conditions in the Southern U.S. improved YoY which we expect helped ETR exceed consensus, and should also be helpful to NEE and SO. Due to the timing of rate case revenue EIX likely also beat consensus and the company could discuss their contribution to the wildfire insurance fund and the legislation on their call. Canadian utilities likely miss consensus with mild weather for CU, FTS and H, and EMA capped on ROE in NS despite better weather.

Power:
Our expectations for Adj. EBITDA are similar to 1Q where we see NRG results of $486mln below current consensus due to annual estimates not being seasonally weighted enough to 3Q, whereas we see VST results of $718mln above consensus due to estimates not being seasonally weighted enough away from 3Q. Overall results should not be significantly impacted by the lower power prices year on year as NRG was 93%/82% hedged in ERCOT/PJM as of the 1Q call and VST was 100% hedged to natural gas and 94% hedged to heat rate in ERCOT and 94%-95% hedged in the northeast as of the 1Q call. Despite forward curves being lower management should discuss on the call the offsetting effects of expanding retail margins. In addition to discussion of these sensitivities, investors are likely to focus on integration of the Crius acquisition for VST, implementation of the retail lite strategy for NRG, and any updates on target leverage and use of FCF, as well as the upcoming PJM capacity auction.

Alternative Energy: Waiting for 2H19
We expect muted 2Q19 results given most companies in the space point towards a 2H19 ramp in demand and earnings. 2Q19 should be a small loss for FSLR (Buy) before the ramp in Series 6 volume and transition cost declines. 2H19E adj. EPS of $3.18/sh compares to 1H19E adj. loss per share of $0.67/sh. Similarly, we expect TPIC (Buy) y/y EBITDA ramp to begin in 3Q19 as 1H19 was impacted by one-off labor and production issues. We see potential upward guidance revisions for 2019 module shipments, particularly for the Chinese exposed names CSIQ and JKS.

Environmental Services: Headwinds make 2019 guidance increases unlikely
We expect the focus to be on two headwinds: 1) a 64% YTD decline in recycled fiber pricing and 2) a 10% YTD decline in Permian Basin E&P rig count. However, 2019 guidance is likely to be maintained across the group, in our view, driven by strong core MSW price and volume and incremental M&A offsetting the commodity headwinds. WCN (Buy) remains our top pick.

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Figure 1: Electric Utilities Universe

Rating	Ticker	Company	7/19/2019 Price	Price Target	Total Return inc. Div. Yld	UBS 2018A EPS	UBS 2019E EPS	UBS 2020E EPS	UBS 2021E EPS	2020 P/E Ratio	2020 Prem/ Disc	2021 P/E Ratio	2021 Prem/ Disc	Current Dividend Yield	5 Yr EPS Growth	5 Yr DPS Growth	Regulatory Quartile
Neutral (CBE)	PCG	PG&E Corp	$17.79	$24	35%	$4.00	$3.27	$1.90	$2.39	9.4x	(53%)	7.4x	(60%)	0.0%	-4.9%	0.0%	4th
Buy	ACO	ATCO Ltd. (C$)	$43.29	$54	28%	$3.10	$3.22	$3.29	$3.43	13.2x	(32%)	12.6x	(30%)	3.7%	3.8%	6.1%	4th
Buy	PPL	PPL Corporation	$30.17	$36	25%	$2.38	$2.40	$2.54	$2.52	11.9x	(40%)	12.0x	(36%)	5.5%	3.1%	0.9%	2nd
Buy	DUK	Duke Energy	$88.45	$105	23%	$4.72	$4.97	$5.27	$5.57	16.8x	(16%)	15.9x	(15%)	4.3%	5.2%	2.0%	1st
Buy	EXC	Exelon	$47.57	$56	21%	$3.12	$3.19	$3.14	$3.14	15.1x	(24%)	15.2x	(19%)	3.0%	1.7%	5.3%	3rd
Buy	D	Dominion Energy	$76.85	$89	21%	$4.05	$4.22	$4.40	$4.65	17.5x	(12%)	16.5x	(11%)	4.8%	5.2%	4.3%	1st
Buy	FE	FirstEnergy Corp	$43.49	$50	18%	$2.60	$2.47	$2.53	$2.60	17.2x	(14%)	16.7x	(10%)	3.5%	1.9%	3.7%	2nd
Buy	NEE	NextEra Energy	$209.73	$240	17%	$7.70	$8.43	$9.08	$9.84	23.1x	16%	21.3x	14%	2.4%	7.9%	10.0%	1st
Buy	PEG	Public Service Ent Group	$60.18	$68	16%	$3.12	$3.22	$3.62	$3.54	16.6x	(16%)	17.0x	(9%)	3.1%	5.2%	5.0%	2nd
Buy	FTS	Fortis Inc (C$)	$51.62	$58	16%	$2.51	$2.54	$2.73	$2.93	18.9x	(2%)	17.6x	(3%)	3.5%	6.1%	6.0%	3rd
Buy	ES	Eversource Energy	$76.77	$86	15%	$3.25	$3.46	$3.67	$3.87	20.9x	5%	19.8x	6%	2.8%	5.9%	5.9%	2nd
Buy	AEP	American Electric Power	$90.28	$100	14%	$3.94	$4.10	$4.39	$4.75	20.5x	3%	19.0x	2%	3.0%	6.1%	7.0%	1st
Neutral	CU	Canadian Utilities Ltd (C$)	$35.80	$39	14%	$2.24	$2.21	$2.28	$2.38	15.7x	(18%)	15.1x	(17%)	4.6%	3.0%	5.4%	4th
Neutral	ED	Consolidated Edison	$87.24	$96	13%	$4.33	$4.33	$4.70	$4.87	18.6x	(7%)	17.9x	(4%)	3.4%	4.7%	3.0%	4th
Buy	EIX	Edison International	$70.17	$77	13%	$4.09	$4.49	$4.36	$4.58	16.1x	(19%)	15.3x	(18%)	3.5%	3.4%	0.2%	4th
Neutral	PNW	Pinnacle West Capital Corp	$93.59	$103	13%	$4.54	$4.94	$5.28	$5.60	17.7x	(11%)	16.7x	(10%)	3.2%	6.9%	6.0%	4th
Neutral	DTE	DTE Energy	$128.79	$141	12%	$6.30	$6.29	$6.56	$6.96	19.6x	(1%)	18.5x	(1%)	2.9%	4.8%	7.0%	1st
Buy	ETR	Entergy Corp	$105.60	$115	12%	$6.29	$5.30	$5.51	$5.82	19.2x	(3%)	18.1x	(3%)	3.4%	-0.1%	2.3%	2nd
Buy	EMA	Emera Inc (C$)	$54.02	$58	12%	$2.87	$2.79	$2.82	$3.02	19.1x	(1%)	17.9x	(1%)	4.4%	3.5%	4.3%	1st
Neutral	AEE	Ameren Corp	$75.98	$83	12%	$3.37	$3.25	$3.52	$3.92	21.6x	9%	19.4x	4%	2.5%	5.4%	6.0%	2nd
Buy	SRE	Sempra Energy	$140.05	$150	10%	$5.57	$5.89	$6.99	$7.55	20.0x	1%	18.6x	(0%)	2.8%	8.9%	8.1%	3rd
Neutral	SO	Southern Company	$55.27	$58	9%	$3.07	$3.03	$3.22	$3.36	17.2x	(13%)	16.5x	(12%)	4.5%	4.0%	3.2%	1st
Neutral	OGE	OGE Energy Corp	$42.74	$45	9%	$2.12	$2.11	$2.33	$2.45	18.3x	(8%)	17.5x	(6%)	3.4%	4.3%	7.0%	3rd
Neutral	CUP	Caribbean Utilities Corp Ltd	$16.35	$17	8%	$0.78	$0.82	$0.85	$0.93	19.1x	(1%)	17.6x	(3%)	4.3%	6.7%	5.7%	3rd
Neutral	AES	AES Corp.	$17.22	$18	8%	$1.22	$1.33	$1.46	$1.61	11.8x	(41%)	10.7x	(43%)	3.2%	8.0%	6.0%	2nd
Neutral	CMS	CMS Energy	$58.26	$61	7%	$2.33	$2.51	$2.68	$2.90	21.7x	9%	20.1x	8%	2.6%	6.8%	7.0%	1st
Neutral	XEL	Xcel Energy	$60.77	$63	6%	$2.47	$2.60	$2.77	$2.95	22.0x	11%	20.6x	10%	2.7%	5.7%	6.0%	2nd
Neutral	WEC	WEC Energy Group	$86.31	$87	4%	$3.34	$3.54	$3.74	$3.97	23.1x	16%	21.8x	17%	2.7%	6.0%	6.2%	1st
Neutral	EVRG	Evergy	$60.79	$61	3%	$2.67	$2.83	$3.07	$3.27	19.8x	(0%)	18.6x	(0%)	3.1%	5.7%	6.2%	3rd
Neutral	PNM	PNM Resources	$49.62	$50	3%	$2.00	$2.16	$2.24	$2.38	22.2x	12%	20.8x	12%	2.3%	5.0%	9.3%	4th
Neutral	LNT	Alliant Energy	$49.93	$49	1%	$2.19	$2.26	$2.49	$2.56	20.1x	1%	19.5x	5%	2.8%	4.6%	6.0%	2nd
Sell	POR	Portland General	$54.61	$52	(2%)	$2.37	$2.48	$2.60	$2.74	21.0x	6%	20.0x	7%	2.8%	5.0%	6.0%	3rd
Sell	H	Hydro One Ltd (C$)	$23.34	$21	(6%)	$1.35	$1.35	$1.30	$1.34	18.0x	(10%)	17.4x	(7%)	4.2%	2.5%	4.7%	4th
Sell	HE	Hawaiian Electric Industries	$44.31	$35	(18%)	$1.85	$1.95	$2.05	$2.16	21.6x	9%	20.5x	10%	2.9%	5.0%	3.2%	4th
Overall Average (unnormalized, inc. Gas Midstream)										18.8x		17.8x					
Electric Utility Normalized (including Gas Midstream)										19.9x		18.6x					

Source: FactSet, UBS Equity Research

Figure 2: Water Utilities Universe

Rating	Ticker	Company	7/19/2019 Price	UBS Price Target	Total Return inc. Div. Yld	UBS 2018A EPS	UBS 2019E EPS	UBS 2020E EPS	UBS 2021E EPS	2021E P/E Ratio	2021E Prem/ Disc	Current Dividend Yield	5 Yr EPS Growth	5 Yr DPS Growth
Buy	AWK	American Water	$114.98	$123	9%	$3.30	$3.57	$3.85	$4.17	27.5x	0%	1.6%	8.2%	10.0%
Neutral	SJW	SJW Group	$64.77	$64	1%	$2.51	$2.14	$2.34	$2.49	26.0x	(5%)	1.9%	2.6%	7.0%
Buy	WTR	Aqua America	$41.00	$42	5%	$1.41	$1.48	$1.58	$1.68	24.5x	(11%)	2.1%	6.4%	7.0%
Sell	CTWS	Connecticut Water Service	$69.57	$67	(2%)	$2.29	$2.39	$2.53	$2.77	25.1x	(8%)	1.8%	6.7%	5.0%
Sell	CWT	California Water Service	$52.60	$44	(15%)	$1.44	$1.39	$1.61	$1.70	30.9x	13%	1.5%	5.7%	5.0%
Sell	AWR	American States Water	$76.02	$57	(24%)	$1.73	$1.98	$2.08	$2.20	34.6x	26%	1.4%	7.8%	6.0%
AVERAGE										27.4x				

Source: FactSet, UBS Equity Research

Figure 3: Independent Power Producers

Rating	Ticker	Company	7/19/2019 Price	Price Target	Total Return inc. Div. Yld	UBS 2018A EBITDA	UBS 2019E EBITDA	UBS 2020E EBITDA	UBS 2021E EBITDA	2020 EV/ EBITDA Ratio	2020 Prem/ Disc	2021 EV/ EBITDA Ratio	2021 Prem/ Disc	2019E Net Debt/ EBITDA
Buy	VST	Vistra Energy Corp	$21.83	$35	63%	$2,760	$3,292	$3,212	$2,654	5.4x	(25%)	6.1x	(10%)	2.9x
Buy	NRG	NRG Energy	$35.14	$46	31%	$2,001	$1,970	$1,821	$1,906	5.8x	(20%)	5.2x	(24%)	2.2x
MID-CYCLE MEDIAN										7.2x		6.8x		

Source: FactSet, UBS Equity Research

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Figure 4: Regulated Utilities & Power 2Q19 Earnings Summary

U.S. companies in US$ Cdn companies in C$ CUP in US$		Quarterly						Annual				
Company	Ticker	Scheduled Reporting Date	2Q19E UBS	2Q19E Consensus	UBS Vs. Consensus	UBS Confidence Indicator[1]	2Q18A Adjusted	2019E UBS	2019E Consensus	UBS Vs. Consensus	Trailing 12 Month	2019E Guidance
ELECTRIC UTILITIES												
AES Corp	AES	6-Aug	$0.25	$0.28	($0.03)		$0.25	$1.33	$1.33	($0.00)	$1.22	$1.28-$1.40
ATCO Ltd	ACO.x-TSE	25-Jul	$0.61	$0.61	($0.00)		$0.53	$3.22	$3.11	$0.11	$3.29	N/A
Alliant Energy	LNT	1-Aug	$0.43	$0.45	($0.02)		$0.43	$2.26	$2.25	$0.00	$2.19	$2.17-$2.31
Ameren Corp	AEE	2-Aug	$0.75	$0.78	($0.03)		$0.97	$3.25	$3.26	($0.01)	$3.31	$3.15-$3.35
American Electric Power	AEP	25-Jul	$0.97	$0.99	($0.02)		$1.01	$4.10	$4.13	($0.03)	$4.14	$4.00-$4.20
Canadian Utilities Ltd	CU-TSE	25-Jul	$0.40	$0.43	($0.03)		$0.39	$2.21	$2.18	$0.03	$2.31	N/A
Caribbean Utilities Corporation Ltd	CUP.USD-TSE	2-Aug	$0.21	$0.21	$0.00		$0.21	$0.82	$0.79	$0.02	$0.84	N/A
CMS Energy	CMS	25-Jul	$0.32	$0.46	($0.14)		$0.48	$2.51	$2.50	$0.01	$2.05	$2.47-$2.51
Consolidated Edison	ED	1-Aug	$0.54	$0.59	($0.05)		$0.61	$4.33	$4.35	($0.02)	$4.27	$4.25-$4.45
Dominion Energy	D	31-Jul	$0.76	$0.79	($0.03)		$0.86	$4.22	$4.19	$0.03	$3.91	$4.05-$4.40
DTE Energy	DTE	24-Jul	$1.17	$1.20	($0.03)		$1.36	$6.29	$6.24	$0.05	$6.29	$5.97-$6.33
Duke Energy	DUK	6-Aug	$0.98	$0.98	$0.00		$0.93	$4.97	$4.92	$0.06	$4.71	$4.80-5.20
Edison International	EIX	25-Jul	$1.21	$1.09	$0.12		$0.85	$4.49	$4.67	($0.18)	$4.31	$4.72-$4.92
Emera Inc	EMA-TSE	12-Aug	$0.52	$0.55	($0.03)		$0.48	$2.79	$2.85	($0.07)	$2.98	N/A
Entergy Corp	ETR	31-Jul	$1.40	$1.36	$0.04		$0.83	$5.30	$5.29	$0.02	$6.57	$5.10-$5.50
Evergy, Inc	EVRG	7-Aug	$0.58	$0.69	($0.11)		$0.90	$2.83	$2.90	($0.06)	$2.36	$2.80-$3.00
Eversource Energy	ES	31-Jul	$0.78	$0.75	$0.03		$0.76	$3.46	$3.46	($0.00)	$3.39	$3.40-$3.50
Exelon Corp	EXC	1-Aug	$0.59	$0.65	($0.06)		$0.71	$3.19	$3.14	$0.05	$2.92	$3.00-$3.30
FirstEnergy Corp	FE	23-Jul	$0.58	$0.61	($0.03)		$0.62	$2.47	$2.51	($0.04)	$2.55	$2.45-$2.75
Fortis Inc	FTS-TSE	2-Aug	$0.56	$0.61	($0.05)		$0.59	$2.54	$2.62	($0.08)	$2.51	N/A
Hawaiian Electric Industries	HE	2-Aug	$0.44	$0.45	($0.01)		$0.42	$1.95	$1.95	$0.00	$1.92	$1.85-$2.05
Hydro One Ltd	H-TSE	9-Aug	$0.26	$0.29	($0.03)		$0.33	$1.35	$1.46	($0.12)	$1.37	N/A
NextEra Energy	NEE	24-Jul	$2.31	$2.29	$0.02		$2.11	$8.43	$8.40	$0.03	$8.18	$8.00-$8.50
OGE Energy Corp	OGE	8-Aug	$0.52	$0.52	($0.00)		$0.55	$2.11	$2.14	($0.03)	$2.05	$2.05-$2.20
PG&E Corp	PCG	26-Jul	$1.16	$0.99	$0.17		$1.16	$3.27	$3.81	($0.54)	$4.13	N/A
Pinnacle West Capital Corporation	PNW	8-Aug	$1.37	$1.55	($0.18)		$1.48	$4.94	$4.85	$0.09	$4.56	$4.75-$4.95
PNM Resources	PNM	2-Aug	$0.37	$0.49	($0.12)		$0.53	$2.16	$2.12	$0.04	$1.77	$2.10-$2.18
Portland General	POR	2-Aug	$0.52	$0.51	$0.01		$0.51	$2.48	$2.45	$0.03	$2.48	$2.35-$2.50
PPL Corporation	PPL	6-Aug	$0.55	$0.58	($0.03)		$0.55	$2.40	$2.43	($0.03)	$2.36	$2.30-$2.50
Public Service Enterprise Group	PEG	30-Jul	$0.58	$0.64	($0.06)		$0.64	$3.22	$3.26	($0.03)	$3.17	$3.15-$3.35
Sempra Energy	SRE	2-Aug	$1.17	$1.21	($0.04)		$1.35	$5.89	$6.04	($0.15)	$5.89	$5.70-$6.30
Southern Company	SO	31-Jul	$0.72	$0.72	$0.00		$0.80	$3.03	$3.02	$0.01	$2.81	$2.98-$3.10
WEC Energy Group	WEC	5-Aug	$0.70	$0.72	($0.02)		$0.73	$3.54	$3.51	$0.02	$3.41	$3.48-$3.52
Xcel Energy	XEL	1-Aug	$0.52	$0.54	($0.02)		$0.52	$2.60	$2.62	($0.02)	$2.51	$2.55-$2.65
Average			**$0.73**	**$0.75**	**($0.02)**		**$0.75**	**$3.35**	**$3.38**	**($0.02)**	**$3.32**	
WATER UTILITIES												
American States Water Company	AWR	TBA	$0.58	$0.55	$0.03		$0.44	$1.98	$1.97	$0.01	$1.73	N/A
American Water Works Company	AWK	31-Jul	$0.89	$0.93	($0.04)		$0.83	$3.57	$3.59	($0.02)	$3.31	$3.54-$3.64
Aqua America	WTR	6-Aug	$0.32	$0.38	($0.06)		$0.37	$1.48	$1.39	$0.09	$1.40	$1.45-$1.50
California Water Service Group	CWT	1-Aug	$0.41	$0.37	$0.04		$0.37	$1.39	$1.40	($0.02)	$1.53	N/A
Connecticut Water Service	CTWS	TBA	$0.68	$0.68	$0.00		$0.59	$2.39	$2.36		$2.22	N/A
SJW Group	SJW	24-Jul	$0.63									
Average			**$0.59**	**$0.58**	**($0.00)**		**$0.52**	**$2.16**		**$0.02**		
IPPS - Adjusted EBITDA not EPS	**US$mlns**											
NRG Energy	NRG	7-Aug	$486	$597	($111)		$517	$2,010	$2,023	($13)	N/A	$1,850-$2,050
Vistra Energy	VST	2-Aug	$718	$688	$30		$653	$3,210	$3,347	($137)	N/A	$3,220-$3,420

1. UBS Confidence Indicator: Green = high confidence in estimate vs. consensus; Red = low confidence in estimate vs. consensus; Yellow = mid confidence in estimate vs. consensus

2. Not meaningful. UBS estimate and company guidance reflect UPO-only earnings.

3. UBS estimates reflected above remove the estimated NRG Yield assets results from prior and current quarter and consensus for comparison purposes as they were sold on 8/31/18

Source: FactSet, company filings, UBS Equity Research

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Regulated Utilities 2Q19 preview

Key Calls this Quarter

AES Corp. We expect a discussion of development in Vietnam of 450 TBTU of LNG capacity and 2 GW of combined cycle gas or projects totalling $3B. The projects could come on-line in the 2023-2025 timeline. AES would look to use partner equity in the project while still growing net income up to $100M in our estimation.

Alliant Energy. With intervenor testimony in the IP&L rate case 8/1 the company may be in a position to comment. An update on 2020 equity needs will wait until the third quarter call.

Ameren Corp. We expect a discussion on Missouri renewables and financing needs. We raised our assumption for 2019 equity need to $700M from $500M due to the acquisition of an incremental 400 MW if wind.

American Electric Power. Management could discuss the North Central Wind Energy facilities at SWEPCO and PSO which total 1,485 MW and represent $2B in rate base. The company could use up to 50% equity to finance these projects which would provide for $0.07-$0.10/share of accretion. Another topic is the numerous rate cases in which the company is involved including Arkansas, Indiana, Michigan, and Texas.

CMS Energy. Despite a light Q2'19 ($0.32E versus $0.48 last year) we believe there is a reasonable bridge to 2019 guidance of $2.47-$2.51 due to the absence of reinvestment spending in 2018 which could add $0.23/share along with contingency.

DTE Energy. We look for a discussion of how the company thinks about the company's 5 year forecast at the Gas, Pipelines & Storage segment and plans to spend $4-$5B.

Edison International. With wildfire legislation having passed in California the company could raise its forecast of capital needs for its contribution to the wildfire insurance fund from the $1.5B equity need discussed on the first quarter call. EIX stands out as one of the potential beats versus consensus due to $0.22/share of rate relief.

Emera Inc. We expect EMA to spend time on the call on August 12 discussing the Maine intervenor testimony filed in the pending EmeraMaine sale to ENMAX at the Maine Public Service Commission on August 5 and provide an update on the process.

FirstEnergy. We expect FE to maintain 2019 EPS guidance of $2.45-$2.75 but following a Ohio Supreme Court decision they are collecting the Distribution Modernization Rider subject to refund.

OGE Energy. We expect investors to revive the issue of dividend payout although we do not necessarily expect news beyond the previously stated policy of 10% annual growth in the dividend through 2019.

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Weather

Weather was broadly milder year over year in the second quarter, with weather in all regions below normal and the country 4% below normal on degree days. Regionally the West North Central Region, Middle Atlantic, and East North Central region experienced the fewest degree days versus normal for the quarter, while the Pacific region and the Southeast had the closest to normal weather experience. Year over year, the Middle Atlantic, Mountain, Pacific, and East North Central regions were down the most, while the East & West South Central regions were actually better year on year and the West North Central region was flat.

Figure 5: 2Q19 Regional Degree Days

Q2'19 Degree Days (April , May, June)	2Q19	2Q18	2Q Normal	2Q19 vs. 2Q18	2Q19 vs. Normal
New England	927	966	1,055	-4%	-12%
Middle Atlantic	749	885	945	-15%	-21%
East North Central	858	961	1,072	-11%	-20%
West North Central	947	951	1,232	0%	-23%
South Atlantic	883	747	900	18%	-2%
East South Central	809	758	960	7%	-16%
West South Central	961	880	1,073	9%	-10%
Mountain	756	886	823	-15%	-8%
Pacific	693	811	741	-15%	-6%
United States	4,882	4,778	5,073	2%	-4%

Source: NOAA, UBS

We also looked at the states that had the biggest shifts in year-on-year weather. We sorted them on the largest percentage change although 2Q degree days are not that significant in some areas.

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Figure 6: Top 10/Bottom 10 States' Change in Degree Days

Q2'19 Degree Days	2Q19	2Q18	2Q Normal	2Q19 vs. 2Q18	2Q19 vs. Normal
Oregon	62	47	29	32%	114%
Washington	62	53	28	17%	121%
Delaware	436	373	264	17%	65%
Alabama	771	697	568	11%	36%
Maryland	407	368	263	11%	55%
Florida	1,234	1,120	1,010	10%	22%
Louisiana	959	894	838	7%	14%
Georgia	713	678	516	5%	38%
Mississippi	776	743	657	4%	18%
South Carolina	760	737	550	3%	38%
Kansas	323	590	395	-45%	-18%
Utah	94	173	144	-46%	-35%
Illinois	193	356	256	-46%	-25%
North Dakota	108	203	124	-47%	-13%
Minnesota	115	232	143	-50%	-20%
Wyoming	33	74	60	-55%	-45%
Colorado	59	155	60	-62%	-2%
Michigan	69	182	156	-62%	-56%
Wisconsin	61	182	133	-66%	-54%
Maine	6	25	29	-76%	-79%

Source: NOAA, S&P Global Market Intelligence, UBS

Electric Utilities

- **AES.** We expect flat EPS in Q2'19 at $0.25 and the company's growth to be more back-end loaded this year with OPGC II in India coming on line in the second quarter and renewable capacity funded by tax equity in the fourth quarter. Otherwise the Changuinola outage in Panama is a negative driver though in guidance as are asset sales. On the positive side we expect similar drivers to Q1'19 like cost cuts, the Dominican Republic and the U.S. utilities. Despite a light first half AES is in position to make the full year due to start-ups of new renewable capacity primarily in the United States and of the OPGC II coal plant in India.

Figure 7: AES 2019 Earnings Drivers

	2019E	Q1'19A	Q2'19E	Q3'19E	Q4'19E	Comments
Prior Year Start		$0.28	$0.25	$0.35	$0.36	
Asset Sales		-$0.04	-$0.03	-$0.01	-$0.01	
Tax rate		$0.01	$0.01	$0.00	-$0.01	30% for the year
Dominican Republic				$0.02		Absence of outage
Argentina			-$0.01			
Panama			-$0.01			Hydro, outage
Panama, Colon				$0.01	$0.01	Tank vs. floating storage
OPGC II			$0.01	$0.01	$0.01	Start-up of operations
Renewables				$0.03	$0.03	Start-up of operations
Parent Interest		$0.01	$0.01			
SBUSs Other		$0.02				
Sensitivities, F/X			$0.01	$0.01		Interest rates
Other			$0.01			
UBS 2019 Forecast	$1.33	$0.28	$0.25	$0.42	$0.39	
Tax rate 2018			36%	28%	24%	

Source: Company reports, Factset, UBS Equity Research

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- **ACO.** We see ATCO Ltd earnings in line with 2Q'18 at C$0.61. Year over year earnings drivers will be from the S&L business segment where seasonally the largest contributions are in the 2nd and 4th quarters. S&L growth to the full year run rate is expected to be more back-end loaded in 2019 due to the ramp at construction facilities as work force has begun ramping up in the quarter. Year on year, earnings are likely to be higher at S&L vs. 2Q'18 related to the close of the Mexico acquisition in late February. The production factory in Chile was completed in 2Q'18 and could contribute year over year. Sanctioning of new projects related to LNG Canada, Coastal GasLink, and the Silvertip Mine, among others are still ramping up and likely to contribute more in the back half of the year vs. the 2Q. The Naltume Ports acquisition was closed in September 2018 and will be a year on year contributor at the expected run rate of about C$4mln/qtr. Given the ownership stake in Canadian Utilities, earnings will also be impacted by the drivers discussed for that company, which are provided below.

- **LNT.** We see LNT's Q2'19 EPS flat at $0.43 versus $0.43 in Q2'18. The absence of above normal weather in Q2'18 is -6 cents and weather was below normal this year. Rate relief at WP&L should add 5 cents and interim rate relief at IP&L could add 8 cents. IP&L wind going into service at the end of March could add 2 cents. Negative drivers are depreciation and interest expense including $600M at IP&L at rates of 3.0-3.6%.

Figure 8: LNT Q2'19 EPS Drivers

	Q2'19E	Q1'19A	Q2'18A
IP&L	$0.26	$0.23	$0.22
WP&L	$0.19	$0.28	$0.17
Utils & Corp	$0.45	$0.52	$0.41
ATC	$0.03	$0.03	$0.03
Non-utility	-$0.03	-$0.02	-$0.01
Total	$0.43	$0.53	$0.43
Shares MM	238	237	232

Q2'18	$0.43
Weather to normal	-$0.06
Weather below normal	-$0.02
IP&L interim rates	$0.08
WP&L rates	$0.05
IP&L wind in service	$0.02
IP&L depreciation	-$0.02
Interest expense-unregulated	-$0.02
Interest expense-regulated	-$0.02
Q2'19	$0.43

Source: Company reports, Factset, UBS Equity Research

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- **AEE.** We look for a decline in AEE's EPS in Q2'19 to $0.75 from $0.97. A normalized Q2'18 is $0.74 with normal weather (-$0.19/share), Callaway outage timing (-$0.09/share) and Missouri taxation (+$0.04/share). Otherwise we see $0.02 from Ameren Transmission rate base growth and $0.03 from Ameren Illinois Electric and Gas growth offset by -$0.04 for below normal June weather in Missouri and other expenses of -$0.02/share.

Figure 9: AEE Q2'19 EPS Drivers

Q2'18	$0.97
Weather to normal	-$0.19
(10 year not 30 year average)	
Callaway	-$0.08
Missouri taxation	$0.04
Normalized Prior Year	$0.74
Q2'19 Drivers	
Ameren Transmission rate base	$0.02
Ameren Illinois rate base	$0.03
Ameren Illinois electric ROE impact	-$0.01
Below normal weather, other	-$0.04
Q2'19	$0.75

Source: Company reports, Factset, UBS Equity Research

- **AEP.** We expect a small decline in AEP's EPS in Q2'19 to $0.97 from $1.01. We expect a decline of $0.12 to normal weather. Rate relief likely added $0.09/share or $0.06 to Vertically Integrated and $0.03 to T&D Utilities. O&M and depreciation increases reduced EPS by $0.05 or more.

Figure 10: AEP Q2'19 Earnings Drivers by Segment

	Q2'19E	Q1'19A	Q2'18A	
Adjusted Earnings	$0.97	$1.19	$1.01	Earnings Drivers
Vertically Integrated	$0.50	$0.63	$0.56	Normal weather -12 cents
				Rates +6, D&A -3, O&M -1
T&D Utilities	$0.23	$0.32	$0.23	Rates +3 cents, O&M -1, D&A
AEP Trans Holdco	$0.26	$0.25	$0.21	
Gen & Marketing	$0.04	$0.09	$0.05	
Corp & Other	-$0.06	-$0.10	-$0.04	

Source: Company reports, Factset, UBS Equity Research

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- **CMS.** We see a decline in CMS' EPS in Q2'19 to $0.32 from $0.48. Michigan experienced below normal weather versus an $0.11/share positive in Q2'18. Carrying costs that we expect the company can pick-up in electric and gas rate case recovery such as depreciation, interest and taxes was potentially a -$0.05/share impact or more. We also look for a decline at CMS Enterprises from lower sales and revenue. Positives include rate case margins (25% of revenue) which add $0.06/share and other items. We believe the company can meet EPS guidance due to reinvestment in 2018.

Figure 11: CMS Q2'19 EPS Drivers

	2019E	Q1'19A	Q2'19E	Q3'19E	Q4'19E	Comments
Prior Year Start		$0.86	$0.48	$0.59	$0.40	
Weather		$0.08				
Storm Costs		-$0.10				
O&M reinvestment				$0.07	$0.16	Absence of '18 impact
Rates & Investment		$0.03				
Usage, Enterprises & Other		-$0.12				
Weather to normal			-$0.11	-$0.12	-$0.01	Absence of '18 impact
Weather			-$0.03			
Rate case recoverable costs (D&A, interest)			-$0.05			
Debt, parent dilution			-$0.01			
Enterprises sales and revenue			-$0.04	$0.04	$0.04	
Gain on asset sales			$0.03			
Electric Rate Case			$0.06	$0.06	$0.06	
Gas Rate Case					$0.13	Effective 10/1
Taxes			-$0.02			
Other			$0.01	$0.01	$0.01	Charitable, other
UBS 2019 Forecas	$2.48	$0.75	$0.32	$0.65	$0.79	

Source: Company reports, Factset, UBS Equity Research

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- **CU.** We expect investors on the conference call to want to discuss the potential use of proceeds given the company's announced sale of the Alberta Power business and the Alberta Power Line. We anticipate that management will reiterate the focus to potentially target utility or utility like infrastructure or long term contracted assets that would provide not only adequate capital returns but also geographic diversity outside of Alberta. For scale once the asset sales are closed we would expect acquired assets could range in the C$1 – C$3Bln range and that the higher end of that range could require preferred equity financing. A larger scale transaction would be possible but management would likely seek a financial partner in such a scenario. For the quarter we expect earnings of C$0.40 versus C$0.39 last year. We anticipate that management will report the Alberta Power and Alberta Powerline segments as assets held for sale, but include them in both reported and adjusted earnings. The quarterly results will be most impacted by significantly lower Alberta power prices in the C$30/MWh range due to mild June and July weather vs. warm weather in 2Q '18. Regulatory decisions in Alberta for the transmission and pipeline segments will be +C$2mln year on year, and the electric transmission application order will book make up revenue of ~C$13mln for 2018 and ~C$4mln for Q1'19 as well as the Q2'19 impacts in the quarter. Other topics of interest for the call will be the IT common matters decision and how that ties to the sale of IT services in as well as the approval of the Hanna transmission project.

- **CUP.** We expect Caribbean utilities to report an in-line quarter at $0.21. Year over year drivers will be increased usage from economic growth mostly driven by likely increased overnight tourism visits and increased financial sector activity. In 1Q'19 customer growth was 2% year on year with 5% usage growth leading to 4% sales growth overall. Year over year the revised rates for large commercial demand customers that were awarded in June 2018, as well as the 1.8% rate increase under the RCAM mechanism will have an impact. Further we expect slight reductions in financing and operating costs year on year.

- **ED.** We see lower EPS for ED in Q2'19 at $0.56 versus $0.61 last year. 3 considerations are: 1) Steam added 3 cents in Q2'18 which unlikely to occur; 2) Stagecoach earnings sharing steps down to 50% from 60% starting 6/6; and 3) An increase in the stock price has a negative impact on the mark to market which was -4 cents as a reference in Q1'19. In Q2'18 CECONY earned a 9.6% ROE although comp mark-to-market could contribute to reducing that to 9.0% which would be a -3 cent reduction. Other drivers include a reduction in the Clean Energy Businesses ($0.06 versus $0.09) potentially offset by cost control.

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Figure 12: ED Q2'19 EPS Summary

	Q2'19E	Q1'19A	Q2'18A	Earnings Drivers
CECONY	$0.45	$1.28	$0.48	Q2'18 was 9.6% ROE and 48% equity ratio equity dilution, comp -3
O&R	$0.02	$0.10	$0.02	
CEBs	$0.06	-$0.04	$0.09	
CET	$0.04	$0.04	$0.04	StageCoach 50% of Crestwood not 60% start 6/6
Parent	$0.00	$0.01	-$0.02	
Total	$0.54	$1.39	$0.61	Reflects share dilution
Shares MM	327	322	311	

Source: Company reports, Factset, UBS Equity Research

D. We expect D to report adjusted EPS of $0.76 vs. consensus of $0.79, and 2Q'18 results of $0.86. The guidance range for the quarter is $0.70-$0.80. Negative yr/yr drivers include a Millstone refueling outage (historical cost range is $0.07-$0.09), share dilution (approx. $0.16), assets sales and more normal weather. Positive yr/yr drivers include the earnings contribution from the Southeast Energy Group ($0.18 before financing considerations) and rate base earnings growth. Beyond the earnings and regular business report, we expect investors to focus on updates around the Atlantic Coast Pipeline and Supply Header. While an order from the 4th Circuit addressing the biological opinion is expected in early August (90 days after oral arguments), the more important US Supreme Court decision on whether to take up the case won't be issued till late 2019.

- **DTE.** We forecast lower EPS for DTE in Q2'19 at $1.17 versus $1.25 last year. We see 3 adjustments in Q2'18 which are: 1) Weather was $0.17 above normal and this year was unseasonably cold; 2) There will be 1.5 months of the DTE Electric rate increase which we forecast as a 25% margin and 3) Rate base expenses are up to -$10M after-tax per quarter for DTE Electric and DTE Gas combined. We also see some impact from the absence of NEXUS AFUDC and depressed volumes.

Figure 13: DTE Q2'19 EPS and Net Income Summary (Dollars in Millions)

	Q2'19E	Q1'19A	Q2'18A	Earnings Drivers
DTE Electric	$150	$147	$163	Weather -$31M to normal and Q2 was cold Rate relief +$30M; Rate base costs -$10M
DTE Gas	$10	$151	$14	Volume weighted impact $47M rate increase rate-base costs -$3M; tax timing reveral -$10M
GS&P	$50	$48	$60	Lower volumes; absence of AFUDC but on track
P&I	$33	$26	$43	1/3 of result to guidance
Corp & Other	-$35	-$3	-$41	1/3 of result to guidance
Energy Trading	$5	$5	$8	
DTE Energy	$214	$374	$247	
EPS	$1.17	$2.05	$1.36	
Shares MM	182	182	181	

Source: Company reports, Factset, UBS Equity Research

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- **DUK.** We expect DUK to report adjusted EPS of $0.98 vs. consensus of $0.98 and 2Q'18 results of $0.93. Earnings in the quarter should benefit from better than normal weather, load growth, new rates (SC) and incremental rate base (Citrus County & Rosamont). Midstream will show modest growth (AFUDC) and the commercial renewables segment should show a marked improvement over Q1 as the shape of earnings from that segment adjust. Beyond earnings and guidance, we expect investors to focus on legislative and coal ash updates from North Carolina, the Atlantic Coast Pipeline and the legal appeal of the rate decision in South Carolina.

- **EIX.** We forecast Q2'19 EPS for EIX of $1.21 versus $0.85 last year. The big driver is $0.22 from the general rate case which is the company discussed on the Q1'19 investor call. We also expect for the regulatory lag on non-fuel O&M recovery to dissipate. Other positives include transmission rate base growth and lower financing costs. At Edison Energy and Parent we assume -$0.05 versus -$0.06 last year.

Figure 14: Southern California Edison Q2'19 EPS Summary

Q2'18 SCE	$0.91
Rate case	$0.22
O&M	$0.08
Financing	$0.05
FERC	$0.03
D&A & other	-$0.03
Q2'19 SCE	$1.26

Source: Company reports, Factset, UBS Equity Research

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- **EMA.** We expect EMA to report C$0.52 vs. C$0.48 last year. Drivers will be the sale of the New England generation assets year over year and mild weather outside the Southeast will be a drag on results in Maine and on the remaining energy segment. In 2Q'18 the power plants has a pre-interest allocation earnings of C$13.5mln. Interest expense at the plants allocated to corporate was C$6mln. Maine should show better results year on year given non-recurring storm expenses in 2Q'18. Further Maine received a distribution rate increase of US$15.7mln in July of 2018. At Nova Scotia Power, weather has been colder than normal which is a driver of demand for electric heat. However, upside is limited from strong weather as a result of a capped ROE sharing mechanism at 9.25%, which is 25bps above the allowed ROE of 9%. As a result, earnings in 2Q will not be as strong as weather might otherwise indicate. In Florida, unlike most of the United States, weather was favorable vs. last year with the warmest May on record and the tail end of June was also warm. The solar under the SOBRA program now has 405MWs earning returns vs. 145MWs booking AFUDC last year. FX average is also approximately 1.33 vs. 1.29 year on year and each +0.01 in FX is about +C$0.01/share to EMA. On the call we expect investors to be focused on the approval process for the sale of Emera Maine and the management take on the intervenor testimony which will be filed on August 6, vs. the earnings call date of August 12.

- **ETR.** We expect ETR to report adjusted EPS of $1.40 vs. consensus of $1.39 and 2Q'18 results of $1.23. Weather for the quarter should be positive vs. normal, but below last year, while rate increases in Arkansas and Louisiana and rate base growth in Louisiana (St. Charles power station) should all represent yr/yr growth. Our estimate assumes a ratable allocation of targeted O&M savings over the remainder of the year, but we recognize that the actual realization of these savings could be uneven. We expect ETR will update investors on its continued exit from the EWC business, the various proceedings at the regulated entities and any residual impact from the recent hurricane.

- **EVRG.** We forecast Q2'19 Adjusted EPS of $0.58 versus $0.90 pro-forma last year. Weather conditions made a significant swing in the quarter from $0.22/share above normal last year to below normal this year. Deferred taxes was a negative driver as well. Another negative is a reduction in pro-forma merger transaction costs under accounting rules which is a $35-$36M pre-tax change (Q2'18 10-Q p. 66). Positive drivers include plant shutdowns at the end of 2018 (Montrose and Sibley), merger synergies and the share buyback.

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Figure 15: EVRG Q2'19 EPS Drivers

	Q2'19E	Q1'19A	Q2'18A	Earnings Drivers
Pro-forma, adjusted	$0.58	$0.44	$0.90	
Weather to normal	-$0.22	$0.05	$0.22	
Weather	-$0.02			Cooling days 14% below normal
Rates	$0.00	$0.05		
O&M, absence w-off	$0.03	$0.05		
O&M	-$0.10			Reduction in pro-forma transaction costs
D&A	-$0.01	-$0.08		Schedule changes offset in revenue
Tax Rate	-$0.19	-$0.01	$0.19	Change in deferred taxes
Bill Credits	$0.01			3 months versus 5 months
Severance		$0.06		
Plant shutdowns	$0.06			Sibley (400 MW) and Montrose (330 MW)
Merger Synergies	$0.07			
Share buyback	$0.04			
Shares Quarter Ended	247	252		
Avg Shares-MM	250	253	272	
GAAP				
EPS	$0.58	0.39	0.56	
Shares-MM	250	253	181	

Cooling Degree Days	Q2'19	Norm	Q2'18
Missouri	322	354	569
Kansas	323	395	590
Total	645	749	1159
Q2'19 vs.		-14%	-44%

Source: NOAA, Company reports, Factset, UBS Equity Research

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- **ES.** We expect ES to report adjusted EPS of $0.78 vs. consensus of $0.77 and 2Q'18 results of $0.76. We look for ES to benefit modestly from the 2018 CL&P rate case implementation, the transmission rate base true up that occurs in the second quarter, ongoing cost control efforts, the investment portfolio mark and the Nstar Electric rate increase. Offsetting these benefits will be the impact of decoupling at Yankee Gas, higher property tax and interest expense, and the loss of generation earnings. We expect the investor call to focus on incremental growth opportunities (GridMod spending in CT/Mass/NH, offshore wind, water M&A), and changes in regulatory personnel.

- **EXC.** We expect EXC to report $0.59 v. $0.71 last year. Overall this expectation is below the mid-point of the company's $0.55-$0.65 2Q'19 guidance range provided on the 1Q'19 conference call. Factors not incorporated into the guidance range at the time were mild weather impacts at the non-decoupled utilities, especially PECO. Further, the planned outage at the Salem nuclear plant lasted approximately 30 days beyond likely initial projections which would have increased costs by ~$30mln on pre-tax basis. NDT will also likely be a drag quarter over quarter as of the $0.07 of NDT gains in 2018, $0.05 were recorded in 2Q'18. Milder weather is unlikely to impact the nuclear fleet all that much as run times were likely around-the-clock regardless although it could have some small impact on the much smaller non-nuclear generation fleet. Power prices and spreads are lower year on year, however, financial and retail hedging as well as the zero emission credits in New York, New Jersey, and Illinois will protect the majority of the nuclear fleet from significant volatility in EBITDA.

- **FE.** We forecast Q2'19 EPS of $0.58 versus $0.62 last year. Weather to normal was -3 cents versus last year and conditions were below normal this year. The absence of a renewable energy credit is a -3 cent item too. Offsetting that is cost cuts and rate base growth. This compares to the company's $0.55-$0.65 guidance for the quarter.

Figure 16: FE Q2'19 EPS (Dollars in Millions)

	Q2'19E	Q1'19A	Q2'18A	Earnings Drivers
Adjusted Earnings	$0.58	$0.67	$0.62	
Regulated Distribution	$0.50	$0.62	$0.55	Weather -3 cents to normal and below normal in 2019; renewable credit reversal -3 cents, D&A -1 to -2 cents, FE Tomorrow +1 cents
Regulated Transmission	$0.21	$0.19	$0.19	+2-3 cents of rate base growth
Corporate/Other	-$0.13	-$0.13	-$0.12	

Source: Company reports, Factset, UBS Equity Research

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- **FTS.** We expect that consistent with Q1'19 reporting Fortis will report results excluding mark to market impacts from the Aitken Creek storage facility and adjust prior periods to exclude them as well. As a result 2Q '18 will be restated to C$0.59. For the current quarter we expect lower earnings year on year of C$0.56 mainly driven by significantly milder weather in Arizona. Further 2Q'18 included nonrecurring items related to the positive hydrology impacts in Belize and the Hurricane Irma insurance receipts. Offsetting this will be rate base and sales growth as well as positive timing impacts related to the timing of plant outages in Arizona. Lastly, the sale of the Waneta hydroelectric plant will have a greater than anticipated drag on the quarterly results as the majority of earnings contribution was seasonally in the second quarter. We expect that on the call investors will be focused on execution of any potential incremental capital projects that could increase or extend current growth rates, and any updates on the Federal Energy Regulatory Commission transmission ROE review process and the ongoing rate case for Tucson Electric Power in Arizona.

- **HE.** We expect HE to report adjusted EPS of $0.44 vs. consensus of $0.45 and 2Q'18 results of $0.42. Yr/Yr earnings will benefit from interim rates at Maui Electric ($12.2mm; effective Aug '18) and the interim recovery mechanism (MPIR) for the Schofield project. We expect Bank earnings to benefit from asset sales and lease expirations at some point this year (3-5 cents) but believe these will be one time benefits. We expect the earnings conference call to focus on the regulatory climate and proceedings in Hawaii, and capital spending opportunities.

- **H.** We expect H to report C$0.26 v. C$0.32 last year, mainly driven by milder weather year on year. Peak loads in Ontario in May were down 20% year on year and overall peak loads were down 9% quarter over quarter. Further, there were significant storm costs in Ontario in 2Q'18 which are helpful to earnings as they are capitalized, so lack of storm costs will likely increase O&M year on year given a return to normal work patterns. Further, lack of storms has likely allowed for an acceleration of work related to maintenance and vegetation management which would also increase O&M year on year. Further, interest expense will tick a bit higher given the term out of C$1.5Bln in debt issued in April 2019, composed of C$700mln at 2.54% due 2024, C$550mln at 3.02% due 2029, and C$250mln at 3.64% due 2050. On the call we expect investor focus to be on any improvement in controllable costs, the recently announced changes to the Board of Directors, and any insights into the status of the change out of several senior management positions, and how new CEO Mark Poweska's strategy for the company continues to evolve.

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- **NEE.** We expect NEE to report $2.31 v. $2.28 last year. Year over year we anticipate drivers at FPL to be new investment growth (+$0.07). The acquisition of Gulf Power will also be additive year on year (+$0.10). At NEER, results will be driven by growth for existing assets (+$0.08) and increased earnings due to new investments related to execution of the backlog (+$0.05). Offsetting these positive drivers will be share dilution (-$0.05), and lower results at Corp & Other (-$0.12). We expect not much of an update informationally on the conference call versus the recently held Analyst Day in New York. Investors will be focused on any updates on wind backlog at NEER, and any insights into the further integration efforts for recently acquired Gulf Power.

- **OGE.** We forecast a decline in Q2'19 EPS at OGE to $0.52 from $0.55 last year. The absence of above normal weather is -5 cents and we estimate the impact of below normal conditions (particularly June) in Oklahoma was -2 cents. That said July has started off well and OGE is on track for the year.

Figure 17: OGE Q2'19 EPS Summary

OGE EPS Summary			
	Q2'19E	Q1'19A	Q2'18A
OGE	$0.52	$0.24	$0.55
OG&E	$0.41	$0.14	$0.46
OGE Energy Holdings	$0.12	$0.12	$0.11
Hold Co.	-$0.01	-$0.01	-$0.02

OG&E Earnings Drivers	
Q2'18	$0.46
Weather to normal	-$0.05
Below normal	-$0.02
Rate design	$0.01
AFUDC/D&A	-$0.01
Interest expense	$0.01
O&M	$0.01
Q2'19	$0.41

Source: Company reports, Factset, UBS Equity Research

- **PCG.** PCG will report Q2'19 EPS results on July 26 and we see $1.16 versus $1.16 last year. Tax timing is a regular driver for the company that nets to zero for the year. The company began to record formula rates for the 2020 transmission rate case on May 1. PG&E requested a 12.5% ROE. There was not a nuclear outage in the quarter.

Figure 18: PCG Q2'19 EPS Summary

PCG Q2'18	$1.16
Tax timing	-$0.05
Non-fuel O&M	-$0.02
Shares	-$0.01
Rate base	$0.04
Reduction in insurance	$0.04
PCG Q2'19	$1.16

Source: Company reports, Factset, UBS Equity Research

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- **PNM.** We expect PNM to report adjusted EPS of $0.37 vs consensus of $0.49 and 2Q'18 results of $0.53. Our estimate is consistent with guidance issued by the company of $0.36-$0.38 on 7/12 which reflects substantially milder temperatures in the service territory during the second quarter. We expect investor attention will focus on the company's earning profile through the remainder of the year, weather trends that have been observed quarter to date and the contributing factors to the revised annual guidance.

- **PNW.** We expect PNW to report Q2'19 EPS of $1.37 versus $1.48 last year. There are some significantly negative drivers including a decline in cooling degree days 28% from 2018 and 30% versus normal (about 130 days). In Q1 PNW had 1.0% weather normalized sales growth which could continue. Other drivers include several timing related items versus last year like pension and transmission income. PNW also provides guidance on quarterly outage spending.

Figure 19: PNW Q2'19 EPS Summary

Q2'18	$1.48
O&M	$0.10
Sales	$0.02
LFCR	$0.01
Interest	$0.01
Depreciation	-$0.02
Outage O&M	-$0.03
Transmission	-$0.04
Pension	-$0.05
Weather	-$0.11
Q2'19	$1.37

Source: Company reports, Factset, UBS Equity Research

- **POR.** We forecast flat EPS in Q2'19 of $0.52 versus $0.51 last year. The absence of plant O&M should add 4-5 cents and normal weather conditions adds 2 cents. We don't see much of a story here for the quarter.

Figure 20: POR Q2'19 EPS Summary

Q2'18	$0.51
Weather	$0.02
Carty	$0.03
Plant O&M maintenance	-$0.04
Rate case	$0.03
Q2'19	$0.52

Source: Company reports, Factset, UBS Equity Research

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- **PPL.** We expect flat EPS for PPL in Q2'19 at $0.55 versus $0.55 last year. At a high level we see +3 cents from F/X hedges (1.41x UK sterling to US dollar) for the company's U.K. utility and Kentucky rate relief offset by non-fuel O&M and weather.

Figure 21: PPL Q2'19 EPS Summary

	Q2'19E	Q1'19A	Q2'18A	Earnings Drivers
EPS	$0.55	$0.70	$0.55	
Pennsylvania	$0.11	$0.16	$0.11	Weather -1 cent, Transmission +1
Kentucky	$0.12	$0.17	$0.12	Rates +2 cents, weather -1
U.K.	$0.37	$0.42	$0.36	F/X +3 cents, O&M -2 cents
Other	-$0.03	-$0.05	-$0.04	
Shares MM	728	723	698	

Source: Company reports, Factset, UBS Equity Research

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- **PEG.** We expect PEG to report $0.58 v. $0.65 last year. One of the key drivers will be timing related to tax reform impacts for excess deferred income taxes. This factor was +$0.05 in 1Q'19 and we expect that to reverse out in 2Q'19. On the PEG Power side both the Keys Energy Center and Sewaren 7 were put into service in late 2Q '18 and will add 1,300MWs of capacity to the generation fleet for the majority of the quarter year over year. Zero Emission Credits were also put into place in New Jersey in April 2018 and will be a positive driver of results as they will have a full quarter of impact in 2Q'19. However this positive impact is likely to be mostly offset by lower capacity prices year over year as prices reset on the June 1 capacity year. Last year capacity prices were $205/MW-day on 9,600MWs of capacity while this year pricing as of June 1 was $115/MW-day on 9,000MWs of capacity. Capacity prices in New England were also lower ($2.31/kW-month vs. $3.14/kW-month) despite capacity being +500MWs for the new capacity year. Re-contracting will also be a headwind to results as PEG management indicated a $3/MWh drag although because of seasonal impacts we expect a lower drag on results in 2Q than the ($0.08) seen in 1Q'19. Off-system sales for gas will be lower year over year due to milder weather, and results will be impacted by outage timing as the planned outage at the Salem nuclear facility extended by a likely 30 days beyond projected timelines. However, the Salem plant is only 50% owned by PEG whereas Hope Creek had an outage in 2Q'18 and that plant is 100% owned by PEG. D&A and interest expense are projected to tick higher due to the new plant in service. At the utility we expect the transmission formula rate to be +$0.03 year on year, and despite the distribution rate increase settled on Nov 1 expect that to not have large impacts in 2Q given seasonality of load. Changes to OPEB will add roughly +$0.01 as in 1Q'19 and there will be some incremental benefit from the operating contract at LIPA booked in parent & other. Interest expense will be up slightly at parent and other for the $750mln at 2.875% in debt issued on June 1 slightly offset by the retirement of $350mln at LIBOR +80bps earlier in the quarter.

- **SRE.** We expect SRE to report $1.17 v. $1.21 last year mainly driven by continued drag related to the GRC decision in California. A final decision would be retroactive to 1/1/19 but cannot be booked until received. Our latest expectation for GRC resolution in year-end 2019. We expect interest expense to be slightly higher given issuances of $400mln at SDE&G and $390mln at SoCalGas at around 4%. Offsetting the drag somewhat are likely to be increased earnings for the pipeline program and energy efficiency awards. At Oncor results should be higher year on year related to the close of the InfraREIT transaction on 5/16, although volumes are likely to be lower on milder weather in ERCOT. At South America there were no one-time items in 2Q'18 although there will likely be an FX drag year on year. In Mexico the Peso averaged 19.9 to the USD at 2Q'19 vs. 18.3 at Q2'18 versus hedged levels of 20.72. The TDN plant is uncontracted into the SoCal market and SP15 pricing is down year over year. Renewables will have negligible to no impact in the quarter as the transaction with AEP is now closed. LNG and midstream will continue to be a little bit of a drag on results as expected until the completion of the Cameron LNG facility. We expect corporate and other to be roughly in-line with 1Q'19. There will likely be slightly higher interest expense related to $700mln in debt issuance at 7.5% year over year and the proceeds from the storage and wind sale of $500mln paid off short term debt at a 2.5% - 3% rate.

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- **SO.** Southern reported $0.80 in 2Q'18 and issued guidance for 2Q'19 on their first quarter call of $0.71 versus our estimate of $0.72. The main drivers year over year will be the divestitures of the Florida assets to NextEra Energy. In 1Q'19 this was a ($0.11) year over year impact, and we anticipate about a ($0.09) impact in 2Q'19. Another significant driver will be weather as April was significantly milder than normal, May was a touch warmer than normal, and June was cooler than normal all vs. warmer than normal weather last year. Management may be able to shift O&M timing to mitigate some of the negative impact of cooler weather. PowerSecure in Puerto Rico was a ($0.03) drag in Q1 '19 and we would expect a slightly smaller drag in 2Q'19. Higher share count will also be a year on year negative driver. We expect lower interest expense year on year given the debt retired with the proceeds of the Florida assets sales, and expect sales and rate base growth to also be positive drivers in the quarter. On the call we expect investors will be focused on the ongoing Vogtle new nuclear project (the Georgia PSC staff comments on the project rebasing are due the same day as the earnings call), as well as other regulatory matters in Georgia. While the integrated resource plan will be settled by the time of the call, most of the financial implications of the IRP will be determined within the context of the Georgia Power general rate case which was filed at the beginning of the month. Hearings for the GRC begin on September 30th and we expect the biggest discussion points to be around return on equity and coal ash mitigation spending and recovery. We see the Atlanta Gas Light rate case as less potentially contentious and view the Mississippi Power rate case to be filed in November potentially positive given two of the three commissioners in that state have decided to not stand for reelection.

- **WEC.** We expect WEC to report toward the low end of their 2Q'19 guidance range of $0.70-$0.72 at $0.70 vs. $0.73 last year and consensus estimates of $0.72. Weather will be a driver as both heating degree days and cooling degree days are down year over year, and 2Q'18 results included a +$0.04 impact for above normal weather. Upstream Wind and Bishop Hill have come online year over year and Presque Isle's retirement will save about $40mln in O&M on an annualized basis although that will be weighted away from the 2Q shoulder period. The RICE units came on-line at the end of March and will be $8-$10mln additive to O&M year over year. Management guided to a 3%-4% reduction in O&M in 2019 vs. 2018 but that could be lumpy throughout the year vs. a normalized +$0.02 per quarter. ATC also had a non-recurring charge in 2Q'18 of $3.7mln on a FERC Audit which will be +$0.01 year on year. There were several debt issuances year on year, and at the Hold Co. there was $350mln issued at 3.1% due 2022 while late in '18 $250mln was retired at 1.65%, which will be a slight increase in interest expense year over year.

- **XEL.** We expect XEL to report adjusted EPS of $0.52 vs. consensus of $0.54 and 2Q'18 results of $0.52. Yr/yr earnings should benefit from higher rates in Minnesota/Colorado/New Mexico, and improved O&M management vs. Q1'19. These benefits will be offset by weather which we estimate was either close to, or below normal during the quarter (vs. a $0.04 benefit in Q2'18).

Water Utilities

Following a traditionally slow start to the year, water use and capital investment tends to pick up for the group in the second and third quarter. We expect earnings growth at AWR as a result of new rates and higher Contracted Services. AWK will

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continue to benefit from the Pivotal acquisition, and rate increases. Both WTR and SJW results will be negatively impacted by share dilution, while CWT and CTWS will report largely in line with consensus.

- **AWR.** We expect AWR to report adjusted EPS of $0.58 vs consensus of $0.55 and 2Q'18 results of $0.44. Growth in the quarter is driven by modest growth at the Water utility (new rates), and higher earnings at Contracted Services.

- **AWK.** We expect AWK to report adjusted EPS of $0.89 vs consensus of $0.93 and 2Q'18 results of $0.83. Rate increases are expected to provide growth in the quarter, offset by slightly higher expenses. The Pivotal acquisition, which closed after 1Q'18 should contribute to be a positive year-over-year variance.

- **WTR.** We expect WTR to report adjusted EPS of $0.32 vs consensus of $0.38 and 2Q'18 results of $0.37. Quarter over quarter earnings growth is driven by rate increases and normal customer growth, which will be more than offset by share dilution. We expect a gain in the quarter associated with the closing of an interest rate hedge ($11mm gain) to be adjusted out of given its one time nature. An ALJ recommendation in the company's pending acquisition is expected by the end of August, with a final PSC decision in late October.

- **CWT.** We expect CWT to report adjusted EPS of $0.41 vs consensus of $0.37 and 2Q'18 results of $0.37. Quarterly earnings benefit from higher rates in CA, WA and HI, that will be somewhat offset by higher expenses. This year is the third year of CQT's rate case cycle in CA, which usually generates the largest gap in cost recovery.

- **CTWS.** We expect CTWS to report adjusted EPS of $0.68 vs consensus of $0.68 and 2Q'18 results of $0.59. Earnings in the quarter will benefit from rate increases in Connecticut and Maine. Our estimates exclude the impact of merger related costs.

- **SJW.** We expect SJW to report adjusted EPS of $0.63 vs consensus of $0.56 and 2Q'18 results of $0.72. Earnings in the quarter benefit from higher rates in California, however, this benefit is more than offset by higher expenses and share dilution.

Independent Power Producers

- **NRG.** We expect NRG to report adjusted EBITDA of $486mln vs. $843mln last year and the main driver of the results to be the asset sales of renewables, NYLD, and the South Central assets year over year. We do believe consensus is too high as estimates continue to not be seasonally weighted enough to the third quarter which is not fully reflected of NRG's more ERCOT heavy business mix post asset dispositions. Further, booking generation to retail transfer pricing on an expected average basis over the course of the year, naturally weights earnings to the third quarter. While actual power prices were significantly lower year over year, we expect NRG's matched generation and retail book to have significantly reduced volatility of EBITDA in the quarter. Forward curves are also lower by $2-$4/MWh which lowers the mark to market of EBITDA forecasts in future years. However, key to the conference call will be discussion of the expansion of retail margins as generation margins decline and the true sensitivity of future year's EBITDA to changes in the forward curves. Disclosed hedging levels for NRG at 1Q'19 were 93%/82% in ERCOT/PJM for

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the balance of 2019 and 56%/35% in ERCOT/PJM for 2020. Also on the call management could begin to further discuss the "retail-lite" strategy around contracting assets under purchased power agreements which would further lower volatility of EBITDA and cash flows.

- **VST.** We expect VST to report adjusted EBITDA of $718mln vs. $653mln last year. We believe consensus is too low as the Dynegy acquisition has led to a diversity of the portfolio outside of ERCOT, and therefore less seasonality of results toward the third quarter. Further, given the higher generation prices at which management hedged the third quarter earlier in the year, and the booking of actual transfer price experience between retail and generation throughout the year, we expect this year to have greater retail margins in Q1,Q2, and Q4 and thinner retail margins in Q3. This was discussed in detail by management on the 1Q'19 conference call. While VST is more exposed than NRG to the reduction in power prices on the forward curve given their 50% retail to generation match, we also expect management to address the lower volatility of EBITDA and cash flows to forward curve changes than in the past given in place hedging and offsetting expansion of retail margins. Hedging disclosures on the 1Q'19 call showed for ERCOT 100%/100% for natural gas; 94%/52% for heat rates for '19/20 respectively. Outside of ERCOT hedge levels were 74%/94%/95% and 37%/32%/67% on volumes in '19/20 for MISO/CAISO, NENY, and PJM respectively. On the call investors will also likely focus on the recent close of the Crius acquisition and what incremental factors management has learned since owing the business.

Figure 22: Power Price Comparisons ($/MWhr)

ISO	Hub	2Q '19	2Q '18	Change
ISO NE	Internal Hub	24.02	31.02	(6.99)
NYISO	Zone G	20.98	28.52	(7.54)
PJM	AEP-Dayton	24.38	34.94	(10.57)
PJM	Eastern	22.48	29.92	(7.44)
PJM	N Illinois	22.19	26.08	(3.89)
PJM	PSEG	21.54	27.95	(6.41)
PJM	Western	24.07	33.76	(9.69)
MISO	Indiana	25.23	33.16	(7.93)
MISO	Michigan	25.67	32.20	(6.52)
ERCOT	North	25.09	27.76	(2.67)
ERCOT	Houston	26.28	28.08	(1.79)
ERCOT	West	23.34	22.60	0.73
CAISO	NP15	21.18	24.56	(3.37)
CAISO	SP15	21.64	24.87	(3.23)

Source: S&P Global Market Intelligence, UBS Equity Research

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Figure 23: Spark Spread Rate Trends ($/MWh)

Period	ISO	Hub	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7
Q219	ISO NE	Internal Hub	$ 10.92	$ 12.49	$ 11.90	$ 8.72	$ 5.71	$ 6.54	$ 6.20
Q218	ISO NE	Internal Hub	$ 11.70	$ 11.51	$ 12.28	$ 10.45	$ 10.67	$ 8.00	$ 8.53
		Change	$ (0.78)	$ 0.97	$ (0.38)	$ (1.73)	$ (4.96)	$ (1.47)	$ (2.33)
Q219	PJM	Eastern	$ 13.60	$ 12.36	$ 11.82	$ 11.69	$ 11.24	$ 11.12	$ 11.54
Q218	PJM	Eastern	$ 16.40	$ 14.33	$ 15.30	$ 15.28	$ 15.04	$ 14.21	$ 13.97
		Change	$ (2.80)	$ (1.97)	$ (3.48)	$ (3.59)	$ (3.80)	$ (3.09)	$ (2.42)
Q219	PJM	Western	$ 14.47	$ 15.50	$ 14.61	$ 14.53	$ 14.28	$ 13.66	$ 14.08
Q218	PJM	Western	$ 16.73	$ 18.05	$ 18.63	$ 18.35	$ 17.96	$ 17.42	$ 17.17
		Change	$ (2.25)	$ (2.55)	$ (4.03)	$ (3.81)	$ (3.68)	$ (3.77)	$ (3.09)
Q219	ERCOT	Houston	$ 22.74	$ 22.67	$ 20.44	$ 17.41	$ 15.01	$ 12.05	$ 9.39
Q218	ERCOT	Houston	$ 30.04	$ 23.69	$ 22.11	$ 19.84	$ 16.66	$ 14.49	$ 10.59
		Change	$ (7.30)	$ (1.02)	$ (1.67)	$ (2.43)	$ (1.65)	$ (2.44)	$ (1.21)

Source: S&P Global Market Intelligence, UBS Equity Research

Alternative Energy 2Q19 preview

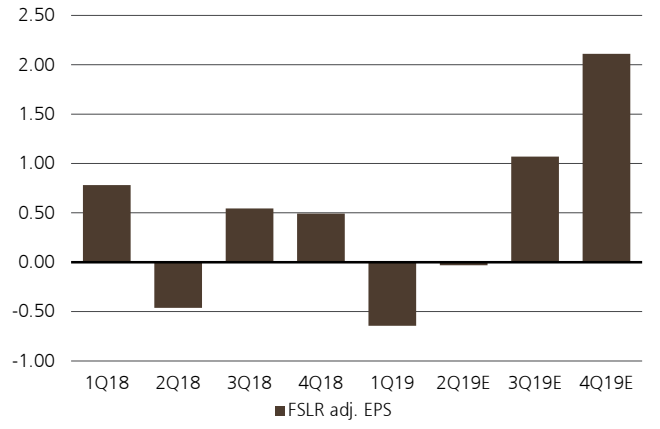
Key issues for the quarter

For Buy rated FSLR and TPIC we expect relatively weak 2Q19 results ahead of an inflection in y/y and sequential earnings growth in 3Q19.

FSLR is nearing the end of its manufacturing transition to Series 6, which is expected to drive increased production capacity and margin expansion. Despite ~breakeven EPS for FSLR being flagged on the 1Q earnings call we expect volatility in the stock on results.

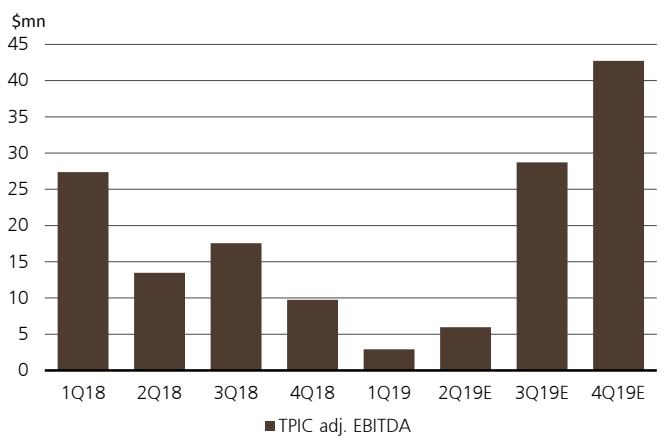
For TPIC, the company was impacted by one-off labor and production issues in 1H19 which offset the positive tailwind from manufacturing line transitions and startups. We model a significant earnings ramp starting in 2H19 through 2020, but expect 2Q19 adj. EBITDA of just $6mn, down 56% y/y. We expect a key focus to be on maintained 2020 financial targets.

Figure 24: FSLR 2018-2019 quarterly adj. EPS



Source: Company reports, UBS estimates

Figure 25: TPIC 2018-2019 quarterly adj. EBITDA



Source: Company reports, UBS estimates

For the module manufacturers we expect stronger than previously expected China solar demand in 2019 to support potential upward guidance revisions for 2019

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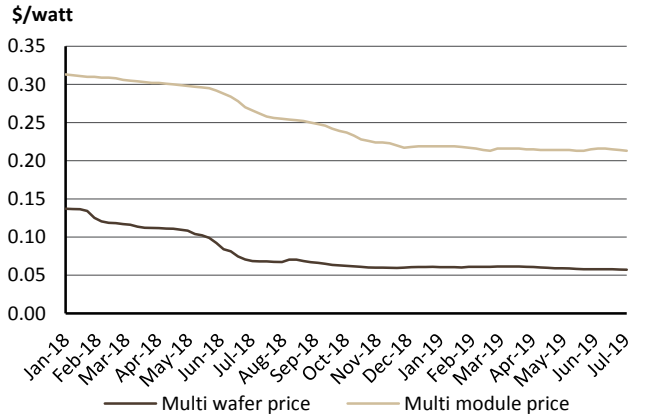
module shipments, particularly for the Chinese exposed names CSIQ and JKS. Please see China Utilities Analyst Alex Liu's recent note: NEA: 50GW solar projects to start construction in 2019.

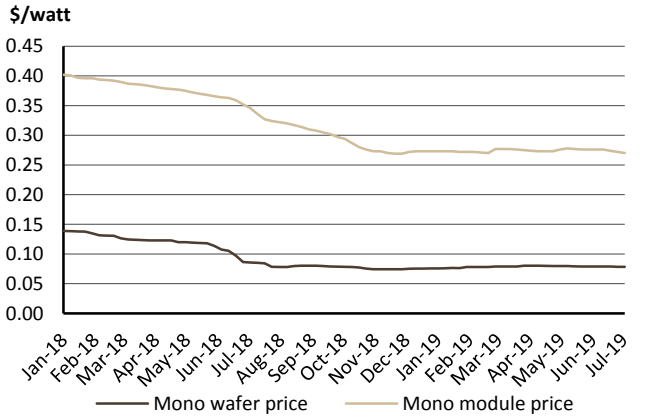
Commodity multi silicon module pricing declined just 1% q/q in 2Q19 while multi silicon wafer pricing declined 3.7% over the same period. Pricing for mono silicon modules increased 0.4% q/q, while mono wafer pricing increased 1.9% q/q suggesting continued strong demand for high efficiency solar products. We expect the increased input costs for mono wafer to result in potential 2Q19 margin pressure for JKS which has a relatively larger proportion of capacity dedicated to mono. Please see: Downgrade to Neutral.

Figure 26: Multi silicon wafer and module ASP, $/watt



Source: PV Insights, UBS research

Figure 27: Mono silicon wafer and module ASP, $/watt



Source: PV Insights, UBS research

Company specific focus areas

- **FSLR**: We expect a 2Q19 loss of $3mn ($0.03/sh) driven by Series 6 ramp and start up charges, while approximately 75% of Series 6 2019 sales will occur in 2H. Consensus 2Q19 adj. EPS is currently $0.00/sh. We currently forecast 2H19 adj. EPS of $3.18/sh compared to 1H19 adj. EPS of ($0.67)/sh. 4Q19 Series 6 cost per watt is expected to be 30% lower than 1Q19 cost. We also look for an update on FSLR's progress restructuring its EPC organization to ease labor constraints and equipment supply issues. As of the 1Q19 earnings call FSLR had sold 50% of 1Q21 capacity with new bookings in the mid-$0.30/watt range. We expect strength in bookings demand for 2021 deliveries could increase the likelihood of FSLR converting its 3rd Malaysia manufacturing facility to Series 6, a development we would view positively.

- **SPWR**: We expect a slowdown in 2Q19 residential solar installations in the CA market driven by abnormally wet weather. SPWR's residential business is relatively more weighted to the CA market compared to other national installers as a result of its leading share in the CA new homes market. SPWR had previously guided to 60-70MW of residential deployments for 2Q19 and 280-310MW deployments for the full year. We expect a key focus will be on any development in potential sources of funding for both NGT manufacturing capacity expansion and safe harboring of modules to capture the full 30% investment tax credit in 2020 and beyond as SPWR had expected to begin executing on financings in 2H19.

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- **CSIQ**: 2Q19 guidance is for 1.95-2.05GW module shipments, $970-1,010mn revenue, and 13-18% gross margin (16-18% excluding impact of low margin Mustang solar project sale). We see potential upward bias to 2019 guidance which is currently 7.4-7.8GW module shipments, and revenue $3.5-3.8bn due to China National Energy Administration's announcement that it expects 50GW of solar to begin construction in 2019. See: NEA: 50GW solar projects to start construction in 2019. We also look for an update on the status of CSIQ CEO Dr. Shawn Qu's medical leave of absence. Yan Zhuang, SVP, COO, and President of the MSS segment has stepped in as acting CEO.

- **JKS**: JKS has secured 70% of orders for 2H19 providing relatively good demand visibility for the rest of the year. JKS is well positioned to benefit from stronger solar demand from China in 2H19 driven by finalization of 2019 solar subsidy policy. However, we expect gross margin to be lower than the 16.6% 1Q19 margin due to ongoing manufacturing capacity expansion and a higher contribution from lower-margin sales in the China market. We expect 2019 capex of $450mn for mono wafer and PERC cell capacity expansion. 2Q19 guidance is for shipments of 3.2-3.3GW and gross margin between 14-15%, with a high level of confidence given JKS reported 1Q19 earnings on 28 June.

- **RUN**: We expect abnormally wet weather in CA to contribute to a sluggish 2Q for residential solar installations, however RUN is less exposed to the CA market than peer SPWR. RUN previously provided 2Q19 deployment guidance of 102-104MW and FY2019 deployment growth guidance growth of 16-18%. RUN highlighted 100% y/y growth in the Brightbox storage business in 2019. The ramp in storage is likely to continue to drive higher customer acquisition cost given the higher entry price for solar with attached storage. For more on RUN's battery storage strategy in our note: Value stacking residential storage.

- **SEDG**: Focus will be on the status of SEDG's manufacturing ramp in a new Vietnam facility which is expected to provide tariff-free inverter supply to the North America market. 2Q19 guidance was previously provided for revenue $310-320mn, gross margin of 32-34%, and solar product gross margin of 33-35%. We expect revenue from the acquired SMRE, Kokam, and Gamatronic businesses will see gradual sequential q/q revenue growth in 2019 from supply chain and channel sales improvements, and guidance implies 2Q19 non-solar revenue of $20mn. By YE19 we expect acquired revenues to comprise less than 10% of sales.

- **HASI**: Long term core EPS growth guidance of 2-6% off a 2017 baseline remains intact implying core EPS of $1.37 in 2019 at the midpoint. We model 2Q19 core EPS of $0.34.

- **ORA**: We forecast 2Q19 adj. EPS of $0.36 and adj. EBITDA of $90mn reflecting typical seasonality of electricity generation. 2Q results are also expected to include $4mn of business interruption insurance proceeds related to the Puna plant. Current 2019 guidance is for revenue of $720-742mn and adj. EBITDA of $370-380mn.

- **TPIC**: Slower than expected replacement hiring and training time in Mexico has led to production delays and triggered significant liquidated damages which are expected to continue through 3Q19 (included in the $25mn Mexico related reduction). We model a significant earnings ramp starting in 2H19 through 2020, but expect 2Q19 adj. EBITDA of just $6mn, down 56% y/y. We expect a key focus to be on maintained 2020 financial targets.

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Figure 28: Alternative Energy key estimates

Company	Ticker	Quarterly				Annual		
		Scheduled Reporting Date	2Q19E UBS	2Q19E Consensus	UBS Vs. Consensus	2019E UBS	2019E Consensus	UBS Vs. Consensus
ALTERNATIVE ENERGY								
Sunpower	SPWR	July 30 est.	($0.16)	($0.16)	$0.00	($0.30)	($0.42)	$0.12
Hannon Armstrong	HASI	Aug 2 est.	$0.34	$0.34	$0.00	$1.39	$1.39	($0.00)
SolarEdge	SEDG	Aug 2 est.	$0.77	$0.83	($0.06)	$3.09	$3.18	($0.09)
First Solar	FSLR	Aug 6 est.	($0.03)	($0.00)	($0.03)	$2.51	$2.44	$0.06
TPI Composites	TPIC	Aug 7	($0.23)	($0.19)	($0.04)	$0.06	$0.02	$0.04
Ormat Technologies	ORA	Aug 7 est.	$0.36	$0.33	$0.03	$1.62	$1.68	($0.07)
SunRun	RUN	Aug 7 est.	$0.43	$0.25	$0.18	$1.09	$0.60	$0.49
Canadian Solar	CSIQ	Aug 14 est.	$0.66	$0.35	$0.31	$2.20	$2.41	($0.21)
Jinko Solar Holding Company	JKS	Aug 22 est.	$0.37	$0.28	$0.09	$1.93	$2.79	($0.86)

Source: Company reports, Factset, UBS research estimates.

Environmental Services 2Q19 preview

Key issues for the quarter

We expect the majority of investor questions to be focused on the impact of two headwinds to MSW earnings growth: 1) a 64% YTD decline in recycled fiber pricing and 2) a 10% YTD decline in Permian Basin E&P rig count. 2019 guidance, which is typically set in February, largely reflects a "steady state" outlook and we anticipate management commentary to focus on the incremental headwinds from continued commodity price and drilling activity declines. Broadly we see continued above average acquisition activity in 2019 helping to offset these headwinds.

WCN has already flagged a potential $3-5mn EBITDA headwind per quarter due to the decline in E&P activity and $5mn EBITDA headwind per quarter due to commodity price weakness. WCN has the largest E&P exposure of the MSW group at 5% of revenue followed by WM at ~3%.

MSW 2019 guidance is typically updated with 2Q19 results, however given these headwinds we see a bias towards reaffirming existing guidance rather than the historically common beat-and-raise.

We remind investors that MSW was able to overcome a 2018 ~50% y/y decline in recycling prices due to strong underlying macro conditions supporting the ~95% of revenue from the core disposal business. See: UBS Evidence Lab Inside: Housing survey read-throughs for waste volumes, March 2019.

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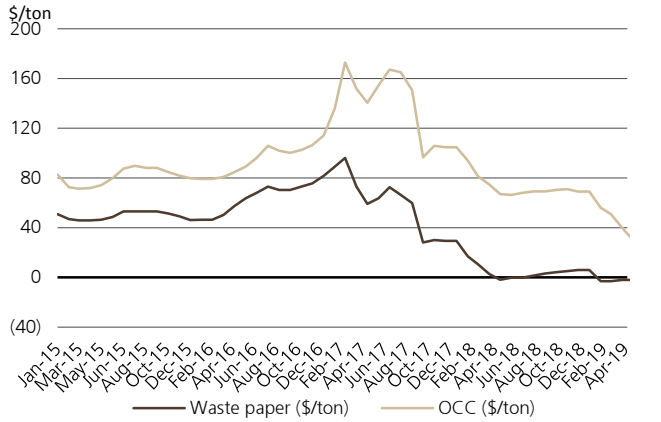
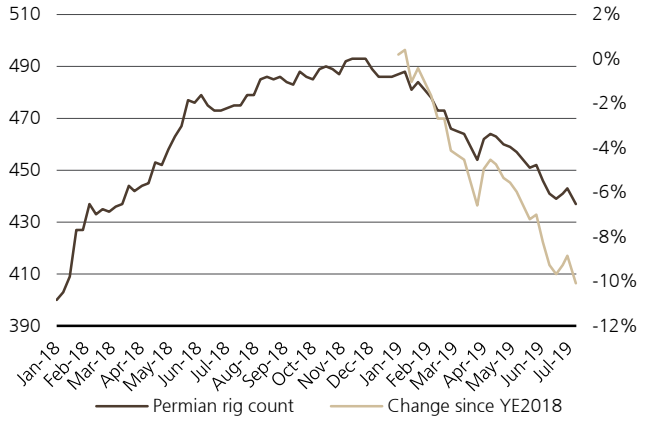
Figure 29: Recycled commodity pricing, $/ton



Source: RISI, UBS Research

Figure 30: U.S. Permian E&P rig count



Source: Baker Hughes, UBS Research

Figure 31: Environmental Services business mix

Metric 2019E	WM	RSG	WCN	ADSW	CWST	CVA
2019 revenue ($bn)	15.5	10.5	5.4	1.6	0.7	1.9
N. American market share	26%	17%	9%	3%	1%	3%
Geographic						
U.S. Northeast	22%	18%	22%	26%	100%	47%
U.S. South	24%	34%	17%	36%	0%	33%
U.S. Midwest	23%	20%	12%	38%	0%	7%
U.S. West	24%	28%	33%	0%	0%	10%
Canada/other	7%	0%	16%	0%	0%	3%
Total	100%	100%	100%	100%	100%	100%
Revenue composition						
Residential collection	16%	19%		25%	17%	0%
Commercial collection	22%	25%		23%	18%	0%
Industrial collection	15%	18%		15%	17%	0%
Total collection	53%	62%	60%	63%	52%	0%
Other operations						
Transfer	9%	11%	10%	10%	9%	10%
Disposal	19%	20%	20%	21%	18%	58%
Recycling	8%	3%	2%	1%	7%	5%
E&P	3%	2%	5%	1%	2%	0%
Other operations	8%	2%	3%	4%	12%	27%
Total	100%	100%	100%	100%	100%	100%
Cost composition						
SGA as % of revenue	9.8%	10.4%	11.0%	11.6%	12.8%	6.2%
Opex as % of revenue	62%	61%	58%	64%	68%	75%

Source: Company reports, UBS research estimates

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Company specific focus areas

- **RSG**: As of the 1Q19 call RSG flagged a $0.07 EPS headwind from recycled commodity pricing assuming current pricing holds. Pricing has since fallen by an additional $15/ton implying potential $0.12/sh total EPS headwind. RSG had previously reiterated 2019 EPS guide of $3.23-3.28 and FCF of $1.125-1.725bn. However the previously increased 2019 M&A spend target of $300mn should help mitigate commodity pricing pressures. RSG's $142mn current YTD spend is expected to contribute $55mn in annualized revenue.

- **WCN**: We revise our 2Q19 adj. EBITDA to $426mn from $436mn previously and our FY2019 adj. EBITDA to $1,708mn from $1,713mn previously. On 4 June WCN flagged 2 potential headwinds to 2Q19 results; first, a $5mn EBITDA headwind from 30% decline in recycled commodity values, second, a $3-5mn EBITDA headwind driven by 10% YTD reduction in E&P rig count.2Q19 guidance was previously provided for revenue of $1,360mn and adj. EBITDA of $434mn. These headwinds are expected to be offset by contribution from acquisitions in 2H19 with WCN still achieving current 2019 adj. EBITDA guidance of $1,705mn. We expect WCN to potentially provide an updated 2019 outlook on the 2Q19 earnings call.

- **CWST**: Since the 1Q19 earnings call CWST has acquired $11.5mn annualized revenue ($18.5mn YTD) and announced an asset purchase agreement to buy RSG waste assets in NY and MA. The asset purchase will add $30mn of annualized revenue and is expected to close by the end of 3Q19. Based on these acquisitions we estimate CWST tracking well ahead of its FY2019 guidance for $152-156mn adj. EBITDA. We forecast 2Q19 adj. EBITDA of $43.3mn (consensus $41.6mn) which should be relatively unaffected by recent commodity price declines given offsetting fees recouped through CWST's SRA program. Recycling adj. EBITDA was up $2mn y/y in 1Q19 driven by these fees.

- **CVA**: We update our 2Q19 adj. EBITDA estimate to $98mn from $112mn previously to reflect a revision to our expected plant maintenance expense in the quarter. The increase in maintenance expense compared to our prior estimate is to account for the impact of the Palm Beach plant which CVA acquired in 4Q18. Maintenance spend is historically heavier in 1H for CVA. Our EPS estimates are revised in-line with the EBITDA change.

- **CLH**: We forecast 2Q19 adj. EBITDA of $151mn or +8.2% y/y, a slowdown from the 15.2% y/y 1Q19 growth due to more difficult y/y comps. We expect earnings to benefit from a business interruption insurance recovery related to CLH's Deer Park facility outage ($3.5mn EBITDA headwind in 1Q19). CLH has been working to reposition some oil inventory to the southern part of U.S. to try to mitigate future shortfalls/transport limitations driven by weather. Closed loop oil sales are tracking to the 15mn gallon target in 2019. Management noted at the UBS Industrials Conference in June that the Environmental Services pipeline was the strongest it has ever been and expect this to drive solid growth through 2020. See: UBS Global Industrials Conference takeaways.

- **ECOL:** We forecast 2Q19 adj. EBITDA of $35mn or +10% y/y driven by contribution from 2018 acquisition activity. ECOL's planned merger with NRCG received FTC antitrust clearance on 16 July and is still subject to approval from both ECOL and NRCG shareholders. The merger faces pushback from certain holders of NRCG's 7.0% Series A Convertible Preferred Stock who have asked NRCG to reconsider the terms for conversion of the preferred stock. We have

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incorporated the contribution from NRCG in our model assuming 31 Dec 2019 deal closure (see: Updating model for NRCG merger).

Figure 32: Environmental Services EPS estimates

Company	Ticker	Quarterly				Annual		
		Scheduled Reporting Date	2Q19E UBS	2Q19E Consensus	UBS Vs. Consensus	2019E UBS	2019E Consensus	UBS Vs. Consensus
ENVIRONMENTAL SERVICES								
Republic Services	RSG	July 25	$0.76	$0.77	($0.01)	$3.27	$3.23	$0.04
Covanta Holding Corp	CVA	July 25	($0.07)	($0.05)	($0.02)	$0.16	$0.22	($0.06)
Waste Connections	WCN	July 29	$0.67	$0.69	($0.02)	$2.71	$2.75	($0.04)
Clean Harbors	CLH	July 31	$0.61	$0.61	($0.00)	$1.77	$1.78	($0.01)
Casella Waste System	CWST	Aug 1	$0.32	$0.27	$0.05	$1.01	$0.85	$0.16
US Ecology	ECOL	Aug 1	$0.58	$0.61	($0.02)	$2.27	$2.24	$0.03

Source: Company reports, Factset, UBS research estimates.

Figure 33: Environmental Services EBITDA estimates ($mn)

Company	Ticker	Quarterly				Annual		
		Scheduled Reporting Date	1Q19E UBS	1Q19E Consensus	UBS Vs. Consensus	2019E UBS	2019E Consensus	UBS Vs. Consensus
ENVIRONMENTAL SERVICES								
Republic Services	RSG	July 25	722	725	-0.4%	2,972	2,955	0.6%
Covanta Holding Corp	CVA	July 25	98	101	-2.8%	444	452	-1.7%
Waste Connections	WCN	July 29	426	431	-1.1%	1,708	1,717	-0.5%
Clean Harbors	CLH	July 31	151	146	3.7%	530	526	0.8%
Casella Waste System	CWST	Aug 1	43	41	3.2%	159	156	2.3%
US Ecology	ECOL	Aug 1	35	36	-3.2%	139	140	-0.5%

Source: Company reports, Factset, UBS research estimates.

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Valuation Method and Risk Statement

Regulated Utilities: Our valuation methodology for the group is price to earnings based. The adjustments applied fall into 5 categories. These are as follows: 1) Group Valuation Bias: Flowing from our valuation work comparing Baa corporate yields to group dividend yields and RU price to earnings ratios to those for the S&P 500, we incorporate a positive or negative adjustment to our group multiple representing the gap we calculate to the nearest 5%; 2) Growth Adjustment: We adjust our valuations based on the growth quartile each utility occupies. First quartile receives a 5% premium, second quartile a 2% premium, third quartile a 2% discount and fourth quartile a 5% discount; 3) Regulatory Adjustment: Our valuation adjustments for regulation are based on our proprietary Regulatory Rankings. First quartile jurisdictions receive 5%, second quartile 2%, third quartile -2% and fourth quartile -5%; 4) Multi Utility Diversified Valuation: For multi utilities (those with more than 15% diversified or foreign earnings), we perform a sum-of-parts analysis applying business/region appropriate valuations to those diversified businesses; 5) One-off Adjustments: In special situations, we value risk on an issue specific basis. Common areas where we apply such an adjustment include: ESG advantage, large project construction risk, legal risk, and announced M&A completion risk. We identify the following risk factors for the sector overall: rising interest rates; regulatory and policy risks; operational risks; construction risks; cybersecurity risk to the transmission grid and/or customer data, and extreme weather events.

Our valuation methodology for the Alternative Energy space is based on a variety of metrics including P/BV, EV/EBITDA, P/E, and retained equity value per share. Our target multiples are derived from historical group averages with adjustments for expected growth rates, leverage, and earnings growth confidence. We identify the following risks for the sector: Demand for new renewable installations has historically been volatile around changes in state and federal policy, and we expect this volatility to continue. In addition, margins for product manufacturers can be impacted by swings in raw materials pricing and the overall level of energy prices.

Our valuation methodology for the Environmental Services space is based on EV/EBITDA with adjustments made to the target EV/EBITDA multiple based on relative growth rates, Free Cash Flow (FCF) conversion, expected earnings stability, and the general level of risk and our confidence in future earnings estimates. We identify the following risks for the sector: Housing remains a key driver of incremental municipal solid waste volume growth, and a slowdown in new housing starts could put downward pressure on sales growth. In addition, pricing tends to follow GDP growth, and a slowdown in economic growth could drive lower ability to raise pricing driving potential contraction in margins. For more industrial-exposed names, swings in commodity prices can impact the overall level of waste-generating activity, contributing to earnings volatility.

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Required Disclosures

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	45%	30%
Neutral	FSR is between -6% and 6% of the MRA.	40%	28%
Sell	FSR is > 6% below the MRA.	15%	20%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 June 2019.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

KEY DEFINITIONS:Forecast Stock Return (FSR) is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months. In some cases, this yield may be based on accrued dividends. **Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium). **Under Review (UR)** Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation. **Short-Term Ratings** reflect the expected near-term (up to three months) performance of the stock and do not reflect any change in the fundamental view or investment case. **Equity Price Targets** have an investment horizon of 12 months.

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UBS Securities LLC: Daniel Ford, CFA; Jon Windham, CFA; Ross Fowler, CFA; Gregg Orrill; Paul Cole; William Grippin, CFA.

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Company Disclosures

Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
AES Corp[16]	AES.N	Neutral	N/A	US$17.22	19 Jul 2019
Alliant Energy Corp[16]	LNT.O	Neutral	N/A	US$49.93	19 Jul 2019
Ameren Corp[16]	AEE.N	Neutral	N/A	US$75.98	19 Jul 2019
American Electric Power Inc[7, 13, 16]	AEP.N	Buy	N/A	US$90.28	19 Jul 2019
American States Water Co[16]	AWR.N	Sell	N/A	US$76.02	19 Jul 2019
American Water Works Co[16]	AWK.N	Buy	N/A	US$114.98	19 Jul 2019
Aqua America Inc[16]	WTR.N	Buy	N/A	US$41.00	19 Jul 2019
ATCO Ltd	ACOx.TO	Buy	N/A	C$43.24	19 Jul 2019
California Water Service Group[16]	CWT.N	Sell	N/A	US$52.60	19 Jul 2019
Canadian Solar Inc[6c, 7, 13, 16, 20a]	CSIQ.O	Neutral (CBE)	N/A	US$20.94	19 Jul 2019
Canadian Utilities Ltd	CU.TO	Neutral	N/A	C$35.78	19 Jul 2019
Caribbean Utilities Corp	CUPu.TO	Neutral	N/A	US$16.35	19 Jul 2019
Casella Waste Systems Inc[2, 4, 6a, 16]	CWST.O	Neutral	N/A	US$42.15	19 Jul 2019
Clean Harbors Inc[16]	CLH.N	Neutral	N/A	US$70.99	19 Jul 2019
CMS Energy Corp[16]	CMS.N	Neutral	N/A	US$58.26	19 Jul 2019
Connecticut Water Service Inc[16]	CTWS.O	Sell	N/A	US$69.57	19 Jul 2019
Consolidated Edison Inc[16]	ED.N	Neutral	N/A	US$87.24	19 Jul 2019
Covanta Holding Corp[4, 16]	CVA.N	Neutral	N/A	US$17.54	19 Jul 2019
Dominion Energy Inc[6c, 7, 16, 26a]	D.N	Buy	N/A	US$76.85	19 Jul 2019
DTE Energy Co[7, 16]	DTE.N	Neutral	N/A	US$128.79	19 Jul 2019
Duke Energy Corp[4, 6a, 7, 16]	DUK.N	Buy	N/A	US$88.45	19 Jul 2019
Edison International[7, 16]	EIX.N	Buy	N/A	US$70.17	19 Jul 2019
Entergy Corp[7, 16]	ETR.N	Buy	N/A	US$105.60	19 Jul 2019
Evergy, Inc[16]	EVRG.N	Neutral	N/A	US$60.79	19 Jul 2019
Eversource Energy[7, 16]	ES.N	Buy	N/A	US$76.77	19 Jul 2019
Exelon Corp[7, 16]	EXC.N	Buy	N/A	US$47.57	19 Jul 2019
First Solar Inc[16]	FSLR.O	Buy	N/A	US$66.53	19 Jul 2019
FirstEnergy Corp[16]	FE.N	Buy	N/A	US$43.49	19 Jul 2019
Fortis Inc[7, 16]	FTS.TO	Buy	N/A	C$51.58	19 Jul 2019
Hannon Armstrong Sustainable Infra[2, 4, 6a, 13, 16]	HASI.N	Neutral	N/A	US$27.53	19 Jul 2019
Hawaiian Electric Industries Inc[16]	HE.N	Sell	N/A	US$44.31	19 Jul 2019
Hydro One	H.TO	Sell	N/A	C$23.35	19 Jul 2019
JinkoSolar Holding Co Ltd[13, 16]	JKS.N	Neutral	N/A	US$20.23	19 Jul 2019
NextEra Energy Inc[2, 4, 6a, 7, 16, 26c]	NEE.N	Buy	N/A	US$209.73	19 Jul 2019
NRG Energy Inc[7, 16]	NRG.N	Buy	N/A	US$35.14	19 Jul 2019
OGE Energy Corp[16]	OGE.N	Neutral	N/A	US$42.74	19 Jul 2019
Ormat Technologies Inc[16]	ORA.N	Neutral	N/A	US$63.15	19 Jul 2019
PG&E Corp[7, 16, 20b]	PCG.N	Neutral (CBE)	N/A	US$17.79	19 Jul 2019
Pinnacle West Capital Corp[7, 16]	PNW.N	Neutral	N/A	US$93.59	19 Jul 2019
PNM Resources Inc[7, 16]	PNM.N	Neutral	N/A	US$49.62	19 Jul 2019
Portland General Electric Co[16]	POR.N	Sell	N/A	US$54.61	19 Jul 2019

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
PPL Corp[4, 6a, 6b, 6c, 7, 16]	PPL.N	Buy	N/A	US$30.17	19 Jul 2019
Public Service Enterprise Group[7, 16]	PEG.N	Buy	N/A	US$60.18	19 Jul 2019
Republic Services Inc[13, 16, 26b]	RSG.N	Neutral	N/A	US$87.11	19 Jul 2019
Sempra Energy[4, 6a, 6c, 7, 16]	SRE.N	Buy	N/A	US$140.05	19 Jul 2019
SJW Group[2, 4, 6a, 16]	SJW.N	Neutral	N/A	US$64.77	19 Jul 2019
SolarEdge Technologies Inc[16]	SEDG.O	Buy	N/A	US$63.37	19 Jul 2019
Southern Co[2, 4, 6a, 6b, 7, 16]	SO.N	Neutral	N/A	US$55.27	19 Jul 2019
SunPower Corp[13, 16, 20a]	SPWR.O	Neutral (CBE)	N/A	US$10.99	19 Jul 2019
Sunrun Inc[16, 20a]	RUN.O	Neutral (CBE)	N/A	US$19.77	19 Jul 2019
TPI Composites Inc[16]	TPIC.O	Buy	N/A	US$26.22	19 Jul 2019
US Ecology Inc[16]	ECOL.O	Neutral	N/A	US$62.24	19 Jul 2019
Vistra Energy Corp[2, 4, 6a, 16]	VST.N	Buy	N/A	US$21.83	19 Jul 2019
Waste Connections Inc[16]	WCN.TO	Buy	N/A	C$123.55	19 Jul 2019
Waste Connections Inc[16]	WCN.N	Buy	N/A	US$94.58	19 Jul 2019
WEC Energy Group Inc[16]	WEC.N	Neutral	N/A	US$86.31	19 Jul 2019
Xcel Energy Inc[16]	XEL.O	Neutral	N/A	US$60.77	19 Jul 2019

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date

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bcobrien@aquaamerica.com Ben O'Brien 07/24/19 02:14:58 PM Aqua America Inc

Aqua America Inc

Downgrade to Neutral; Valuation reflects attractive fundamentals & strong prospects; PT to $45

Equities

Americas
Water Utilities

12-month rating	**Neutral** *Prior: Buy*
12m price target	**US$45.00** *Prior: US$42.00*
Price	**US$42.06**

RIC: WTR.N **BBG:** WTR US

Trading data and key metrics

52-wk range	US$42.06-32.37
Market cap.	US$7.50bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	302
Avg. daily value (m)	US$12.3
Common s/h equity (12/19E)	US$2.15bn
P/BV (12/19E)	3.5x
Net debt / EBITDA (12/19E)	5.1x

EPS (UBS, diluted) (US$)

	12/19E			
	From	To	% ch	Cons.
Q1	0.28	0.28	0	0.28
Q2	0.32	0.25	-22	0.25
Q3E	0.47	0.47	0	0.39
Q4E	0.41	0.43	3	0.38
12/19E	1.48	1.48	0	1.41
12/20E	1.58	1.58	0	1.57
12/21E	1.68	1.68	0	1.67

WTR has tightened the valuation gap vs. peers

Since the announcement of the Peoples Gas acquisition (10/18), the completion of the associated equity financing (4/19) and successful progression through its regulatory calendar, WTR has closed the relative valuation gap to its peer group by 25%. While we are raising our valuation target to reflect our confidence in both the business model and management execution, we are lowering our rating to Neutral from Buy to reflect the lower total potential return profile.

Q2 Adjusted EPS in line with market expectations

WTR reported Q2'19 adjusted EPS of $0.37/share vs. UBSe $0.32/sh, consensus $0.38/sh, and 2Q'18 of $0.37/sh. The adjusted EPS excludes merger-related expenses of $11.9mm (net of tax), comprising of a loss on the extinguishment of debt ($18.9mm), transaction related expenses ($12.7mm), a favourable mark-to-market adjustment on the settlement of interest rate swaps ($11mm) and interest income ($7.4mm). Fundamentals of the core business remain strong, with quarter over quarter revenue growth of 3.3%, and relatively flat O&M expenses.

Guidance and growth forecast reiterated; strong acquisition pipeline

In conjunction with its Q2'19 earnings report, WTR reaffirmed its full year earnings guidance of $1.45-$1.50/sh, infrastructure investment target of $550mm for 2019 ($269 invested 1H) and $1.4 billion through 2021, annual rate base growth of 7% and total customer growth of between 2% and 3%. The acquisition pipeline is strong; WTR announced exclusive discussions with the Delaware County Regional Water Control Authority (DELCORA, serves approximately 500,000 people, PA) and the purchase of the Campbell, Ohio water system (3,200 customers). Including DELCORA, the pipeline of potential water and wastewater acquisitions WTR is pursuing has approximately 400,000 customers in four states the company already serves.

Valuation: $45 Price Target

We are raising our PT to $45 from $42. The PT is predicated on a 3% discount to the average water group multiple of 27.4x, applied to our 2021e EPS of $1.68. The modest discount multiple reflects the blended gas/water business model. Our prior PT of $42 was premised on a 3% discount to a group average multiple of 25.2x.

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Highlights (US$m)	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
Revenues	820	810	838	881	921	956	995	1,033
EBIT (UBS)	326	329	337	370	399	425	454	482
Net earnings (UBS)	234	240	251	265	281	299	319	342
EPS (UBS, diluted) (US$)	1.32	1.35	1.41	1.48	1.58	1.68	1.79	1.92
DPS (US$)	0.74	0.79	0.88	0.94	1.00	1.07	1.15	1.23
Net (debt) / cash	(1,891)	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)

Profitability/valuation	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
EBIT margin %	39.7	40.6	40.3	42.0	43.3	44.5	45.6	46.7
ROIC (EBIT) %	9.0	8.4	7.9	8.0	8.0	8.1	8.3	8.4
EV/EBITDA (core) x	16.2	17.0	17.6	19.2	18.4	17.7	17.0	16.1
P/E (UBS, diluted) x	23.9	24.8	25.0	28.3	26.7	25.1	23.5	22.0
Equity FCF (UBS) yield %	0.2	(1.6)	(1.6)	(1.8)	0.2	0.5	0.8	1.2
Net dividend yield %	2.3	2.4	2.5	2.2	2.4	2.6	2.7	2.9

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$42.06 on 07 Aug 2019 16:43 EDT

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UBS Research THESIS MAP a guide to our thinking and what's where in this report

PIVOTAL QUESTIONS

Q: Has WTR's earnings and growth outlook changed, 2019-2021?

We are not changing our '19-'21 earnings estimates of $1.48/$1.58/$1.68/share. These estimates are consistent with WTR's rate base growth target of 7% through 2021, also reflecting the guidance of modest accretion in the first calendar year for the Peoples acquisition. We believe the Peoples acquisition is likely to receive final approval (PA) in the autumn given the close to unanimous settlement with parties to the proceeding (all but 2 parties either signed on, or agreed not to oppose). WTR's absolute growth profile should improve as Peoples rate base growth (8%-10%) outpaces WTR's by 100-300 basis points on the deployment of capital to improve aging infrastructure.

Q: Can WTR be successful as a combined water and gas utility company?

Yes. We believe WTR can successfully lever its regulatory, operating and cost management experience to combine with Peoples Gas while continuing to execute on its infrastructure improvement commitments and customer growth ambitions. Acquisition and integration are key skill-sets that WTR has developed through its ongoing muni acquisition program.

UBS VIEW

WTR's share price reflects the value of its combined regulated water and gas business model. We impute a modest discount of 3% vs. the water peer group average P/E to reflect the premium regulatory jurisdictional exposure, Fair Value profile and blending of a lower multiple for the gas business. 2019 should be a transition year for WTR as it closes the Peoples acquisition (autumn) and concludes the Peoples rate case (autumn). Beginning in 2020, we expect to see continued focus on municipal water acquisitions and possible realization of merger benefits.

EVIDENCE

PA is currently WTR's largest jurisdiction, with ~69% of rate base; therefore the growth outlook in PA tends to be indicative for the company overall. Additional sources of growth include organic customer growth, which averages ~1%/yr and a steady diet of tuck-in acquisitions. In 2019/2020, WTR estimates adding approximately 20k new customers. We estimate the Peoples acquisition to be ~neutral to EPS in 2020 and accretive over time as Peoples rate base growth outpaces WTR's.

WHAT'S PRICED IN?

WTR has tightened the relative valuation gap vs its peers by 25% since announcing the proposed acquisition of Peoples and completing the associated equity financing. Once the Peoples transaction is closed, we look for WTR to trade at roughly a 3% discount to the average Water P/E on 2021e EPS of $1.68, or $45, representing upside of ~12% including the 2.26% dividend yield.

UPSIDE / DOWNSIDE SPECTRUM

Value drivers	Peer Avg. P/E Multiple	Premium/discount	EPS CAGR '19-'21	2021e EPS
$49 upside	29.0x	0.0%	7.0%	$1.70
$45 base	26.5x	-3.0%	6.0%	$1.68
$34 downside	21.0x	0.0%	5.0%	$1.62

Source: UBS

more→

COMPANY DESCRIPTION

Aqua America, Inc. provides regulated utility water and wastewater services to approximately 972,000 customers in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey,...

more →

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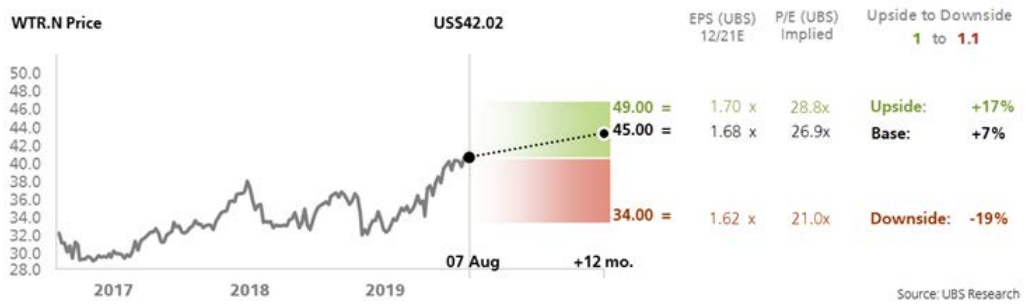
UPSIDE / DOWNSIDE SPECTRUM

return ↑



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$34 downside	21.0x	0.0%	5.0%	$1.62

Source: UBS

Risk to the current share price is heavily skewed (1:1.1) to the upside

Upside (US$49): Our upside scenario is predicated upon a 0% premium applied to a 29.0x P/E multiple, which reflects the average small cap peer group multiple. We also assume the 2019–2021 earnings growth rate is 100 basis points higher than our base case estimates, matching the rate base growth forecast proposed by the company.

Base (US$45): Our base case is predicated upon a 3% discount applied to the average water utility P/E multiple on WTR standalone 2021e EPS. We estimate the Peoples acquisition could be neutral to ~$0.03 accretive to 2021e EPS. The 3% discount reflects the net of: 5% discount to account for the water group average multiple near historical highs relative to the broad market, 5% premium for WTR's regulatory jurisdiction ranking, 6% premium for the seven Fair Market Value states in which WTR operates, and a 9% discount to reflect the impact of 30% of earnings derived from lower multiple gas assets.

Downside (US$34): Our downside scenario is predicated on the trough absolute average water utility P/E experienced since 1/1/18. We also assume the 2019–2021 earnings growth rate is 100 basis points lower than our base case estimates which would reflect a failure to execute on incremental tuck in acquisitions.

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COMPANY DESCRIPTION

return ↑

Aqua America, Inc. provides regulated utility water and wastewater services to approximately 972,000 customers in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana, and Virginia. Operations in Pennsylvania account for approximately 52% of revenues and 74% of net income. Aqua Resources provides unregulated services such as operating and maintenance contracts with municipal authorities and other parties, as well as water and wastewater line repair service, Aqua Infrastructure provides unregulated raw water supply services for firms in the natural gas drilling industry.

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Industry outlook

Infrastructure spending and consolidation will continue to be the underlying drivers of industry growth for the next 5-10 years. Capital spending should remain at or near peak levels for the next 12 months, and is forecast to remain elevated through at least 2020. We would expect water utilities to follow the pattern of electric utilities with a bias toward upward revision in the spending forecast. Factors that could increase the pace of consolidation include broader adoption of fair value legislation, enhanced focus on water quality and accountability standards, or macro trends that instigate budgetary pressures or risk-off strategies at the municipal level. We expect conservation and efficiency to continue to reduce the trend of water usage nationally, and drought could be a disruptive event regionally.

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Forecast returns

Forecast price appreciation	+7.0%
Forecast dividend yield	2.3%
Forecast stock return	+9.3%
Market return assumption	6.6%
Forecast excess return	+2.7%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 3% discount to the 2021 average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 9% discount to reflect impact of lower P/E associated with gas earnings.

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	45%	30%
Neutral	FSR is between -6% and 6% of the MRA.	40%	28%
Sell	FSR is > 6% below the MRA.	15%	20%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 June 2019.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
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UBS Securities LLC: Daniel Ford, CFA; Paul Cole.

Company Disclosures

Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Aqua America Inc[16]	WTR.N	Suspended	N/A	US$41.15	06 Aug 2019

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date
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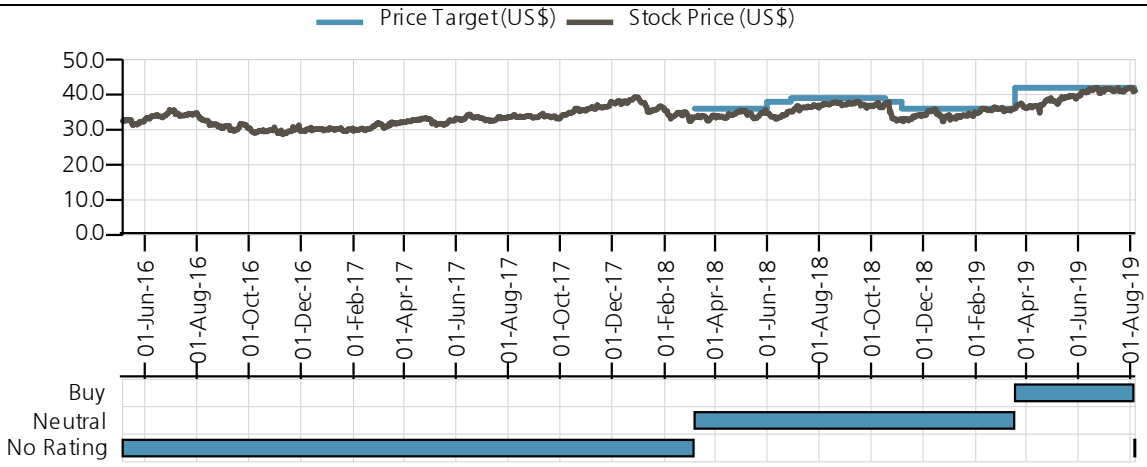
Aqua America Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2016-05-06	32.49	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy
2019-08-06	41.15	-	No Rating

Source: UBS; as of 06 Aug 2019

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bcobrien@aquaamerica.com Ben O'Brien 08/08/19 12:39:05 PM Aqua America Inc

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First Read

Aqua America Inc

PA PUC ALJ recommends approval of Peoples Natural Gas Co. acquisition

Equities

Americas
Water Utilities

12-month rating	**Neutral**
12m price target	**US$45.00**
Price (28 Oct 2019)	**US$44.90**

RIC: WTR.N **BBG:** WTR US

Trading data and key metrics

52-wk range	US$46.58-32.37
Market cap.	US$8.01bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	322
Avg. daily value (m)	US$14.2
Common s/h equity (12/19E)	US$2.15bn
P/BV (12/19E)	3.7x
Net debt / EBITDA (12/19E)	5.1x

EPS (UBS, diluted) (US$)

	12/19E	
	UBS	Cons.
Q1	0.28	0.28
Q2	0.25	0.37
Q3E	0.47	0.43
Q4E	0.43	0.38
12/19E	1.48	1.41
12/20E	1.58	1.59
12/21E	1.68	1.71

Final PUC decision expected late 2019/early 2020

In an opinion issued on 10/28, the Pennsylvania Public Utility Commission (PUC) Administrative Law Judge (ALJ) recommended approval of the Peoples Natural Gas Company acquisition by Aqua America. All parties to the proceeding will now have 30 days to file exceptions and reply exceptions before final PUC action either in December or early 2020. We expect the analyst day that the company had tentatively planned to follow the merger close in early December will now get pushed out in line with the revised consideration schedule.

The Goodwin and Tombaugh gathering system

A point of contention through the consideration process is the treatment of the Goodwin and Tombaugh gathering system. The ALJ approval recommends that the bare steel pipeline system be replaced within 7 years (starting 3 months after merger close) at a cost of $120mm (which will be recovered through base rates). Offsetting this cost, all ratepayers will receive a $13mm bill credit by the end of 2019.

Q3'19 earnings report scheduled for 11/4

We expect WTR to report Q3'19 earnings of $0.47/share vs. prior year earnings of $0.44/share. Quarter-over-quarter earnings growth is driven by rate increases, normal customer growth and acquisitions. We expect the company will address the ongoing Peoples acquisition process, the DELCORA approval process as well as further M&A plans on the conference call following the earnings release.

Valuation:

We believe the ALJ recommendation to approve the Peoples acquisition should be well received by investors as it moves this process closer to completion. We are maintaining our Neutral rating and $45/share price target.

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Paul Cole
Analyst
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Highlights (US$m)	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
Revenues	820	810	838	881	921	956	995	1,033
EBIT (UBS)	326	329	337	370	399	425	454	482
Net earnings (UBS)	234	240	251	265	281	299	319	342
EPS (UBS, diluted) (US$)	1.32	1.35	1.41	1.48	1.58	1.68	1.79	1.92
DPS (US$)	0.74	0.79	0.88	0.94	1.00	1.07	1.15	1.23
Net (debt) / cash	(1,891)	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)

Profitability/valuation	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
EBIT margin %	39.7	40.6	40.3	42.0	43.3	44.5	45.6	46.7
ROIC (EBIT) %	9.0	8.4	7.9	8.0	8.0	8.1	8.3	8.4
EV/EBITDA (core) x	16.2	17.0	17.6	20.2	19.3	18.6	17.8	16.9
P/E (UBS, diluted) x	23.9	24.8	25.0	30.2	28.5	26.8	25.1	23.4
Equity FCF (UBS) yield %	0.2	(1.6)	(1.6)	(1.7)	0.2	0.5	0.8	1.1
Net dividend yield %	2.3	2.4	2.5	2.1	2.2	2.4	2.6	2.7

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$44.90 on 28 Oct 2019 19:47 EDT

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Forecast returns

Forecast price appreciation	+0.2%
Forecast dividend yield	2.2%
Forecast stock return	+2.4%
Market return assumption	6.6%
Forecast excess return	-4.2%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 3% discount to the 2021E average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 9% discount to reflect impact of lower P/E associated with gas earnings.

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Buy	FSR is > 6% above the MRA.	45%	29%
Neutral	FSR is between -6% and 6% of the MRA.	40%	29%
Sell	FSR is > 6% below the MRA.	15%	21%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 September 2019.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Aqua America Inc[16]	WTR.N	Neutral	N/A	US$44.90	28 Oct 2019

Source: UBS. All prices as of local market close.
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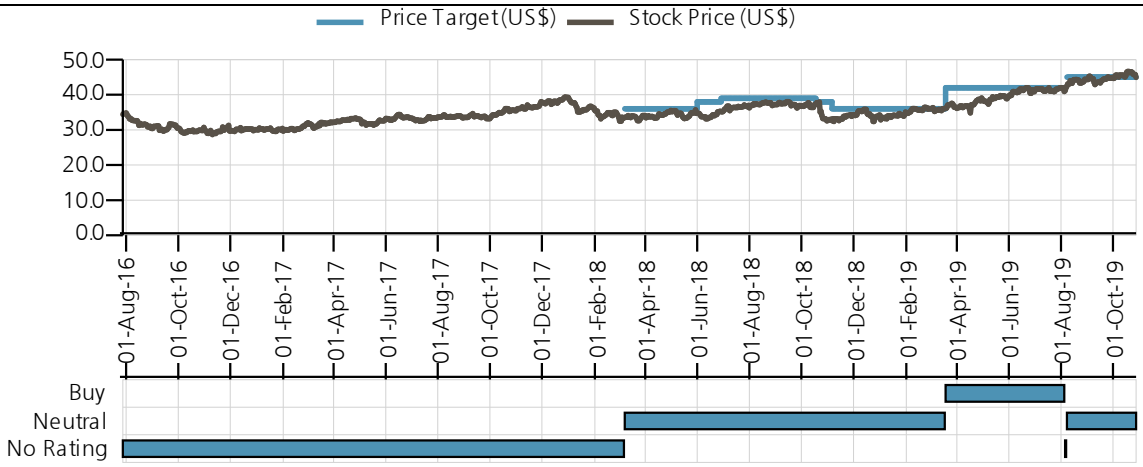
Aqua America Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2016-07-28	34.39	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy
2019-08-06	41.15	-	No Rating
2019-08-08	42.47	45.0	Neutral

Source: UBS; as of 28 Oct 2019

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This report is intended exclusively for:
bjdingerdissen@ aquaamerica.com

First Read

Aqua America Inc

3Q'19 GAAP $0.38; Ex-transaction $0.48

Q: How did the results compare vs expectations?

A: 3Q'19 GAAP EPS of $0.38 vs. 3Q'18 of $0.44; on an ex-transactional basis (excluding Peoples related dilution & costs), operating EPS of $0.48 was ahead of UBS and consensus estimates of $0.47 & $0.38 respectively.

Q: What were the most noteworthy areas in the results?

A: Net income increased in the quarter ($88.5mm vs. 78.2mm in Q3'18) helped by higher rates, customer and volume growth, offsets included growth related costs

Q: Has the company's outlook/guidance changed?

A: Operating EPS guidance (ex: Peoples dilution & expense) for '19 of $1.45-$1.50; Cap-ex for '19 ($550), and through '21 ($1.4 bill.); rate base CAGR (7%); customer growth (between 2-3%); Peoples closing date (late'19/early '20) all reaffirmed.

Q: How would we expect investors to react?

A: Noisy quarterly report; investor focus remains on the pending approval and close of the Peoples & DELCORA acquisitions; potential analyst day with updated guidance.

Key metrics ($)

	Consensus estimates	UBS estimates	Actual	% diff vs. consensus
GAAP Earnings	$0.38	$0.47	$0.37	0.0%

Source: Factset, UBS Equity Research, Aqua American Q3 Earnings Press Release

Equities

Americas

Water Utilities

12-month rating	**Neutral**
12m price target	**US$45.00**
Price (04 Nov 2019)	**US$43.56**

RIC: WTR.N **BBG:** WTR US

Trading data and key metrics

52-wk range	US$46.58-32.37
Market cap.	US$7.77bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	326
Avg. daily value (m)	US$14.5
Common s/h equity (12/19E)	US$2.15bn
P/BV (12/19E)	3.6x
Net debt / EBITDA (12/19E)	5.1x

EPS (UBS, diluted) (US$)

	12/19E	
	UBS	Cons.
Q1	0.28	0.28
Q2	0.25	0.37
Q3E	0.47	0.38
Q4E	0.43	0.35
12/19E	1.48	1.39
12/20E	1.58	1.58
12/21E	1.68	1.71

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Highlights (US$m)	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
Revenues	820	810	838	881	921	956	995	1,033
EBIT (UBS)	326	329	337	370	399	425	454	482
Net earnings (UBS)	234	240	251	265	281	299	319	342
EPS (UBS, diluted) (US$)	1.32	1.35	1.41	1.48	1.58	1.68	1.79	1.92
DPS (US$)	0.74	0.79	0.88	0.94	1.00	1.07	1.15	1.23
Net (debt) / cash	(1,891)	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)

Profitability/valuation	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
EBIT margin %	39.7	40.6	40.3	42.0	43.3	44.5	45.6	46.7
ROIC (EBIT) %	9.0	8.4	7.9	8.0	8.0	8.1	8.3	8.4
EV/EBITDA (core) x	16.2	17.0	17.6	19.7	18.9	18.1	17.4	16.5
P/E (UBS, diluted) x	23.9	24.8	25.0	29.3	27.6	26.0	24.3	22.7
Equity FCF (UBS) yield %	0.2	(1.6)	(1.6)	(1.7)	0.2	0.5	0.8	1.2
Net dividend yield %	2.3	2.4	2.5	2.2	2.3	2.5	2.6	2.8

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$43.56 on 04 Nov 2019 19:34 EST

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Forecast returns

Forecast price appreciation	+3.3%
Forecast dividend yield	2.3%
Forecast stock return	+5.6%
Market return assumption	6.6%
Forecast excess return	-1.0%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 3% discount to the 2021 average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 9% discount to reflect impact of lower P/E associated with gas earnings.

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Buy	FSR is > 6% above the MRA.	45%	29%
Neutral	FSR is between -6% and 6% of the MRA.	40%	29%
Sell	FSR is > 6% below the MRA.	15%	21%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 September 2019.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

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UBS Securities LLC: Daniel Ford, CFA; Paul Cole.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Aqua America Inc[16]	WTR.N	Neutral	N/A	US$43.56	04 Nov 2019

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date
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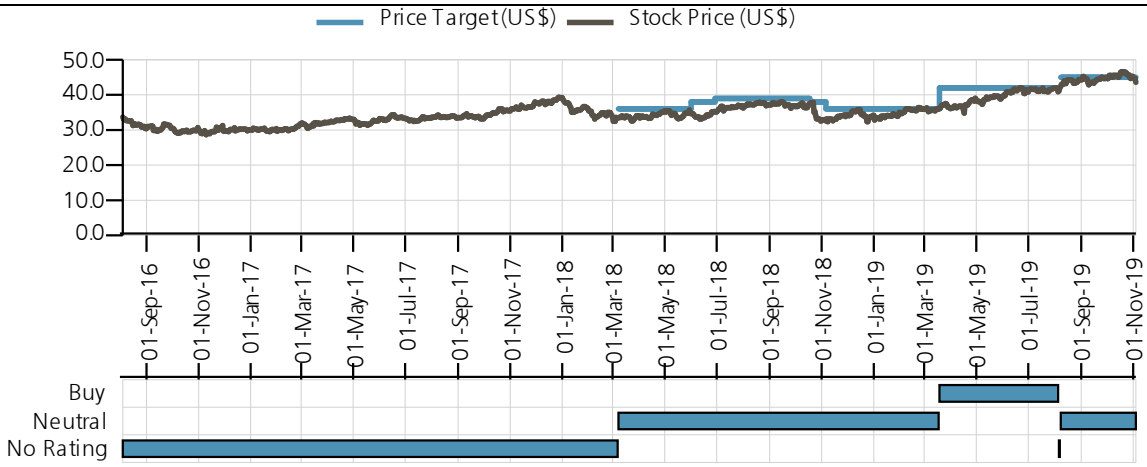
Aqua America Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2016-08-04	33.72	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy
2019-08-06	41.15	-	No Rating
2019-08-08	42.47	45.0	Neutral

Source: UBS; as of 04 Nov 2019

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First Read

Essential Utilities Inc

Q4/2020 Adj. EPS in-line; '21 guidance unchanged

Q: How did the results compare vs expectations?

A: In line. WTRG reported Q4/full year 2020 adjusted EPS of $0.46/$1.58. These results are in line with consensus and UBS estimates of $0.45/$1.57 and $0.45/$1.58, respectively, and are above prior period results of $0.28/$1.47. Full year 2020 EPS guidance was $1.53-$1.58 (top end).

Q: What were the most noteworthy areas in the results?

A: Full year results benefited from the acquisition of Peoples Gas (customer credits are excluded from the adjusted results), higher rates and volume growth (driven by favorable weather and work-from-home orders). Vs. the prior year fourth quarter, results benefited from the Peoples Gas acquisition, higher rates and volume growth.

Q: Has the company´s outlook/guidance changed?

A: Earnings guidance for 2021 is unchanged at $1.64-$1.69. The projected EPS CAGR is 5-7% through 2023, driven by water rate base growth of 6-7% and gas rate base growth of 8-10%. WTRG currently has six signed purchase agreements for additional water and wastewater systems serving approximately 227,000 customers/$438mm of rate base, including the DELCORA system. WTRG has rate proceedings pending in Virginia and Indiana.

Q: How would we expect investors to react?

A: In line. On the investor call, we are looking for an update on the DELCORA (and other) acquisitions, the catch-up repairs tax proceeding, and the performance of both the Peoples Gas and Texas based subsidiaries through the recent polar vortex event.

Key Metrics ($)

	Consensus estimates	UBS estimates	Actual	% diff vs. UBS
Q4 Adj. EPS	$0.45	$0.45	$0.46	+2.2%
2020 Adj. EPS	$1.57	$1.58	$1.58	0.0%

Source : UBS Equity Research, FactSet, Company Reports

Equities

Americas

Water Utilities

12-month rating	**Neutral**
12m price target	**US$45.00**
Price (24 Feb 2021)	**US$44.09**

RIC: WTRG.N **BBG:** WTRG US

Trading data and key metrics

52-wk range	US$50.31-32.65
Market cap.	US$7.99b
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	411
Avg. daily value (m)	US$19.1
Common s/h equity(12/20E)	US$2.35b
P/BV(12/20E)	4.8x
Net debt to EBITDA(12/20E)	4.0x

EPS (UBS, diluted) (US$)

	12/20E	
	UBS	Cons.
Q1	0.60	0.60
Q2	0.29	0.29
Q3	0.23	0.23
Q4E	0.45	0.45
12/20E	1.58	1.54
12/21E	1.68	1.67
12/22E	1.79	1.79

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Highlights(US$m)	12/17	12/18	12/19	12/20E	12/21E	12/22E	12/23E	12/24E
Revenues	810	838	881	1,049	956	995	1,033	1,072
EBIT (UBS)	329	337	370	527	425	454	482	512
Net earnings (UBS)	240	251	265	403	299	319	342	365
EPS (UBS, diluted) (US$)	1.35	1.41	1.48	1.58	1.68	1.79	1.92	2.05
DPS (net) (US$)	0.79	0.88	0.91	0.97	1.04	1.11	1.19	1.27
Net (debt) / cash	(2,121)	(2,376)	(2,670)	(2,744)	(2,931)	(3,066)	(3,186)	(3,293)
Profitability/valuation	**12/17**	**12/18**	**12/19**	**12/20E**	**12/21E**	**12/22E**	**12/23E**	**12/24E**
EBIT (UBS) margin %	40.6	40.3	42.0	50.3	44.5	45.6	46.7	47.7
ROIC (EBIT) %	8.4	7.9	8.0	10.6	8.1	8.3	8.4	8.6
EV/EBITDA (UBS core) x	17.0	17.6	18.7	15.6	18.4	17.6	16.7	16.2
P/E (UBS, diluted) x	24.8	25.0	27.3	28.4	26.7	25.0	23.4	21.9
Equity FCF (UBS) yield %	(1.6)	(1.6)	(1.8)	1.7	0.5	0.8	1.1	1.5
Dividend yield (net) %	2.4	2.5	2.2	2.2	2.3	2.5	2.7	2.8

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$ 44.09 on 24-Feb-2021

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Forecast returns

Forecast price appreciation	+2.1%
Forecast dividend yield	2.4%
Forecast stock return	+4.4%
Market return assumption	5.1%
Forecast excess return	-0.7%

Company Description

Essential Utilities, Inc. provides regulated water and wastewater services to approximately 3m people in Pennsylvania, Ohio, Texas, Illinois, North Carolina, New Jersey, Indiana, and Virginia and distributes natural gas to approximately 2m people in western Pennsylvania, West Virginia and Kentucky. WTRG's water operations represent approximately $5.5bn of rate base value, while its gas distribution operations represent approximately $2.5bn of rate base. Growth is generated by infrastructure investment (pipes, plants, etc.), strategic M&A (water/ wastewater) and management of private water systems.

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events. Our price target is premised upon a 7% discount to the 2021E average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 7% premium to reflect operations in six Fair Market Value states, and 14% discount to reflect impact of lower P/E associated with gas earnings.

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	51%	31%
Neutral	FSR is between -6% and 6% of the MRA.	37%	29%
Sell	FSR is > 6% below the MRA.	12%	18%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 31 December 2020.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
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UBS Securities LLC: Daniel Ford, CFA, Paul Cole.

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Company Name	Reuters	12-month rating	Price	Price date
Essential Utilities Inc[16]	WTRG.N	Neutral	US$44.09	24 Feb 2021

Source: UBS. All prices as of local market close.
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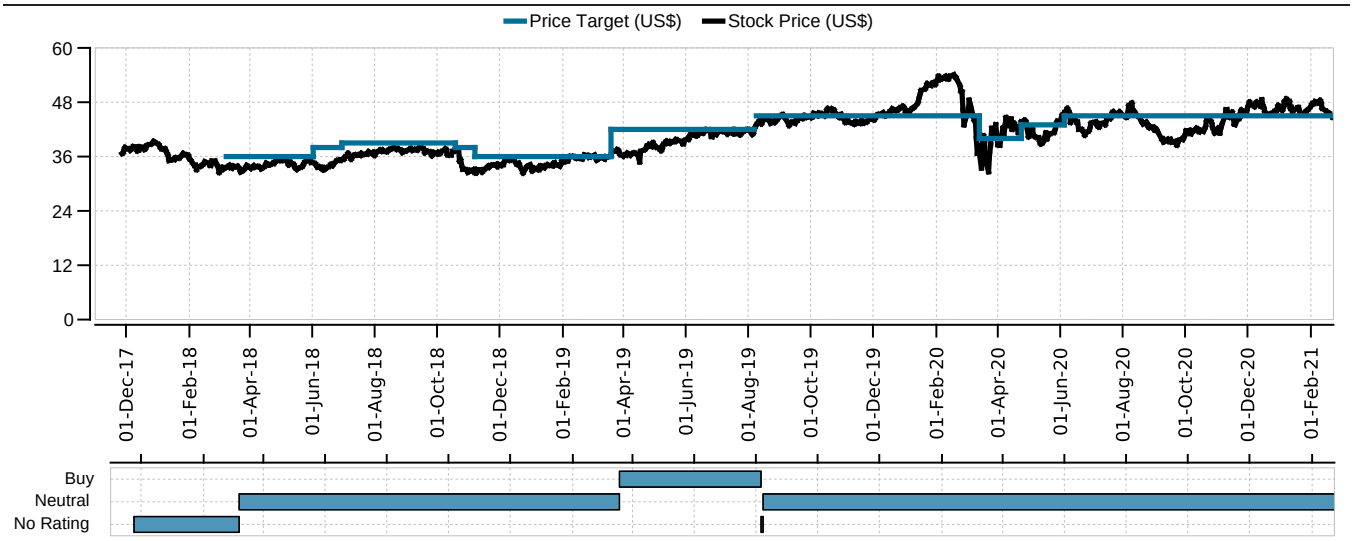
Essential Utilities Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2017-11-24	36.57	-	No Rating
2018-03-08	33.52	36.00	Neutral
2018-06-01	34.71	38.00	Neutral
2018-06-29	35.18	39.00	Neutral
2018-10-18	37.23	38.00	Neutral
2018-11-06	32.59	36.00	Neutral
2019-03-19	36.12	42.00	Buy
2019-08-06	41.15	-	No Rating
2019-08-08	42.47	45.00	Neutral
2020-03-13	38.43	40.00	Neutral
2020-04-23	42.62	43.00	Neutral
2020-06-04	44.51	45.00	Neutral

Source: UBS; as of24-Feb-2021

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First Read

Essential Utilities Inc

Q4/2019 Adj. EPS & 2020 Guidance

Q: How did the results compare vs expectations?

A: Q4/full year EPS adjusted for transaction costs and equity dilution $0.34/$1.47 vs. consensus/UBSe $0.31/$1.48 - $0.37/$1.48; prior year $$0.31/$1.41.

Q: What were the most noteworthy areas in the results?

A: Yr/yr results improved due to higher rate & surcharge revenues, commentary suggests that O&M (absent transactions costs) increased in line with expectations.

Q: Has the company's outlook/guidance changed?

A: Illustrative guidance for 2020 of $1.53-$1.58 vs consensus $1.58; EPS growth CAGR off '19 adjusted base through '22 of 5-7%; rate base growth for water, 6-7% and gas, 8-10% through '22; and infrastructure investment through '22 of $2.8 bill.

Q: How would we expect investors to react?

A: Subject to incremental detail at the investor day, we expect a muted reaction to earnings and growth guidance that is modestly lower than current consensus.

Key metrics ($)

	Consensus estimates	UBS estimates	Actual	% diff vs. consensus
Q4 Adj. EPS	$0.31	$0.37	$0.34	+9.6%
2019 Adj. EPS	$1.48	$1.48	$1.47	-0.6%

Source: FactSet, UBS estimates, Essential Utilities Press Release

Equities

Americas

Water Utilities

12-month rating	**Neutral**
12m price target	**US$45.00**
Price (26 Feb 2020)	**US$50.31**

RIC: WTRG.N **BBG:** WTRG US

Trading data and key metrics

52-wk range	US$54.07-34.82
Market cap.	US$8.98bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	419
Avg. daily value (m)	US$20.5
Common s/h equity (12/19E)	US$2.15bn
P/BV (12/19E)	4.2x
Net debt / EBITDA (12/19E)	5.1x

EPS (UBS, diluted) (US$)

	12/19E	
	UBS	Cons.
Q1	0.28	0.28
Q2	0.37	0.37
Q3	0.46	0.48
Q4E	0.37	0.31
12/19E	1.48	1.48
12/20E	1.58	1.57
12/21E	1.68	1.68

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Highlights (US$m)	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
Revenues	820	810	838	881	921	956	995	1,033
EBIT (UBS)	326	329	337	370	399	425	454	482
Net earnings (UBS)	234	240	251	265	281	299	319	342
EPS (UBS, diluted) (US$)	1.32	1.35	1.41	1.48	1.58	1.68	1.79	1.92
DPS (US$)	0.74	0.79	0.88	0.94	1.00	1.07	1.15	1.23
Net (debt) / cash	(1,891)	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)

Profitability/valuation	12/16	12/17	12/18	12/19E	12/20E	12/21E	12/22E	12/23E
EBIT margin %	39.7	40.6	40.3	42.0	43.3	44.5	45.6	46.7
ROIC (EBIT) %	9.0	8.4	7.9	8.0	8.0	8.1	8.3	8.4
EV/EBITDA (core) x	16.2	17.0	17.6	22.0	21.0	20.2	19.3	18.3
P/E (UBS, diluted) x	23.9	24.8	25.0	33.9	31.9	30.0	28.1	26.3
Equity FCF (UBS) yield %	0.2	(1.6)	(1.6)	(1.5)	0.2	0.4	0.7	1.0
Net dividend yield %	2.3	2.4	2.5	1.9	2.0	2.1	2.3	2.4

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$50.31 on 26 Feb 2020 18:41 EST

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Forecast returns

Forecast price appreciation	-10.6%
Forecast dividend yield	2.0%
Forecast stock return	-8.6%
Market return assumption	6.2%
Forecast excess return	-14.8%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 3% discount to the 2021 average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 9% discount to reflect impact of lower P/E associated with gas earnings.

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	44%	32%
Neutral	FSR is between -6% and 6% of the MRA.	41%	29%
Sell	FSR is > 6% below the MRA.	15%	20%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 31 December 2019.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Essential Utilities Inc[16]	WTRG.N	Neutral	N/A	US$50.31	26 Feb 2020

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date
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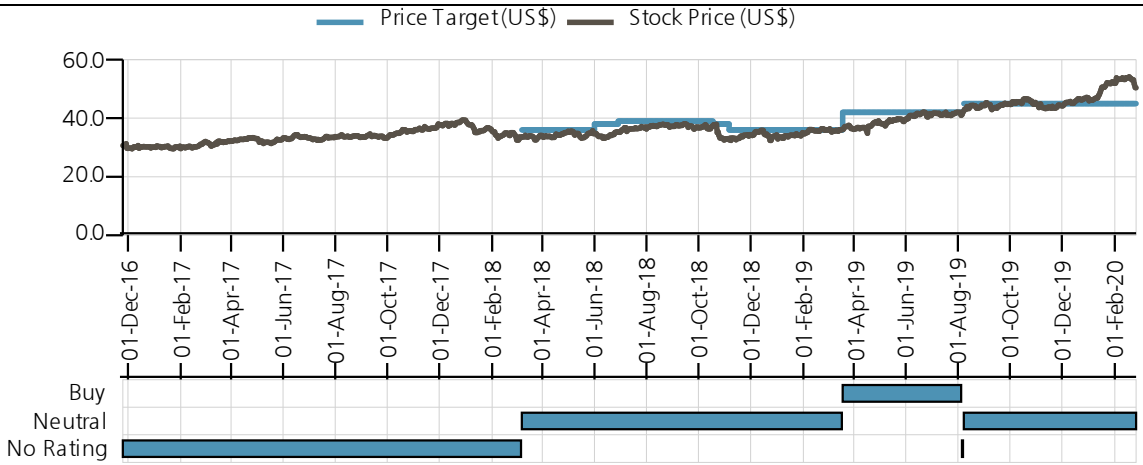
Essential Utilities Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2016-11-25	30.6	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy
2019-08-06	41.15	-	No Rating
2019-08-08	42.47	45.0	Neutral

Source: UBS; as of 26 Feb 2020

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This report is intended exclusively for:
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First Read

Essential Utilities Inc

Q2'20 EPS $0.29 vs. UBSe $0.26, Consensus $0.22

Q: How did the results compare vs expectations?

A: Better. WTRG reported Q2'20 EPS of $0.29 vs. the prior year quarter of $0.25. UBS and consensus expectations for the quarter were $0.26 and $0.22, respectively.

Q: What were the most noteworthy areas in the results?

A: Vs. the prior year qtr, revenues increased due to the addition of Peoples Gas, higher rates, weather derived volumes and customer growth. Residential water sales were +10% quarter over quarter, while commercial & industrial sales were -16% and -11% respectively. O&M expenses in the quarter rose as a result of the Peoples Gas combination, but were helped by the absence of transaction & integration costs.

Q: Has the company's outlook/guidance changed?

A: Full year '20 guidance of $1.53-$1.58 unchanged, as is the EPS CAGR of 5-7%, rate base growth of 6-7% in water and 8-10% in gas, and projected infrastructure spending of $2.8 billion. Guidance for EPS dispersion across the year is unchanged.

Q: How would we expect investors to react?

A: Better EPS & affirmation of guidance should be well received by investors.

Key metrics ($)

	Consensus estimates	UBS estimates	Actual	% diff vs. consensus
EPS	$0.22	$0.26	$0.29	+26.0%

Source: UBS Equity Research, FactSet, Essential Utilities Inc.

Equities

Americas

Water Utilities

12-month rating	**Neutral**
12m price target	**US$45.00**
Price (05 Aug 2020)	**US$44.69**

RIC: WTRG.N **BBG:** WTRG US

Trading data and key metrics

52-wk range	US$54.07-32.65
Market cap.	US$7.97bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	415
Avg. daily value (m)	US$17.8
Common s/h equity (12/20E)	US$2.25bn
P/BV (12/20E)	3.5x
Net debt / EBITDA (12/20E)	5.1x

EPS (UBS, diluted) (US$)

	12/20E	
	UBS	Cons.
Q1	0.60	0.60
Q2E	0.26	0.22
Q3E	0.27	0.26
Q4E	0.45	0.47
12/20E	1.58	1.48
12/21E	1.68	1.66
12/22E	1.79	1.80

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Highlights (US$m)	12/17	12/18	12/19	12/20E	12/21E	12/22E	12/23E	12/24E
Revenues	810	838	881	921	956	995	1,033	1,072
EBIT (UBS)	329	337	370	399	425	454	482	512
Net earnings (UBS)	240	251	265	281	299	319	342	365
EPS (UBS, diluted) (US$)	1.35	1.41	1.48	1.58	1.68	1.79	1.92	2.05
DPS (US$)	0.79	0.88	0.94	1.00	1.07	1.15	1.23	1.32
Net (debt) / cash	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)	(3,378)

Profitability/valuation	12/17	12/18	12/19	12/20E	12/21E	12/22E	12/23E	12/24E
EBIT margin %	40.6	40.3	42.0	43.3	44.5	45.6	46.7	47.7
ROIC (EBIT) %	8.4	7.9	8.0	8.0	8.1	8.3	8.4	8.6
EV/EBITDA (core) x	17.0	17.6	18.7	19.2	18.5	17.7	16.8	16.3
P/E (UBS, diluted) x	24.8	25.0	27.3	28.4	26.7	25.0	23.3	21.8
Equity FCF (UBS) yield %	(1.6)	(1.6)	(1.8)	0.2	0.5	0.8	1.1	1.5
Net dividend yield %	2.4	2.5	2.3	2.2	2.4	2.6	2.8	2.9

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$44.69 on 05 Aug 2020 18:42 EDT

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Forecast returns

Forecast price appreciation	+0.7%
Forecast dividend yield	2.3%
Forecast stock return	+3.0%
Market return assumption	5.1%
Forecast excess return	-2.1%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 3% discount to the 2021 average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 9% discount to reflect impact of lower P/E associated with gas earnings.

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	49%	32%
Neutral	FSR is between -6% and 6% of the MRA.	39%	30%
Sell	FSR is > 6% below the MRA.	13%	20%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 30 June 2020.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Essential Utilities Inc[16]	WTRG.N	Neutral	N/A	US$44.69	05 Aug 2020

Source: UBS. All prices as of local market close.
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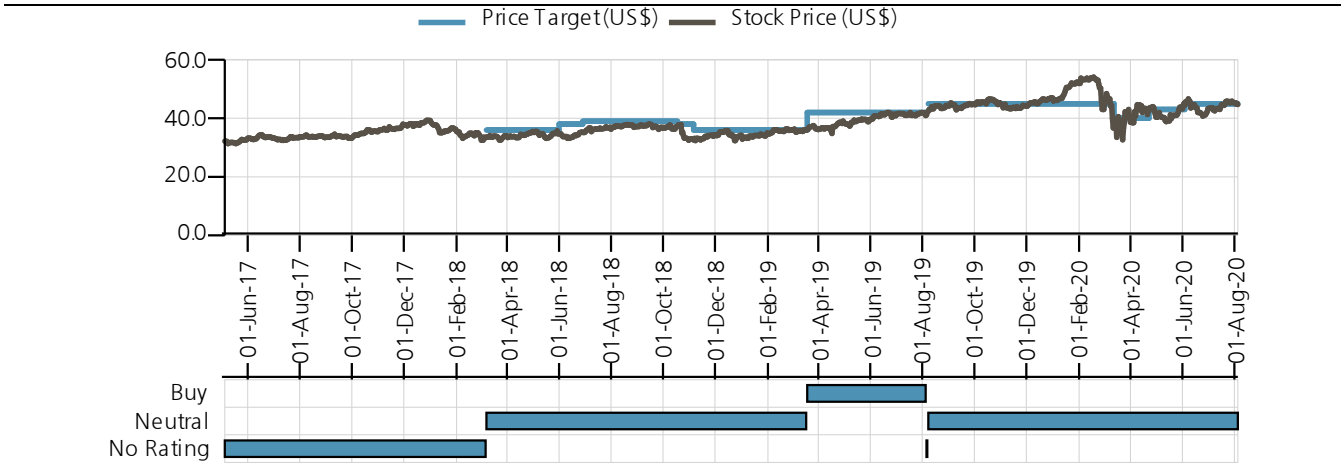
Essential Utilities Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2017-05-05	32.16	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy
2019-08-06	41.15	-	No Rating
2019-08-08	42.47	45.0	Neutral
2020-03-13	38.43	40.0	Neutral
2020-04-23	42.62	43.0	Neutral
2020-06-04	44.51	45.0	Neutral

Source: UBS; as of 05 Aug 2020

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Flash Comment

Utilities

Utility & Infrastructure Daily

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Quick thoughts from Wells Fargo Securities, LLC Utility & Infrastructure Team:

Utilities

Aqua America (WTR/Market Perform)(Reeder) – Yesterday afternoon (9/17), WTR announced that an asset purchase agreement was signed with the Delaware Country Regional Water Quality Control Authority (DELCORA) to purchase the municipal authority's wastewater assets for $276.5M. The agreement marks the culmination of a roughly two month exclusivity period between the two parties to explore a combination, which WTR discussed on the Q2 call in early August. The transaction is subject to Pennsylvania Public Utilities Commission (PaPUC) approval and would more than double WTR's existing 128,000 wastewater connections by adding the equivalent of 165,000 retail customers across 42 Southeast PA municipalities. While the purchase price is a bit north of DELCORA's $220-240M net PP&E value, WTR does not expect the transaction to create any goodwill which seems to suggest that the PaPUC will be asked to approve the deal under the state's fair market value (FMV) law. We expect PaPUC approval could take roughly 12 months and then once the deal closes, another 2-3 years before WTR is able to earn a return on the equity portion of the $276.5M rate base commensurate with the remainder of the water/wastewater business. In addition, we believe DELCORA could add as much as $150M of capex to our prior 2019-23 water capex (ex. M&A) forecast of $2.3B. In terms of equity needs, we think WTR could need to raise an additional $150-175M in 2020 & beyond (likely through establishment of an at-the-market program per management's Q2 call comments) with the bulk needed when the deal closes in 2H'20. Net-net, we believe minimal accretion is likely in 2020 with the DELCORA deal eventually adding roughly $0.05, or 2-3%, to EPS power by 2023. As a reminder, our current WTR 2019-23E EPS (pro forma for the pending Peoples deal but excluding any potential uplift from the planned election of repairs tax deduction at Peoples) are $1.32, $1.57, $1.68, $1.78 & $1.90.

Bigger picture, we are extremely encouraged by WTR's ability to find and get the deal signed with DELCORA for three reasons. First, it shows that management has not taken their eye off growing the regulated water/wastewater business despite the pending move into the gas LDC (local distribution company) business nor has the move into gas soured counterparties willingness to transact with WTR. Second, it further demonstrates that municipals are willing to come to the M&A negotiating table as a way to solve impending challenges. For DELCORA it was an estimated $1.2B of capital investment needed through 2041 which included a substantial amount to comply with Environmental Protection Agency (EPA) mandates to resolve combined sewer overflow problems – rather than put the burden on customer bills, DELCORA plans to place the sales proceeds into a trust to create a "rate stabilization plan" that should help offset those capital needs and save the average retail customer $1,400. Third, the addition of a substantial wastewater presence in Southeast PA could open the door to additional wastewater growth opportunities in the region, much the way WTR expanded its water footprint to the greater Philadelphia suburbs in the 1990s and perhaps to those same communities where the company already serves water.

Please see page 3 for rating definitions, important disclosures and required analyst certifications.
All estimates/forecasts are as of 09/18/19 unless otherwise stated. 09/18/19 05:35:12 ET

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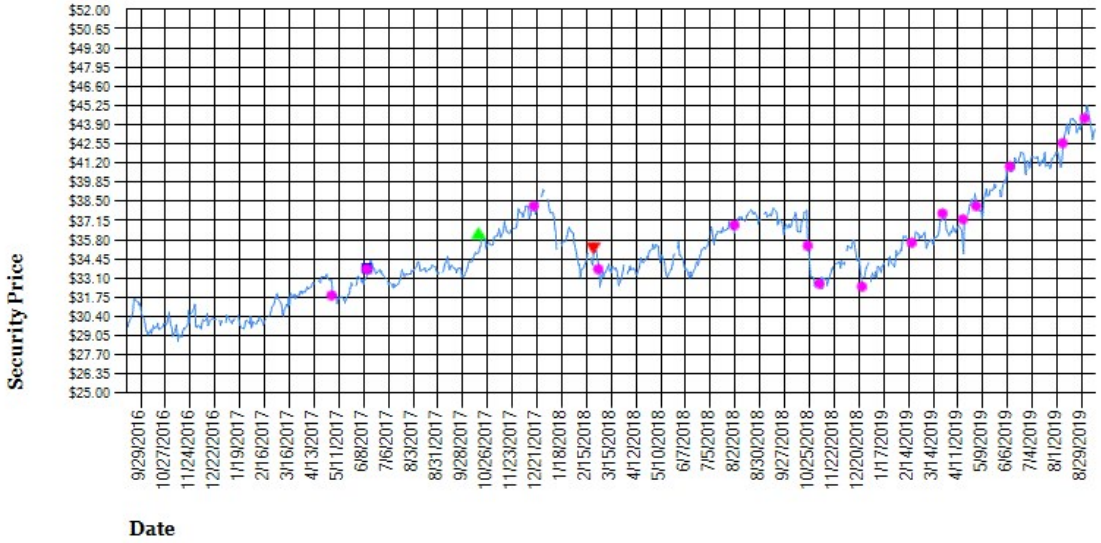
Aqua America, Inc. (WTR)/Market Perform (2)
Price as of 9/17/2019: $43.90
FY 19 EPS: $1.32
FY 20 EPS: $1.57
Shares Out.: 215.7 MM
Market Cap.: $9,469.23 MM

Rating Basis Information:
WTR Thesis: We are attracted to WTR's strong fundamentals - a proven EPS growth strategy, a growing rate base, constructive regulation, efficient operations and a strong balance financial profile. Our Market Perform rating reflects valuation considerations in light of WTR's pending agreement to acquire Peoples (a gas utility) and the associated P/E multiple, regulatory and deal execution/integration related risks.

DISCLOSURE APPENDIX

Required Disclosures

Aqua America, Inc. (WTR) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	9/13/2016		Kalton				
	9/13/2016	NA	2	NE	31.00	33.00	29.73
●	5/4/2017	31.70	2	NE	32.00	34.00	31.73
■	6/13/2017		Reeder				
●	6/13/2017	33.62	2	35	NE	NE	33.62
▲●	10/19/2017	35.30	1	40	NE	NE	36.03
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Outperform/Buy	SR	Suspended
2	Market Perform/Hold	NR	Not Rated
3	Underperform/Sell	NE	No Estimate

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Utilities

Utility & Infrastructure Daily

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Quick thoughts from Wells Fargo Securities, LLC Utility & Infrastructure Team:

Utilities

Essential Utilities (WTRG/Overweight) (Reeder) - We admittedly missed the ruling by Judge Dozor in the Court of Common Pleas of Delaware County last Monday (12/28). In what we consider to be a very positive development, the judge ruled in favor of DELCORA and WTRG on both matters disputed by Delaware County - the validity of the asset purchase agreement as well as the ability to put the proceeds of the $277M sale into a trust to be used to stabilize ratepayers' bills in the years ahead (keep increases to 3% annually so long as the fund is solvent while ensuring WTRG earns its authorized ROE). While Delaware County has indicated an intention to continue to argue its case as part of the pending PaPUC regulatory approval process (has yet to decide whether to appeal Judge Dozor's ruling), we believe the 12/28 ruling clears the way for WTRG to close the DELCORA deal by Q2'21.

We find it unlikely that the PaPUC will be overly sympathetic to Delaware County's contention that the $277M agreed to sales price that was blessed by the prior County Council undervalues the fair market value (FMV) of the system. It is our understanding that DELCORA struck that price during exclusive negotiations with WTRG in '19 perhaps knowing that it might be less than a closer to $400M price tag defensible by PA's FMV legislation. Rather the lower sales price would serve as a balancing act to help keep the subsequent rate increases to DELCORA customers manageable as WTRG recovers the FMV of the initial investment as well as the roughly $700M of capital investments required by 2028 to keep the system viable. Further, we believe the PaPUC's FMV approval process if anything is geared to protect against the opposite – a utility overpaying FMV and then trying to socialize those higher costs across its entire customer base.

We look towards WTRG's 1/11 investor event for additional insights into getting the deal across the finish line as well as the expected longer-term benefits. As we have previously opined, we believe the DELCORA deal represents material long-term value (that is not currently reflected in the share price!) given meaningful capex needs that fall beyond the current 5-year forecast as well as the likely substantial wastewater tuck-in deals that could transpire in the area. In other words, we believe the DELCORA deal should, at a minimum, allow WTRG to continue to target a 5-7% EPS CAGR through the end of the decade.

Infrastructure

Brookfield Infrastructure (BIP/BIPC)(Overweight) & Brookfield Renewable (BEP/BEPC)(Equal Weight) (Reeder) – Brookfield Asset Management (BAM/Not Covered) along with institutional partners made a public offer before the open on 1/4 to acquire the remaining units of one of its publicly traded

Please see page 4 for rating definitions, important disclosures and required analyst certifications.
All estimates/forecasts are as of 01/05/21 unless otherwise stated. 01/05/21 08:12:41 ET

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vehicles, Brookfield Property Partners L.P. (BPY/Not Covered), that it does not already own for $16.50/unit or a roughly 15% premium to the 12/31 close. We touched base with a Brookfield Infrastructure contact to confirm our suspicions – this situation is very much unique to BPY and should not be viewed as a potential read-through to either BEP/BEPC or BIP/BIPC. BAM has expressed frustration with the public valuation of BPY's underlying assets since prior to the onset of the pandemic and the stock's underperformance over the last 10 months, ostensibly related to longer term concerns regarding the health of the commercial real estate market, has only exacerbated that frustration. This contrasts to BEP/BEPC and BIP/BIPC which have been warmly embraced by investors, particularly (1) in the wake of the pandemic, (2) amidst the secular shifts towards renewables and infrastructure investment strategies and (3) following the creation of c-corp share classes in '20. As such, investors should not be thinking a potential take-private offer could be coming from BAM for either Brookfield Infrastructure or Brookfield Renewable absent a meaningful, and what we would consider an unexpected, re-rating down in the respective unit/share prices.

Acronyms:

DELCORA – Delaware County Regional Water Quality Control Authority

PaPUC – Pennsylvania Public Utility Commission

Essential Utilities, Inc. (WTRG)/Overweight
Price as of 1/4/2021: $46.19
FY 20 EPS: $1.58
FY 21 EPS: $1.65
Shares Out.: 245.2 MM
Market Cap.: $11,325.79 MM

Brookfield Infrastructure Partners L.P. (BIP)/Overweight
Price as of 1/4/2021: $49.49
FY 20 FFO/sh: $3.08
FY 21 FFO/sh: $3.50
Shares Out.: 465.0 MM
Market Cap.: $23,012.85 MM

Brookfield Infrastructure Corporation (BIPC)/Overweight
Price as of 1/4/2021: $70.29
FY 20 FFO/sh: $3.08
FY 21 FFO/sh: $3.50
Shares Out.: 465.0 MM
Market Cap.: $32,684.85 MM

Brookfield Renewable Partners LP (BEP)/Equal Weight
Price as of 1/4/2021: $44.26
FY 20 FFO/sh: $1.35
FY 21 FFO/sh: $1.43
Shares Out.: 646.0 MM
Market Cap.: $28,591.96 MM

Brookfield Renewable Corporation (BEPC)/Equal Weight
Price as of 1/4/2021: $57.95
FY 20 FFO/sh: $1.35
FY 21 FFO/sh: $1.43
Shares Out.: 464.0 MM
Market Cap.: $26,888.8 MM

Rating Basis Information:

WTRG Thesis: Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived and near-term regulatory risk is low as both the water and gas utilities completed rate cases in 2019), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

BIP Thesis: We believe attractive roughly 10% FFO/unit and 8% distribution/unit CAGRs are achievable over the next 5-years driven by a robust capital backlog and a savvy management team that has shown a consistent ability to execute and be good stewards of investor capital. In addition, we are drawn to BIP's diversified business mix – both strategically and geographically – as well as the highly regulated/contracted cash flow profile. We believe the near-term pressures from COVID-19 economic fallout, the strong U.S. dollar, etc. will be offset in the long run by value creating M&A opportunities, some of which may result from pandemic related disruptions in global equity and debt markets.

BIPC Thesis: We believe attractive roughly 10% FFO/unit and 8% distribution/unit CAGRs are achievable over the next 5-years driven by a robust capital backlog and a savvy management team that has shown a consistent ability to execute and be good stewards of investor capital. In addition, we are drawn to BIPC's diversified business mix – both strategically and geographically – as well as the highly regulated/contracted cash flow profile. We believe the near-term pressures from COVID-19 economic fallout, the strong U.S. dollar, etc. will be offset in the long run by value creating M&A opportunities, some of which may result from pandemic related disruptions in global equity and debt markets.

BEP Thesis: We consider BEP – as one of the few sizeable, publicly traded, pure play global renewable companies – to be a compelling way for investors to gain exposure to the decades-long global transformation towards carbon-free electric generation and growing ESG investing mantra. BEP is led by a proven management team with a track record of efficiently deploying (and recycling) capital across the portfolio. BEP's conservative philosophy of amassing a well-diversified global portfolio of predominantly contracted, carbon-free generation assets that are backed by an investment grade balance sheet and healthy cash flows results in a relatively low risk profile versus other renewable asset owners/developers. We believe units of BEP offer investors attractive long-term total return potential comprised of at least 7% FFO/unit growth and a roughly 3% yield with mid-to-upper single digit distribution/unit growth. That said, our Equal Weight rating reflects current valuation considerations.

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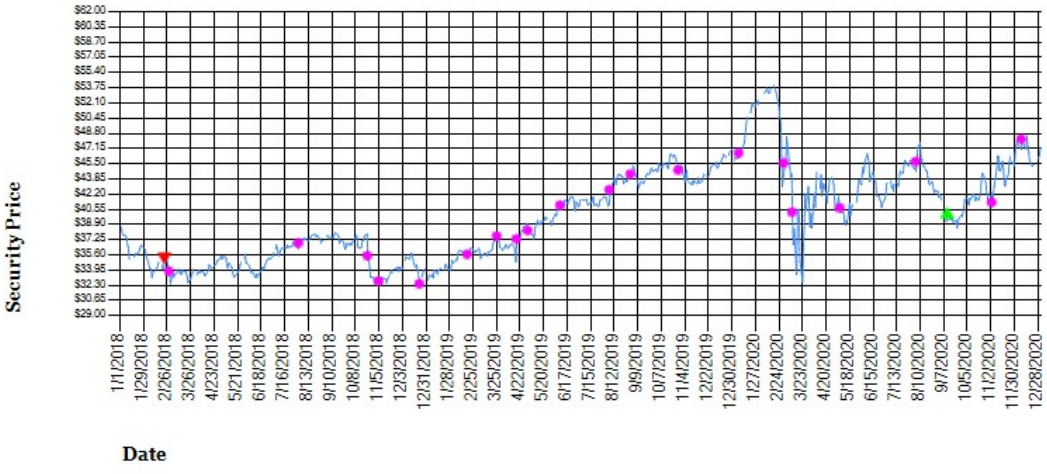
DISCLOSURE APPENDIX

Required Disclosures

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	1/1/2018		Reeder				
	1/1/2018	NA	1	43	NE	NE	38.65
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51
●	3/2/2020	43.01	2	45	NE	NE	45.44
●	3/11/2020	44.41	2	48	NE	NE	40.03
●	5/7/2020	40.49	2	42	NE	NE	40.53
●	8/6/2020	45.56	2	45	NE	NE	45.56
▲	9/14/2020	39.35	1	45	NE	NE	39.82
●	11/4/2020	41.19	1	47	NE	NE	41.19
●	12/10/2020	47.70	1	52	NE	NE	48.02

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Source: Wells Fargo Securities, LLC estimates and Reuters data

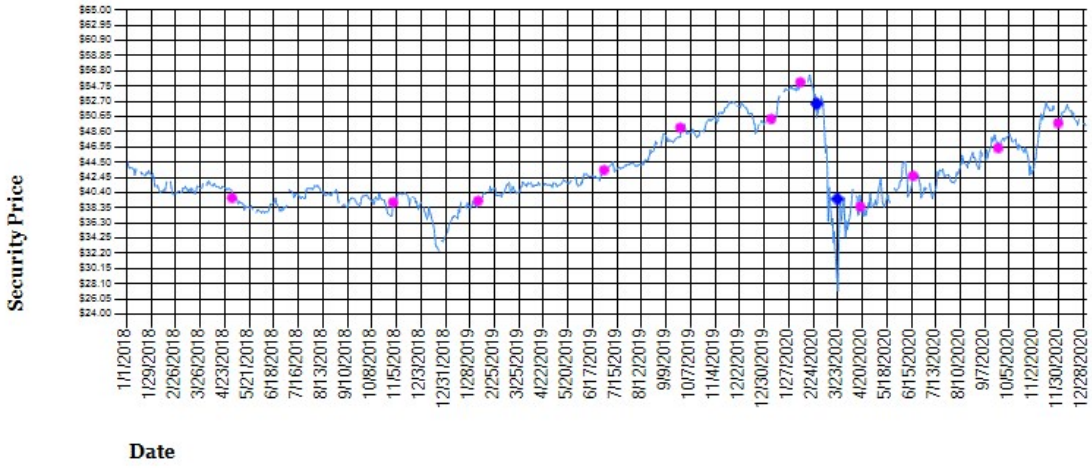
Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

Brookfield Infrastructure Partners L.P. (BIP) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	1/1/2018		Reeder				
	1/1/2018	NA	1	47	NE	NE	44.64
●	5/2/2018	39.59	1	46	NE	NE	39.57
●	11/2/2018	38.89	1	44	NE	NE	38.83
●	2/7/2019	39.20	1	46	NE	NE	39.15
●	7/1/2019	43.47	1	49	NE	NE	43.32
●	9/27/2019	49.30	1	54	NE	NE	49.05
●	1/8/2020	50.15	1	56	NE	NE	50.15
●	2/11/2020	55.03	1	60	NE	NE	55.05
◆●	3/2/2020	52.10	SR	NE	NE	NE	52.10
◆●	3/26/2020	38.23	1	50	NE	NE	39.22
●	4/20/2020	40.06	1	47	NE	NE	38.29
●	6/19/2020	42.49	1	48	NE	NE	42.46
●	9/23/2020	46.18	1	51	NE	NE	46.14
●	12/1/2020	49.61	1	56	NE	NE	49.61

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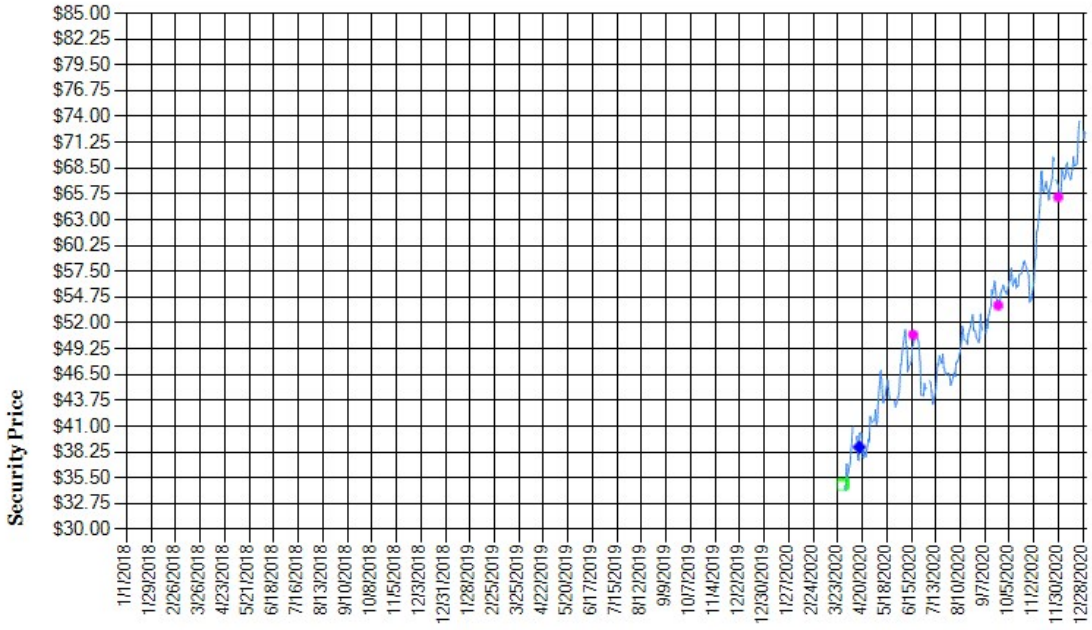
Brookfield Infrastructure Corporation (BIPC) 3-yr. Price Performance



Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
3/31/2020		Listed on NYSE, TSX exchanges				
4/19/2020		Reeder				
4/20/2020	40.27	1	47	NE	NE	38.47
6/19/2020	50.00	1	53	NE	NE	50.59
9/23/2020	53.58	1	57	NE	NE	53.66
12/1/2020	65.18	1	70	NE	NE	65.18

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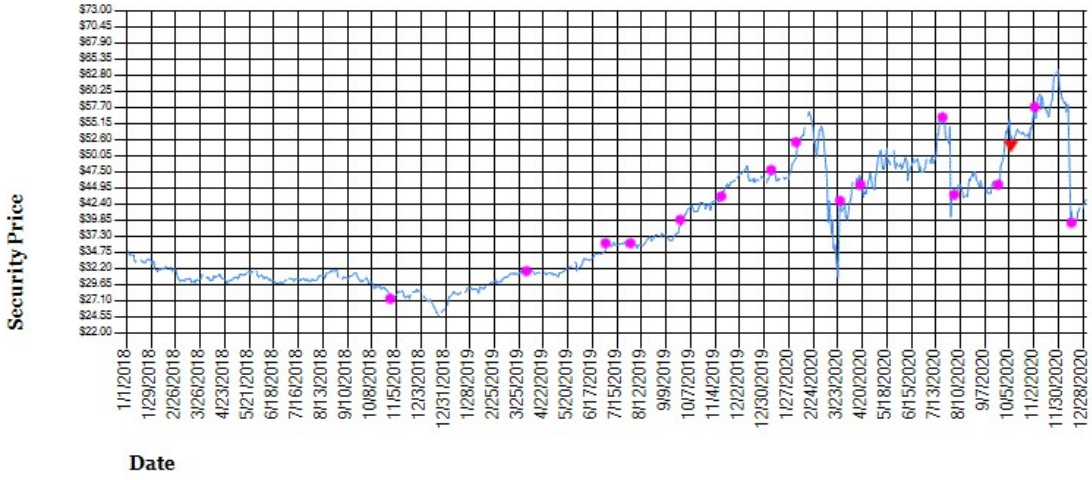
Brookfield Renewable Partners LP (BEP) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	1/1/2018		Reeder				
	1/1/2018	NA	1	37	NE	NE	34.92
●	10/31/2018	27.48	1	34	NE	NE	27.25
●	4/4/2019	31.46	1	36	NE	NE	31.46
●	7/3/2019	36.03	1	38	NE	NE	35.99
●	7/31/2019	35.91	1	39	NE	NE	35.85
●	9/27/2019	39.24	1	42	NE	NE	39.70
●	11/12/2019	43.39	1	46	NE	NE	43.27
●	1/8/2020	47.44	1	51	NE	NE	47.44
●	2/6/2020	52.20	1	57	NE	NE	52.02
●	3/26/2020	41.54	1	47	NE	NE	42.75
●	4/20/2020	46.95	1	52	NE	NE	45.22
●	7/22/2020	55.90	1	60	NE	NE	55.90
●	8/4/2020	44.81	1	48	NE	NE	43.50
●	9/23/2020	44.95	1	50	NE	NE	45.27
▼●	10/8/2020	53.11	2	53	NE	NE	51.27
●	11/5/2020	55.91	2	55	NE	NE	57.50
●	12/16/2020	41.14	2	40	NE	NE	39.31

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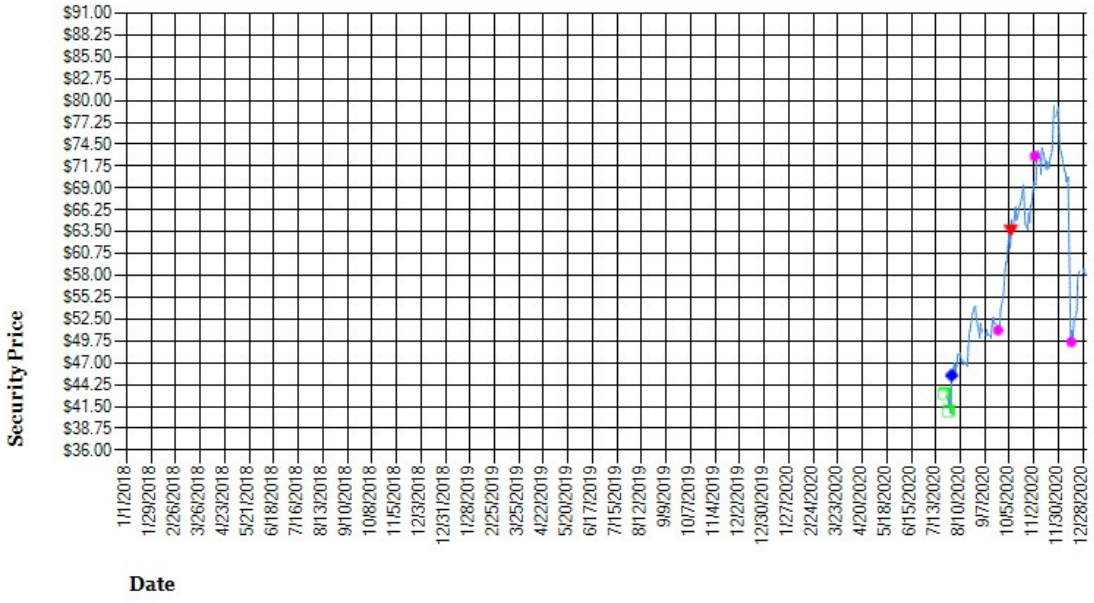
Brookfield Renewable Corporation (BEPC) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
▫	7/24/2020		begins when issued trading				
▫	7/30/2020		beings trading after unit split (1 for 4) from BEP shares				
	8/3/2020		Reeder				
◆	8/4/2020	47.00	1	51	NE	NE	45.17
●	9/23/2020	51.15	1	55	NE	NE	50.91
▼●	10/8/2020	64.98	2	60	NE	NE	63.43
●	11/5/2020	69.42	2	62	NE	NE	72.87
●	12/16/2020	51.06	2	47	NE	NE	49.46

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WTRG: Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.
BIP: Key risks, in our view, include prolonged economic fallout from the COVID-19 outbreak, the potential for a strategic misstep, foreign exchange risks, exposure to foreign governments, regulatory/contract risks and capital markets risks.
BIPC: Key risks, in our view, include prolonged economic fallout from the COVID-19 outbreak, the potential for a strategic misstep, foreign exchange risks, exposure to foreign governments, regulatory/contract risks and capital markets risks.
BEP: Key risks, in our view, include prolonged economic fallout from the COVID-19 outbreak, the potential for a strategic misstep, foreign exchange risks, exposure to foreign governments, contract risks and capital markets risks.
BEPC: Key risks, in our view, include prolonged economic fallout from the COVID-19 outbreak, the potential for a strategic misstep, foreign exchange risks, exposure to foreign governments, contract risks and capital markets risks.

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1=Overweight: Total return on stock expected to be 10%+ over the next 12 months. BUY
2=Equal Weight: Total return on stock expected to be 0-10% over the next 12 months. HOLD
3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

VOLATILITY RATING
V=A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: January 5, 2021

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11% of companies covered by Wells Fargo Securities, LLC Equity Research are rated Underweight.	Wells Fargo Securities, LLC has provided investment banking services for 32% of its Underweight-rated companies.

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WELLS FARGO SECURITIES

Essential Utilities, Inc.

WTRG: ALJ Recommendation a Setback but DELCORA Deal Far from Dead

Reiterate Overweight

Overweight/$52

Water Utilities

Company Note

- **Key Points.** The ALJ recommendation in the pending DELCORA deal was posted to the PaPUC website on 1/12. It recommends denial as (1) ongoing litigation regarding DELCORA's ability to transfer assets under the asset purchase agreement and (2) failure to attach the rate stabilization plan to the application make it too difficult to make an informed recommendation regarding if the deal is in the public interest. WTRG plans to file objections. This is no doubt a setback but in no way does it appear to kill the DELCORA deal. For starters, it does not necessarily convey the PaPUC commissioners' view (the PaPUC order is due by 3/26). We believe there is still a reasonable pathway to approval – perhaps through settlement – however it could push deal closure beyond early Q2'21. Reiterate Overweight.
- **Ongoing Litigation.** These lawsuits are separate from the 12/28 ruling in favor of DELCORA/WTRG regarding the APA's validity and ability to put the $210M of net proceeds into a trust. Rather five of the 49 municipalities served by DELCORA (represent 9% of annual revenues) have not yet consented to the transfer of the assets and/or assignment of contracts to WTRG – though WTRG reached a settlement on 1/8 with one (Trainer) resolving its issues. Three of the munis (SWDCMA, Lower Chichester and Upland) filed lawsuits in early November in the Delaware County Court of Common Pleas.
- **Path Forward.** At this time it is unclear to us what the path forward would be if settlements are not reached with the remaining four munis and/or the section of the APA that contemplated such a scenario is not upheld/enforced. Can they be carved out of the deal? Once those issues are resolved, the reasonableness of the purchase price under PA's FMV law as well as the public interest determination can be made. The ALJ indicates a new application should be filed to reflect those updates along with the rate stabilization plan and tariff provisions outlining the bill credit mechanism to limit customers' rate increases to a 3% compound annual maximum (so long as the trust remains solvent). If a new application is indeed required, we believe it would push the potential closing date to late '21 or early '22.
- **Reiterate Overweight.** First, getting the $277M DELCORA deal closed is more important than the timing. The near-term EPS impact is minimal. The strategic value is longer-term, including the fact that the bulk of DELCORA's $700M capex needs through '28 fall in the 2026-28 period. Second, our Overweight thesis is not solely predicated on DELCORA closing. As previously stated, though the DELCORA deal is highly supportive of WTRG's growth aspirations, we consider the future to be bright without it, driven by elevated pipeline infrastructure investment needs for the foreseeable future supplemented by municipal M&A trends. We believe relatively low risk, regulated EPS growth of at least 6% is achievable and that rate of growth would simply be enhanced if DELCORA closes.

$ EPS	2019A	2020E Curr.	2020E Prior	2021E Curr.	2021E Prior
Q1 (Mar.)	0.28	0.60 A	NC	0.67	NC
Q2 (June)	0.37	0.29 A	NC	0.25	NC
Q3 (Sep.)	0.48	0.23 A	NC	0.25	NC
Q4 (Dec.)	0.34	0.46	NC	0.50	NC
FY	1.47	1.58	NC	1.67	NC
CY	1.47	1.58		1.67	
FY P/EPS	31.9x	29.7x		28.1x	
Rev.(MM)	890	1,931		2,055	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile
Adjusted EPS excludes items considered non-recurring.
WTRG expects 2021 adjusted EPS of $1.64-1.69 range and targets a 5-7% EPS CAGR through 2023 off the 2019 adjusted base of $1.47.
WTRG expects 2020 adjusted EPS at the top end of the $1.53-1.58 range.

Ticker	WTRG
Price Target/Prior:	**$52/NC**
Price (01/13/2021)	**$46.88**
52-Week Range:	$30-55
Shares Outstanding: (MM)	245.2
Market Cap.: (MM)	$11,495.0
S&P 500:	3,809.84
Avg. Daily Vol.:	923,308
Dividend/Yield:	$1.00/2.1%
LT Debt: (MM)	$5,277.4
LT Debt/Total Cap.:	53.2%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	7.0%
CY 2021 Est. P/EPS-to-Growth:	4.0x
Last Reporting Date:	11/03/2020 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Please see page 3 for rating definitions, important disclosures and required analyst certifications. All estimates/forecasts are as of 01/14/21 unless otherwise stated. 01/14/21 05:39:16 ET

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Acronyms:

ALJ – Administrative Law Judge
APA – Asset Purchase Agreement
DELCORA – Delaware Country Regional Water Quality Control Authority
FMV – Fair Market Value
PaPUC – Pennsylvania Public Utility Commission
SWDCMA – Southwest Delaware County Municipal Authority

Price Target

Price Target: $52 from NC

Our $52/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.80. For WTRG's water utility multiple, we ascribe a roughly 5% discount to the 21E multiple we use for AWK (34-34.5X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The roughly 5% discount reflects a modestly lower earnings growth rate (we forecast roughly 7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 17.0-17.5X (based on ATO, NWN, OGS & SR) and then apply a roughly 10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive PA regulatory framework. Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

Investment Thesis

Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived and near-term regulatory risk is low as both the water and gas utilities completed rate cases in 2019), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

Company Description

Headquartered in Bryn Mawr, PA, Essential Utilities (WTRG) - formerly Aqua America - is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTRG's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total water customer base and nearly 70% of consolidated water rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio.

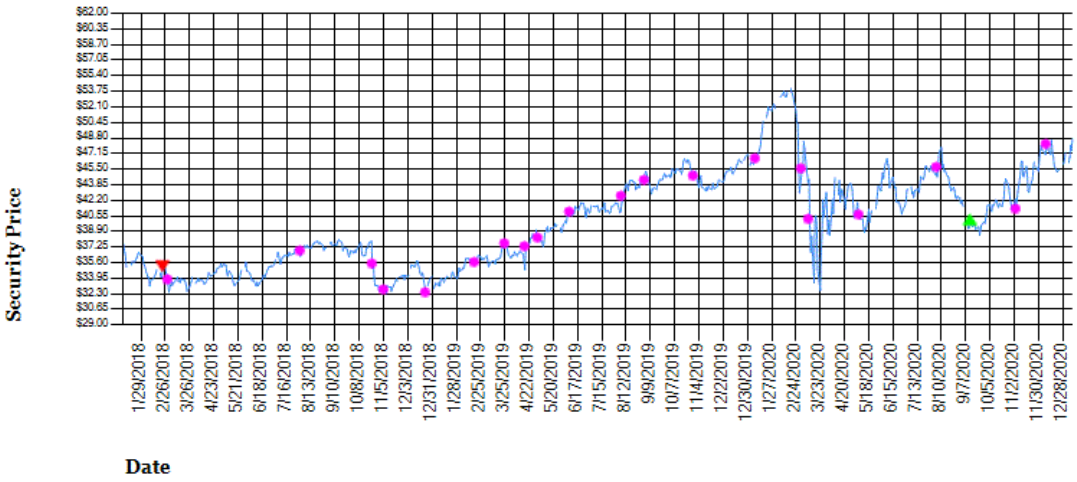
In March 2020, WTRG closed on the acquisition of Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, WTRG paid 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to other gas utility transactions at the time. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

Regulated operations account for more than 99% of consolidated revenues. Consolidated EPS is expected to be driven roughly 70% by water utility operations with the gas utility contributing the remaining 30%.

In February 2020, the new name Essential Utilities, Inc. and new ticker WTRG became effective. Prior, the company was known as Aqua America Inc. and traded under the ticker WTR.

Required Disclosures

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	1/8/2018		Reeder				
	1/8/2018	NA	1	43	NE	NE	37.71
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51
●	3/2/2020	43.01	2	45	NE	NE	45.44
●	3/11/2020	44.41	2	48	NE	NE	40.03
●	5/7/2020	40.49	2	42	NE	NE	40.53
●	8/6/2020	45.56	2	45	NE	NE	45.56
▲	9/14/2020	39.35	1	45	NE	NE	39.82
●	11/4/2020	41.19	1	47	NE	NE	41.19
●	12/10/2020	47.70	1	52	NE	NE	48.02

*Effective December 7, 2019, Wells Fargo Securities' Equity Research modified its ratings definitions. Complete definitions of current ratings can be found below. For information related to prior ratings definitions, please contact equityresearch1@wellsfargo.com.

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
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WTRG: Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

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3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

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As of: January 14, 2021

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Company Update — February 25, 2021

Water Utilities

Essential Utilities, Inc. (WTRG)

WTRG: Recent Weakness Provides Attractive Entry Point – We Remain Bullish on WTRG's LT Growth Prospects

Our Call

We believe the recent weakness provides an attractive entry point as the fundamental narrative has not changed. Since 1/8, shares of WTRG are down 11%. This trails "larger cap" water utility peers (-0% to -8%), gas LDCs (+6%) & S&P Utilities (-5%). We reiterate our Overweight rating and $52/sh price target (29X our 22E). WTRG's YE'20 update was consistent with the mid-January guidance event including '21 diluted EPS guidance of $1.64-1.69 (cold YTD weather has Peoples off to a strong start), a 5-7% EPS CAGR target through '23 and $3B of capex over the 2021-23 period which will drive underlying 6-7% water and 8-10% gas rate base CAGRs. Our 21-25E EPS remain $1.67, $1.80, $1.93, $2.07 & $2.20. Our forecast results in an EPS CAGR near the upper end of WTRG's 5-7% range which we believe is reasonable given strong underlying rate base growth driven by accelerated pipeline replacement needs and a municipal M&A strategy that continues to gain momentum.

A Very Healthy Municipal Deal Pipeline. Following a solid 2020 ($63M of deals), 2021 is shaping up to be even better (signed $90M of new deals in 2020). Besides the $277M DELCORA deal, WTRG has five other signed APA's which will add $161M in rate base – includes four separate chunky wastewater deals (East Whiteland, PA $55M; Lower Makefield, PA $53M; Bourbonnais, IL $32M; Williston Township, PA $17.5M). In addition there is the $12M purchase of Shenandoah, PA's water assets – the borough council approved the deal in late November and the APA is still being finalized. WTRG's deal development pipeline remains robust and management continues to express optimism that activity will start ramping up in the years ahead in the four states that only somewhat recently adopted FMV legislation (NC & OH in '18; TX in '19; VA in '20). Our model reflects primarily announced deal closures over the 2020-22 period plus a $75M/year placeholder in '23 & beyond. This could prove conservative if the recent pace continues.

Big Picture DELCORA Thoughts. We believe the deal will close as discussed in greater detail later in this note. Getting DELCORA across the finish line is more important than the timing of it given the longer-term strategic value it represents. Beyond the $277M rate base pick up at closure (expected early Q2'21), we are attracted to (1) the $700M of capital investments – $25-50M/year for typical repair/replace work plus roughly $300M over the 2026-28 period related to DELCORA's treatment plant – as well as (2) the likely substantial wastewater tuck-in deals that could transpire in the area. But our Overweight thesis is not solely predicated on DELCORA closing. We believe relatively low risk, regulated EPS growth in the 5-7% range is achievable without driven by pipeline replacement needs and municipal M&A momentum. That rate of growth would simply be enhanced if DELCORA closes as it should allow WTRG to extend it through the end of the decade and perhaps even raise it.

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Rating	Overweight
Ticker	**WTRG**
Price Target/Prior:	**$52.00/NC**
Upside/(Downside) to Target	**19.6%**
Price (02/25/2021)	**$43.49**
52 Week Range	$30.40 - 52.00
Shares Outstanding	245,271,727
Market Cap (MM)	$10,667
Enterprise Value (MM)	$16,023
Average Daily Volume	979,436
Average Daily Value (MM)	$43
Dividend (NTM)	$1.00
Dividend Yield	2.3%
Net Debt (MM) - last reported	$5,357
ROIC - Current year est.	9%
3 Yr EPS CAGR from current year (unless otherwise noted)	7%

$ EPS	2020A	2021E Curr.	2021E Prior	2022E Curr.	2022E Prior
Q1 (Mar)	0.60 A	0.67 E	NC	-	NC
Q2 (Jun)	0.29 A	0.25 E	NC	-	NC
Q3 (Sep)	0.23 A	0.25 E	NC	-	NC
Q4 (Dec)	0.46 A	0.50 E	NC	-	NC
FY	1.58 A	1.67 E	NC	1.80 E	NC
P/E	27.6x	26.1x		24.1x	

ROIC - Current year est.: ROIC is actually ROE Source: Company Data, Wells Fargo Securities estimates, and Refinitiv.
NA = Not Available, Volatility = Historical trading volatility

All estimates/forecasts are as of 2/25/2021 unless otherwise stated. 2/25/2021 12:52:32 EST. Please see page 5 for rating definitions, important disclosures and required analyst certifications. Wells Fargo Securities, LLC does and seeks to do business with companies covered in its research reports. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of the report and investors should consider this report as only a single factor in making their investment decision.

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Next PA Rate Cases

WTRG does not have any major rate-setting procedures pending. The next PA water & wastewater rate case filing is expected around mid-'21 while the next gas one might be made in late '22. While WTRG's PA rate cases can never be overlooked given the meaningful % of rate base represented (more than 70% on the water/wastewater side), the utility has a long history of reaching constructive outcomes via settlement agreements. In addition, despite the pandemic-related economic challenges faced by many ratepayers that has led to heightened rate sensitivity in some states, the PA regulatory environment has upheld its constructive reputation – includes the recent NI rate case outcome as well as the ALJ recommendation in the pending AWK case which honors the 10/30 settlement agreement.

Peoples Repairs Tax Deduction Settlement

Management noted that a verbal settlement has been reached with intervenors that will give back 100% of the catchup benefits to ratepayers over a 5-year period. This contrasts with WTRG's proposal where 40% of the benefits would have been shared directly with ratepayers through surcredits on bills and the remaining 60% used as an increasing income tax expense offset over the 2023-25 period in order to avoid implementing a gas base rate increase prior to 1/1/2026. We view the move as goodwill gesture on WTRG's part to help provide customers with some additional bill relief as they deal with the economic impacts of the pandemic. As noted above, we expect Peoples next base rate filing could occur in late '22.

A Deeper Dive Into The DELCORA Approval Process

Since the ALJ recommendation for denial of the $277M deal was posted to the PaPUC website on 1/12, a few developments have occurred.

(1) **Delaware County on 1/21 appealed the 12/28 decision** by Judge Barry Dozor in the Court of Common Pleas of Delaware County. Recall, Judge Dozer ruled against Delaware County's two claims and in favor of DELCORA and WTRG regarding the validity of the asset purchase agreement as well as the ability to put the net proceeds of roughly $200M from the sale into a trust to be used to stabilize ratepayers' bills in the years ahead.

(2) **Settlements have been reached with two more of the municipalities** that had not yet consented to the transfer of the assets and/or assignment of contracts to WTRG from DELCORA and each has discontinued its Complaint in the Court of Common Pleas of Delaware County. One was SWDCMA which constitutes ~5% of DELCORA's annual revenues or the bulk of the 9% represented by all of the holdouts. That leaves only two remaining (the Townships of Edgmont and Lower Chichester) out of the 49 total municipalities served. Discussions remain ongoing and the parties do not oppose the PaPUC approving the DELCORA transaction with the condition that these contractual issues be resolved prior to closing.

(3) **WTRG and DELCORA withdrew the proposed customer assistance bill payment that the ALJ recommendation concluded was a "rate stabilization" plan**. Rather than show it as a credit against the amount due on wastewater bills, DELCORA customers will get the $200M of net benefits from the transaction through direct mail, quarterly payments.

We continue to believe the DELCORA deal will eventually be approved by the PaPUC and close. For starters, the ALJ recommendation does not necessarily convey the PaPUC commissioners' views. That point was highlighted just recently in the constructive conclusion of NI's rate case despite an ALJ recommendation to deny the requested increase altogether. Approval just may take some additional time beyond WTRG's early Q2'21 target. We cannot rule out the potential need to re-file the PaPUC application and/or extend the current statutory timeframe beyond the 3/26 deadline. With only four of the five PaPUC commissioner chairs filled right now, it is possible a 2-2 stalemate occurs.

But under the assumption the ALJ recommendation is consistent with where commissioner heads were in mid-January, WTRG has largely addressed the concerns expressed, in our opinion. Recall, ALJ rationale for denial was that (1) ongoing litigation regarding DELCORA's ability to transfer assets under the asset purchase agreement and (2) WTRG's failure to attach the rate stabilization plan to the application make it too difficult to make an informed recommendation regarding if the deal is in the public interest.

We believe the 12/28 Court of Common Pleas order combined with the additional municipal settlements (and likely two future ones) should allow the reasonableness of the purchase price under

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PA's FMV law as well as the public interest determination to be made by the PaPUC. Reaching a settlement with Delaware County – an outcome that management continues to strive for, possibly even after the 3/26 PaPUC decision deadline – that results in dismissal of the appeal would seemingly de-risk the conclusion even further. Finally, the withdrawal of the "rate stabilization" plan should make the ALJ's concern on that point moot.

Acronyms Used:

ALJ – Administrative Law Judge

APA – Asset Purchase Agreement

DELCORA – Delaware Country Regional Water Quality Control Authority

FMV – Fair Market Value

PaPUC – Pennsylvania Public Utility Commission

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Price Target Basis and Risk

Price Target for WTRG: $52.00 from NC

Our $52/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.80. For WTRG's water utility multiple, we ascribe a roughly 5% discount to the 21E multiple we use for AWK (34X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The roughly 5% discount reflects a modestly lower earnings growth rate (we forecast roughly 7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 18.0-18.5X (based on ATO, NWN, OGS & SR) and then apply a roughly 10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive PA regulatory framework.

Risk for WTRG

Key downside risks include adverse regulatory decisions, issues with the Peoples gas deal integration and earnings accretion, missteps with regards to the M&A strategy and execution as well as potential anti-gas sentiment and ESG concerns stemming from the ownership of a gas utility.

Investment Thesis

WTRG

Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived and near-term regulatory risk is relatively low as both the water and gas utilities completed rate cases in 2019), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

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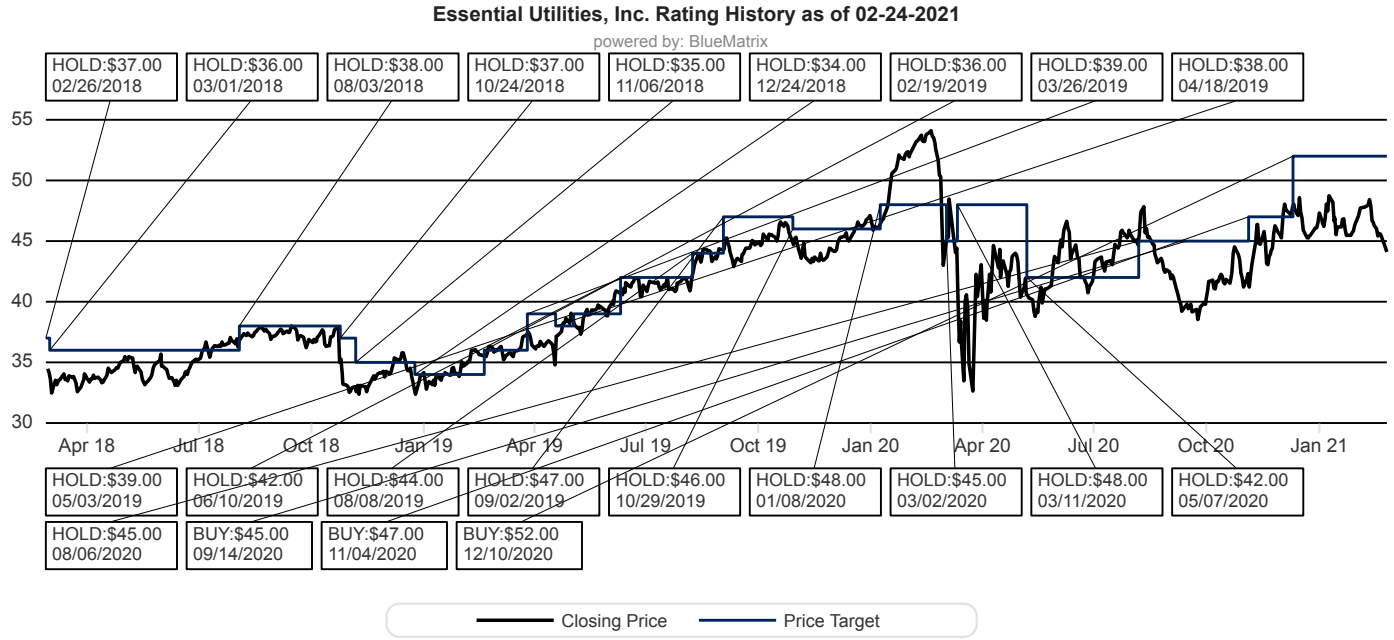

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2=Equal Weight: Total return on stock expected to be 0-10% over the next 12 months. HOLD

3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

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WELLS FARGO SECURITIES

Flash Comment

Utilities

Utility & Infrastructure Daily

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Sarah Akers, CFA, Senior Analyst (314) 875-2040
Jonathan Reeder, Senior Analyst (314) 875-2052
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Quick thoughts from Wells Fargo Securities, LLC Utility & Infrastructure Team:

Utilities

Aqua America (WTR/Market Perform)(Reeder) – We had the chance to catch up with WTR regarding the company's disclosure yesterday (6/12) that a settlement agreement was filed with the PA Public Utilities Commission (PaPUC) in the Peoples merger approval docket (A-2018-3006061). Because there is an outstanding issue between two of the intervenors that prevented a unanimous settlement from being reached – relates to the preferred path forward for a 1,600 customer system – the remainder of the docket must play out as scheduled so that the PaPUC can decide the issue. This is what pushes the expected close of the merger into fall 2019. It is our understanding that the settlement agreement does not address any Peoples revenue requirement issues. Rather the appropriate revenue requirement going forward will be determined as part of the pending Peoples rate case. This could include (1) the potential election and treatment of repairs tax deduction at Peoples (discussed on the Q1'19 earnings call) and (2) the potential to realize (and retain) any merger synergies. We continue to expect a constructive outcome in the Peoples rate case later this year and believe the potential election of repairs tax deduction could be a powerful bargaining chip for the utility as settlement discussions take place. Rate case hearings are scheduled to begin June 18.

In terms of our EPS outlook, as we stated yesterday (6/12), the delayed merger close is likely to negatively impact our current 19E EPS of $1.37 which was predicated on a mid-'19 close. Our preliminary analysis suggests pushing it to the end of Q3'19 could have up to a ($0.10) impact. Importantly, we do not have any reason to believe at this point that our 20-23E of $1.56, $1.66, $1.78 & $1.90 are not still within reason. Given the multiple moving parts in '19 related to the merger and rate relief, we believe investors should focus on '20 & beyond for a better sense of WTR's ongoing EPS power. Our '20 & beyond outlook is predicated on earned ROEs at both the water and gas utilities of 10-10.5%.

Aqua America, Inc. (WTR)/Market Perform (2)
Price as of 6/12/2019: $41.12
FY 19 EPS: $1.37
FY 20 EPS: $1.56
Shares Out.: 178.1 MM
Market Cap.: $7,323.47 MM

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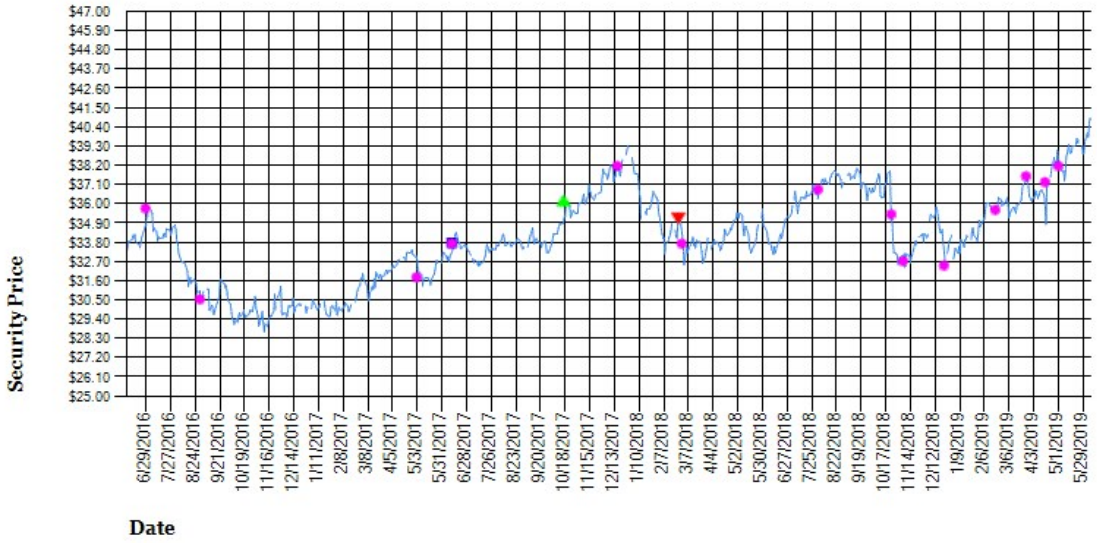
Rating Basis Information:
WTR Thesis: We are attracted to WTR's strong fundamentals - a proven EPS growth strategy, a growing rate base, constructive regulation, efficient operations and a strong balance financial profile. Our Market Perform rating reflects valuation considerations in light of WTR's pending agreement to acquire Peoples (a gas utility) and the associated P/E multiple, regulatory and deal execution/integration related risks.

DISCLOSURE APPENDIX

Required Disclosures

Aqua America, Inc. (WTR) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	6/7/2016		Kalton				
	6/7/2016	NA	2	NE	33.00	34.00	33.21
●	6/30/2016	35.39	2	NE	35.00	36.00	35.66
●	8/31/2016	30.38	2	NE	31.00	33.00	30.41
●	5/4/2017	31.70	2	NE	32.00	34.00	31.73
■	6/13/2017		Reeder				
●	6/13/2017	33.62	2	35	NE	NE	33.62
▲●	10/19/2017	35.30	1	40	NE	NE	36.03
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Outperform/Buy	SR	Suspended
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3	Underperform/Sell	NE	No Estimate

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3=Underperform: The stock appears overvalued, and we believe the stock's total return will be below the market over the next 12 months. SELL

SECTOR RATING
O=Overweight: Industry expected to outperform the relevant broad market benchmark over the next 12 months.
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As of: June 13, 2019

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WELLS FARGO SECURITIES

Aqua America, Inc.

WTR: EPS Outlook Updated As ALJ Recommends Approval Of Peoples Acquisition

Market Perform/$46

Water Utilities
Market Weight

Earnings Estimate Revised Down

- **EPS Outlook Updated As Peoples Merger Close Timing Comes Into Focus.** The assigned Administrative Law Judge (ALJ) to the Peoples merger docket issued the long awaited recommended decision (RD) on 10/28. ALJ Long's RD not only approves WTR's acquisition of the Peoples Companies but adopts the non-unanimous settlement agreement in its entirety. This includes the proposed $120M investment over a 7-year period to update the deteriorated 1,700 customer, 368 mile Goodwin and Tombaugh (G&T) gathering system and replace the existing bare steel pipe as well as a one-time $13M rate credit offered by WTR to partially offset this cost. WTR and the seven other settling parties, including key intervener Office of Consumer Advocate (OCA), support updating the G&T system as the preferred path forward and socializing those costs across Peoples entire customer base whereas the PaPUC's Bureau of Investigation & Enforcement (I&E) and Office of Small Business Advocate believe those customers that cannot be updated economically should be abandoned and forced to convert to an alternative energy source. In fact, ALJ Long goes as far as to characterize the remediation of the G&T system as the most significant benefit of the transaction.

  As we previously discussed, parties have 30 days from the RD to file exceptions and it is likely that the PaPUC (Pennsylvania Public Utilities Commission) may take at least 30 days after that to render a final decision (absent the parties reaching unanimous settlement in light of the ALJ's RD). As such, WTR now anticipates a December 2019 or early 2020 close. We are encouraged by the ALJ's RD and anticipate the PaPUC is likely to ultimately adopt the RD.

  We lower our 19E EPS to $1.19 from $1.32 to reflect an assumed YE'19 close by removing the roughly two months of Peoples net income benefit from our previously assumed end of October '19 deal close. In addition, we made a few other tweaks to our model, primarily related to external financing assumptions including correcting an error that overstated some cash inflows in 2019. As a result, we adjust our 2020-23E EPS down modestly to/from $1.57/$1.58, $1.70/$1.71, $1.80/$1.82 & $1.92/$1.94. This results in a 6.5-7.0% EPS CAGR. As a reminder, our outlook continues to exclude any potential uplift from the planned election of repairs tax deduction at Peoples in 2020. We reiterate our Market Perform rating but lower our 12-18 month price target to $46/share from $47 to reflect lower peer multiples since our last update.

$ EPS	2018A	2019E Curr.	2019E Prior	2020E Curr.	2020E Prior
Q1 (Mar.)	0.29	0.28 A	NC	NE	
Q2 (June)	0.37	0.35 A	NC	NE	
Q3 (Sep.)	0.44	**0.39**	**0.40**	NE	
Q4 (Dec.)	0.31	**0.19**	**0.30**	NE	
FY	1.41	**1.19**	**1.32**	**1.57**	**1.58**
CY	1.41	1.19		1.57	
FY P/EPS	31.8x	37.7x		28.6x	
Rev.(MM)	838	895		1,979	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile
WTR's 2019 ongoing diluted EPS guidance of $1.45-1.50 excludes ALL Peoples related impacts. Our estimates are pro-forma Peoples, ex costs to complete.

Ticker	WTR
Price Target/Prior:	**$46/$47**
Price (10/28/2019)	**$44.90**
52-Week Range:	$32-47
Shares Outstanding: (MM)	215.7
Market Cap.: (MM)	$9,684.9
S&P 500:	3,022.55
Avg. Daily Vol.:	1,029,020
Dividend/Yield:	$0.94/2.1%
LT Debt: (MM)	$2,749.0
LT Debt/Total Cap.:	40.4%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	7.0%
CY 2019 Est. P/EPS-to-Growth:	5.4x
Last Reporting Date:	08/06/2019 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Price Target

Price Target: $46 from $47

Our $46/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 2.5% discount to our 70% water/30% gas utility hybrid multiple to our 2021E of $1.71. The 2.5% discount reflects merger execution/integration risk. For WTR's water utility multiple, we start with AWK's 2020 P/E multiple of 30.3X (AWK represents the closest publicly traded peer) and apply a 5% discount (given AWK's higher growth rate and best-in-class management team). For WTR's gas utility multiple, we utilize the 2020 pure play gas LDC median of 24.6X. Key risks include regulatory and M&A strategy execution related.

Investment Thesis

We are attracted to WTR's strong fundamentals - a proven EPS growth strategy, a growing rate base, constructive regulation, efficient operations and a strong balance financial profile. Our Market Perform rating reflects valuation considerations in light of WTR's pending agreement to acquire Peoples (a gas utility) and the associated P/E multiple, regulatory and deal execution/integration related risks.

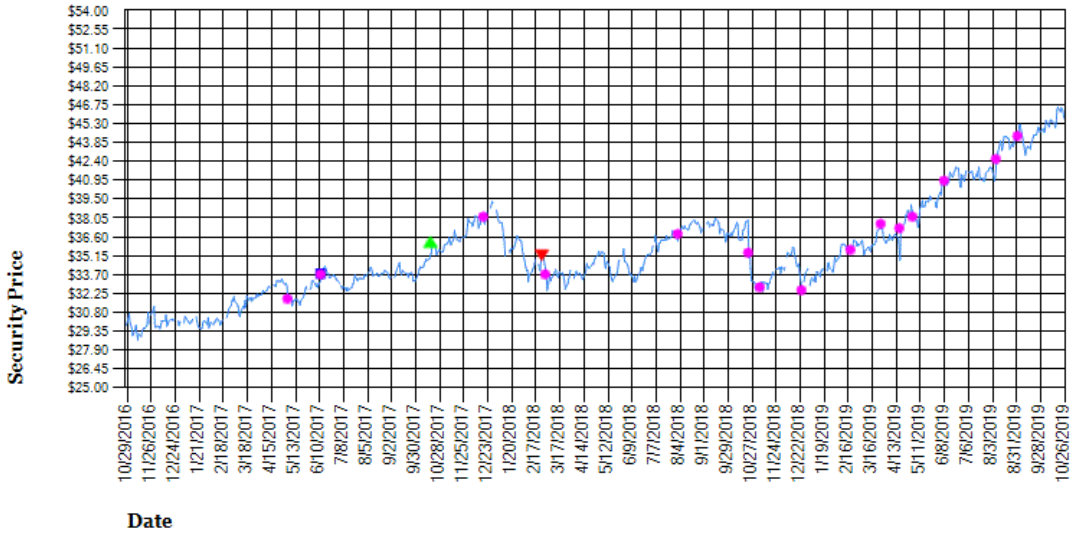
Company Description

Headquartered in Bryn Mawr, PA, Aqua America (WTR) is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTR's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total customer base and nearly 70% of consolidated rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio. Regulated operations account for more than 99% of consolidated revenues.

On 10/23/18, WTR announced a deal to acquire Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, the deal appears to be 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to what we have seen in recent gas utility transactions. WTR expects to close the deal around YE'19, subject to receiving the final necessary regulatory approval from PA. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

Required Disclosures

Aqua America, Inc. (WTR) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	10/26/2016		Kalton				
	10/26/2016	NA	2	NE	31.00	33.00	29.86
●	5/4/2017	31.70	2	NE	32.00	34.00	31.73
■	6/13/2017		Reeder				
●	6/13/2017	33.62	2	35	NE	NE	33.62
▲●	10/19/2017	35.30	1	40	NE	NE	36.03
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Outperform/Buy	SR	Suspended
2	Market Perform/Hold	NR	Not Rated
3	Underperform/Sell	NE	No Estimate

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3=Underperform: The stock appears overvalued, and we believe the stock's total return will be below the market over the next 12 months. SELL

SECTOR RATING
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As of: October 29, 2019

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2020 EEI Conference Takeaways

Utilities

- **Key Points.** We hosted virtual meetings with 38 companies at the EEI Financial Conference on November 8-11th. The tone of the conversations were positive with sales recovering nicely and most utilities finding offsets (cost controls and regulatory support) to COVID impacts. Further, the de-carbonization theme was in full force with no shortage of investment opportunities to modernize the electric generation fleet as well as the enabling T&D infrastructure. On the strategic front, conversations centered around the trend toward pure play utility models and interest in M&A, particularly on the LDC side given depressed valuations.
- **Strategic Questions Abound.** This year's conference featured many discussions around strategic options as diversified utilities were asked about transitioning to pure play models and combo electric/gas utilities were asked about their appetite for LDC acquisitions. Among the diversified names, ED and SRE expressed the most openness to strategic moves, in our view. Separately, CNP and OGE were fairly reserved on their comments on ENBL, though we expect to hear more from CNP at the 12/7 analyst day. Companies that are in the midst of divesting or potentially divesting assets (EXC, DTE, PEG, PPL) faced questions about whether they would entertain regulated M&A opportunities post-divestiture (assuming they have greater financial flexibility).

  On the LDC front, reviews were mixed with most mgmt. teams expressing confidence in the long-term business model, but some not willing to add gas to the mix. Companies that expressed the most openness to acquiring LDC systems, in our view, were ALE, BKH, MDU, SO and WEC (not without some cautious language). And for good measure, there was a mid-EEI Reuters report suggesting that NEE made a recent offer for EVRG, which both companies talked down.
- **Optimism on Sales**. Most utilities expressed cautious optimism that C&I sales are coming back and some portion of the uptick in residential could be sustainable given a new working environment. Certain utilities in desirable areas (IDA, NWE and POR, for example) also discussed strong in-migration trends as a result of increased mobility/flexibility in the work place.
- **Guidance Updates.** A few utilities used the EEI conference to update capex/growth forecasts. AEP laid out a robust capex refresh that was heavy on renewables and wires investment (surprise, surprise) and continued to support the 5-7% EPS CAGR. ALE lowered the 2019-2024 EPS CAGR to 4% from 5-7% reflecting COVID impacts and pressure on wind returns. And NWE initiated 2021 EPS guidance and increased the 5-year capex budget, which continues to support the mid-point of the 3-6% EPS CAGR.
- **Company-Specific Takeaways in Body of Note.**

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ALLETE Inc. (ALE/Equal Weight/$58.30) (Akers)

Growth Rate Buckles Under COVID Pressures. ALE is one of the more COVID-exposed companies within our universe because of Minnesota Power's industrial (especially taconite) heavy customer base. Taking various pressures under consideration (electric demand, down-sized transmission project, lower assumed equity issuance price, pressure on wind returns, etc.), mgmt. revised the EPS CAGR to 4% (through '24 off the '19 adjusted base of $3.35) from 5-7%. The growth rate assumes 3% growth at the utility operations and 30% at ALLETE Clean Energy (ACE). The company acknowledged that the 4% CAGR could be conservative should an economic recovery prove faster/stronger than anticipated. On the positive side, ALE is seeing a pickup in steel demand and, importantly, Keetac recently indicated plans to reopen in December, which provides more certainty into 2021, though Verso's future remains unclear. MP filed a request to defer the lost revenue associate with Keetac and Verso – upside to '20E & '21E if approved – and plans to file a general rate case in November '21.

Tone Change on ACE. Mgmt. indicated that ACE is beginning to see pressure on wind returns stemming from increased competition and lower power prices. As a result, the previous target of adding 2-3 wind projects annually may prove challenging. ALE will continue to evaluate wind opportunities, but is also looking at other services, such as solar, storage and grid resiliency as potentially more attractive growth avenues. On the Q3 call, which was during EEI, mgmt. also mentioned the possibility of optimizing the ACE portfolio, which we expect could include asset sales.

Ameren Corporation (AEE/Overweight/$82.37) (Kalton)

Waiting on the CapEx Refresh. EEI is not a big event for AEE as the company provides prompt year EPS guidance and the 5-yr capex refresh in conjunction with Q4 earnings. That being said, we picked up a few tidbits on pending items. First, the renewables RFP in MO is ongoing and it is doubtful that results will be in on time to include in the '21-25 capex refresh – mgmt. is always hesitant to get too far in front of the regulatory approval process in terms of officially adding capital to the base plan. That being said, we think there are plenty of capital investment needs outside the RFP to support a 6%+ EPS CAGR well into the 2020s. As an aside, mgmt. noted that capex spending on technology is up many multiples in MO since the MoPSC approved the PISA mechanism – the reduced regulatory lag allows for improved returns for short lived assets. If/when new MO renewables comes into the fold it remains an open question as to whether it will be purely incremental to the '21-25 plan or whether there will be some capex shifting (factors will include customer rate considerations and financing needs). No new developments on the IL legislative front – mgmt. continues to work with stakeholders as everyone eyes comprehensive energy legislation in the Spring '21 session (and not the Nov. '20 veto session). At issue for AEE are the existing formula rate structure and the allowed ROE methodology for the electric distribution operations and (maybe) the investment rider for the gas utility.

American Electric Power Company, Inc. (AEP/Overweight/$91.15) (Kalton)

New Robust CapEx Plan. While AEP's 5-yr capex refresh ('21-25) was higher than we anticipated ($37B vs. $35B), the underlying drivers were exactly as we expected (wires + renewables). Renewables represents nearly 15% of the planned capex vs. 7% in the original '20-24 capex guidance. Yes, the $2B North Central Wind project was officially added to the capex schedule but other regulated renewables are coming into the fold at AEP's vertically integrated utilities. Renewable additions (owned & PPA) in these jurisdictions are expected to total over 4,600 MW during '21-25 with another 3,400 MW planned for '26-30. As for wires, there is plenty of spend across the board with seams solutions offering potential significant upside in the mid-20s and beyond as transmission grid spend will likely accelerate to better allow for the flow of renewable power across regions. AEP's large geographic footprint combined with strong transmission expertise positions the company for this coming opportunity. All told, the phrase "long capex runway" gets thrown around a lot in the utility sector, but it's clearly appropriate when framing AEP's investment opportunities.

Thoughts on EPS Guidance / Asset Sales. AEP also rolled out initial '21 EPS guidance of $4.51-$4.71, the mid-point of which represents a 6% increase over the '20 EPS guidance mid-point of $4.35 – consistent with AEP's 5-7% EPS CAGR goal. We view the '21 guide as solid but not exceptional (our 21E EPS is $4.70). Notably, the '21 forecasted ROE of 9.0% is a smidge below our estimate of 9.2%. While 20 bps doesn't sound like much, it equates to ~$0.20, or 4%, of EPS power. Keep in mind, the earned ROE guidance heading into '19 was 9.65% and heading into '20 was 9.1% (however, '20 was characterized as a transition year due to a heavy rate case cycle). We think the overall downward trend in allowed ROEs is playing a role in the ROE guidance but it is not the only factor. Mgmt. noted that 30% of the company's capital spend does not have formula or rider rate type recovery, which results in regulatory lag especially as capital spend goes up. This is an area of focus for mgmt. and could result in longer-term

upside if AEP can improve the regulatory frameworks. Last, in our view, there was no discernible change to mgmt.'s thought process around the potential sale of operating utilities. A number of factors go into the calculus including the ability to efficiently recycle capital and the organic growth prospects of the underlying asset (operating utility) in question.

American Water Works (AWK/Equal Weight/$164.37) (Reeder)

If It Ain't Broke, Don't Fix It. This should not come as a shock but management made it clear that the proven strategy and values that have yielded success over the years will continue to be adhered to going forward and it is up to them to continue to execute. Pursuing timely recovery of much needed water/wastewater infrastructure spend while keeping operating costs in check to maintain customer affordability is the core and can lead to attractive 5-7% risk-adjusted EPS growth on its own. Then layer on top a tuck-in acquisition strategy that has gained momentum in recent years and should remain at these elevated levels (if not further accelerate) as (1) states continue to adopt policies to encourage consolidation, (2) COVID and other financial stresses challenge municipal budgets and (3) regulatory requirements make it increasingly difficult to efficiently and effectively operate small-to-mid sized systems. And finally, management is committed to the non-regulated businesses and believe both are complimentary, capital-light ways of augmenting the regulated growth. As such, the 7-10% growth triangle is likely to persist well into the future.

Other Tidbits. Committed To Water/Wastewater. Management believe investors ascribe a high value to the fact that AWK is a pure play water/wastewater utility – and all of the positive long-term fundamentals of the industry like decades long elevated capex needs, consolidation potential, etc. – and is committed to remain that way. The focus is on continuing to build the tuck-in M&A pipeline which is already very strong. Military Marches On. While AWK has won 5 of the last 6 military base awards, the company is by no means resting on its laurels and continues to try to bring value and solutions to the bases under operation to boost its competitive position. AWK is involved in 4 open solicitations, including a Navy base (the first Navy base to embark down the privatization path), and 2 are expected to be awarded within the next 3-6 months. Management indicated the universe of bases yet to be privatized that AWK would be interested in (i.e. sizeable) stands at about 70. External Equity. The plan remains to close the NY American Water cash sale to AQN in Q1 and look to externally raise about $500M of equity in mid-'22. The timing of equity is driven by the rate of capital deployment and would only be accelerated if there is a near-term uptick in municipal deals.

Alliant Energy Corporation (LNT/Overweight/$57.42) (Kalton)

Plenty of Renewables & Distribution. LNT has a wonderfully straightforward story; but there were a couple of nuggets to note from EEI: (1) LNT's recently announced Clean Energy Blueprint in IA includes 400 MW of solar. Notably the solar qualifies for advanced rate making principles including an enhanced ROE (set for the life of the asset). LNT's IA wind farms receive an 11.0% ROE and recent precedent for IA neighbor MidAmerican suggest the solar spend could qualify for a 10.5-10.7% ROE. (2) Both IPL & WPL have been systematically undergrounding their electric distribution systems at a pace of 1.5-2.0% per year and currently sit at 25% undergrounding of LNT's 45,000 mile distribution system (skewed more toward WPL). Given strengthening storms (the recent derecho is an example) and the increasing focus on resiliency/reliability, policymakers may be open to LNT to accelerate the program (it sounds like early days, but mgmt. is evaluating). While we do not expect anything in the near-term, we think this remains an intriguing long—term investment opportunity. At an estimated cost of $100,000-300,000 per mile, we think the undergrounding opportunity is several billion dollars. Again, the work is currently ongoing – but it could be accelerated and be another lever (along with generation transformation) to extend the targeted 6% rate base CAGR well beyond the mid'20s.

AVANGRID (AGR/Overweight/$51.44) (Kalton)

EPS Outlook. Fresh off the heels of AGR's Investor Day, mgmt. helped fill in the blanks on a few of the assumptions underlying the EPS CAGR of 6-8% (off the adjusted '20 EPS base of $2.10) and the '21 & '22 EPS guidance ranges. Our take: we think mgmt. has prudently erred on the side of conservatism particularly as it relates to the regulated utility operations. While the '21-25 guidance contemplates the NY utilities eventually reaching the allowed ROE levels, our sense is that the near-term EPS guidance reflects continued underearning as NYSEG & RG&E continue to ramp up vegetation management spend in order to improve system resiliency. We also think the outlook reflects a pragmatic approach to the pending PNM acquisition taking into account integration risk. However, we believe there could be potential to best AGR's baseline internal goals via (1) the potential for higher capex vs. PNM's current guidance and (2) modest cost savings (sharing of best practices, etc.). In terms of merchant wind pricing,

AGR's near-term guidance reflects flattish power and REC prices of $20-25/MWh and $10/MWh, respectively. Mgmt. remains highly committed to reducing merchant price exposure over time via recontracting.

Offshore Update. Mgmt. remains very excited about AGR's position in the nascent U.S. offshore wind market. In the near-term, Vineyard Wind is one of the three bidders into NY's pending RFP for up to 2,500 MW (AGR owns 50% of Vineyard Wind). The other two bidders are Equinor/BP and Ørsted/ES. Mgmt. noted that Vineyard's bid was for a large amount of capacity given the distance between the company's lease area (off the coast of MA) and NY – the electricity would land onshore in MA and then be wheeled to NY. The winning bid(s) are expected to be announced by YE'20.

Black Hills Corp. (BKH/Equal Weight/$63.63) (Akers)

Next Stop: Growth Rate. BKH plans to provide an EPS growth target in conjunction with the YE update. The company believes there's good line of sight on the gas side given programmatic pipe investments while the electric side can be lumpy depending on IRP/RFP outcomes (likely continue to be somewhat conservative on that front). We expect the growth rate will be in the 5-7% range and we look to the July 2021 IRP filing in WY for additional insight on generation opportunities (could include discussion of carbon capture as WY remains supportive of the coal plants); there's also potential to expand the Renewable Ready subscription program.

ESG & LDCs (and M&A). BKH rolled out plans to reduce GHG emission intensity 70% by 2040 at the electric operations with 50% GHG reductions targeted at the gas utilities by 2035. On the gas side, CO is in the spotlight as there are ongoing discussions – including a recent Commission Informational Meeting – on what the LDCs can do to comply with environmental initiatives. While there are some parties pushing for electrification, BKH appeared encouraged that the utility stakeholders (including electrics) understand the affordability challenges of electrification along with customer choice considerations. As further evidence of the company's comfort with the gas outlook, mgmt. expressed openness to acquisitions within the company's existing jurisdictions. More specifically, BKH would evaluate CNP's AR LDC if it comes up for sale (though the company noted that the service territory is lower growth than its own AR utility).

CenterPoint Energy, Inc. (CNP/Equal Weight/$24.07) (Akers)

What a Difference a Year Makes. We had a very constructive conversation with new CFO Jason Wells. He reiterated that the plan to deliver at the high end of the 5-7% growth rate (off 2020 Utility guidance basis EPS of $1.12-1.20) already contemplates various headwinds/scenarios – these include the 2021 equity dilution headwind, the roll-off of equity returns on transition/securitization bonds at CEHE, one to two LDC sales, and potential strategic alternatives at ENBL that could require more parent debt to be allocated to the utility. Similarly, Mr. Wells confirmed that the $16B capex plan and 10% rate base CAGR already account for the LDC sales (no negative re-basing ahead). On the O&M front, company has already identified meaningful cost cuts for the 2021/2022 time frame and, longer-term, envisions a culture of continuous improvement.

Strategic Update. We look to the 12/7 analyst day for details on the LDCs sale candidates and for insight into the direction on ENBL. On the latter, mgmt. clearly intends for utility earnings to be a bigger piece of the pie over time, but we still think an exchange of shares into a larger MLP (vs. outright cash sale) is a viable option in the review process. Shifting to the LDCs sales, we think a combination of OK, MS, LA and AR could be sale candidates or, on the bigger side, CNP could elect to sell OH. We do not expect the LDCs in TX or IN would be considered given the company's goal to reduce/simplify regulatory jurisdictions and, separately, we suspect MN may be a bit bigger than what CNP needs. The company indicated that the LDC sales are not driven by any long-term electrification concerns and reiterated that their states remain highly supportive of natural gas. That said, having a more electric-centric mix was mentioned as being consistent with the ESG focus, along with making renewable-enabling investments in TX and modernizing the generation fleet in IN (new plan envisions more utility-ownership of renewables).

CMS Energy (CMS/Overweight/$67.01) (Kalton/Reeder)

On Point, As Expected. One did not have to meet with CMS management to know what they would say. And that is not a bad thing! Just the opposite. As CFO Rejji Hayes put it, CMS will give folks "as much certainty on the E as they can and let investors determine the P." It is that de-risked approach to the business – a utility franchise that sports an extensive capex backlog amidst a constructive regulatory backdrop (that is expected to remain steady going forward) and led by a proven management team with a track record of effective cost management in order to deliver consistent 7% EPS growth (why bother even

saying 6-8%!) – that results in an attractive risk-adjusted total return proposition. Then layer on aggressive decarbonization goals for the ESG-friendly crowd and what is there not to like – other than some (not us!) would argue the "P"?

Food For Thought. More COVID Shutdowns. In the event COVID concerns lead to additional restrictions, CMS does not believe commercial & industrial load will be nearly as hard hit as it was in Q2'20 given evidence that businesses have been largely effective at maintaining operations while protecting employees. That said, should headwinds occur that a residential load uptick would not fully offset, you guessed it – costs can be managed! June 2021 IRP Filing. Planning has begun but it does not sound like, at least on a preliminary basis, the plan will look all that different than the prior iteration, even in the context of a potential Biden administration, given CMS's already aggressive stance towards decarbonizing the fleet (0% net emissions by 2040). Management is monitoring storage in terms of both the cost curve decline and increased efficacy but the urgency is not as great as other utilities in terms of balancing the intermittency of renewables given the Ludington Pumped Storage Facility essentially offers CMS more than 1 GW of battery-like capacity. Committed To Non-Regulated. CMS already has a small non-utility earnings mix (~7% with a guide to no more than 10%) which is where some other companies seem to be trying to get. Plus CMS runs the non-utility portion of the portfolio like a utility in terms of the predictability of earnings.

Consolidated Edison Inc. (ED/Equal Weight/$81.72) (Akers)

COVID Impacts. We gained insight into the COVID impacts and impact on guidance. The $0.05 reduction to the top end of the 2020 range (now $4.15-4.30) reflects the continued inability to collect late charges and disconnection/connection fees. The bad debt expense triggered the materiality threshold, which allowed the utilities to book a $50mm deferral, but that was already contemplated in the guidance range. Looking ahead, the company expects commercial fees could resume in Q1 and the timing on residential remains uncertain. ED is seeking approval to defer the lost revenue in a regulatory proceeding, which could provide upside to near-term EPS if approved.

ESG Focus. Mgmt. highlighted opportunities across the platform to advance de-carbonization efforts. These include the EE, EV-enabling and battery storage initiatives at CECONY (not all captured in rate base but all earn returns and, in some cases, incentives), direct investments in renewables at the Clean Energy Business, renewable-enabling electric transmission projects (including offshore wind) and ongoing efforts to reduce emissions from the gas utility operations. ED is also engaging with stakeholders in an effort to allow the utility to invest in large-scale renewables in NY – those discussions are ongoing. Regarding the Clean Energy Business, ED intends to utilize tax equity (a change from prior practice), but continues to see the annual capex run-rate around $400mm. Shifting to the midstream investments, there was no change in tone from the ESG analyst day when mgmt. expressed an openness to divestitures. Specifically to MVP, we sense the company would wait for the project to go online in order to garner a better valuation. Lastly, when asked about potentially acquiring an LDC, mgmt. indicated that it may not be the most attractive opportunity given policy uncertainty going forward, particularly in the Northeast.

DTE Energy (DTE/Overweight/$130.06) (Kalton)

Full Steam Ahead. Post the separation of GSP, DTE has the ability to be one of the fastest growing utilities within our coverage universe as the company targets 5-yr electric and natural gas utility earnings CAGRs of 7-8% and 9%, respectively. When we asked about upside to the already robust $17B regulated utility '21-25 capex plan, mgmt. suggested there was no shortage of capex opportunities and pointed to the company's recent capex refreshes (generally result in 10-20% increases in cumulative 5-yr capex). Switching gears to GSP, mgmt. plans to get out in front of investors as much as possible in front of the planned spin-off in mid '21. CEO Elect David Slater remains excited about the company's organic growth prospects in both the Marcellus and Haynesville shale basins. We also asked whether Spinco would continue to be acquisitive post-spin. It sounds like this remains an open question as mgmt. continues to evaluate the post-spin strategy. In terms of market comparisons for Spinco, DTE views WMB and EQT as most closely resembling Spinco's asset mix/profile, which suggests a valuation range of 8.5-10.0X EV/EBITDA (higher than the 8X multiple assumed in our price target).

Duke Energy (DUK/Equal Weight/$97.31) (Kalton)

Pivoting to Growth. We thought Chair, President & CEO Lynn Good made a highly compelling case for DUK's long-term EPS growth prospects and why it could trend towards the high end of the targeted 4-6% CAGR (off the preliminary '21 EPS base of $5.15). In our view, DUK's messaging to investors has noticeably improved in '20. We point to a focus and execution on cost management along with better

crystallizing (for investors) the long-term generation transformation rate base growth opportunities. Front and center is the recently filed Carolinas IRP, which contemplates substantial spend aimed at decarbonizing DUK's coal heavy generation fleet (hearings are expected to begin in NC during Q2'21). The initial spend is likely to center on solar/battery storage and natural gas-fired generation. Looking beyond the 2020s, the next leg of investment will depend on a number of factors including carbon policies and technology trends. We believe it is at this point that offshore wind could come into the fold (depending upon legislative support) – or not, if it makes more sense to continue down the solar/natural gas path.

Dominion Energy Inc. (D/Equal Weight/$85.68) (Akers)

Execution, Execution, Execution. The message from CEO Bob Blue and CFO Jim Chapman was one of execution with a focus on regulated operations in premium jurisdictions. The company aims to deliver consistent EPS growth aligned with the 6.5% target and appears to be off to a solid start based on the Q3 update. Mgmt. did not express discomfort with the remaining 10-15% of non-utility exposure, noting that it is largely contracted.

Regulatory/Political Update. As it relates to VA, mgmt. acknowledged that it can (and will) get noisy on the political/regulatory front, but highlighted a history of supportive outcomes. The company expects there will be that same opportunity into the 2021 triennial review, particularly given the various items in the toolkit (write-offs, CCROs, etc). The company also expressed cautious optimism heading into the COP process at BOEM given strong local support and project-specific considerations (don't have the same fishery and shipping lane dynamics as other projects); from a timing perspective, being behind other projects may also be beneficial as D can gain insight from others' experience. Shifting to South Carolina, the immediate focus remains on the rate case. Mgmt. indicated nothing out of the ordinary thus far, but acknowledged some uncertainty with recent turnover in the commission (could make it more difficult to settle). Lastly, on the LDCs, D has not seen any anti-gas undertones in the company's service territories and remains very comfortable with those assets in the mix.

Edison International (EIX/Equal Weight/$62.90) (Kalton/Reeder)

Making The Case That Wildfire Risk Is Actually Pretty Low. Management believes the wildfire mitigation plans, Public Safety Power Shutoff policies and improved containment/suppression strategies have vastly reduced the risk of a major California wildfire caused by investor-owned utility equipment. The '19 & '20 wildfire seasons are evidence of that. And planned future mitigation efforts – installing covered conductors, vegetation management with expanded clearances where possible, increasing situational awareness, etc. – should further the cause. Couple the lower event risk with CPUC-sanctioned wildfire insurance programs that are backstopped by the provisions of AB1054, including the liability cap and $21B wildfire fund, means the risk of triggering substantial shareholder liability is pretty low. We note that PCG conveyed a similar message. While this may very well be the case, management acknowledged that it may still take a few more years of benign wildfire seasons for investors, ratings agencies and even insurers to fully recognize the progress that has been made.

Attractive Core Story That Is (Appropriately?) Overshadowed By Wildfire Risk. Excluding the wildfire risk, the underlying EIX story remains attractive with a long runway of transmission and distribution as well as renewable/storage investments needed to support the state's goal to de-carbonize the broad economy. CA regulators have generally been supportive of utility efforts over the years and the framework offers a plethora of cost recovery mechanisms that enable the state's utilities to earn at or above authorized levels. Even the timeliness of CPUC decisions may be improving under President Batjer. EIX's current plan results in a 6.5-7.5% rate base CAGR. Gating factors include the ability to simply execute on all of the work as well as maintain affordability for ratepayers by trying to keep average annual rate increases at or below inflation. Although the average electric bill in CA is roughly 30% below the national average and EIX's bills are roughly 30% lower than in-state peers, O&M efficiency efforts remain a priority.

Emera Inc. (EMA/Equal Weight/$56.24) (Kalton)

Lots Going in FL. Tampa Electric, along with NEE's & DUK's FL electric utilities, are gearing up for base rate filings in 1H'21 for new rates beginning Jan '22. While we consider the FPSC to be a highly constructive regulatory body, rate cases – particularly in the midst of a weak economy – always create a little bit of uncertainty. With that in mind, we view Peoples Gas recent base rate settlement to be a positive date point. Key elements include allowed ROE of 9.9% with an 8.9-11.0% range. This compares with Tampa Electric's current ROE range of 9.25-11.25% - there is an argument to be made that electric

utilities should be awarded a premium ROE to gas LDCs given greater technology risk. Separately, Tampa Electric's growth runway remains robust driven by renewables and reliability spend under the new Storm Protection Plan. On the solar front, Tampa Electric is well into the first 600 MW of planned solar and has an additional 600 MW plus about 30 MW of battery storage planned by '23. Even with these additions, renewables will only represent 12% of Tampa Electric's power supply (natural gas makes up the high majority of the rest). EMA continues to evaluate the optimal resource mix going forward but the full expectation is that solar will grow meaningfully from the 12% level.

News from the North. In late September, Canada Prime Minister Justin Trudeau's Throne Speech (think State of the Union) addressed power transformation and, in particular, the Atlantic Loop transmission project. The Atlantic Loop would bring excess hydro and thermal power from Quebec and New Brunswick, respectively, to Nova Scotia and Newfoundland. If completed, the project would allow Nova Scotia to accelerate the planned retirement of coal generation from 2040 to 2030 (consistent with Canada's target). As a major transmission project that spans multiple regions, Atlantic Loop faces plenty of challenges (including cost allocation). That being said, it also represents a potential meaningful investment opportunity for EMA. Stay tuned!

Entergy Corp. (ETR/Overweight) ($109.83)

Regulatory Updates. ETR's mgmt. team has been making the rounds quite a bit recently between the late September Investor Day, a number of fireside chats in October and the Q3 earnings call. So, we used our EEI meeting to catch up on a few recent developments in what has become a surprisingly straightforward and, in our view, highly compelling rate base growth story. On the regulatory front, ETR recently reached a partial settlement in E-AR's annual FRP filing – the separate request to extend the FRP has a 12/4/20 settlement deadline. In addition, E-LA recently filed a request to extend the company's FRP by three years (through '23) under largely the same terms as the existing FRP (ROE of 9.2%-10.4%). One difference to E-LA's FRP is a proposed distribution recovery mechanism for annual investment in excess of $100mm. Mgmt. stressed that they have a long track record of achieving settlement agreements and we did not get the sense that there were any meaningful roadblocks to prevent settlements in AR & LA (LA is very early in the process). Switching to the pending SERI case at the FERC. ETR does not expect likely commissioner changes at FERC under a Biden administration to have an impact on the resolution (positive or negative). Mgmt. thinks we could gain clarity on the ROE/equity ratio in 1H'21 (already taken into account in ETR's EPS guidance) but the timing of resolution on the broader policy question around uncertain tax positions remains unclear. While mgmt. remains of the opinion that they have a strong argument, should the FERC adopt the ALJ recommendation it presents a $0.15-0.20, or 2-3%, risk to annual EPS power before potential mitigation efforts.

Essential Utilities (WTRG/Overweight/$46.37) (Reeder)

DELCORA Discussion. We devoted a good deal of time to the pending DELCORA transaction as we believe the current share price does not, perhaps appropriately, reflect the considerable long-term benefits from the deal including the meaningful capex needs that fall beyond the current 5-year forecast as well as the likely substantial wastewater tuck-in deals that could transpire in the area. We had three main takeaways. (1) Investors should not rule out the prospects for a settlement in the legal challenge and perhaps optimism in this regard is in part attributable to the confidence that management has conveyed regarding being able to close the deal around the end of Q1'21. (2) Management is pretty comfortable with the PaPUC approval process based on the concerns expressed by the intervening parties as well as previous experience with FMV deal approval in the state. (3) Assuming 1H'21 closure, DELCORA will start earning its full keep in '22 as it will be incorporated in the next PA water/wastewater rate case filing.

Other Notables. Next PA Water Rate Case. Aqua Pennsylvania is likely to file for new rates during 2H'21 with the new rates effective perhaps late 1H'22. Management continues to think PA water rate cases will occur at a 3-year cadence going forward. M&A Strategy. WTRG continues to be focused on bringing other water/wastewater tuck-in deals to bear, including in states beyond PA and IL. OH perhaps offers the most near-term opportunity out of the "new" states. The deal pipeline is robust and water/wastewater tuck-ins are definitely the focus as the company looks to continue to capitalize on the somewhat accelerated pace of municipal deal activity/interest in the sector. Management also reiterated a low (to no?) likelihood of doing another gas deal in the near-term. Guidance Refresh. Finally, the guidance refresh could come as early as January (before the YE2020 call in late February) and is expected to include not only '21 EPS but also refreshes to the 3-year EPS CAGR and capex outlooks.

Evergy, Inc. (EVRG/Overweight/$57.30) (Akers)

Fake News. EVRG issued a statement mid-EEI confirming that there has been no change in strategic direction since the decision to pursue the Sustainability Transformation Plan (STP) and that there is no outstanding offer or bid for the company. That followed a Reuters report that NEE made an offer in the mid-$60s and a statement from Elliott that EVRG should reengage with NEE. For its part, NEE suggested investors not believe everything that shows up in print. All things considered, there's no reason to think there is merit to the Reuters report at this point.

Path Ahead. Mgmt. is focused on executing the STP with a focus on a modern T&D system and kick-starting the ESG aspect of the story, which includes the de-carbonization of the generation fleet. The plan will require supportive regulation, which is a key consideration in the CEO selection process (someone that understands the importance of having strong regulatory relationships) – CEO decision still expected by YE. The cost cutting initiative is also a key component of the story including its role in mitigating customer rate increases. Shifting to capex, we were encouraged to hear that the ~$700mm of renewable (solar) capex in the plan is not dependent on having securitization in place. We look to the 2021 IRP filings for additional insight into the generation outlook.

Eversource Energy (ES/Overweight/$94.42) (Kalton)

CapEx Drivers. We expect ES's upcoming capex refresh in conjunction with Q4 earnings will be more of the same – higher and supportive of a 5-7% EPS CAGR from the base business (ex-offshore wind). ES has already noted a few things that could impact the plan such as (1) the inclusion of Eversource Gas Company of MA (Columbia Gas), which we think could be additive to ES's rate base CAGR, (2) electric transmission including new reliability projects in southeastern MA totaling $175mm and (3) new MA solar legislation that, if passed (likely), would allow NSTAR Electric to develop an additional 230 MW of solar (~$400mm opportunity). It remains unclear whether ES will have clarity on the CT AMI program in time to include it in the refresh. In addition, mgmt. remains optimistic that the MA Grid Mod Plan (2022-2024) will be supportive of AMI. We think the potential CT & MA AMI programs represent a ~1B investment opportunity over a 5-7 year period.

Other Tidbits. (1) Offshore Wind – despite (not unexpected) permitting delays, ES remains bullish on the company's offshore wind program noting that any negative impact of the delays on returns should be mitigated or offset by the positive impact of being able to use larger turbines along with favorable vessel developments afforded by the extra time. In addition, mgmt. thinks President-elect Biden's administration could help speed the process up at BOEM. ES/Ørsted are one of the three bidders participating in NY's offshore wind solicitation for up to 2,500 MW of capacity (a decision is expected by YE'20). While the companies' award in the 1st auction (the 880 MW Sunrise project) bodes well for pending auction, mgmt. emphasized bidding discipline considering there are plenty of other RFPs upcoming in the region (RI, MA, NY). (2) Connecticut – following the public/political outcry to ES's performance in the immediate aftermath of Isaias, it appears that cooler heads are prevailing. PURA's PBR docket will sequence in mid '21 and ES welcomes the opportunity to work under a PBR scheme. ES is also working to insure better storm response with a focus on outage duration and customer communication.

Exelon Corp. (EXC/Overweight/$43.84) (Kalton)

All About the Breakup. EXC's recent proclamation that the company is in fact in the early stages of evaluating separating ExGen from the regulated utility operations took center stage at the company's EEI meetings. We entered the conversation somewhat skeptical that EXC would go down the break-up path nearer-term given our base assumption that IL will pass constructive nuclear-related legislation in the Spring '21 session and that, by doing so, it might prove diplomatically difficult for EXC to immediately turn around and effectuate a spin (or sale). We exited the conversation less skeptical as mgmt. downplayed – to some degree – potential policymaker resistance. In our view, there is a clear industrial logic to separating the businesses (investors prefer pure play regulated utilities, the separated companies will likely have better strategic flexibility, etc.). In addition, once the genie is out of the bottle it is hard to put back. Even though mgmt. was careful to caveat the evaluation process – noting the unique complexities of separating the companies – once the notion is put out into the world the share price embeds an expectation.

IL Clean Energy Update. EXC indicated that there was strong momentum for clean energy legislation heading into the Spring '21 session and noted that, thus far, Gov. Pritzker's carbon price proposal has not seemed to gain much traction. Instead, it sounds like either the Fixed Resource Requirement (FRR) option could still be in play and/or likely changes to the MOPR under a soon-to-be Democrat regime at FERC could provide the Illinois legislature with additional tools to support nuclear. While IL clean energy

legislation conjures up images of Lucy pulling the football away from Charlie Brown, we remain of the strong opinion that the legislature will take the necessary action to keep the state's nuclear fleet operational.

FirstEnergy Corp. (FE/Overweight/$29.79) (Kalton)

A Tough Road Ahead. This was not an easy EEI for FE's mgmt. team coming on the heels of former CEO Chuck Jones' recent termination for code of ethics violations as part of an ongoing internal investigation into FE's potential involvement in the House Bill (HB) 6 bribery scandal. In addition, it sounds like it could be some time before we get clarity on both the pending FBI investigation and FE's internal investigation (mgmt. hoped to have further updates on the internal investigation by the Q4'20 earnings release in early '21). Under this backdrop, we thought Acting CEO Steve Strah did a commendable job in our meeting and came across as very direct and authentic in discussing the serious issues confronting FE. That being said, regaining the trust of FE's constituents (regulators, customers, investors) will not be an easy task and it remains an open question as to whether or not Mr. Strah will be able to pull it off given his lengthy tenure within the company. We also remain mindful that the investigations are ongoing and it is far from clear to what extent FE was involved in the HB 6 scheme – although, Mr. Jones' termination along with several other recent executive terminations and departures from the firm point to some level of wrongdoing.

OH ROEs. FE provided a bit more color on the age-old question of the OH utilities' earned ROE. Per the SEET test (in legislation), FE is allowed to use book equity in the ROE calculation (FE's book equity is higher than equity rate base due to the inclusion of $2.2B of goodwill related to an acquisition in the 1990s). This, along with some other adjustments, helps explain why FE's SEET ROE always results in a lower ROE than what the rate base math suggests. FE plans to provide even more detail in conjunction with the Q4 earnings release. Keep in mind, the OH utilities' current ESP runs through 5/31/24.

Hawaiian Electric Industries (HE/Underweight/$37.05) (Reeder)

Solid Footing Despite COVID. Despite the challenges presented by COVID, particularly in HI where tourism is essentially the lifeblood of the economy, HE is in pretty solid shape and remains focused on helping the state reach the long-term renewables and decarbonization goals. The utility benefits from decoupled rates and COVID expense deferral accounting. The bank's conservative philosophy and strong starting position has allowed it to "bend but not break" under the challenges of COVID. As such, there remains no need for incremental equity at the holding company nor a need for the holding company to invest any capital into the bank, 2021 refinancing needs have been prefunded and HE is committed to maintaining an investment grade structure. As for the dividend, management does not foresee any risk to the current level and reiterated an intent to grow it in-line with earnings over the long-term while maintaining a payout ratio that is commensurate with peers (60-70%).

Here Comes The Sun? The bank's low cost of funds and ability to offset some of the loan loss provision spike with strong mortgage re-financing activities and opportunistic securities sales have kept the bank safely profitable. And management's recent comments regarding the performance of the loan portfolio and the potential for underlying economic conditions to improve as the state recently started re-opening its doors to tourists give reason to believe the worse of the bank could be behind it. While businesses in HI are struggling, customers and the communities served have been resilient, the bank is staying very close to their customers and the high asset quality in the state provide a safeguard. Management reiterated a belief that the bank is well provisioned after Q3 and that the provision is determined based on forward looking information. As such, if tourism gradually returns, another widespread outbreak of COVID is avoided in the coming months (no new shutdowns) and an effective vaccine becomes widely available in '21, it is possible that a good portion of the provision recorded in 2020 could reverse as the economy improves. 76% of deferred loans have already returned to payment and, typically, if there are 6 months of good performance, the loans are eligible to be upgraded and the associated provision reversed.

PBR Me ASAP? The utility continues to believe the transition to a 5-year Performance Based Ratemaking (PBR) framework at some point in '21 will be a net positive in terms of ability to earn close to the allowed ROE. Once implemented, there may be only 30-40 bps of structural regulatory lag remaining. That said, while there seems to be many areas of consensus that have developed amongst parties throughout the PBR proceeding, the devil will be in the details ultimately approved by the commission particularly as they relate to things like how the annual revenue adjustment mechanism works, what the consumer dividend might be and the type and magnitude (collectively up to 100-200 bps of ROE?) of the new performance incentive mechanisms (PIMs). Execution will be critical which also requires cost efficiency improvements, including delivering on the committed $25M of savings by 2022.

IDACORP, Inc. (IDA/Equal Weight/$94.80) (Akers)

Same (Good) Story Near-Term. Mgmt. continues to see strong growth in the Idaho Power Company (IPC) service territory driven by in-migration from surrounding states along with new large load customers. Combined with a strong cost containment efforts, low borrowing costs and creative regulatory solutions, this has allowed IPC to stay out of rate cases while managing to earn reasonable ROEs and deliver on financial targets.

Rate Base Growth Opportunities Brewing Long-Term. Over time, customer growth and coal retirements will drive incremental resource needs. There's also the opportunity for IDA to take over BPA's stake in the Boardman-to-Hemingway (B2H) project and, possibly, to offer a green tariffs that could lead to renewable ownership opportunities over time. Lastly, IDA has been clear that once the new Hells Canyon license is issued (2022 or later), that will result in higher capital and operating expenses. While some of these items could be handled via regulatory solutions (rider-type treatment), the bigger items may require a full vetting in a rate case.

MDU Resources Group, Inc. (MDU/Equal Weight/$24.99) (Akers)

Strategic Update. When asked about the current trend toward pure play models in the utility sector, mgmt. highlighted (1) MDU's general focus on infrastructure, which spans electric/gas utilities, pipelines and construction and (2) a successful track record since divesting the E&P asset. On the M&A front, construction activity has slowed but the company remains active in the pursuit of acquisitions. Mgmt. is also open to adding scale at the regulated utilities including LDCs so long as it makes economic sense (accretive, credit supportive, cost and/or capex levers, etc.). Of note, S&P already raised the FFO/Debt threshold to 22% from 15% due to the non-regulated EBITDA contribution so while utility acquisitions would help the business risk profile, MDU is comfortable with the revised thresholds and, in fact, has a healthy cushion on FFO/Debt.

Construction. Mgmt. disclosed a ~50/50 breakdown between aggregates and vertically integrated activities (hulling, converting to ready-mix, delivering, laying, etc.) within the Materials segment; this is more in-line with peers Summit and Granite vs. pure plays Vulcan and Martin Marietta. Regarding the decline in backlog reported in Q3'20, the company did not appear overly concerned and pointed to the Q1'21 bidding season as the next key data point. Positive drivers include the extension of the FAST Act budget and favorable housing trends. Shifting to Services, mgmt. has been encouraged by the strong performance through the pandemic. While new hospitality projects in Vegas could slowdown, there is line of sight into 2021 from existing projects and, more broadly, MDU is seeing strong growth in the high tech sector, chip manufacturing and data centers along with healthy electric T&D spending trends.

Pipeline. Mgmt. highlighted the largely take-or-pay nature of the pipeline operations and noted that gas volumes are bouncing back in the Bakken (~85% pre-pandemic levels). The company expressed confidence that the revised agreements with shippers on the North Bakken Expansion project are firm and that the project remains on track to secure FERC approval and meet the late '21 in-service target. When asked about threats from de-carbonization, mgmt. expressed skepticism that natural gas can be reasonably replaced on a btu equivalent basis and highlighted gas as a key backstop for renewables.

NextEra Energy (NEE/Overweight/$77.54) (Kalton)

Chasing Our Tails. During EEI, Reuters reported that NEE had made an offer to acquire EVRG for $66/sh. As the story evolved, it became clear that the bid was likely made many months ago while EVRG was in the midst of a strategic evaluation (ultimately, mgmt. and the Board decided not to pursue a sale of the company). For its part, NEE's mgmt. simply indicated that investors should not believe everything they read and intimated that there could be ulterior motives behind the reports. Does NEE remain interested in regulated M&A? Yes, but per our EEI conversation it remains very much a "want" vs. a "need" and the company will only move forward if a transaction checks all the boxes (including EPS accretion factoring in the balance sheet). Looking ahead to '21, the Santee Cooper privatization opportunity in SC remains a possibility as the legislature is expected to take up the issue again in the general session (typically runs through May). Recall, NEE's bid was deemed to be the best option should the legislature decide to sell Santee Cooper. While we tend to think a Santee Cooper privatization is unlikely, it is worth paying attention to heading into '21. We continue to think an acquisition could be immediately 3%+ accretive to EPS and up to 5% within a few years.

NEER is in the Cat Bird Seat. We spent much of our time discussing NEER's competitive advantages along with the overall size of the renewables pie. We always want to remain mindful of the risk of intensifying competition in the renewables arena as energy players increasingly look towards wind & solar

as growth avenues. That being said, we find ourselves agreeing with NEER President John Ketchum in that the company has built such a competitive moat that it will be difficult for newcomers to enter the space and effectively compete. Developing renewables is not as easy as simply buying some equipment and setting up a wind or solar farm. There are all kinds of considerations related to optimal sites, access to transmission, technical expertise, etc. that NEER has spent decades perfecting. Not to mention NEE enjoys enormous scale benefits related to vendor relationships, cost of capital, etc. As for the size of the market – mgmt. continues to believe EIA's projection for 30% wind/solar market share by 2030 as a percent of U.S. power supply (vs. ~10% currently) will prove to be conservative. And green hydrogen has the potential to materially accelerate renewables development looking out beyond '30 – it is clear that NEE sees a lot of potential for hydrogen and we expect (small) announcements on this front will pick up steam in the coming months and years.

NiSource Inc. (NI/Overweight/$24.64) (Akers)

Sensitive to Financing Concerns. No change to the financing plans laid out at the analyst day, but mgmt. was very responsive to concerns on dilution and the equity overhang. We look to the 2021 financing including $600-1,000mm of equity-rich securities (sounds like leaning toward convertibles) as the first major data point informing 2022-2023 block equity needs (currently $500-700mm). Mgmt. also reiterated an openness to portfolio optimization (asset sales) if it is in the best interest of shareholders. We expect the company will take some time to evaluate options and we look to CNP's upcoming LDC sales as a directional data point on gas utility valuations, which could be instructive for NI (and the rest of the combos/LDCs). Separately, we note that NI's financing plans do not include the ongoing $200-300mm of ATM equity needs after 2023 as investments – including the renewable program – are recognized in rates and generate cash.

Perspective on Gas. Mgmt. opined that the valuation de-rating of the LDCs is overdone given both strong demand for the product and readily available low cost supply. The company also sees strong policy support in its remaining service territories and highlighted the high energy content requirements of winter peak energy needs. NI believes it is not a question of whether the distribution pipe system will be used and useful in the future, but rather what will be flowing through the pipes (RNG, hydrogen, etc.).

NorthWestern Corp. (NWE/Overweight/$59.30) (Reeder)

'21 Guidance. Management offered preliminary '21 EPS guidance of $3.40-3.60 but will likely tighten the range to the typical $0.15 variance with the YE'20 report in February. We got the sense the extra $0.05 in the preliminary range was subtracted from what would have otherwise been the bottom end if not for COVID-related uncertainties. The midpoint of the '21 range is 4% above the midpoint of the revised '20 range ($3.30-3.45) but is overall consistent with the original '20 range ($3.45-3.60). It reflects a 0.7-1.0M increase in the diluted average shares out from '20, continued improvement in operating expense levels and decoupling is expected to be implemented at the MT electric utility in mid-'21. Lastly, NWE indicated an expectation that the dividend will be at the upper end of the 60-70% targeted payout ratio – if at 70% while continuing the recent $0.10 annual dividend increase trend, it implies '21 EPS of $3.57.

Capex Budget Increased. NWE rolled out a $2.1B investment plan over the 2021-25 period. The budget represents a $300M increase over the previous 5-year plan and is distributed fairly evenly across the states and utilities (electric vs. gas) relative to each's size. Management characterized the projects as mostly small and relatively low execution risk. The budget is driven by gas and electric transmission and distribution work to accommodate growth across the systems, deal with the shutdown of fossil resources and comply with regulations as well as things like hydro generation facility upgrades and technology (including automated metering infrastructure). The $400M+/year capital plan puts NWE at the midpoint of the 3-6% EPS CAGR target and management noted the growth could be somewhat lumpy based on rate case timing. In addition, it sounds like external equity will be needed fairly regularly to fund the budget and maintain an FFO/Debt ratio in the 14-15% range.

MT Generation Still Upside – And Growing? NWE has bid several projects into the pending 285 MW RFP and reiterated that the $200M capex bogey that they have talked about is based on a level of comfort of what they might win – winning all would be more than $200M. The 3rd party administrator has yet to notify NWE that any of their projects have been eliminated from consideration and management remains confident that their projects are well positioned given the RFP specifications around long duration, flexible capacity. If a NWE project wins, the MT pre-approval process allows AFUDC to be earned as the capital is deployed but then that turns into a cash return with a project-specific ROE once it enters service. The recent termination of the Puget deal (for an increased stake in Colstrip) restores the full 725 MW capacity hole that NWE intends to ultimately fill through multiple RFPs. And the risk of the Colstrip facility shutting down this decade (vs. NWE's 2043 planning assumption) seems elevated, perhaps even more so by

Talen's announcement this week to shut down coal capacity in favor of a more ESG-friendly strategy, which has the potential to add another 222 MW deficit to NWE's MT portfolio.

MT Regulatory Environment. Republicans swept all state offices and the three Montana Public Service Commission (MPSC) elections. While party affiliation has never been a guarantee of constructiveness in MT, we are hopeful that the new MPSC will continue what seemed to be a gradual improvement in the challenging regulatory environment over the last 2 years prior to more recent adverse decisions around COVID expense recovery as well as Colstrip replacement power costs. We also believe it bodes well for the recognition that natural gas needs to play a role in the new generation capacity picture versus some of the Democratic candidates that were more fervent renewables supporters. We were somewhat concerned by the MPSC comments earlier this year around NWE's supply plan perhaps being overly reliant on gas – particularly since we believe NWE's self-build advantages are likely for gas-fired generation.

OGE Energy Corp. (OGE/Overweight/$33.95) (Akers)

Feeling Good. CEO Sean Trauschke struck an optimistic tone on the utility operations, particularly on sales trends. Commercial load flipped to positive in September (vs. year ago period) and mgmt. expects some of the uptick in residential will be sustainable based on work-from-home trends. The company is also bullish on industrial activity and expects Public Authority sales (mostly schools) will pick-up as students return to the classroom. Mgmt. is hopeful that the pre-COVID momentum toward customer growth >1% will return. On the regulatory front, OG&E is focused on executing manageable, straightforward proceedings with a continued focus on customer bills. Lastly, the company plans to file an IRP by October 2021, which could shed light on resource needs. We do not expect any major project revelations, but rather a series of smaller investments (plant conversions to gas and solar additions at the distribution level) along with EE and DR. Overall, things seem to be moving in a positive direction.

Strategic Comments. Mgmt. continues to play its hand close to the vest as it relates to ENBL. The team fully acknowledges the public market dynamics (negative sentiment toward midstream, preference for pure plays) and believes the midstream exposure has overshadowed the utility story. When it comes to potentially selling/swapping into a bigger MLP, OGE considers the aforementioned market/valuation dynamics along with cash flow and credit implications. Separately, when asked about the company's interest in acquiring an LDC (in the context of CNP potentially selling an LDC or two), mgmt. confirmed that gas utilities are not on the company's list.

PG&E Corporation (PCG/Equal Weight/$10.71) (Kalton)

Wildfires Still Top of Mind. First, the lack of a new Safety Certificate from the CPUC remains a little bit disconcerting. That being said, PCG stressed that the prior safety certificate remains in effect until a new one is issued and it is not necessarily uncommon that the issuance has slipped beyond 90 days. In addition, thus far there have been no communications from the CPUC to suggest any major issues with PCG's request. Without a valid Safety Certificate PCG is not afforded the protections of the liability cap under AB1054 (limits wildfire liability to 20% of electric T&D equity rate base, or ~$3B currently). Safety Certificate aside, PCG highlighted substantial progress on wildfire risk mitigation efforts and improvements in the PSPS program vs. '19. Combined with improved containment/suppression strategies, the risk of catastrophic wildfires caused by utility-owned equipment appears to be declining. That being said, we think it may take a few years of benign activity to substantially improve investor confidence. Not surprisingly, mgmt. indicated that the legislature still has little appetite to address the inverse condemnation (IC) doctrine. While AB1054 provides substantial protections, the state's electric utilities still face significant risk relative to utilities in other states as a result of IC. On the capex front, there is no shortage of investment needs as PCG deploys capital to improve grid resiliency, mitigate wildfire risk and support CA's ambitious GHG emission goals. Last, it sounds the like the search for a new CEO is winding down with an announcement expected by YE'20.

Pinnacle West Capital Corp. (PNW/Overweight/$89.59) (Akers)

ACC Profile. The 2020 ACC election resulted in Republican Lea Márquez Peterson retaining her seat with the other two open seats to be filled by Republican Jim O'Connor and Democrat Anna Tovar. It appears that three of the five Commissioners are supportive of a de-carbonization agenda (Peterson, Tovar and sitting Commissioner Kennedy), which aligns with PNW's de-carbonization plan. Favorably, this agenda would appear to conflict with sitting Commissioner (and possible future Chairman) Olson's desire to pursue deregulation. While we reserve judgement until policy discussions are underway and, more so, rate case decisions are issued, our initial view is favorable given both a pro-clean energy and Republican majority. Beyond the ACC make-up, we are encouraged by PNW's focus on improving the company's

position in the state via consensus-building and improved customer service/experience. We think improved regulatory relationships and outcomes would address a key investor concern and allow greater focus on the clean energy growth story, strong balance sheet, effective cost management and strong customer growth.

Rate Case Update. APS filed rebuttal testimony on 11/6 with three key updates: (1) a $15mm reduction to the $184mm rate request reflecting a reduction in the ROE request (to 10.0% from 10.15%), a lower fair value increment (to 0.8% from 1%) and updates to the fuel rates; (2) a proposed Advanced Energy Mechanism (AEM), which would provide rider recovery for clean energy investments and incorporate the DSM and LFCR updates (simplification); and (3) a Coal Community Transition proposal, which is a comprehensive plan to address the Four Corners coal retirement along with various economic development initiatives for the Navajo Nation. It is our understanding that the Navajo Nation is supportive of the coal transition plan along with the AEM. While it is yet to be seen whether other stakeholders support the AEM (key to mitigating regulatory lag and extending the time between rate case filings), we view the updated testimony as an incrementally positive step.

PNM Resources (PNM/Equal Weight/$49.09) (Reeder)

AGR Deal Update. It was not for a lack of effort but we were unable to squeeze out much additional insight regarding how the Avangrid deal (announced 10/21) came about. Management reiterated that a very strategic type of approach was taken to find the right strategic partner for PNM and the communities served. Therefore it was not solely about the price offered. More details will be included in the proxy which is expected to be filed around Christmas. Management believes the prospects of receiving what PNM would deem to be a superior proposal are quite low (again, not just about price) and pretty much shut the door to the prospects of a financial suitor emerging (as was the case in the recent acquisition of PNM's neighbor El Paso Electric) given the need for an acquirer to be strategically aligned. The response to the deal announcement has been positive in NM (governor, legislature, environmental community, etc.) based on AGR's commitment to renewables and the environment and management noted that NM regulators have never turned down a merger application. Both NM and TX are net benefit states and generally those conditions are satisfied by way of rate credits which AGR/PNM stand prepared to offer. Merger approval applications will likely be filed by the end of the month.

Other Business Updates. Constitutional Amendment Passage. The NM regulatory body will be transition to a 3-person appointed commission in 2023 as the amendment passed. Management believes it will not only improve the predictability/stability of the regulatory decisions in the state but also the quality. Therefore, NM has the potential to improve from the commonly held investor notion that the regulatory environment is below average. Four Corners Deal. Management believes NM regulators will be hard pressed to turn down the recently announced deal for PNM to exit Four Corners early given the customer savings associated with it. EPS Power. No real changes in the EPS power of the company looking forward. 2021 EPS power is $2.30-2.40 however PNM will be rolling out guidance in December taking into consideration the latest thoughts around COVID, cost savings and the lack of rate relief or decoupling (both of which were anticipated at one point in '20 to be of help to '21 EPS). Beyond '21, PNM will be deferring to AGR to communicate the growth.

Portland General Electric Company (POR/Equal Weight/$44.57) (Akers)

Mgmt. Bullish on Growth. CFO Jim Lobdell highlighted that growth in POR's service territory has proven resilient with healthy in-migration trends, which may be further helped by COVID as people have more flexibility to work from desirable locations, and continued growth in high tech. This led the company to bring back capex on the Q3 update that was previously removed from the plan. The company still expects 1% sales growth long-term, which could be bolstered by electrification efforts (transportation, but also considering new premise incentives for electric heating, etc.). Separately, Mr. Lobdell spoke of a continued focus on cost controls including greater use of technology and coal unit retirements among a slew of other efforts.

In addition to service territory growth and expense controls, the company's 4-6% EPS growth target is driven by investment in aging infrastructure along with the Wheatridge Renewable Energy Facility. Looking ahead, there could be additional opportunities for generation ownership (upside to the plan) related to one or two RFPs planned for 1H'21 to procure 150 average MW (~450 MW nameplate) of renewables and 700 MW of capacity. Lastly, discussions are ongoing in phase 2 of the Green Future program, which could potentially include utility ownership (TBD).

Regulatory & Other Updates. There was no new information on wildfires (still no evidence that POR's equipment ignited any fires) and the trading loss (investigation ongoing). On the regulatory front, mgmt.

continues to evaluate the timing of the next rate case and highlighted positive data points on the COVID deferral and wildfire deferral, which was approved in ~30 days. While the company still sees 85-90 bps of structural lag related to unrecoverable expenses, there are other areas which could be addressed, such as the PCAM (tightening the deadbands?), storm balancing accounts and the decoupling mechanism, which is set to expire after 2022.

PPL Corporation (PPL/Equal Weight/$29.41) (Kalton)

U.K. Sale & Go-Forward Strategy. The sale of the U.K. utilities continues to progress and mgmt. remains encouraged by the level of interest. An upcoming data point regarding U.K. decarbonization goals will provide parties with guidance into the expected level of long-term investment in the electric distribution systems (arguably a more important driver of value than near-term allowed returns). Timing remains 1H'21 for both the transaction announcement and potential completion given typically quick regulatory approval processes in the U.K. (1-3 months). Post sale, mgmt. is keeping their options open with regard to use of proceeds with share repurchases, regulated M&A (preference towards electric) and additional contracted renewables investment (via Safari Energy) all possibilities.

Kentucky Update. PPL recently filed a notice of intention to file for base rate relief for the KY utilities starting 7/1/21. The filing will include a proposed sur-credit that will be used to mitigate the rate impact on customers via the use of regulatory liabilities. Separately, we spent a good deal of time discussing upside capex opportunities including AMI (a ~$300mm program that PPL intends to revisit with the Kentucky PSC) and generation transformation. The KY utilities own 3,800 MW of coal-fired generation that was developed between 1971-1984 and could be ripe for retirement over the next 10-20 years. PPL characterized the PSC as being most concerned about cost and reliability and is not wedded to fuel type when considering asset replacement proposals. Mgmt. further noted that the economic proposition for solar/battery storage is not quite there (yet).

Public Service Enterprise Group Inc. (PEG/Overweight/$60.88) (Kalton)

Lots to Talk About. (1) Non-nuclear generation sale – mgmt. characterized initial interest in the proposed sale of the fossil fuel generation fleet and solar portfolio as healthy (private equity interest). The solar portfolio is expected to be put up for sale this month with the fossil fuel plants to follow in December. Bids are due in Q1'21 with a sale expected to be announced in mid '21. (2) CEF Filings – mgmt. is optimistic that the New Jersey BPU will bless the $600mm AMI proposal. Conversely, it is unclear to what extent the BPU wants regulated utility involvement in the proposed EV ($300mm) and battery storage ($100mm) programs. Decisions are expected in Q1'21. (3) Stimulus Investment – PSE&G is engaged in early discussions with the BPU Staff around a potential acceleration of Gas System Modernization Program spend and/or electric reliability spend. Should the talks advance, we could see a formal filing within the next 3-6 months. (4) Transmission ROE Discussions – it sounds like the parties (PSE&G, the BPU Staff and the Consumer Advocate) despite being close are currently at a stalemate. From here, either the stalemate breaks or the Staff/Consumer Advocate could launch a formal challenge at FERC (likely a multi-year process). (5) Offshore Wind – PEG expects to make a decision as to whether or not to take up to a 25% interest in Ørsted's 1,100 MW Ocean Wind project by the end of November. We continue to think it is likely that PEG participates. (6) Nuclear – not much new here. PEG has made it clear that the $10/MWh ZEC payment will not be sufficient to keep the company's nuclear units operational longer-term. We expect more clarity on this issue by mid/late '21.

Sempra Energy (SRE/Equal Weight/$133.64) (Akers)

Strategic Capital & LNG. Based on the Q3 call and mgmt. comments at EEI, it appears likely to us that SRE is looking to sell an interest in the LNG portfolio. This would serve two complementary purposes: one, to get an attractive valuation marker for the LNG business; and two, to keep the business mix more heavily weighted toward the regulated utility operations (improves perceived risk profile, which is important to both investors and rating agencies). We do not think a spin of the LNG operations is timely as it provides a competitive advantage to operate under the SRE umbrella. Shifting to Mexico, mgmt. remains bullish long-term while acknowledging challenges presented by the current administration. The company views ECA as a critical asset in Mexico and expressed confidence that the export permit will be received this month with FID by year-end. More broadly, the tone on LNG was constructive as mgmt. indicated that conversations with potential off-takers have picked up and pricing has improved.

Gas in CA. The company expects the friction between SoCalGas and certain environmental interests could continue near-term, but (1) noted that regulatory outcomes have been very supportive of continued investment in the gas infrastructure and (2) expressed confidence that there's a significant long-term role

for the gas LDC infrastructure in a clean energy future (RNG, hydrogen, carbon capture). SoCalGas is making a significant push in RNG and noted that while it appears expensive, costs should be driven down with scale and additional investment (similar to solar and wind in their infancy). We did not get the sense, however, that SRE would look to acquire additional gas utility assets as the company prefers to position the portfolio more directly in alignment with the electrification trend.

Southern Company (SO/Equal Weight/$63.92) (Kalton/Reeder)

The Here and Now. With the finish line nearing on Vogtle Unit 3, it is clear that SO is not taking success for granted. The three risk areas to get to the next major milestone of hot functional testing, in order of increasing importance, are (1) sub-contractor work, (2) bulk electrical work and (3) paperwork – making sure the "as built" condition of the modules conform to the engineering plans so that the requisite ITAACs can be verified by the NRC. If for some reason the inspections, tests, analyses and acceptance criteria (ITAAC) process would uncover the need to submit a license amendment request (LAR), it could potentially take a few weeks to resolve – we believe it is important to note that the NRC is highly supportive of the project as it enters the final stages and has vowed to work expeditiously on their end. That said, management does not believe a LAR is any more likely than some sort of metallurgical condition popping up as the hot functional test ramps up the temperature of the plant components. Overall, management is confident heading into hot functional testing and the overall ability to bring Unit 3 in-service before the end of November '21. And Unit 4 should go better than Unit 3.

Beyond New Nuclear. Assuming the remainder of the new nuclear project goes relatively smoothly, SO is primed to deliver 6%+ EPS growth and this higher growth rate could be fleshed out as part of the YE2020 update. Excluding the "debt only" return penalties imposed by Georgia regulators when the higher price tag and longer schedule had to be recertified, SO has been growing at like 6%. But once both units go online it is projected to add about $200M of net income and generate an additional roughly $800M of cash flow. This should put SO in a position of strength which could include accelerating the dividend growth, upping the capex forecast (assuming rate affordability can be balanced) and/or further improving the credit metrics/rating. In other words, SO could support $8-9B/year of capex without the need to issue equity. A big driver of rate base growth could be early retirement of most of SO's large coal-fired plants and replacing them with renewables and gas as the O&M savings could serve to keep customer bills flat. Embarking on this sort of plan would require the buy-in of AL, GA & MS, including state regulators, and could be propelled forward under a Biden administration with a Republican senate where carbon reduction goals are accelerated.

Growth Outside The Core Regulated Franchises. Three things came up. (1) Renewable deals that meet Southern Power's return hurdles are tough to come by right now. (2) Management did not entirely rule out buying another gas LDC at the right price. (3) SO has clearly been exploring the idea of a synthetic approach to municipal/gov't owned system M&A. SO would lend expertise by operating the system and perhaps even allow access to SO's pool of assets as scale matters in the transition from fossil to zero carbon. This type of approach could overcome the challenge inherent in buying municipal assets including the fact that they are 100% financed with cheap debt and the loss of local ownership.

WEC Energy Group, Inc. (WEC/Equal Weight/$104.43) (Kalton)

Diving Into the '21-25 Capital Plan. Mgmt. provided additional details on the company's '21-25 capital investment plan (called the ESG Progress Plan) – $16.1B plan represents a $1.1B increase from '20-24. The refresh leans more heavily on renewables (25% of the spend) including new regulated solar (800 MW), wind (100 MW) and battery storage (600 MW). The amount of battery storage was a little bit of a surprise to us but mgmt. indicated that the storage integrates nicely into the system. Separately, the contracted renewables bucket (Energy infrastructure) consists of $2.2B of planned investment during the period and incorporates the already announced $400mm Thunderhead project. If WEC executes on the full $2.2B we think Energy Infra's EPS contribution would be ~8% of consolidated EPS in '25, which would still give the company some wiggle room under the 10% threshold (WEC wants to limit non-utility EPS to 10% of total EPS max).

Other Tidbits. (1) Mgmt. indicated that the capital investment plan supports a 5-yr EPS CAGR of just above 6%. Other assumptions underlying this statement include earned ROEs at the allowed levels (little change to allowed ROEs during the period) and equity ratios at the mid-point of the equity ratio ranges of 50-55% for the WI utilities. Optimizing the equity ratio represents a not insignificant EPS opportunity in and of itself. For context, we estimate annual EPS could be $0.10-0.15 higher by '25 if the WI utilities earned the allowed ROEs at a 55% equity layer, which could add 50bps to the 5-yr EPS CAGR. Keep in mind, there is also an opportunity to retain a portion of earnings above the ROE thresholds. Optimizing the WI utilities earnings will depend on a number of factors including future rate case outcomes, sales trends and effective cost management. That being said, the equity ratios provide yet another lever to

help achieve an EPS CAGR toward the upper end of the company's 5-7% goal and/or help offset unforeseen pressures. (2) WEC remains very comfortable with owning gas LDCs and we got the sense they would consider a gas LDC purchase as long as it fit mgmt's famous three criteria: (1) EPS accretive in first full year, (2) credit neutral, and (3) long-term earnings growth prospects consistent with WEC's organic growth. Executive Chairman Gale Klappa suggested that the growth criteria could prove to be an impediment.

Xcel Energy, Inc. (XEL/Equal Weight/$74.69) (Kalton)

CapEx Discussion. Our EEI discussion centered on XEL's recent 5-yr capex refresh for '21-25. As a reminder, the base plan of $22.6B (vs. the '20-24 guidance of $22.0B) results in a rate base CAGR of 6.3% (off the 20E base). In addition, XEL provided a separate analysis including the $1.4B upside related to NSPM's Minnesota Relief & Recovery Proposal consisting of wind repowering ($750mm) and new solar ($650mm). The "incremental" plan would result in a 6.9% rate base CAGR. Mgmt. remains optimistic that the MPUC will approve the spend and noted that the opposition's arguments are consistent with prior arguments in similar proposals (questioning the long-term customer benefits based on NSPM's power price assumptions). Our capex outlook includes the $1.4B of incremental spend. Separately, mgmt. poured cold water on our question as to whether XEL held back other capex from the base plan while NSPM's request is pending – they characterized the base capex plan as fully representing the assessed needs while also pointing out that additional capital tends to come into the plan over time (both traditional capex along with potential PPA buyouts). On the PPA front, mgmt. indicated that while discussions with parties are always ongoing, things tend to heat up around the operating utilities' IRPs.

Hydrogen. We have long viewed XEL as being ahead of the game in terms of long-term system planning and understanding new technology (not to be confused with early adoption as mgmt. carefully considers technology risk and customer rate implications). On that note, mgmt. is evaluating hydrogen as a future fuel source to help bridge the last mile to zero carbon. Our take is that XEL is skeptical that green hydrogen production will be economically attractive and, instead, pointed out that using excess nuclear output from the company's existing nuclear facilities to produce hydrogen could be 1/3 more cost effective. Fun fact: nuclear produced hydrogen is referred to as Purple Hydrogen.

Acronyms

ALJ – Administrative Law Judge
AMI – Advanced Metering Infrastructure
ATM – At the Market
BOEM – Bureau of Ocean Energy Management
BPU – Board of Public Utilities
CCRO – Customer Credit Reinvestment Offset
CEF – Clean Energy Future
CEHE – CenterPoint Energy Houston Electric
COP – Construction and Operations Plan
DR – Demand Response
DSM – Demand-Side Management
ECA – Energía Costa Azul
EE – Energy Efficiency
EIA - Energy Information Administration
ESG – Environmental, Social and Governance
EV – Electric Vehicle
FID – Final Investment Decision
FRP – Formula Rate Plan
FPSC – Florida Public Service Commission
GHG – Greenhouse Gas
IRP – Integrated Resource Plan
LDC – Local Distribution Company
LFCR – Lost Fixed Cost Recovery
LNG – Liquefied Natural Gas
MOPR – Minimum Offer Price Rule
MPUC – Minnesota Public Utilities Commission
MVP – Mountain Valley Pipeline
PBR – Performance Based Ratemaking
PISA – Plant-in-Service Accounting
PPA – Power Purchase Agreement
PURA – Public Utilities Regulatory Authority
REC – Renewable Energy Credit
RFP – Request for Proposals
ZEC – Zero Emission Credit

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3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

VOLATILITY RATING
V=A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: November 12, 2020

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2020 Utility Symposium Takeaways

Highlighting PEG, WTRG & ATO

Utilities

$	Rating		Price	FY EPS				Price Target	
				2020E		2021E			
Ticker	Curr.	Prior	12/09/20	Curr.	Prior	Curr.	Prior	To	From
Diversified Electric Utilities									
PEG	1	NC	56.89	3.43	NC	3.38	NC	69.00	NC
Natural Gas LDCs									
ATO	1	NC	97.75	4.72A	NCA	5.00	NC	114.00	NC
Water Utilities									
WTRG	1	NC	47.70	1.58	NC	1.65	NC	52.00	47.00

Source: Company data and Wells Fargo Securities, LLC estimates

1= Overweight, 2 = Equal Weight, 3 = Underweight, V = Volatile
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful

- **Summary.** On 12/8 & 12/9, over 35 electric, gas and water utilities participated in virtual investor meetings at the 2020 Virtual Midstream and Utility Symposium. The tone of conversations was quite positive with companies cautiously optimistic on sales growth into 2021 and poised to advance de-carbonization strategies. In the comments below we expand on general industry takeaways and highlight PEG, WTRG (also increase price target) and ATO as timely investment ideas.

- **No Shortage of Investment Opportunities…** Between aging wires and pipes and the push toward de-carbonization, companies touted significant infrastructure investment opportunities with visibility well beyond the 5-year planning horizons. On the electric generation front, a number of utilities are scheduled to file IRPs in 2021 (BKH, CMS, EVRG, NI, OGE, XEL) with most executives pointing to renewables and peaking gas as the most likely resource solutions. In terms of coal retirements, companies generally are not expecting significant pressure from the Biden EPA only because many have already taken steps to accelerate coal retirements. That said, stricter emission regulations could provide greater justification for local stakeholders to accelerate retirements as several companies are still working out the details on recovery of the un-depreciated plant balances with securitization discussions going on in a number of states.
- **…Gating Factor is Customer Rates.** Utilities are always mindful of customer rate pressure, but we sensed a heightened sensitivity in light of COVID-related considerations. Regulators and politicians have pushed back on requested rate increases during the pandemic with the most recent example being the PA ALJ recommendation to deny NI's rate increase along with less overt actions including downward pressure on allowed ROEs (AZ). In response, many utilities are increasing programs to support low income customers and tightening their belts on the O&M front. Should utilities be able to create rate headroom via cost controls, fuel savings (steel for fuel) and, for certain utilities, customer growth, it could support the acceleration of capex and rate base growth.
- **Comments continue on page 2.**

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- **New Technology Roundup.** We continue to sense a greater willingness on the part of the historically risk averse utility sector to embrace new technologies. We think this is being driven by a confluence of factors including (1) real and perceived policy pressure (at the state & federal levels), (2) customer demand for clean energy (both C&I and residential) and (3) the growing influence of ESG investing – is it just us or do company executives sound increasingly apologetic if stated generation resource plans still include coal in 2040? Several utilities indicated the potential to either accelerate or scale-up investments in battery storage (CMS) and EV-related infrastructure (DTE, XEL). And, in a mini eyebrow raising move, on 12/8 NEE acquired eIQ Mobility, a provider of software solutions to help assess fleets for a potential transition to electricity or hydrogen fuel. NEE indicated that the acquisition was part of the ongoing "dip your toes" approach into green hydrogen – and that the technology is still several years away from being a "needle mover" from an earnings standpoint – but the momentum continues to build.
- **M&A.** There was a lot of chatter regarding CNP's recent announcement regarding plans to sell LDCs in AR and OK. Nearby utilities BKH and OGS indicated a general openness to giving the assets a look, but not at valuations in the 1.5-2X rate base range – both expressed skepticism that their bids (if they bid) would prevail and appeared content to see a higher valuation from another party, which could lend support for LDC valuations overall. Northern utilities ALE and WEC did not express an interest in the assets and AQN commented that while they haven't ruled LDC acquisitions out, mgmt. prefers electric and water. SR provided broad comments that the company has been out of the M&A space due to frothy takeout multiples and would re-engage at more reasonable valuations along with cultural and regulatory considerations. While not categorically ruling out M&A, NWE noted they like the current electric/gas mix as well as serving areas where gas is not under attack and therefore cannot imagine moving outside of their Midwest region (but did not specify if AR and OK are in their region). Lastly, SWX expressed an openness to acquisitions, which would bolster the utility portion of the earnings mix, but did not comment specific to CNP's assets. More broadly, we think the need to create rate headroom in order to accelerate de-carbonization strategies could drive strategic combinations that offer scale and synergies.
- **Gas LDCs Strike A Positive Tone.** With the LDC utility business model in the spotlight as the electrification theme looms, we sensed greater comfort among gas executives that key stakeholders are acknowledging the role of gas distribution infrastructure in the pursuit of affordable de-carbonization (even in NJ). Companies also highlighted continued strong demand for LDC service including healthy new customer connect trends and opportunities to build-out the gas system into new areas. Consistent with the Q3 calls, most of the companies are actively exploring RNG opportunities and beginning to research the potential of adding hydrogen to the gas mix (early days). When asked whether RNG/hydrogen will detract from natural gas' affordability argument, executives drew a parallel with renewables in their infancy suggesting there's a need and expectation that the cost curves will be driven down over time. The LDCs also touted energy efficiency programs as a much more cost effective avenue toward de-carbonization.

Featured Picks

- **Public Service Enterprise Group (PEG/Overweight)**
  We like the set up for PEG heading into '21 as the company continues to transition to an appealing clean energy, predominantly regulated utility story (85% of earnings). Potential catalysts include (1) completion of the planned sale of the non-regulated fossil fuel and solar generation assets, which will simplify and "clean" up the story, (2) likely additional regulated capex arising out the CEF filings (Cloud & EV) and a new potential accelerated infrastructure investment program and (3) greater clarity on the long-term earnings profile for the nuclear fleet pending the outcome of an ongoing NJ BPU investigation. In the near-term, mgmt. is quite optimistic that the BPU will bless the $721mm CEF-Energy Cloud (AMI) (an all or nothing proposal) but is a little bit more iffy on the $261mm CEF-EV proposal. Evidentiary hearings on both the Energy Cloud and EV filings have been suspended as parties engage in settlement discussions. Separately, we touched on PEG's recent decision to acquire a 25% ownership interest in Ørsted's Ocean Wind project. While not unexpected, the decision frees up mgmt. to discuss the longer-term offshore wind opportunities that will likely sequence after Ocean Wind. Ørsted has 2,400 MW remaining in the Ocean Wind lease area and PEG/Ørsted jointly own the 1,000 MW Garden State Offshore Energy (GSOE) lease area. Now that PEG has opted into Ocean Wind 1, we fully expect Ørsted/PEG to jointly pursue future solicitations in NJ and the Mid-Atlantic (i.e., MD); this could set up for additional growth opportunities post '25 that will supplement PSE&G's strong rate base growth. As for the initial Ocean Wind stake, PEG will generate a substantial amount of cash upfront by taking the ITC & MACRS tax benefits (PEG has a U.S. tax appetite whereas Ørsted does not). We reiterate our Overweight rating and maintain our $69/sh price target.

- **Essential Utilities (WTRG/Overweight)**
  We came away from our WTRG meeting incrementally more bullish on the name and believe there are potential near-term catalysts to build upon the stock's recent strength. First, CEO Chris Franklin expressed confidence in the ability to get the pending DELCORA deal done and believes the judge may rule by Christmas on Delaware County's two legal challenges – the most important of which is the validity of the asset purchase agreement. Mr. Franklin reiterated that the County's concerns seem to be around the price and use of proceeds as opposed to be against actually selling to WTRG. As we have previously opined, a last minute settlement still cannot be ruled out. We believe the DELCORA deal represents material long-term value given meaningful capex needs that fall beyond the current 5-year forecast as well as the likely substantial wastewater tuck-in deals that could transpire in the area. Second, management believes investors will find the 1/11 guidance event constructive both in terms of the updated 3-year EPS and rate base growth outlook as well as environmental commitments at Peoples. Finally, we talked about the water and wastewater M&A pipeline and there continues to be attractive, sizeable opportunities that not too long ago WTRG would have never thought possible. We reiterate our Overweight rating and increase our 12-18 month price target to $52/share (29X our 22E EPS of $1.78) from $47.

- **Atmos Energy Corporation (ATO/Overweight)**
  ATO is our top pick in the Gas LDC space. We see the opportunity for multiple expansion from the current ~10% premium to gas peers. ATO is not a catalyst rich name, but offers consistent 6-8% EPS growth, a relatively low-risk regulated strategy, a strong balance sheet with well above-average credit metrics, supportive regulatory mechanisms and an excellent track record in our view. ATO also operates in gas-friendly states with ~70% of rate base in TX where we expect to see legislation proposed in 2021 that would prohibit the adoption of local bans on new gas hookups. We think continued execution through 2021 along with improving sentiment toward the LDC group will drive outperformance. We reiterate our Overweight rating and maintain our $114/sh price target.

Acronyms:

ALJ – Administrative Law Judge
AMI – Advanced Metering Infrastructure
BPU – Board of Public Utilities
C&I – Commercial & Industrial
DELCORA – Delaware Country Regional Water Quality Control Authority
EPA – Environmental Protection Agency
ESG – Environmental, Social, Governance
EV – Electric Vehicle
IRP – Integrated Resource Plan
ITC – Investment Tax Credit
LDC – Local Distribution Company
MACRS – Modified Accelerated Cost Recovery System
MW - Megawatt
O&M – Operations & Maintenance
RNG – Renewable Natural Gas

Rating Basis Information:

ATO Thesis: We are attracted to ATO's highly visible growth outlook, pure play regulated gas strategy and strong balance sheet. We do not believe these positive features are adequately reflected in the current share price.

PEG Thesis: We believe PEG shares offer investors an attractive risk/reward proposition. Key features include (1) a premier utility with well-above average rate base & EPS growth prospects, (2) a carbon-free nuclear generation fleet that generates significant FCF and (3) a strong balance sheet, which provides the company with financial flexibility.

WTRG Thesis: Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived and near-term regulatory risk is low as both the water and gas utilities completed rate cases in 2019), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

Price Target Information:

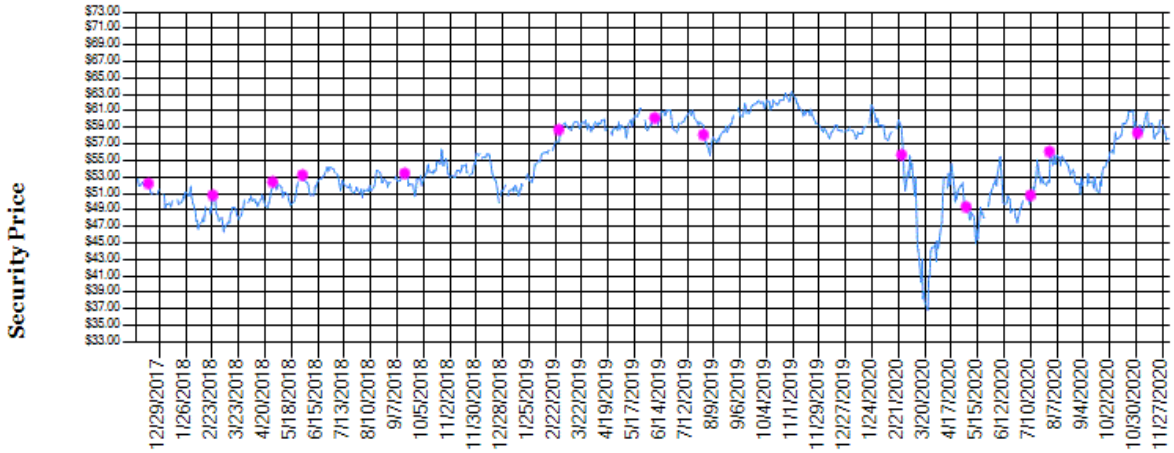
PEG Basis and Risks: Our $69/sh price target is based on a sum-of-the-parts analysis consisting of (1) $60.50/sh for PSE&G/Enterprise/Other (~20.5X our 22E EPS of $2.94) and (2) $8.50/sh for PSEG Power based on a DCF analysis. Risks to our valuation include earnings sensitivity to commodity prices, operational risks, unfavorable regulatory/political developments particularly as it relates to PEG's nuclear fleet.

ATO Basis and Risks: Our price target is based on a P/E multiple analysis (apply a 15-20% premium to the Gas LDC peer group multiple of ~18X on our '22E EPS). Key risks include regulatory risk (primarily in TX), potential pushback to rate increases, risk of gas-related incidents, and fluctuations in the Rider Rev mechanism at APT.

WTRG Basis and Risks: Our $52/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.78. For WTRG's water utility multiple, we ascribe a roughly 5% discount to the 21E multiple we use for AWK (34-34.5X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The roughly 5% discount reflects a modestly lower earnings growth rate (we forecast 6-7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 19X (based on ATO, NWN, OGS & SR) and then apply a 5-10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive PA regulatory framework. Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

Required Disclosures

Public Service Enterprise Group Incorporated (PEG) 3-yr. Price Performance



Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
12/4/2017		Kalton				
12/4/2017	NA	1	56	NE	NE	52.89
12/18/2017	52.30	1	59	NE	NE	51.97
2/25/2018	50.53	1	56	NE	NE	50.53
4/30/2018	52.02	1	57	NE	NE	52.15
5/31/2018	52.98	1	63	NE	NE	52.98
9/16/2018	53.27	1	60	NE	NE	53.27
2/27/2019	58.56	1	66	NE	NE	58.56
6/9/2019	60.01	1	72	NE	NE	60.01
7/30/2019	57.87	1	69	NE	NE	57.89
2/26/2020	55.57	1	67	NE	NE	55.57
5/4/2020	49.14	1	57	NE	NE	49.14
7/12/2020	50.59	1	65	NE	NE	50.59
7/31/2020	55.94	1	68	NE	NE	55.94
11/1/2020	58.15	1	69	NE	NE	58.15

*Effective December 7, 2019, Wells Fargo Securities' Equity Research modified its ratings definitions. Complete definitions of current ratings can be found below. For information related to prior ratings definitions, please contact equityresearch1@wellsfargo.com.

Source: Wells Fargo Securities, LLC estimates and Reuters data

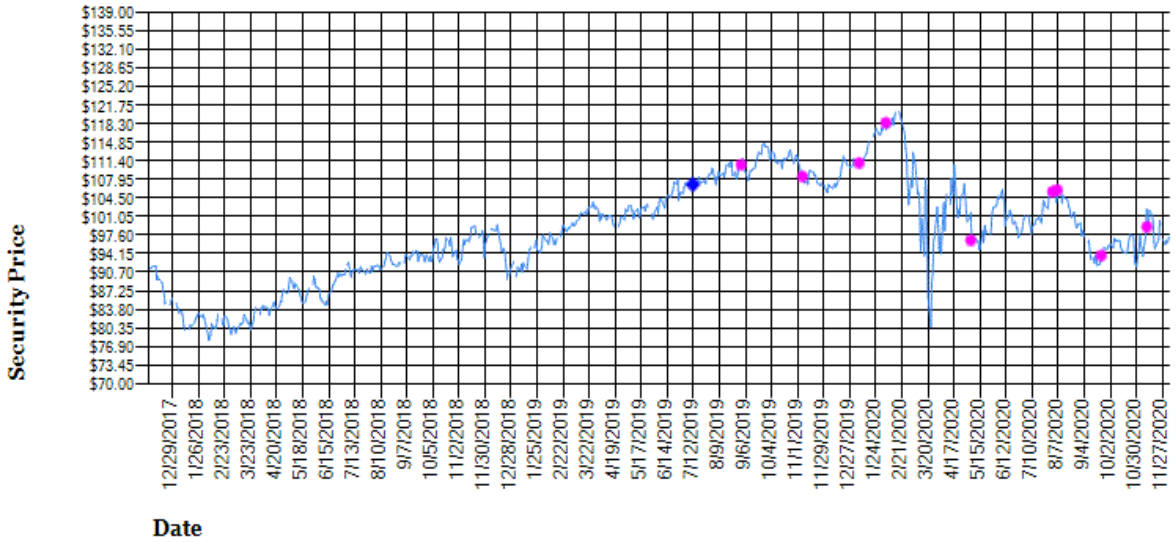
Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

Atmos Energy Corp. (ATO) 3-yr. Price Performance



Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
7/14/2019		Akers				
◆ 7/14/2019	106.46	1	119	NE	NE	106.46
● 9/2/2019	110.23	1	123	NE	NE	110.23
● 11/7/2019	108.40	1	119	NE	NE	108.18
● 1/8/2020	110.74	1	122	NE	NE	110.74
● 2/5/2020	116.82	1	131	NE	NE	118.28
● 5/7/2020	96.55	1	108	NE	NE	96.38
● 8/3/2020	105.31	1	115	NE	NE	105.31
● 8/7/2020	104.70	1	117	NE	NE	105.71
● 9/24/2020	92.87	1	104	NE	NE	93.59
● 11/12/2020	98.72	1	114	NE	NE	98.72

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Source: Wells Fargo Securities, LLC estimates and Reuters data

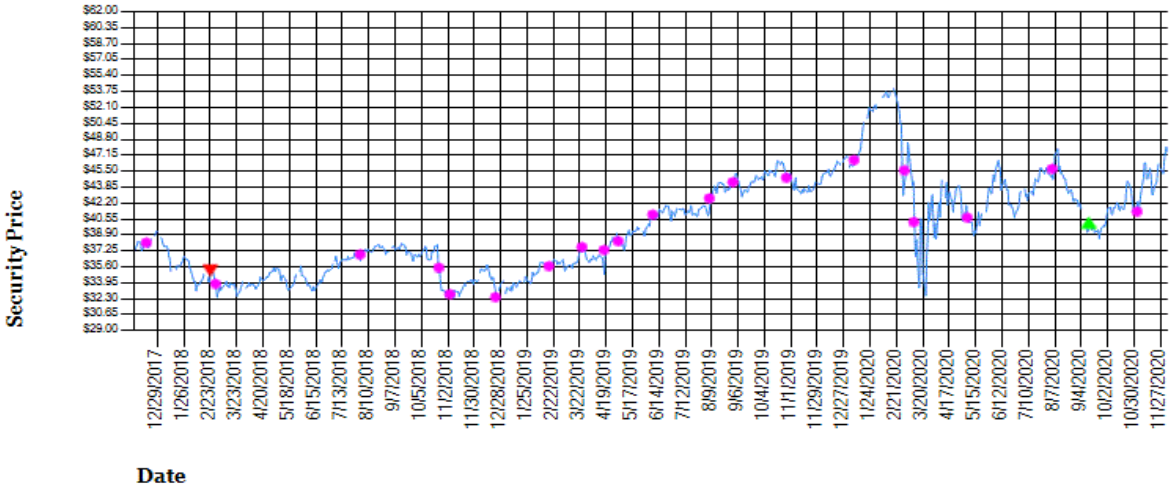
Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ◨ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	12/4/2017		Reeder				
	12/4/2017	NA	1	40	NE	NE	37.67
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
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●	10/24/2018	35.01	2	37	NE	NE	35.29
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●	8/8/2019	42.06	2	44	NE	NE	42.47
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▲	9/14/2020	39.35	1	45	NE	NE	39.82
●	11/4/2020	41.19	1	47	NE	NE	41.19

*Effective December 7, 2019, Wells Fargo Securities' Equity Research modified its ratings definitions. Complete definitions of current ratings can be found below. For information related to prior ratings definitions, please contact equityresearch1@wellsfargo.com.

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

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ATO: Key risks include regulatory risk (primarily in TX), potential pushback to rate increases, risk of gas-related incidents, and fluctuations in the Rider Rev mechanism at APT.
PEG: Risks to our valuation include earnings sensitivity to commodity prices, operational risks, unfavorable regulatory/political developments particularly as it relates to PEG's nuclear fleet.
WTRG: Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

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2=Equal Weight: Total return on stock expected to be 0-10% over the next 12 months. HOLD
3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

VOLATILITY RATING
V=A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: December 10, 2020

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WELLS FARGO SECURITIES

Essential Utilities, Inc.

WTRG: Solid Update Provided at 1/11 Guidance Event

WTRG Remains Our Favorite Water Utility Pick

Overweight/$52

Water Utilities

Earnings Estimates Revised Up

- **Key Points.** We viewed WTRG's 1/11 guidance event as supportive of our Overweight thesis. The '21 EPS guidance range of $1.64-1.69 was consistent with investor expectations and management extended the 5-7% EPS CAGR through '23. New items include (1) two new municipal transactions totaling $87M as well as (2) red meat for ESG conscience investors. We nudge up our 2021-24E EPS to/from $1.67/$1.65, $1.80/$1.78, $1.93/$1.91 & $2.07/$2.03. We also introduce our 25E of $2.20. Our forecast results in an EPS CAGR near the upper end of WTRG's targeted 5-7% range which we believe is reasonable given strong underlying rate base growth driven by accelerated pipeline replacement needs supplemented by a municipal M&A strategy that continues to gain momentum.
- **2 New M&A Deals Revealed – Positive Momentum Continues.** WTRG closed four municipal deals in 2020 for total rate base of $63M. In the pending column, the $277M DELCORA deal steals the show however WTRG has four other transactions with a combined value of $144M – includes three separate chunky wastewater deals (East Whiteland, PA $55M; Lower Makefield, PA $53M; Bourbonnais, IL $32M). WTRG has also been announced the winning bidder of two additional systems with a combined value of $30M which will move into the pending column once APA's are finalized. The company's deal development pipeline remains robust and management continues to express optimism that activity will start ramping up in the years ahead in the four states that only somewhat recently adopted FMV legislation (NC & OH in '18; TX in '19; VA in '20). Our model reflects primarily announced deal closures over the 2020-22 period plus a $75M/year placeholder in '23 & beyond.
- **Spotlighting DELCORA (Again!).** As we have previously opined, we believe the DELCORA deal represents material long-term value that is not currently reflected in the share price. Following the favorable court rulings on 12/28, PaPUC approval is the remaining hurdle with next key milestones including a 1/20 anticipated ALJ recommendation and a 3/11 commission approval deadline. Beyond the $277M rate base pick up at closure (expected early Q2'21), we are attracted to (1) the $700M of capital investments – $25-50M/year for typical repair/replace work plus roughly $300M over the 2026-28 period related to DELCORA's treatment plant – as well as (2) the likely substantial wastewater tuck-in deals that could transpire in the area. Simply put, we believe the DELCORA deal should, at a minimum, allow WTRG to continue to target a 5-7% EPS CAGR through the end of the decade if not bump it up to 6-8%.
- We offer some additional highlights from the 1/11 update on p.2 including (1) extension of the rate base growth targets, a brief discussion of the relatively low near-term regulatory risk profile and (3) announcements to hopefully lessen the ESG overhang.

$ EPS	2019A	2020E Curr.	2020E Prior	2021E Curr.	2021E Prior
Q1 (Mar.)	0.28	0.60 A	NC	0.67	NE
Q2 (June)	0.37	0.29 A	NC	0.25	NE
Q3 (Sep.)	0.48	0.23 A	NC	0.25	NE
Q4 (Dec.)	0.34	0.46	NC	0.50	NE
FY	1.47	1.58	NC	**1.67**	**1.65**
CY	1.47	1.58		1.67	
FY P/EPS	32.6x	30.4x		28.7x	
Rev.(MM)	890	1,931		2,055	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile
Adjusted EPS excludes items considered non-recurring.
WTRG expects 2021 adjusted EPS of $1.64-1.69 range and targets a 5-7% EPS CAGR through 2023 off the 2019 adjusted base of $1.47.
WTRG expects 2020 adjusted EPS at the top end of the $1.53-1.58 range.

Ticker	WTRG
Price Target/Prior:	**$52/NC**
Price (01/11/2021)	**$47.98**
52-Week Range:	$30-55
Shares Outstanding: (MM)	245.2
Market Cap.: (MM)	$11,764.7
S&P 500:	3,799.61
Avg. Daily Vol.:	931,178
Dividend/Yield:	$1.00/2.1%
LT Debt: (MM)	$5,277.4
LT Debt/Total Cap.:	53.2%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	7.0%
CY 2021 Est. P/EPS-to-Growth:	4.1x
Last Reporting Date:	11/03/2020 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Please see page 4 for rating definitions, important disclosures and required analyst certifications. All estimates/forecasts are as of 01/11/21 unless otherwise stated. 01/11/21 17:29:09 ET

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Together we'll go far

Other highlights from the 1/11 guidance event and update include:

- **Capex & Rate Base Guidance Largely Upheld.** Management indicated plans to invest $550M on the water/wastewater side (ex. M&A) in '21 and $450M for gas (up from $400M in '20). In total, roughly $3B of spend is expected over the 2021-23 period which will drive underlying 6-7% water/wastewater and 8-10% gas rate base CAGRs through '23. More than 50% of the spend is eligible for rider mechanism recovery

- **WTRG offers investors relatively low near-term regulatory risk.** The next PA water & wastewater rate case filing is expected in late '21. While WTRG's PA rate cases can never be overlooked given the meaningful % of rate base represented (more than 70% on the water/wastewater side), the utility has a long history of reaching constructive outcomes via settlement agreements and the ALJ recommendation in the pending AWK case honors a settlement agreement reached on 10/30.

  Otherwise commission approvals for FMV deals as well as regulatory treatment of the catchup portion of Peoples' repairs tax deduction (RTD) are the main items we are keeping an eye on at the state level. Further on the RTD treatment, a PaPUC order is expected in Q2'20 and we are optimistic that something similar to WTRG's proposal will be adopted. We would not rule out the possibility of a settlement with intervenors and note that evidentiary hearings are scheduled for later this month. Recall, WTRG's proposal would share the benefits 40% with ratepayers (through rate surcredits on bills) with the remaining 60% used as an increasing income tax expense offset over 2023-25 – this would avoid the need for Peoples to file to implement a base rate increase prior to 1/1/2026 while supporting the elevated pace of capex deployment and ensuring a fair opportunity to earn the allowed ROE.

- **Addressing The ESG Overhang.** WTRG committed to reducing annual Scope 1 and 2 GHG emissions by 60% by 2035 (using 2019 baseline) across both the gas and water utility platforms utilizing existing and proven methods and will look to get to net zero once technological advances allow. Other ESG-friendly updates include establishing multi-year plans to increase supplier and employee diversity as well as tying incentive comp to those metrics. Successfully addressing the ESG concerns that arose out of the recent acquisition of the Peoples gas utility and gaining wider spread acceptance by the investment mantra that seems to only be growing in popularity could help close some of the valuation gap between AWK.

Acronyms:

ALJ – Administrative Law Judge
APA – Asset Purchase Agreement
DELCORA – Delaware Country Regional Water Quality Control Authority
ESG – Environmental, Social, Governance
FMV – Fair Market Value
GHG – Greenhouse Gas
PaPUC – Pennsylvania Public Utility Commission

Price Target

Price Target: $52 from NC

Our $52/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.80. For WTRG's water utility multiple, we ascribe a roughly 5% discount to the 21E multiple we use for AWK (34-34.5X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The roughly 5% discount reflects a modestly lower earnings growth rate (we forecast 6-7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 17.0-17.5X (based on ATO, NWN, OGS & SR) and then apply a roughly 10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive PA regulatory framework. Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

Investment Thesis

Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived and near-term regulatory risk is low as both the water and gas utilities completed rate cases in 2019), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

Company Description

Headquartered in Bryn Mawr, PA, Essential Utilities (WTRG) - formerly Aqua America - is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTRG's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total water customer base and nearly 70% of consolidated water rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio.

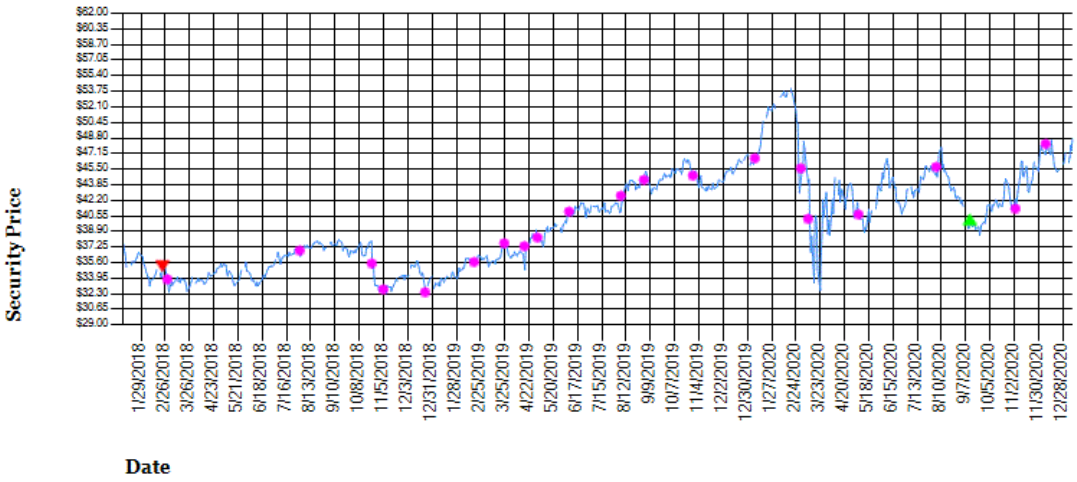
In March 2020, WTRG closed on the acquisition of Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, WTRG paid 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to other gas utility transactions at the time. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

Regulated operations account for more than 99% of consolidated revenues. Consolidated EPS is expected to be driven roughly 70% by water utility operations with the gas utility contributing the remaining 30%.

In February 2020, the new name Essential Utilities, Inc. and new ticker WTRG became effective. Prior, the company was known as Aqua America Inc. and traded under the ticker WTR.

Required Disclosures

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



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Symbol Key

▼ Rating Downgrade
▲ Rating Upgrade
● Price Target/Val Range Change
◆ Initiation, Resumption, Drop or Suspend
■ Analyst Change
❒ Split Adjustment

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WTRG: Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

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2=Equal Weight: Total return on stock expected to be 0-10% over the next 12 months. HOLD
3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

VOLATILITY RATING
V = A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: January 11, 2021

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Essential Utilities, Inc.

WTRG: Analyst Day Wrap Up -- Adjusting EPS Outlook

Equal Weight/$45

Water Utilities

Price Target Change

- **Key Points.** WTRG's 2/27 analyst day provided clarity around the company's EPS power for the next few years. After reporting adjusted '19 EPS of $1.47 (reflects the base water business without the impacts from external financings completed in 2019 for the Peoples acquisition), '20 EPS are expected to be $1.53-1.58 (pro forma for a 1/1 Peoples close vs. the anticipated 3/16). In addition, management forecasts a 5-7% EPS CAGR through '22 off the $1.47 base. This trails expected consolidated rate base growth of roughly 8% due to earned ROEs at recent/pending muni deals not yet earning the full keep plus some dilution. However, once another PA water rate case goes into effect (we assume a '21 filing; rates effective '22), then it sounds like EPS growth should track more closely to rate base growth. After flowing '19 actuals and analyst day disclosures through our model, we lower our 20-22E EPS to/from $1.56/$1.57, $1.65/$1.70 & $1.77/$1.80. We project a 6.5% EPS CAGR through '24. No change to our overall thesis or Equal Weight rating despite recent underperformance (down 10% since 2/18 relative to the S&P Utilities) as shares trade in-line with a 70% water/30% gas LDC blended multiple. We lower our 12-18 month price target to $45/share from $48 (26X our 22E) due primarily to lower peer group multiples since our last update.
- **EPS Outlook.** Our 2020-24E EPS are $1.56, $1.65, $1.77, $1.90 & $2.02. The addition of Peoples (3/16 close expected), including the $0.08-0.12 of EPS benefits anticipated by electing and flowing through the current portion of RTD at Peoples Gas, is what allows WTRG to guide to 2020 pro forma EPS of $1.53-1.58 (as if the deal closed 1/1). Our prior outlook did not include the RTD benefits – which we thought offered $0.10-0.15 upside – however we, as well as most investors that we have talked to, did not appreciate the headwinds facing the base water business in '20. This led to the guidance being viewed as somewhat disappointing and shares underperforming. After reporting adjusted '19 EPS of $1.47, management indicated 2020 base water EPS would have been relatively flat, all else equal. This is because (1) '19 benefited from the PA water repair tax deduction flowing to shareholders until new PA rates were effective mid-May, (2) there is roughly $200M of recent municipal system acquisition rate base additions that are not yet earning the allowed ROE in '20 (may actually be closer to break-even) and (3) the absence of any PA DSIC revenues until '21.
- **WTRG's Strategy.** The core growth drivers remain twofold. (1) Reinvest aggressively in existing systems and seek timely regulatory recovery. 2020 capex is $550M for water and $400M for gas with a total of $2.8B budgeted over the 2020-22 period. And we do not expect any falloff in those levels for the foreseeable future. (2) Actively pursue municipal M&A. ***Comment continues on p. 2***

$ EPS	2019A	2020E Curr.	2020E Prior	2021E Curr.	2021E Prior
Q1 (Mar.)	0.28	0.62		NE	
Q2 (June)	0.37	0.23		NE	
Q3 (Sep.)	0.48	0.24		NE	
Q4 (Dec.)	0.34	0.47		NE	
FY	1.47	**1.56**	**1.57**	**1.65**	**1.70**
CY	1.47	1.56		1.65	
FY P/EPS	29.3x	27.6x		26.1x	
Rev.(MM)	890	1,927		2,058	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile
Adjusted EPS excludes items considered non-recurring.
WTR expects 2020 adjusted EPS of $1.53-1.58 and targets a 5-7% EPS CAGR through 2022 off the 2019 adjusted base of $1.47

Ticker	WTRG
Price Target/Prior:	**$45/$48**
Price (02/28/2020)	**$43.01**
52-Week Range:	$34-55
Shares Outstanding: (MM)	220.8
Market Cap.: (MM)	$9,496.6
S&P 500:	2,954.22
Avg. Daily Vol.:	1,204,010
Dividend/Yield:	$0.94/2.2%
LT Debt: (MM)	$3,077.0
LT Debt/Total Cap.:	44.1%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	6.0%
CY 2020 Est. P/EPS-to-Growth:	4.6x
Last Reporting Date:	02/26/2020 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Please see page 3 for rating definitions, important disclosures and required analyst certifications. All estimates/forecasts are as of 03/02/20 unless otherwise stated. 03/02/20 06:51:16 ET

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Together we'll go far

- **WTRG's Strategy *(continued…).*** Deal activity in the industry remains elevated, in large part due to states adopting FMV legislation, and WTRG is in various levels of discussions with systems representing a total of 320,000 customers. Besides PA and IL, WTRG seems to believe OH, TX and KY hold the most promise. Management's compensation is tied to a $60M/yr deal value target and the goal is to achieve 2-3% customer growth through organic and M&A. Management believes the capex budget can be financed without new equity whereas deal flow would require roughly 50% new equity, perhaps through the establishment of an ATM program in front of the DELCORA deal close (expected late '20). Speaking of DELCORA, enthusiasm remains high for the deal from the immediate rate base addition, meaningful future capex needs ($700M by 2028) as well as potential bolt-on wastewater deals perspectives. Other management priorities outlined at the analyst day include completing/integrating the Peoples and DECLORA transactions as well as maintaining ESG appeal (highlighted recent diversity and governance enhancements).

Acronyms:

ATM – At-the-market
DSIC – Distribution System Improvement Charge
ESG – Environmental, Social, and Governance
FMV – Fair Market Value
RTD – Repairs Tax Deduction

Price Target

Price Target: $45 from $48

Our $45/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 2.5% discount to our 70% water/30% gas utility hybrid multiple to our 2022E of $1.77. The 2.5% discount reflects merger execution/integration risk. For WTRG's water utility multiple, we start with AWK's 2021 P/E multiple of 29.4X (AWK represents the closest publicly traded peer) and apply a 5% discount (given AWK's higher growth rate and best-in-class management team). For WTRG's gas utility multiple, we utilize the 2021 pure play gas LDC median of 21.2X. Key risks include regulatory and M&A strategy execution related.

Investment Thesis

We are attracted to WTRG's strong fundamentals - a proven EPS growth strategy, a growing rate base, constructive regulation, efficient operations and a strong balance financial profile. Our Equal Weight rating reflects valuation considerations in light of WTRG's pending agreement to acquire Peoples (a gas utility) and the associated P/E multiple, regulatory and deal execution/integration related risks.

Company Description

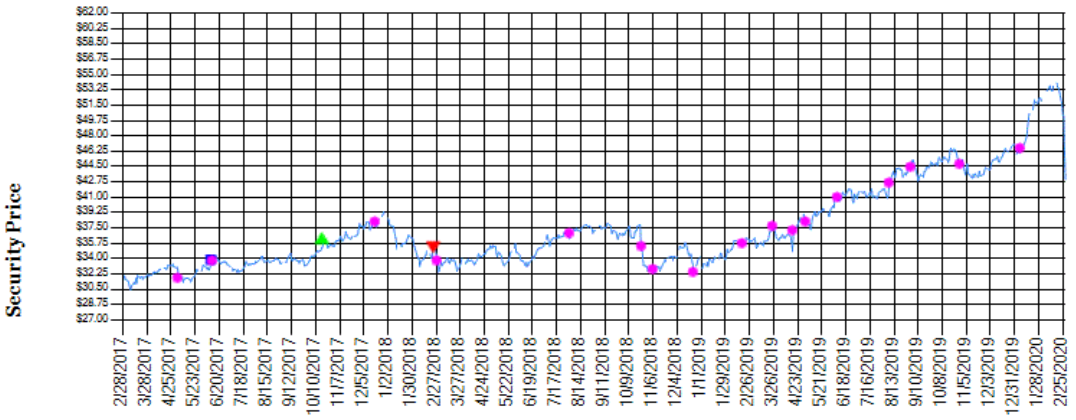
Headquartered in Bryn Mawr, PA, Essential Utilities (WTRG) - formerly Aqua America - is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTRG's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total water customer base and nearly 70% of consolidated water rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio. Regulated operations account for more than 99% of consolidated revenues.

On 10/23/18, WTRG announced a deal to acquire Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, the deal appears to be 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to what we have seen in recent gas utility transactions. WTRG received PA regulatory approval on 1/16 and the deal is expected to close imminently. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

On 2/3, the new name Essential Utilities, Inc. and new ticker WTRG became effective. Prior, the company was known as Aqua America Inc. and traded under the ticker WTR.

Required Disclosures

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	2/28/2017		Kalton				
	2/28/2017	NA	2	NE	31.00	33.00	31.74
●	5/4/2017	31.70	2	NE	32.00	34.00	31.73
■	6/13/2017		Reeder				
●	6/13/2017	33.62	2	35	NE	NE	33.62
▲●	10/19/2017	35.30	1	40	NE	NE	36.03
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51

*Effective December 7, 2019, Wells Fargo Securities' Equity Research modified its ratings definitions. Complete definitions of current ratings can be found below. For information related to prior ratings definitions, please contact equityresearch1@wellsfargo.com.

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

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WTRG: What's In A Name? - Change Ironically A Harbinger Of COVID Resiliency

Equal Weight/$42

Water Utilities

Price Target Change

- **Key Points.** Management affirmed all aspects of guidance provided at the late February analyst day as WTRG's utility businesses are expected to be resilient to the challenges presented by COVID-19. It helps that the bulk of customers and revenues, for both water and gas, are residential and that the gas utility is past the high-demand heating season. In addition, constructive regulatory treatment of any incremental COVID-19 costs is expected. No change to our 2020-24E EPS of $1.56, $1.65, $1.77, $1.90 & $2.02. Our outlook is consistent with management's 2020 pro forma (as if the Peoples deal closed 1/1 and experienced normal weather from 1/1 through the 3/16 close) EPS guidance of $1.53-1.58 and 5-7% CAGR through 2022 off the '19 base. We reiterate our Equal Weight rating but lower our 12-18 month price target to $42/sh (23.5-24.0X our 22E) from $48/sh due to lower peer group multiples since our last update.
- **COVID-19 Impacts – Sales/Expenses.** Although it is early, management mentioned that preliminary April data shows that the increased residential usage is offsetting the decrease in C&I and gov't/public customers on the water side as the month came in right at budget. And with the heavy-use heating season over on the gas side, management does not see a material financial impact from usage but that could depend on how long the stay-at-home orders are in place. WTRG plans to track COVID-19 related expenses with an expectation that regulators will afford constructive recovery, particularly of bad debt expense given the implemented no shutoff policies for non-payment. Bad debt expense rose to 1.1% of revenues in the 2008-09 financial crisis which is about double the 0.5% that has been historically observed and embedded in water rates. That said, there are some costs that are lower which could help defray any increases. Net-net, the overall expense impact is not expected to be material.
- **COVID-19 Impacts – Capex/Liquidity.** In terms of capital deployment, a two week moratorium implemented on water work in PA did set the utility about $30M behind schedule. However, the ground is expected to be made up over the balance of the year and there is no change to WTRG's overall water and gas capex budgets. Access to capital is not an issue. WTRG, like other utilities, have taken precautionary steps to boost near-term liquidity. The capex budget can be financed without equity but M&A deals will require some – we expect about 50% of the purchase price. With that in mind, we think WTRG could be flexible with the exact timing of the $300M of equity needs outlined for later this year to finance DELCORA and other deals in the pipeline.
- Please see p. 2 for discussions of municipal M&A activity (spoiler alert, COVID-19 could increase the deal flow!), regulatory updates and a brief EPS & capex discussion.

$ EPS	2019A	2020E Curr.	2020E Prior	2021E Curr.	2021E Prior
Q1 (Mar.)	0.28	**0.60 A**	**0.62**	NE	
Q2 (June)	0.37	0.23	NC	NE	
Q3 (Sep.)	0.48	**0.25**	**0.24**	NE	
Q4 (Dec.)	0.34	0.47	NC	NE	
FY	1.47	1.56	NC	1.65	NC
CY	1.47	1.56		1.65	
FY P/EPS	27.5x	26.0x		24.5x	
Rev.(MM)	890	1,927		2,058	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile
Adjusted EPS excludes items considered non-recurring.
WTR expects 2020 adjusted EPS of $1.53-1.58 and targets a 5-7% EPS CAGR through 2022 off the 2019 adjusted base of $1.47

Ticker	WTRG
Price Target/Prior:	**$42/$48**
Price (05/07/2020)	**$40.49**
52-Week Range:	$30-55
Shares Outstanding: (MM)	220.8
Market Cap.: (MM)	$8,940.2
S&P 500:	2,879.45
Avg. Daily Vol.:	900,670
Dividend/Yield:	$0.94/2.3%
LT Debt: (MM)	$3,077.0
LT Debt/Total Cap.:	44.1%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	6.0%
CY 2020 Est. P/EPS-to-Growth:	4.3x
Last Reporting Date:	05/06/2020 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Please see page 4 for rating definitions, important disclosures and required analyst certifications. All estimates/forecasts are as of 05/07/20 unless otherwise stated. 05/07/20 16:35:45 ET

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Together we'll go far

- **COVID-19 Impacts – Municipal M&A.** Similar to the thoughts expressed by AWK a few hours earlier, WTRG expects the volume of municipal M&A discussions/deals to be positively impacted by COVID-19. Many municipalities were already challenged financially and some even operationally (complying with increasingly stringent EPA standards) before the pandemic. The economic shutdowns have likely only exacerbated those pressures.

  Management remains upbeat about the pipeline of deals, noted how a number of decent-sized opportunities have been advanced that can hopefully be talked about in the not so distant future and highlighted how fair market value (FMV) legislation continues to open doors. VA adopted FMV earlier this year – all 8 of WTRG's water states now have it – and deal momentum continues to build in other recently adopted states like OH & TX. Having closed on the Campbell, OH water deal earlier this year, WTRG has the New Garden, PA ($30M), East Norriton, PA ($21M) and DELCORA ($277M) wastewater deals pending. The goal remains to achieve 2-3% customer growth through organic and M&A efforts.

- **Regulatory Updates.** WTRG's near-term regulatory calendar is fairly light as the PA water and gas utilities completed major base rate cases last year. The two proceedings of greatest investor interest are the DELCORA acquisition approval (filed in Q1; late '20 close expected) and PA regulatory treatment of the catch-up component of Peoples repairs tax deduction benefit (file this summer; clarity perhaps around YE'20; any retention by WTRG should be incremental to current outlook). Despite the challenges presented by stay-at-home orders, WTRG has not experienced any material regulatory timeline delays.

- **EPS Outlook.** Our 2020-24E EPS are $1.56, $1.65, $1.77, $1.90 & $2.02. The core growth drivers remain (1) capex/rate base growth by aggressively reinvesting in existing systems and seeking timely regulatory recovery and (2) municipal M&A. 2020 capex remains $550M for water and $400M for gas with a total of $2.8B budgeted over the 2020-22 period and we do not expect any falloff in those levels for the foreseeable future.

- In fact, an internally ordered report conducted by Black & Veatch to assess the overall safety of the Peoples gas system, including pressure risk, was completed earlier this month. While the conclusions were that the system is safe, WTRG is evaluating the recommendations made and preparing an action plan. There is an opportunity to invest more to further enhance safety and that will be addressed in future plans with an eye towards rate affordability.

Acronyms:

C&I – Commercial & Industrial
DELCORA – Delaware Country Regional Water Quality Control Authority

Price Target

Price Target: $42 from $48

Our $42/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.77. For WTRG's water utility multiple, we ascribe a 5-10% discount to the 21E multiple we use for AWK (27.0-27.5X). The 5-10% discount reflects both a modestly lower EPS growth rate (we forecast 6.5% for WTRG vs. 8% for AWK) as well as lower ESG appeal (in particular, the recent Peoples deal). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of roughly 21X. Key risks include regulatory and M&A strategy execution related.

Investment Thesis

We are attracted to WTRG's strong fundamentals - a proven EPS growth strategy, a growing rate base, constructive regulation, efficient operations and a strong balance financial profile. Our Equal Weight rating reflects valuation considerations in light of WTRG's recently closed acquisition of Peoples (a gas utility) and the associated P/E multiple, regulatory and deal execution/integration related risks.

Company Description

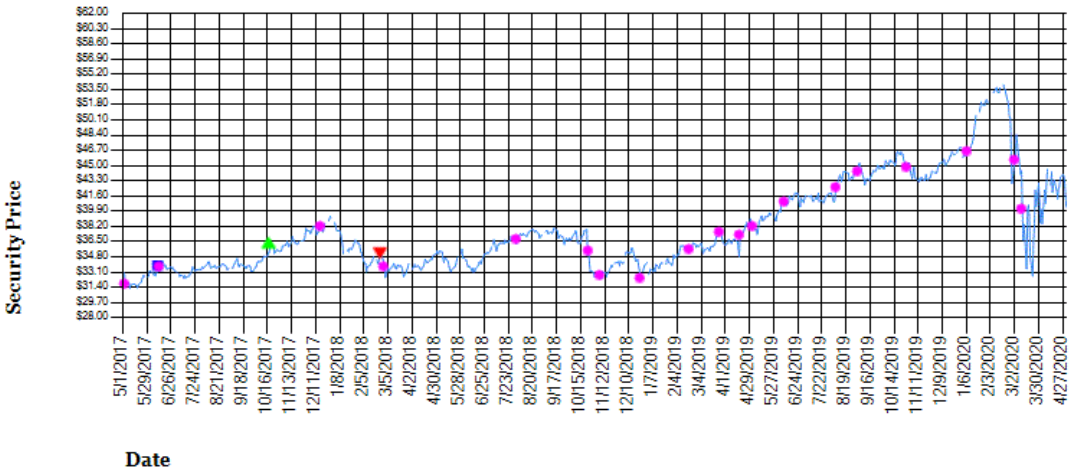
Headquartered in Bryn Mawr, PA, Essential Utilities (WTRG) - formerly Aqua America - is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTRG's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total water customer base and nearly 70% of consolidated water rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio. Regulated operations account for more than 99% of consolidated revenues.

On 10/23/18, WTRG announced a deal to acquire Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, the deal appears to be 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to what we have seen in recent gas utility transactions. WTRG received PA regulatory approval on 1/16/20 and the deal closed two months later on 3/16. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

On 2/3, the new name Essential Utilities, Inc. and new ticker WTRG became effective. Prior, the company was known as Aqua America Inc. and traded under the ticker WTR.

Required Disclosures

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	5/1/2017		Kalton				
	5/1/2017	NA	2	NE	31.00	33.00	32.94
●	5/4/2017	31.70	2	NE	32.00	34.00	31.73
■	6/13/2017		Reeder				
●	6/13/2017	33.62	2	35	NE	NE	33.62
▲●	10/19/2017	35.30	1	40	NE	NE	36.03
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51
●	3/2/2020	43.01	2	45	NE	NE	45.44
●	3/11/2020	44.41	2	48	NE	NE	40.03

*Effective December 7, 2019, Wells Fargo Securities' Equity Research modified its ratings definitions. Complete definitions of current ratings can be found below. For information related to prior ratings definitions, please contact equityresearch1@wellsfargo.com.

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

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WTRG: Key risks include regulatory and M&A strategy execution related.

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2=Equal Weight: Total return on stock expected to be 0-10% over the next 12 months. HOLD
3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

VOLATILITY RATING
V = A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: May 7, 2020

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Essential Utilities, Inc.

WTRG: Recent Pullback Creates Opportunity – Upgrade To Overweight

Overweight/$45

Water Utilities

Rating Change

- **Key Points.** We upgrade our rating on shares of WTRG to Overweight from Equal Weight as we believe the recent underperformance has created an attractive entry point. The cause of the relative pullback is not entirely clear (we offer some potential drivers in this report) but the bottom line is that we do not believe anything that has transpired fundamentally since the Q2'20 report in early August has materially impacted (1) the likelihood of DELCORA closing, (2) our EPS outlook or (3) our investment thesis.

  While the DELCORA deal is highly supportive of WTRG's growth aspirations, we consider the future to be bright without it driven by elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends. We believe relatively low risk, regulated EPS growth of at least 6% is achievable – that rate of growth would simply be enhanced if DELCORA closes given the $700M of required investment needed in the system by 2028 as well as potential further municipal wastewater deals in the region. No change to our 2020-24E EPS of $1.56, $1.65, $1.77, $1.90 & $2.02 (which assumes an end of Q1'21 DELCORA close). Our 12-18 month price target of $45/share (25.4X our 22E) is supported by P/E and DDM analyses.

- **Breaking Down Our P/E Valuation – Water.** Our P/E analysis results in a $45/share value and remains predicated on a 70% water/30% gas utility hybrid P/E multiple applied to our 2022E of $1.77. For WTRG's water utility multiple, we ascribe a 5-10% discount to the 21E multiple we use for AWK (30X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The 5-10% discount reflects a modestly lower earnings growth rate (we forecast 6-7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility).

- **Breaking Down Our P/E Valuation – Gas.** For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 18X (based on ATO, NWN, OGS & SR) and then apply a 5-10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of an accelerated pipeline replacement effort under the PaPUC-approved LTIIP program which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive regulatory framework of the PaPUC which includes fully forecasted test years, infrastructure surcharge mechanism recovery and a history of settled regulatory outcomes. ***(Comments continue on p. 2)***

$ EPS	2019A	2020E Curr.	2020E Prior	2021E Curr.	2021E Prior
Q1 (Mar.)	0.28	0.60 A	NC	NE	
Q2 (June)	0.37	0.29 A	NC	NE	
Q3 (Sep.)	0.48	**0.20**	**0.25**	NE	
Q4 (Dec.)	0.34	**0.47**	**0.43**	NE	
FY	1.47	1.56	NC	1.65	NC
CY	1.47	1.56		1.65	
FY P/EPS	26.8x	25.2x		23.9x	
Rev.(MM)	890	1,926		2,054	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile
Adjusted EPS excludes items considered non-recurring.
WTR expects 2020 adjusted EPS of $1.53-1.58 and targets a 5-7% EPS CAGR through 2022 off the 2019 adjusted base of $1.47

Ticker	WTRG
Price Target/Prior:	**$45/NC**
Price (09/11/2020)	**$39.35**
52-Week Range:	$30-55
Shares Outstanding: (MM)	245.2
Market Cap.: (MM)	$9,648.6
S&P 500:	3,340.97
Avg. Daily Vol.:	1,333,840
Dividend/Yield:	$1.00/2.5%
LT Debt: (MM)	$5,277.4
LT Debt/Total Cap.:	53.2%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	6.0%
CY 2020 Est. P/EPS-to-Growth:	4.2x
Last Reporting Date:	08/05/2020 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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- **Breaking Down Our P/E Valuation – Gas.** For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 18X (based on ATO, NWN, OGS & SR) and then apply a 5-10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort (mainly bare unprotected steel) under the PaPUC-approved LTIIP program which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA (the bulk of Peoples service territory), which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive regulatory framework of the PaPUC which includes fully forecasted test years, infrastructure surcharge mechanism recovery and a history of settled regulatory outcomes. Lastly, with the electrification theme gaining momentum and potentially challenging the long-term outlook for the gas LDC model (existential threat?), we no longer believe the publicly traded LDC multiples really reflect a takeout premium and thus no adjustment is necessary when valuing Peoples.

- **Other P/E Valuation Thoughts.** Shares trade at 23.8X & 22.2X our 21E & 22E EPS or roughly 15% discounts to the "large cap" pure play waters (AWK, AWR, CWT, MSEX & SJW) of 27.9X and 26.1X. That seems a bit steep given a relatively commensurate EPS growth profile, a large concentration of EPS power and growth stemming from the water utility and a similarly large concentration of EPS power stemming from the constructive PA regulatory environment. Perhaps the main differences relate to WTRG's inferior ESG appeal and credit metrics (though S&P assigns WTRG an "A"/Stable credit rating; the same as AWK & MSEX, a notch below AWR & CWT and a notch above SJW). If an in-line water multiple was applied, it would suggest a 12-18 month forward share price of closer to $50/share. It is also interesting to note that shares of WTRG currently trade at P/E multiples similar to high quality electric utilities WEC & XEL despite the water utility group median as a whole trading at roughly 70% premiums to regulated electrics.

- **What If DELCORA Does Not Happen?** At the risk of stating the obvious, we prefer the WTRG story with the DELCORA deal closing than without it. DELCORA is really somewhat of a unique strategic deal in our view given it not only increases WTRG's rate base by $277M out of the gate but offers meaningful future capex needs ($700M by 2028) as well as potential bolt-on wastewater deals in the region, particularly from municipalities that are wholesale wastewater customers of DELCORA's as well as the Tredyffrin Township Municipal Authority's trunk sewer system that WTRG acquired in 2018.

  However, much of the accretion and longer-term benefits of the deal that we love so much do not start impacting WTRG's financials until the back half of our 2020-24 outlook or beyond – in fact, we believe the assumptions embedded in our model could prove conservative if DELCORA closes. On the capex side, we only bump up our '21 & '22 forecast by $25M for DELCORA spend and then modestly grow that in '23 & '24 as it is our understanding that the majority of the $700M of capex actually occurs more in the 2026-28 period as a treatment plant expansion and pipeline is needed to get DELCORA off Philadelphia's wastewater system by 2028. On the M&A side, we do not increase our annual deal value placeholder of $60M for the enhanced opportunity set in the Southeast PA region that DELCORA could provide.

  If we were to completely strip out the DELCORA deal, the aforementioned tick up in capex that we assume in '21-24 and all of the associated external financing (including roughly $150M of equity), it only has a modest $0.03-0.05 impact (less than 3%) on our 2021-24E EPS. Keep in mind that when FMV deals are first consummated, the acquiring utility typically just inherits the existing rates and it therefore takes at least 2-3 years to go through a rate case cycle in order get the acquired system's rate base to earn similar returns as the rest of acquiring utility's water or wastewater operations in the state.

  Put another way, we believe WTRG's future growth would still be attractive even if the DELCORA deal does not come to fruition. There would still be time for management to continue to capitalize on the industry's FMV consolidation momentum – including in OH and TX which recently adopted the legislation and where WTRG is the big fish in the pond – and replace the growth that we believe will transpire in the 2nd half of the decade if the DELCORA deal does close.

- **Dissecting The Underperformance.** Since 8/10, shares of WTRG are -18%. Amongst water peers, SJW is -16% over the same period while the others range from -11% (MSEX) to -5% (AWK). Also worth noting, the gas LDCs are -12% while the S&P Utilities are -5%. So what gives? We have fielded a number of inbound inquiries from investors and have talked to the company but it is honestly hard to pinpoint the reason. We offer three potential contributing factors.

(1) Macro And The Flight To Quality. Utilities as a whole have remained out of favor in the risk-on market and those that investors seemingly want to own have been the highest quality names with generally the strongest credit metrics. This would be AWK & AWR on the water side whereas SJW & WTRG have weaker credit metrics due to recent large scale M&A.

(2) Gas Further Out Of Favor. It also does not help that gas LDCs have fallen further out of favor and again trade essentially in-line with electrics on a P/E basis. Gas LDCs used to trade at a premium to electrics (but below waters) due to higher rate base CAGRs spurred by pipe replacement and relatively lower regulatory risk. However the concern lately seems to be more existential due to natural gas bans being contemplated in cities on both the west and east coasts as well as electrification potential and the rising prospects of renewables plus storage to replace gas-fired generation. Most investors that we talk to use a gas multiple to value the 30% of WTRG's EPS derived from Peoples, which is consistent with our approach.

(3) Management Putting The Cart Before The Horse? Uncertainty exists as to whether the pending $277M DELCORA deal actually closes. We are relatively confident in WTRG's ability to gain PaPUC approval though it remains early days. Recently on 8/31, OCA's request (citing COVID) for a 60-day extension of the statutory deadline to 3/26/21 was granted whereas Delaware County's petition (which was supported by OCA and BI&E) to stay the proceeding in its entirety until the Court of Common Pleas litigation (discussed below) concludes was denied – neither should have caused WTRG shares to underperform in our opinion. Key remaining items under the PaPUC's updated procedural schedule issued 9/4 include standard public input hearings on 9/16, intervenor testimony due on 9/29, evidentiary hearings begin 11/9 and a recommended decision by 1/20. While the PaPUC docket is certainly worth monitoring, we consider the courts to be the critical path to deal closure.

There is a complaint in the Court of Common Pleas of Delaware County filed by Delaware County regarding essentially the County Council's attempt to (1) dissolve DELCORA based on an ordinance the County Council passed on 6/4/20 and/or (2) dispute the legality of the irrevocable trust and therefore gain access to the $210M of net sales proceeds (after DELCORA debt pay down) earmarked for the trust fund. If successful on #1, the County Council may argue that the asset purchase agreement with Aqua Pennsylvania is unenforceable. On #2, the County Council would like to see at least some of the proceeds go for taxpayer benefit (offset forecasted tax increases) versus just ratepayers. DELCORA's plan, as outlined when the deal with WTRG was announced in September 2019, is to create a rate stabilization fund (via the trust) that will keep ratepayers' annual bill increases at 3% or less over the next 8 years despite the massive amount of capital that needs to be invested into the system.

A hearing in the court case was held last Wednesday (9/9). WTRG interpreted the judge's tone as leaning positive based on the strong legal arguments in support of the transaction. However, the timeline for resolution appears like it will (not surprisingly) take longer than management originally thought. It is our understanding that the next scheduled court hearing on 9/23 will predominately focus on the issues around the trust while the final hearings are not slated to conclude until 10/21. As such, the judge's ruling might not come until late October at the earliest unless of course a settlement is reached.

Despite this uncertainty, WTRG pulled the trigger on a roughly $300M forward stock offering in mid-August. WTRG could of course elect cash settlement if all of the equity is not ultimately needed (we estimate roughly half is for non-DELCORA deals). Regardless, it is somewhat reminiscent of the share issuance "jumping of the gun" by WTRG & SJW in the recent Peoples & CTWS mergers where ultimate regulatory approval did not come for another roughly 9 months.

That all being said, it is our understanding that the deal is not necessarily dead if the court rules in Delaware County's favor. According to WTRG management, dialogue from the new all-Democrat County Council members seems to support system privatization efforts. Therefore it could be possible to perhaps re-cut the deal – whether that could be done through exclusive negotiations or if the County Council would put the DELCORA system out for bid is unclear (would open the door for others, like AWK who has previously expressed an interest in acquiring the system, to come in and compete). However, if the court only sides with Delaware County regarding the trust and the County Council is able to get their hands on some/all of the sale proceeds, the deal

could still happen it would just result in higher rates for DELCORA ratepayers as WTRG seeks recovery of the significant capital upgrades needed with lower/no funds set aside to help offset the impact.

- **Quick Repairs Tax Update.** The only other WTRG development since the Q2'20 call worth noting relates to Peoples pending request for treatment of the repairs tax catchup benefit. Initial intervenor statements regarding WTRG's proposal were filed on 8/26. Not surprisingly OCA and BI&E expressed concerns regarding the balance of ratepayer and shareholder interests. That said, WTRG was not surprised by the parties' stated positions.

  Recall, WTRG filed in early August for PaPUC treatment of the catch up portion of the Peoples repairs tax deduction election. The filing outlined a $381M catch up deduction and proposed to share the benefits between customers (40%) and shareholders (60%). For customers it would amount to a $14M/year benefit (in the form of a nearly 2% surcredit on the average monthly bill) over 4 years beginning 1/1/21. The remaining benefit would be deferred and amortized as an offset to income tax expense over the 2023-2025 period – specifically, 5% in 2023, 35% in 2024 and 60% in 2025 – in an effort to offset normal regulatory lag while essentially keeping the earned ROE consistent with allowed levels. This would extend the time between the next base rate case to approximately 6 years (delay the need for a base rate increase effective prior to 1/1/2026 per Peoples' current projections) while supporting the elevated pace of capex deployment needed to replace pipes and drive safety improvements.

  WTRG had communications with regulators and other key parties prior to making this filing which makes us hopeful that the proposal will be positively received and that a constructive outcome will ensue, perhaps via a settlement. Approval of the shareholder benefit aspect of the request would increase our confidence in the gas utilities' ability to achieve our forecast – we assume gas utility earned ROEs of 10-10.3% which we believe is reasonable and consistent with Peoples 2019 rate order. On the flip side, if the PaPUC decides to go a different direction with the catchup benefits, we still believe our 2023 & beyond EPS levels are reasonable within the backdrop of the constructive PA regulatory framework. It could simply necessitate filing for a base rate increase sooner which would bring with it associated regulatory risk.

Acronyms:
BI&E – the PaPUC's Bureau of Investigation and Enforcement
DELCORA – Delaware Country Regional Water Quality Control Authority
ESG – Environmental, Social, Governance
FMV – Fair Market Value
LDC – Local Distribution Company
LTIIP – Long-Term Infrastructure Improvement Plan
OCA – Office of Consumer Advocate
PaPUC – Pennsylvania Public Utility Commission
S&P – Standard & Poor's

Ticker, Rating, Price (9/11/20)

AWK, Equal Weight, $141.1

AWR, Equal Weight, $73.44

SJW, Equal Weight $59.72

Source: Wells Fargo Securities, LLC, FactSet

Price Target

Price Target: $45 from NC

Our $45/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.77. For WTRG's water utility multiple, we ascribe a 5-10% discount to the 21E multiple we use for AWK (30X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The 5-10% discount reflects a modestly lower earnings growth rate (we forecast 6-7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 18X (based on ATO, NWN, OGS & SR) and then apply a 5-10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive PA regulatory framework. Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

Investment Thesis

Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

Company Description

Headquartered in Bryn Mawr, PA, Essential Utilities (WTRG) - formerly Aqua America - is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTRG's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total water customer base and nearly 70% of consolidated water rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio.

In March 2020, WTRG closed on the acquisition of Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, WTRG paid 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to other gas utility transactions. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

Regulated operations account for more than 99% of consolidated revenues. Consolidated EPS is expected to be driven roughly 70% by water utility operations with the gas utility contributing the remaining 30%.

In February 2020, the new name Essential Utilities, Inc. and new ticker WTRG became effective. Prior, the company was known as Aqua America Inc. and traded under the ticker WTR.

Rating Basis Information:

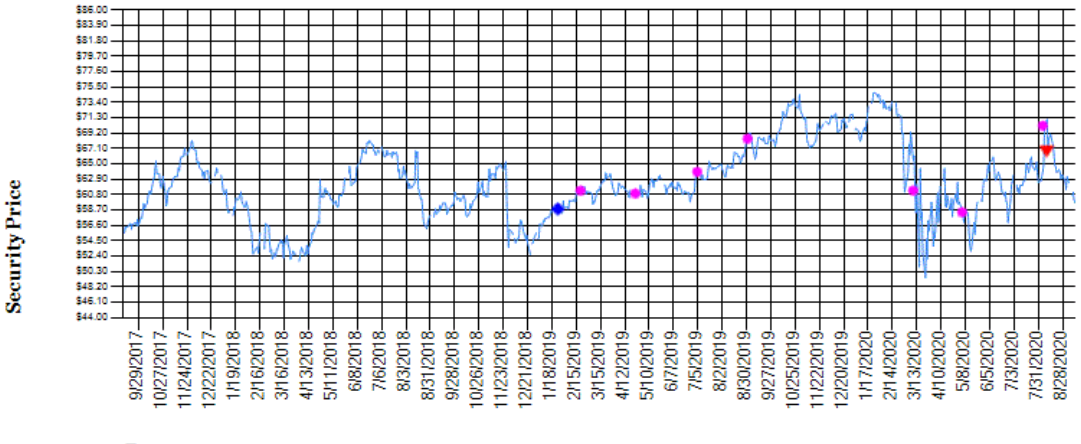
AWK Thesis: We believe AWK is well positioned to capitalize on favorable industry dynamics which should lead to above average rate base, EPS and DPS growth. Our Equal Weight rating reflects the fact that shares trade at roughly 10% premiums to water utility peers on our 21E & 22E EPS which we believe is adequate. While we consider AWK's EPS (8.0-8.5%) and dividend (9%) growth prospects as well as management team best in class for the water industry (as well as top tier for our utility coverage in general), takeout and liquidity/scarcity premiums that are arguably embedded in the water median multiple should not apply to AWK. In addition, we are cognization of the fact that water utilities as a whole trade at roughly 55% premiums to regulated electric and gas peers.

AWR Thesis: We regard AWR as a low risk water utility with a growing dividend that operates under generally constructive CA regulatory principles. That said, the overall constructiveness of CA regulation has been called into question recently and bears monitoring. On the non-regulated side, we believe ASUS could contribute 20-25% to consolidated EPS with upside potential if new military contracts are awarded. Our Equal Weight rating reflects valuation considerations as shares trade at roughly 10% P/E premiums to water utility peers on our 21E & 22E EPS. We consider a 5-10% premium warranted as AWR has the industry's strongest balance sheet and credit metrics (no new equity is needed) as well as a good financial track record (management consistently executes/delivers strong results). However, those positives are partially by offset by an EPS CAGR (6-7%) that is largely commensurate with peers and heightened regulatory risk.

SJW Thesis: We regard SJW as a relatively low-risk water utility with a secure and growing dividend. Despite the CTWS merger which added regulatory diversity, roughly 60% of utility earnings are derived from California. As such, SJW remains highly dependent upon California regulation which offers the state's utilities generally constructive regulatory principles. That said, the constructiveness of CA regulation has been called into question recently and SJW's lack of a full decoupling mechanism exposes earnings to a degree of volatility that other CA water utilities do not currently face. Our Equal Weight rating is premised on the fact that, given recent outperformance, shares of SJW now trade at only 7-8% discounts to "pure play" water utility peers on our 21E & 22E EPS. While we think shares could continue to "re-rate" a little more over time, the pathway and timing combined with the magnitude of upside is less compelling from a risk/reward standpoint today.

Required Disclosures

SJW Group (SJW) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	1/28/2019		Reeder				
◆	1/28/2019	58.50	1	70	NE	NE	58.43
●	2/21/2019	61.24	1	74	NE	NE	61.24
●	4/25/2019	60.66	1	72	NE	NE	60.66
●	7/5/2019	62.79	1	76	NE	NE	63.75
●	9/2/2019	68.33	1	80	NE	NE	68.33
●	3/11/2020	66.10	1	78	NE	NE	61.08
●	5/5/2020	58.80	1	67	NE	NE	58.24
●	8/7/2020	70.04	1	76	NE	NE	70.04
▼	8/11/2020	71.06	2	76	NE	NE	66.43

*Effective December 7, 2019, Wells Fargo Securities' Equity Research modified its ratings definitions. Complete definitions of current ratings can be found below. For information related to prior ratings definitions, please contact equityresearch1@wellsfargo.com.

Source: Wells Fargo Securities, LLC estimates and Reuters data

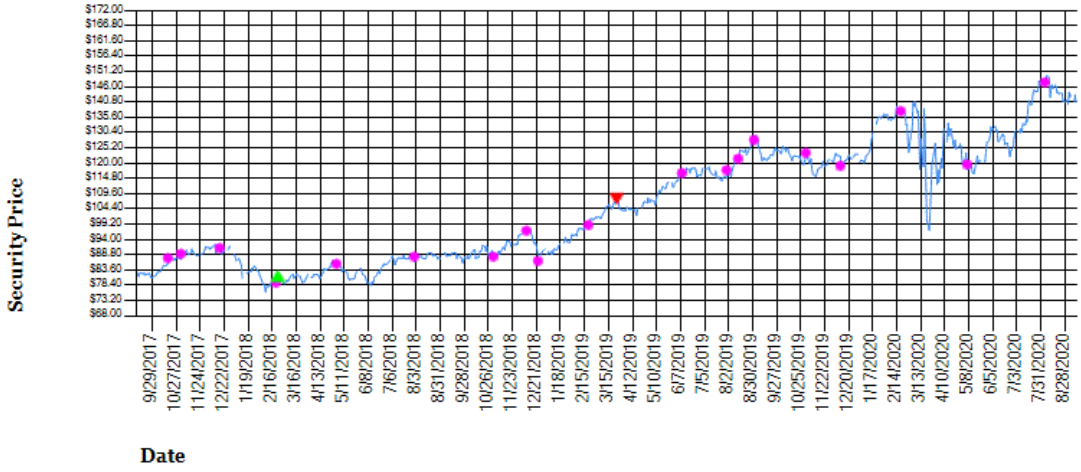
Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

American Water Works Company, Inc. (AWK) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	9/11/2017		Reeder				
	9/11/2017	NA	2	84	NE	NE	82.92
●	10/19/2017	86.22	2	89	NE	NE	87.24
●	11/3/2017	89.45	2	92	NE	NE	88.76
●	12/18/2017	90.82	2	95	NE	NE	90.49
●	2/21/2018	78.85	2	83	NE	NE	78.85
▲●	2/25/2018	80.63	1	88	NE	NE	80.63
●	5/3/2018	85.29	1	95	NE	NE	85.29
●	8/2/2018	87.54	1	100	NE	NE	87.54
●	11/2/2018	88.33	1	97	NE	NE	87.38
●	12/11/2018	96.48	1	104	NE	NE	96.48
●	12/24/2018	91.19	1	101	NE	NE	86.31
●	2/20/2019	98.66	1	109	NE	NE	98.66
▼●	3/26/2019	107.20	2	111	NE	NE	107.20
●	6/9/2019	116.29	2	120	NE	NE	116.29
●	8/1/2019	117.02	2	122	NE	NE	117.02
●	8/14/2019	121.83	2	128	NE	NE	121.20
●	9/2/2019	127.32	2	133	NE	NE	127.32
●	11/1/2019	123.27	2	131	NE	NE	122.78
●	12/12/2019	118.44	2	128	NE	NE	118.43
●	2/20/2020	138.70	2	147	NE	NE	137.30
●	5/7/2020	120.74	2	125	NE	NE	119.08
●	8/6/2020	146.93	2	136	NE	NE	146.97

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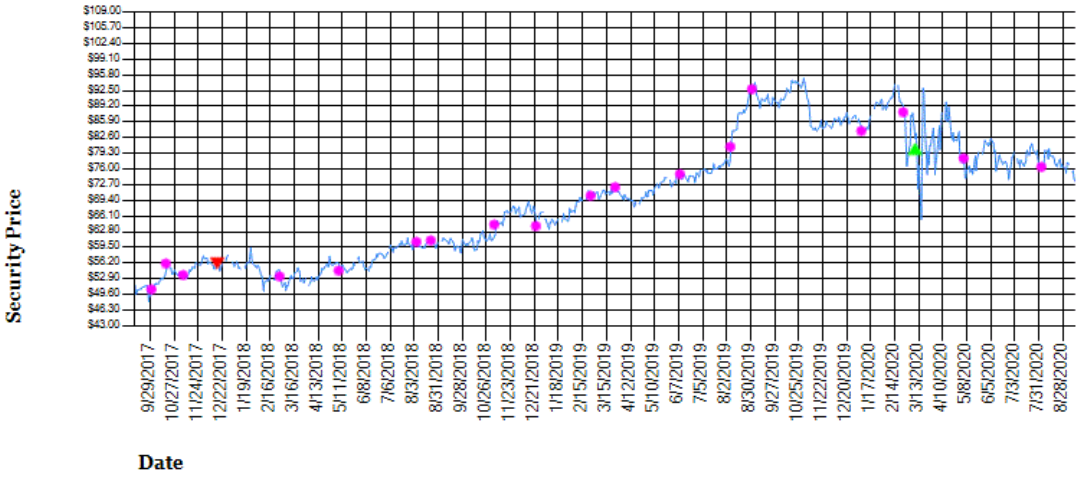
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

American States Water Company (AWR) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	9/11/2017		Reeder				
	9/11/2017	NA	2	46	NE	NE	51.53
●	10/2/2017	49.96	2	48	NE	NE	50.40
●	10/19/2017	55.03	2	51	NE	NE	55.85
●	11/7/2017	53.44	2	50	NE	NE	53.44
▼	12/18/2017	56.68	3	50	NE	NE	55.62
●	2/28/2018	54.29	3	48	NE	NE	53.12
●	5/8/2018	54.42	3	49	NE	NE	54.42
●	8/7/2018	59.98	3	54	NE	NE	60.51
●	8/24/2018	61.06	3	52	NE	NE	60.81
●	11/6/2018	64.05	3	56	NE	NE	64.05
●	12/24/2018	67.38	3	58	NE	NE	63.65
●	2/26/2019	70.12	3	62	NE	NE	70.13
●	3/26/2019	71.94	3	63	NE	NE	71.94
●	6/9/2019	74.72	3	67	NE	NE	74.72
●	8/7/2019	80.41	3	72	NE	NE	80.41
●	9/2/2019	92.53	3	77	NE	NE	92.53
●	1/8/2020	83.59	3	78	NE	NE	83.59
●	2/25/2020	87.67	3	87	NE	NE	87.67
▲●	3/11/2020	83.47	2	84	NE	NE	79.80
●	5/5/2020	77.96	2	76	NE	NE	77.96
●	8/4/2020	76.03	2	79	NE	NE	76.03

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Rating Code Key

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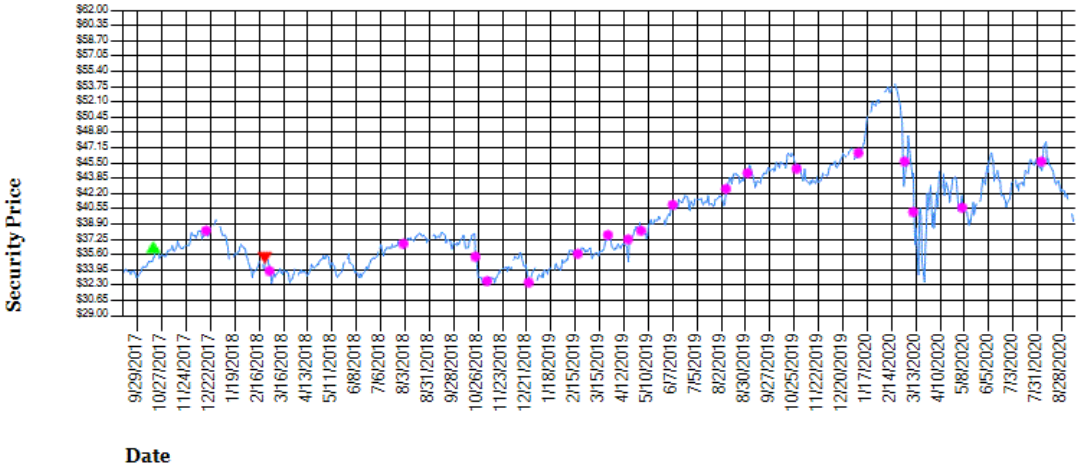
3	Underweight/Sell	NE	No Estimate

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	9/12/2017		Reeder				
	9/12/2017	NA	2	35	NE	NE	33.88
▲●	10/19/2017	35.30	1	40	NE	NE	36.03
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51
●	3/2/2020	43.01	2	45	NE	NE	45.44
●	3/11/2020	44.41	2	48	NE	NE	40.03
●	5/7/2020	40.49	2	42	NE	NE	40.53
●	8/6/2020	45.56	2	45	NE	NE	45.56

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Additional Information Available Upon Request

I certify that:

1) All views expressed in this research report accurately reflect my personal views about any and all of the subject securities or issuers discussed; and
2) No part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by me in this research report.

- Wells Fargo Securities, LLC and/or its affiliates, have beneficial ownership of 0.5% or more of any class of the common stock of American Water Works Company, Inc..
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- Wells Fargo Securities, LLC is currently acting as financial advisor to American Water Works Company, Inc. in the announced sale of its regulated New York operations to Liberty Utilities, the regulated utility business of parent company Algonquin Power & Utilities Corp. This transaction is subject to regulatory approval.
- Essential Utilities, Inc. currently is, or during the 12 month period preceding the date of distribution of the research report was, a client of Wells Fargo Securities, LLC. Wells Fargo Securities, LLC provided investment banking services to Essential Utilities, Inc..
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WTRG: Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

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Essential Utilities Inc. (WTRG): Secular water growth opportunity still under-appreciated; reiterate Buy (on CL)

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We reiterate our Buy rating (on Conviction List) on regulated water/gas utility Essential Utilities (WTRG) following 3Q2020 and a positive guidance revision. As highlighted in our recent upgrade note, we continue to see WTRG as a secular winner to benefit from an estimated $750 billion of water infrastructure investment needs (per the EPA) in a very fragmented market. This represents at least a $7bn opportunity – well above its total current water asset base – excluding any market share gains through municipal and other water utility acquisitions.

We see the market valuing WTRG as a 60% gas utility despite its 70% water earnings composition, given the current 6x (20%) P/E discount for the company's water utility segment versus the only other large-cap water utility American Water (AWK, Buy). With WTRG's normalized EPS growth potential similar to AWK's, one of the highest in our coverage universe, and management's strategy to further increase its water utility exposure over time, we believe WTRG deserves a premium valuation to reflect its high growth, largely ESG-friendly profile.

Below we highlight some key takeaways from the 3Q20 earnings call:

- **WTRG continues to benefit from work-from-home (WFH) demand trends.** The company recorded net positive demand at its utilities in both 2Q20 and 3Q20, given the vast majority of its revenues come from its residential customer base, which more than offset declines in commercial and industrial demand. We see this as a positive indicator of its ability to weather covid-related demand changes, which also allowed WTRG to raise its 2020 guidance to the top end of its range. We raise our 2020 EPS to $1.57 from $1.55 partly to reflect this benefit, while our 2021-2022 estimates remain unchanged.
- **Peoples Gas remains a one-off gas utility acquisition.** Management reiterated that the recent acquisition of PA-based Peoples Gas made sense based on its robust organic growth through decarbonizing gas pipe replacements, as well as its favorable geographic position in the heart of the Marcellus shale that provides low-cost for a region where gas remains a complementary energy source for the long-term. That said, they confirmed that future inorganic growth will only come from municipal water system acquisitions. We see WTRG's 70% water utility earnings exposure that should grow over time as still warranting closer to a water utility premium average.

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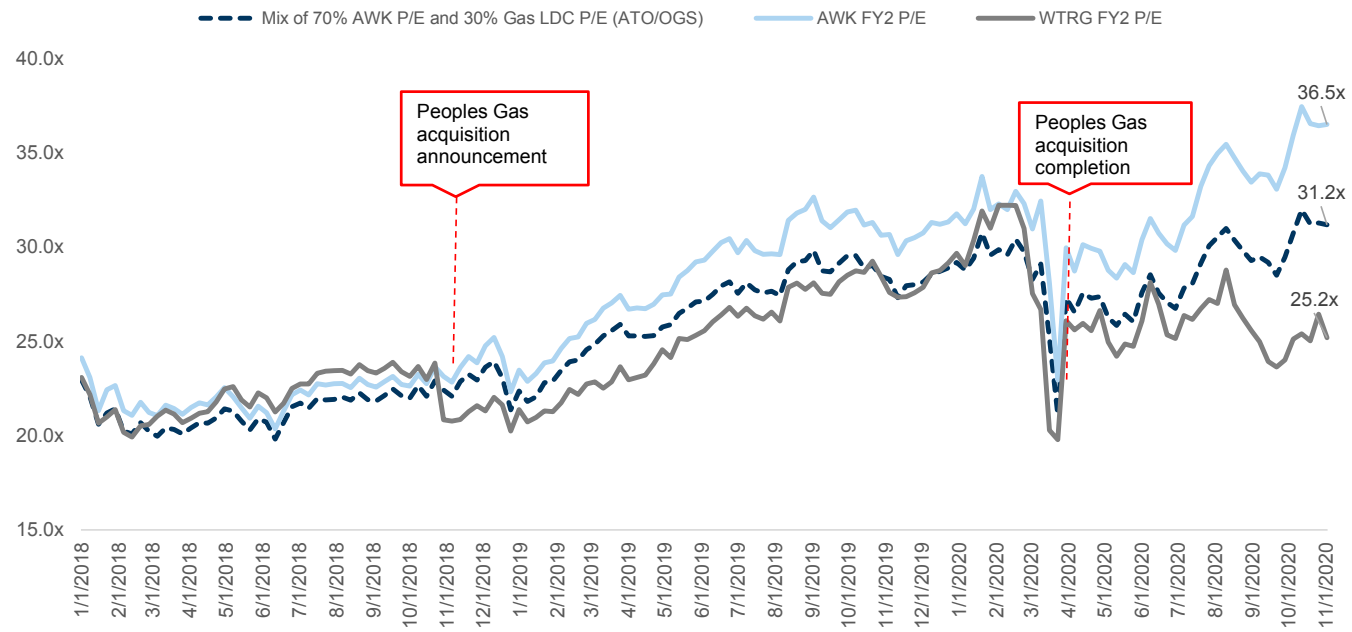
- **Management still expects the DELCORA wastewater acquisition to close in 1H2021.** While awaiting the outcome on the validity of the asset purchase agreement for the proposed acquisition, management remains confident in their ability to close the deal by March or April 2021. We believe WTRG's pipeline of potential acquisitions should still enable the company to sustain its inorganic growth even if the DELCORA deal does not materialize, with ~$300mn in forward equity already priced to help finance the additions. Our model continues to assume 1Q2021 issuance for the equity.

Our $51 12-month price target (unchanged) is based on a SOTP approach, with 35x/22x P/E applied to our 2021 water/gas utility EPS estimates, respectively. **Downside risks to our call include:** 1) PA regulation turns less constructive, which impacts earnings growth potential given the bulk of WTRG's earnings are derived from the state's water/gas operations, 2) the proposed DELCORA municipal water system acquisition fails to receive necessary approvals for completion, which could impact longer-term water rate base growth outlook barring replacement with other municipal acquisitions, and 3) longer-term growth concerns about the gas utility segment further compresses WTRG's valuation, both on an absolute basis and relative to pure-play water utilities.

Exhibit 1: We continue to view WTRG's meaningful relative P/E discount as unwarranted based on its 70%/30% water/gas profile...
FY2 P/E for AWK, WTRG, and an illustrative performance of a 70%/30% water/gas utility



ATO/OGS chosen as illustrative gas utility comps based on company profile, including their status as the two largest gas LDCs by market cap

Source: FactSet, Goldman Sachs Global Investment Research

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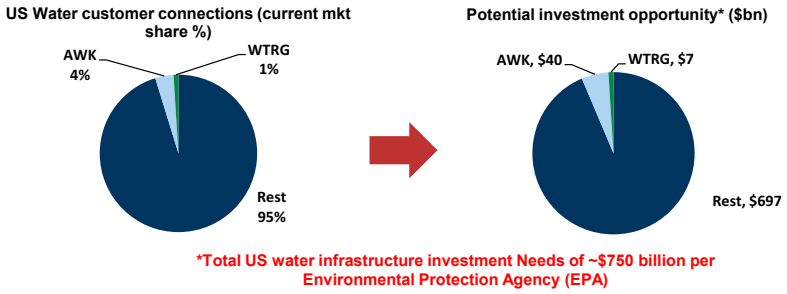
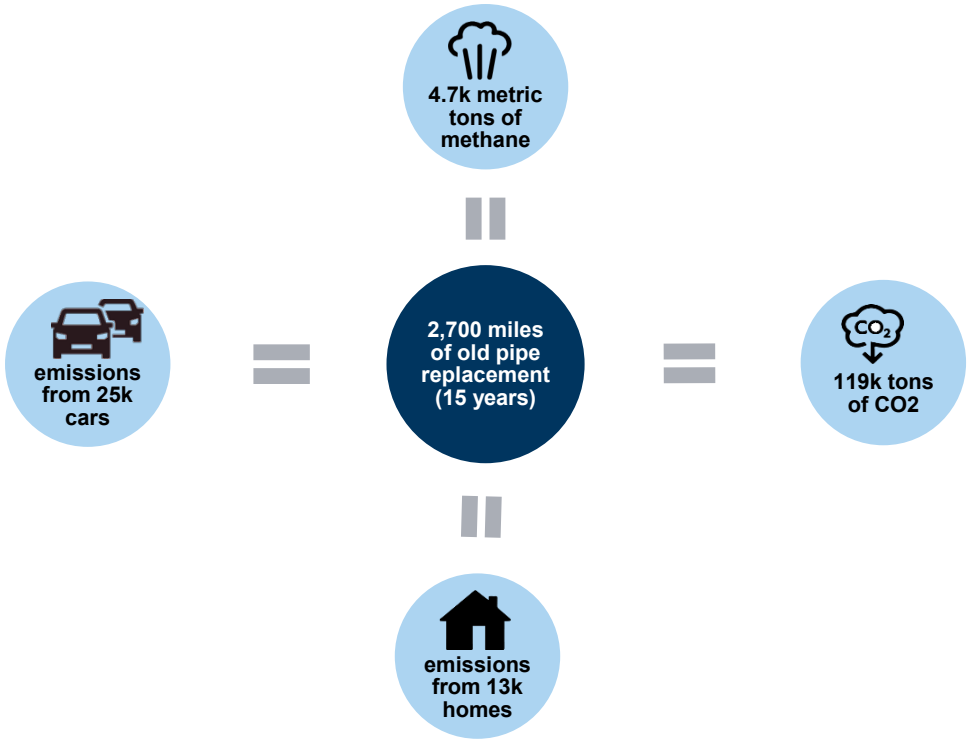
Exhibit 2: ...given a robust long-term visibility of water utility investments that could support at least a $7bn opportunity for WTRG at current market share, well above its total current water asset base...
US water investment needs, potential opportunity for WTRG/AWK



Source: Company data, Goldman Sachs Global Investment Research, EPA

Exhibit 3: ...along with aging gas infrastructure replacement that supports de-carbonization
Potential emission reductions from aging gas pipe replacement



Old pipe replacement refers to bare steel and cast iron pipes

Source: Goldman Sachs Global Investment Research, Company data

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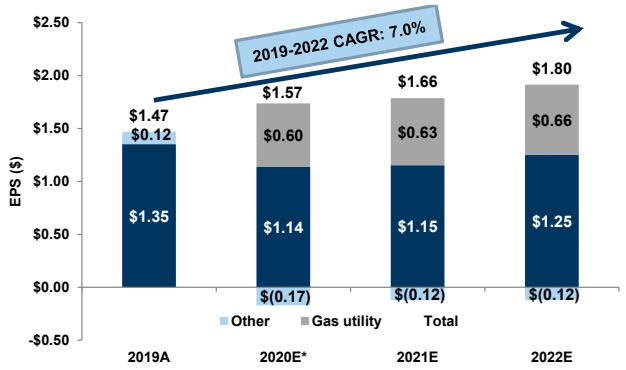
Exhibit 4: We raise our 2020 EPS estimate to reflect better YTD demand, while 2021/2022 estimates remain unchanged...
GSe vs Consensus

	EPS Estimates			% Difference	
	New	Old	Consensus	vs Old	vs Consensus
2019A	$1.47	$1.47	$1.47	0%	0%
2020E	$1.57	$1.55	$1.56	1%	1%
2021E	$1.66	$1.66	$1.66	0%	0%
2022E	$1.80	$1.80	$1.79	0%	0%

Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 5: ...reflecting a robust 7% EPS CAGR through 2022
EPS 2019A-2022E



Source: Goldman Sachs Global Investment Research, Company data

Exhibit 6: Our SOTP-based $51 price target reflects a 23% total return potential versus 10% for Regulated Utilities
WTRG SOTP Valuation

VALUATION	
Water utility EPS 2021	**1.15**
Water utility multiple	30.00x
Assumed premium	5.00x
Adjusted P/E	35.0x
Water utility valuation	**40.36**
Gas utility EPS 2021	**0.63**
Gas utility multiple	20.00x
Assumed premium	2.00x
Adjusted P/E	22.0x
Gas utility valuation	**13.95**
Valuation - Other	**(0.12)**
2020 Blended multiple	30.39x
Other valuation	**(3.73)**
Total valuation	**51.00**
Current price per share	$42.33
Return potential	**20.48%**
Dividend yield	2.21%
Total return potential	**23%**

Share Price as of 11/3/2020 Close

Source: Goldman Sachs Global Investment Research

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WTRG	12m Price Target: **$51.00**	Price: **$41.19**	Upside: **23.8%**

Buy CL

Market cap: $10.5bn
Enterprise value: $16.0bn
3m ADTV: $52.1mn
United States
Americas Utilities
M&A Rank: 3
Americas Conviction List

GS Forecast

	12/19	12/20E	12/21E	12/22E
Revenue ($ mn) New	**889.7**	**1,573.0**	**1,997.2**	**2,114.9**
Revenue ($ mn) Old	889.7	1,571.7	1,995.4	2,113.5
EBITDA ($ mn)	521.4	769.5	1,049.3	1,123.6
EBIT ($ mn)	360.8	514.7	757.0	801.7
EPS ($) New	**1.47**	**1.57**	**1.66**	**1.80**
EPS ($) Old	1.47	1.55	1.66	1.80
P/E (X)	27.6	26.3	24.7	22.9
Dividend yield (%)	2.2	2.4	2.5	2.7
Net debt/EBITDA (X)	2.3	7.2	6.0	6.1

	6/20	9/20E	12/20E	3/21E
EPS ($)	0.29	0.23	0.45	0.69

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 4 Nov 2020 close.

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Reg AC

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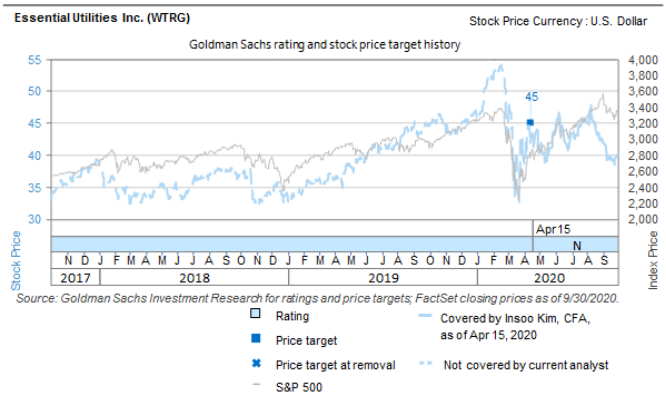

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HSBC Global Research

28 May 2020

Essential Utilities (WTRG US)

Buy: Current challenges a catalyst for integration

Equities
Water Utilities

United States

- Challenges in US water – how Essential is responding
- Guidance intact; bond proxy status unaltered
- Maintain Buy rating and USD50 target price

Growth strategy: Essential Utilities has a 3-pronged growth strategy: A growing core water and wastewater business; opportunistic pursuit of large, regulated utility/infrastructure targets – the company delivered on this with the Peoples gas acquisition (recently completed) and the DELCORA waste water transaction, which is expected to complete regulatory approvals by 2022; and MBAs (Market Based Activities), which are probably going to be less of a priority given the current challenges.

COVID-19 challenges: We analyse the risks to Essential from COVID-19 – many of these are mitigated by its large residential customer base. During its Q1 earnings call, management explained that the Peoples acquisition had been completed on the day that the US went into COVID-19 lockdown. This was a catalyst for harmonising business practices across the two separate businesses, so corporate integration might be quicker than otherwise expected. Its 2020 guidance remains: 2020 EPS of USD1.53 to USD1.58, and 2019-22e earnings CAGR of 5% to 7%.

Bond proxy: Essential's share price has outperformed the S&P 500 by 1% since 1 January 2019. It is trading at a discount to its water peer group's 2020e PE, but in line with some of the US electricity utilities, according to Refinitiv Datastream. This reflects, in our view, its multi-utility status. The US Treasury 10-year yield has fallen sharply. WTRG, as a defensive utility, should be inversely correlated to bond yields.

Maintain Buy rating and target price of USD50: We value Essential Utilities via three methodologies: DCF, dividend yield, and the average of PE multiple and rate-based valuations: We now adopt a lower 2.5% risk-free rate (from 3.0%) set by our equity strategists and used for the other US utilities under our coverage. We maintain our equity risk premium and beta assumptions of 3% and 0.60, respectively. Our DCF valuation increases to USD50.0 (from USD41.1). In our PE multiple-based valuation, we maintain our target multiple in line with market peers, at 30.0x. We use an unchanged water peer group P/B of 2.4x as a proxy for a rate-base valuation. This is consistent with the US utilities under our coverage and a proxy for EV. The average of our PE and rate-based valuations adjusts to USD51.6 (from USD51.9). For our Yield-based valuation, we increase our target yield to 2.13% from 1.75%, in line with Water and Related Utilities peers. This results in a lower Yield-based valuation of USD47.5 (from USD57.8). Overall, these valuations lead to an unchanged TP of USD50.00, which implies 21.0% upside. Consequently, we maintain our Buy rating.

MAINTAIN BUY

TARGET PRICE (USD)	PREVIOUS TARGET (USD)
50.00	**50.00**
SHARE PRICE (USD)	UPSIDE/DOWNSIDE
41.31	**+21.0%**
(as of 26 May 2020)	

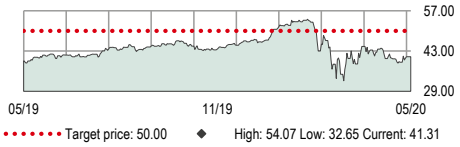
MARKET DATA

Market cap (USDm)	10,123	Free float	100%
Market cap (USDm)	10,123	BBG	WTRG US
3m ADTV (USDm)	59	RIC	WTRG.N

FINANCIALS AND RATIOS (USD)

Year to	12/2019a	12/2020e	12/2021e	12/2022e
HSBC EPS	1.04	1.55	1.67	1.79
HSBC EPS (prev)	1.04	1.56	1.68	1.81
Change (%)	0.0	-0.9	-0.2	-1.2
Consensus EPS	1.48	1.48	1.66	1.80
PE (x)	39.7	26.7	24.7	23.1
Dividend yield (%)	2.3	2.5	2.6	2.9
EV/EBITDA (x)	22.8	17.8	16.5	15.7
ROE (%)	7.6	8.3	7.5	7.6

52-WEEK PRICE (USD)



Source: Refinitiv IBES, HSBC estimates

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Financials & valuation: Essential Utilities

Buy

Financial statements

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Profit & loss summary (USDm)				
Revenue	890	1,884	2,144	2,278
EBITDA	497	817	913	993
Depreciation & amortisation	-157	-239	-267	-292
Operating profit/EBIT	340	578	646	701
Net interest	-131	-150	-170	-192
PBT	212	428	476	509
HSBC PBT	209	428	476	509
Taxation	13	-34	-38	-41
Net profit	225	394	438	469
HSBC net profit	225	394	438	469
Cash flow summary (USDm)				
Cash flow from operations	339	702	723	770
Capex	-550	-950	-1,000	-1,000
Cash flow from investment	-605	-5,225	-1,277	-1,000
Dividends	-189	-257	-286	-309
Change in net debt	-1,352	3,191	540	539
FCF equity	-212	-248	-277	-230
Balance sheet summary (USDm)				
Intangible fixed assets	64	939	939	939
Tangible fixed assets	7,224	11,335	12,345	13,053
Current assets	2,011	2,152	2,189	2,208
Cash & others	1,869	1,869	1,869	1,869
Total assets	9,360	14,488	15,534	16,261
Operating liabilities	1,468	1,678	1,733	1,761
Gross debt	3,077	6,269	6,809	7,347
Net debt	1,208	4,400	4,940	5,478
Shareholders' funds	3,881	5,606	6,058	6,218
Invested capital	5,962	10,879	11,871	12,569

Ratio, growth and per share analysis

Year to	12/2019a	12/2020e	12/2021e	12/2022e
Y-o-y % change				
Revenue	6.2	111.8	13.8	6.3
EBITDA	5.7	64.4	11.8	8.8
Operating profit	5.3	69.9	11.8	8.4
PBT	18.6	102.4	11.2	7.0
HSBC EPS	-3.4	48.9	8.1	7.0
Ratios (%)				
Revenue/IC (x)	0.2	0.2	0.2	0.2
ROIC	6.4	6.3	5.2	5.3
ROE	7.6	8.3	7.5	7.6
ROA	4.1	4.5	4.0	4.1
EBITDA margin	55.9	43.4	42.6	43.6
Operating profit margin	38.2	30.7	30.2	30.8
EBITDA/net interest (x)	3.8	5.4	5.4	5.2
Net debt/equity	31.1	78.5	81.5	88.1
Net debt/EBITDA (x)	2.4	5.4	5.4	5.5
CF from operations/net debt	28.0	16.0	14.6	14.1
Per share data (USD)				
EPS Rep (diluted)	1.04	1.55	1.67	1.79
HSBC EPS (diluted)	1.04	1.55	1.67	1.79
DPS	0.94	1.01	1.09	1.18
Book value	17.97	22.04	23.15	23.76

Valuation data

Year to	12/2019a	12/2020e	12/2021e	12/2022e
EV/sales	12.7	7.7	7.0	6.8
EV/EBITDA	22.8	17.8	16.5	15.7
EV/IC	1.9	1.3	1.3	1.2
PE*	39.7	26.7	24.7	23.1
PB	2.3	1.9	1.8	1.7
FCF yield (%)	-2.1	-2.5	-2.7	-2.3
Dividend yield (%)	2.3	2.5	2.6	2.9

* Based on HSBC EPS (diluted)

ESG metrics

Environmental Indicators	12/2019a
GHG emission intensity*	n/a
Energy intensity*	n/a
CO_2 reduction policy	Yes
Social Indicators	**12/2019a**
Employee costs as % of revenues	n/a
Employee turnover (%)	n/a
Diversity policy	Yes

Governance Indicators	12/2019a
No. of board members	8
Average board tenure (years)	7.0
Female board members (%)	25
Board members independence (%)	87.5

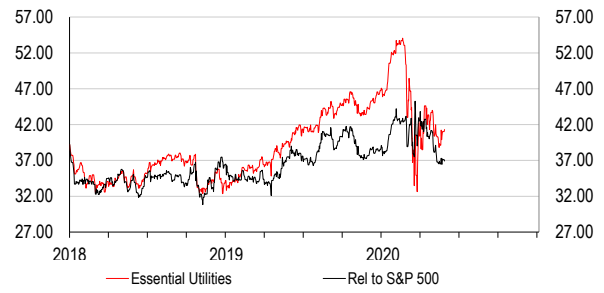
Source: Company data, HSBC

* GHG intensity and energy intensity are measured in kg and kWh respectively against revenue in USD '000s

Issuer information

Share price (USD)	41.31	Free float	100%
Target price (USD)	50.00	Sector	Water Utilities
RIC (Equity)	WTRG.N	Country/Region	United States
Bloomberg (Equity)	WTRG US	Analyst	Verity Mitchell
Market cap (USDm)	10,123	Contact	+44 20 7991 6840

Price relative



Source: HSBC

Note: Priced at close of 26 May 2020

Current challenges a catalyst for integration

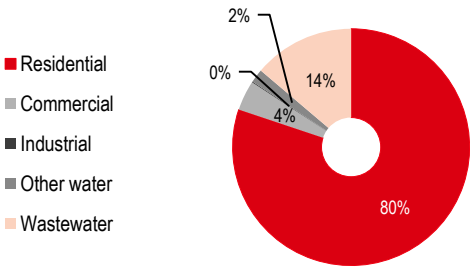
- Challenges in US water – how Essential is responding
- Guidance intact; bond proxy status unaltered
- Maintain Buy rating and USD50 target price

Investment summary: Three-pronged approach

Essential Utilities has core competencies in infrastructure investment (pipes and water production plant), regulatory affairs, and operations. Using these as pillars, Essential has created a 3- pronged growth strategy:

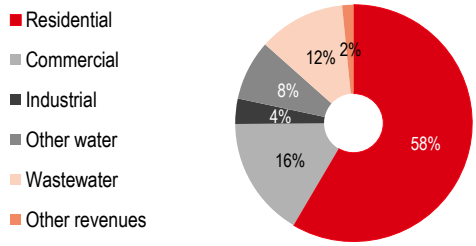
1. Municipal initiative: A growing core water and wastewater business - Aqua. This remains the primary focus for the company;
2. Strategic M&A: Opportunistic pursuit of large, regulated utility/infrastructure targets – the company delivered on this with the Peoples gas acquisition (recently completed) and the DELCORA waste water transaction, which is expected to complete regulatory approvals by 2022.
3. MBAs (Market Based Activities): Complementary to the regulated businesses. Capitalises on broader infrastructure renewals, but are probably going to be less of a priority given the current challenges.

Customer composition at FY2019



Source: Essential Utilities - company presentation data

Revenue composition at FY2019



Source: Essential Utilities - company presentation data

Quick integration

During its Q1 earnings call, management explained that the Peoples acquisition had been completed on the day that the US went into COVID-19 lockdown. This was a catalyst for harmonising business practices across the two separate businesses in order to protect staff, and continue to deliver essential services. This has meant that corporate integration might be quicker than otherwise expected for the two companies.

COVID-19 pandemic related risks for US water and gas utilities

Essential Utilities is a stable company with regulated revenue base. However, it is not completely immune to the impending economic downturn. We highlight some of these risks as follows, how material they are, and discuss how the company is addressing and mitigating them.

- **Customer delinquencies:** Water and gas utilities are expected to experience an increase in customers being delinquent in paying their water bills. However, water utilities will have to continue to provide water to these delinquent customers rather than enact shut-offs. Hence, companies will incur additional costs.
- **Revenue shortfall:** US utilities are likely to experience some revenue shortfall due to declines in commercial, industrial, and institutional water consumption. This revenue shortfall may be offset by an increase in residential user charge revenue due to “stay-at-home” orders. Essential receives only 20% of its revenues from commercial and industrial customers. In April, according to management on the Q1 call, the company saw increased domestic demand from the shutdown offsetting much of the commercial and industrial volume reductions. The same principle applied in the Peoples business.
- **Reduced system development charges:** The COVID-19 crisis may slow the growth in new development and housing starts, which will impact the financial losses of water and gas utilities. A slowing of new customer growth would reduce new system development. Essential however, given its scale, still has growth from infrastructure rehabilitation for its existing customer rate base.
- **Increased personnel expenses:** There may well be some potential for additional costs associated with the pandemic such as for PPE. The company said during the Q1 that these expenses are relatively immaterial.
- **Delayed and reduced capital expenditures:** At Q1, management said only cUSD30m of project work had been delayed compared with its cUSD1bn of capital expenditure run rate.
- **Deferred water and gas rate increases:** Utilities may also experience future revenue losses as a result of deferrals of planned rate increases. These deferrals may exacerbate community economic impacts by further reducing utility capital spending and put the utility sector further behind in addressing its capital infrastructure needs. Essential has pending rate cases in Indiana, New Jersey, North Carolina, and Ohio, with total annualised revenue increase of USD10.1m. Rate cases appear to be proceeding on track and there is no indication of deferrals as yet. Given the rate cases proposed are relatively modest we do not see this as a risk.

Q1 2020 summary

Essential Utilities hosted a conference call for Q1 2020 earnings on 7 May 2020.

- Essential invested USD118.7m in the first three months. This does not include an additional USD53.5m that was invested by Peoples.
- It closed its acquisition of the water system of Campbell, Ohio; a utility with approximately 3,100 customer connections. For the quarter, customer growth for the company's water utilities totalled 0.6%, including organic growth.
- As a preventive measure to address liquidity concerns related to COVID-19 and its potential economic and capital markets impacts, the company secured and borrowed an additional USD500m on a 364-day term loan in early April 2020.

Outlook: FY2020 outlook reiterated

Essential reiterated its FY2020 outlook as follows:

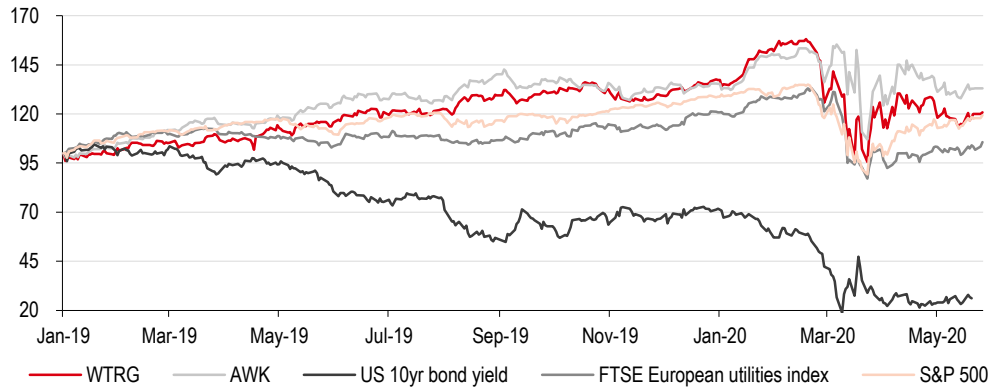
- Essential has signed purchase agreements for other municipal water and wastewater acquisitions that are expected to add the equivalent of over 205,000 water and wastewater retail customers, and approximately USD327m in expected rate base.
- Adjusted income per diluted common share (non-GAAP) of USD1.53 to USD1.58
- 2019-22e earnings CAGR of 5 to 7%
- Regulated water segment infrastructure investments of cUSD550m in 2020
- Regulated natural gas segment infrastructure investments of cUSD400m in 2020 on a full-year basis (adjusted to include capital invested in 2020 prior to Essential's ownership)
- Infrastructure investments of approximately USD2.8bn through 2022 in existing operations to rehabilitate and strengthen water, wastewater, and natural gas systems (including regulated natural gas segment capital invested in 2020 prior to Essential's ownership)
- 2019-22e regulated water segment rate base CAGR of 6% to 7%
- 2019-22e regulated natural gas segment rate base CAGR of 8 to 10%
- Total annual regulated water segment customer growth of between 2% and 3% on average depending upon regulatory approval
- Gas customer count expected to be relatively stable for 2020.

Performance against peers

Essential's share price has outperformed the S&P 500 by 2% since 1 January 2019. It is trading at a discount to its water peer group's 2020e PE, but in line with some of the US electricity utilities according to Refinitiv Datastream. This reflects, in our view, its multi-utility status.

The US Treasury 10-year yield has fallen sharply. WTRG, as a defensive utility, should be inversely correlated to bond yields.

WTRG vs AWK vs UST 10yr bond yield vs FTSE European utilities index vs S&P500



Source: Refinitiv Datastream

Credit metrics analysis

According to Moody's, WTRG needs to maintain its RCF/ net debt ratio in the range of 7%-14% and FFO/ net debt in the range of 11%-18% to maintain its Baa2 credit rating.

During the Q1 2020 conference call, Essential said that as the equity markets recover, the company will look for the appropriate time to issue approximately USD300m of equity in later 2020 or early 2021. That equity, as first mentioned on the Investor Day, is necessary to appropriately capitalise DELCORA and other acquisitions in the pipeline.

We have modelled for this equity issuance as well as completion of this acquisition in 2021. Given the increased equity, the company's credit metrics appear to remain in the target metric range for the current credit rating.

Credit metrics analysis

	2020e	2021e	2022e
RCF/ net debt	8.6%	8.5%	8.3%
FFO/ net debt	14.5%	14.3%	14.0%

Source: HSBC estimates

Change in estimates

We have updated our estimates post the Q1 2020 results posted on 7 May 2020. We have also updated our model for USD300m of equity offering, which has increased our number of shares outstanding and lowered our net debt assumptions for 2021e.

We continue to use pro-forma 2020 assumptions to smooth the effect of the costs and timing of the Peoples deal, excluding transaction costs and assuming the deal was completed to benefit from the gas heating season on a normalised weather basis. This is the basis on which Essential will report its underlying results.

Changes in estimates (USDm)

	2020e	2021e	2022e
EBIT			
Revised	578	646	701
Previous	585	631	689
Change	*-1%*	*2%*	*2%*
Net income			
Revised	394	438	469
Previous	397	426	461
Change	*-1%*	*3%*	*2%*
EPS (USD)			
Revised	1.55	1.67	1.79
Previous	1.56	1.68	1.81
Change	*-1%*	*0%*	*-1%*
DPS (USD)			
Revised	1.01	1.09	1.18
Previous	1.01	1.09	1.18
Change	*0%*	*0%*	*0%*

Source: HSBC estimates

Valuation and risks

We value Essential Utilities via three methodologies: DCF, dividend yield, and the average of PE multiple and rate-based valuations. Taking the average of the three approaches gives us our target price of USD50.00 (unchanged).

- Previously we had used a 3% risk-free rate, in line with the utility methodology set out in our report *European Utilities: The three Rs: Renewables, low rates and low risk* (20 February 2020). We now adopt the lower HSBC 2.5% set by our equity strategists (see *Cost of Equity*, 10 February 2020) and used for other US utilities under our coverage. Our equity risk premium and beta assumptions remain unchanged at 3% and 0.60, respectively. Our DCF valuation increases to USD50.0 (from USD41.1).
- In our PE multiple-based valuation, we maintain our target multiple in line with market peers, at 30.0x. We use a water peer group P/B of 2.4x (unchanged) as a proxy for a rate-based valuation. This is consistent with all US utilities under our coverage and is a proxy for EV. The average of the two declines to USD51.6 (from USD51.9), reflecting our updated estimates.
- For our Yield-based valuation, we increase our target yield to 2.13% from 1.75%, in line with its Water and Related Utilities peers. This results in a decreased Yield valuation of USD47.5 (from USD57.8).

Overall, these changes lead to an unchanged TP of USD50.00, which implies 21.0% upside; we reiterate our Buy rating as we believe the combination of regulated investment and earnings growth is attractive.

Summary of valuation (USD)

Particulars	New	Previous
Current price as on 26-May-20	**41.3**	**NA**
DCF (updated estimates lower risk-free rate	50.0	41.1
Yield 2.13% from 1.75% (sector average)	47.5	57.8
PE and rate-based (updated estimates)	51.6	51.9
Target price (average rounded)	**50.0**	**50.0**
Upside/ downside to target price	21.0%	NA
Rating	**Buy**	**Buy**

Source: HSBC estimates

WACC inputs and DCF valuation

WACC inputs		Equity Valuation	USDm
Cost of debt		**+ DCF value**	**16,221**
Pre-tax cost of debt	8.5%	+ ST marketable assets	0
Marginal tax rate	8.0%	+ Value of associates	0
Cost of equity		+ Other assets	878
Risk-free rate (previously 3%)	2.5%	**EV (asset side)**	**17,100**
Equity risk premium	3.0%	- Net debt (+ if Net cash)	(4,371)
Additional risk		- Quasi debt (pension)	0
Beta (unchanged)	**0.60**	- Value of minorities	0
Debt - 39%	7.8%	Total non-equity claims	(4,371)
Equity - 61%	4.8%	Value of equity	12,729
Cost of capital	**5.9%**	**Value per share (USD)**	**50.0**

Source: HSBC estimates

Multiples and rate base (EV) valuation

	2020e rate base
Regulated water	
Pennsylvania	3,682
Ohio	368
Illinois	382
Texas	319
New Jersey	214
North Carolina	245
Indiana	90
Virginia	83
Regulated gas	**2,451**
Total rate base	7,834
Rate-based valuation assuming 2.4x multiple, in line with sector average P/B	**18,802**
Non-regulated 2020 PE multiple	9
Net debt 2020e, pensions & Minority	(4,371)
Estimated equity value	14,440
Estimated equity value per share (USD)	**56.8**
PE Multiple valuation	
2020 earnings	1.55
2020 PE sector average	30.0
Value per share	**46.4**
Average of rate base valuation and PE multiple valuation	**51.6**

Source: HSBC estimates

Downside risks include:

Essential Utilities failing to achieve the desired rate case revisions and infrastructure surcharges; lacking organic growth from asset replacement; inability to take advantage of the Fair Market Value legislation opportunity; dividend growth at a lower rate than we assume; inability to gain the Fair Market Value premium required in the systems it wants to acquire in Pennsylvania. Its current acquisitions of systems – New Garden and Limerick – are facing challenges to the premium proposed by Aqua.

Disclosure appendix

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From 23rd March 2015 HSBC has assigned ratings on the following basis:

The target price is based on the analyst's assessment of the stock's actual current value, although we expect it to take six to 12 months for the market price to reflect this. When the target price is more than 20% above the current share price, the stock will be classified as a Buy; when it is between 5% and 20% above the current share price, the stock may be classified as a Buy or a Hold; when it is between 5% below and 5% above the current share price, the stock will be classified as a Hold; when it is between 5% and 20% below the current share price, the stock may be classified as a Hold or a Reduce; and when it is more than 20% below the current share price, the stock will be classified as a Reduce.

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Upside/Downside is the percentage difference between the target price and the share price.

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For each stock we set a required rate of return calculated from the cost of equity for that stock's domestic or, as appropriate, regional market established by our strategy team. The target price for a stock represented the value the analyst expected the stock to reach over our performance horizon. The performance horizon was 12 months. For a stock to be classified as Overweight, the potential return, which equals the percentage difference between the current share price and the target price, including the forecast dividend yield when indicated, had to exceed the required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). For a stock to be classified as Underweight, the stock was expected to underperform its required return by at least 5 percentage points over the succeeding 12 months (or 10 percentage points for a stock classified as Volatile*). Stocks between these bands were classified as Neutral.

*A stock was classified as volatile if its historical volatility had exceeded 40%, if the stock had been listed for less than 12 months (unless it was in an industry or sector where volatility is low) or if the analyst expected significant volatility. However, stocks which we did not consider volatile may in fact also have behaved in such a way. Historical volatility was defined as the past month's average of the daily 365-day moving average volatilities. In order to avoid misleadingly frequent changes in rating, however, volatility had to move 2.5 percentage points past the 40% benchmark in either direction for a stock's status to change.

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As of 27 May 2020, the distribution of all independent ratings published by HSBC is as follows:

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Hold	37%	(31% of these provided with Investment Banking Services)
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For the purposes of the distribution above the following mapping structure is used during the transition from the previous to current rating models: under our previous model, Overweight = Buy, Neutral = Hold and Underweight = Sell; under our current model Buy = Buy, Hold = Hold and Reduce = Sell. For rating definitions under both models, please see "Stock ratings and basis for financial analysis" above.

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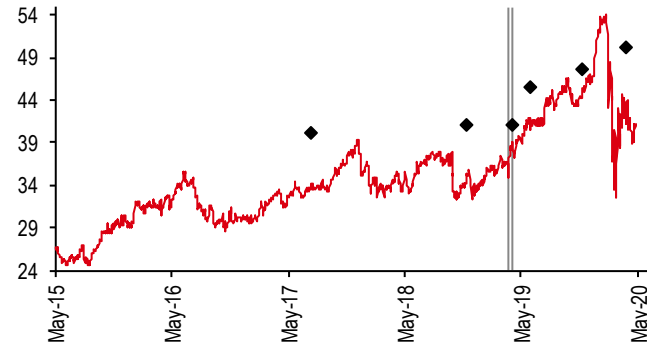
Share price and rating changes for long-term investment opportunities

Essential Utilities (WTRG.N) share price performance USD Vs HSBC rating history



Source: HSBC

Rating & target price history

From	To	Date	Analyst
Buy	Restricted	15 Apr 2019	
Restricted	Buy	30 Apr 2019	Verity Mitchell
Target price	**Value**	**Date**	**Analyst**
Price 1	40.00	08 Aug 2017	Verity Mitchell
Price 2	41.00	06 Dec 2018	Verity Mitchell
Price 3	Restricted	15 Apr 2019	
Price 4	41.00	30 Apr 2019	Verity Mitchell
Price 5	45.50	28 Jun 2019	Verity Mitchell
Price 6	47.50	06 Dec 2019	Verity Mitchell
Price 7	50.00	22 Apr 2020	Verity Mitchell

Source: HSBC

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Company	Ticker	Recent price	Price date	Disclosure
ESSENTIAL UTILITIES	WTRG.N	41.31	26 May 2020	5, 6

Source: HSBC

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[1148009]

First Read

Essential Utilities Inc

Q1'20 EPS $0.60 vs. Consensus $0.60

What happened?

Essential Utilities reported adjusted normalized operating earnings for Q1'20 of $0.60/share. This compares reasonably well with both consensus and UBS estimates of $0.60 and $0.62, respectively. The adjusted and normalized nature of the earnings reflect the closure of the Peoples Gas acquisition on March 16, resulting in 15 days of actual earnings from that subsidiary, and 75 days of estimated assumed normalized earnings. GAAP earnings for the quarter were $0.20. Full year 2020 guidance, which is premised on the same estimated adjusted normalized basis, was affirmed at $1.53-$1.58, as was the long term earnings growth target of 5-7%.

Regulatory & Acquisition Update:

In conjunction with its earnings release, WTRG updated investors on both its ongoing regulatory calendar and water segment acquisitions. With regard to regulatory activities, the company has completed rate case and surcharge proceedings in IL/VA/OH/NC (representing $5.2mm of annualized revenue increases) and has pending cases in IN/NJ/NC/OH (representing $10.1mm of potential annualized increases). The repairs tax benefit in the quarter totalled $5.9mm, the company will be filing for treatment of the 'catch-up' portion over the summer, this 'catch-up' component is not included in current guidance. Year-to-date, WTRG has closed one acquisition (Campbell – rate base $7.5mm) and three acquisitions are pending (New Garden – rate base $29mm/East Norriton – rate base $21mm/DELCORA – rate base $276mm). Management indicated that they continue to see additional, larger, acquisition opportunities.

Operational Update:

Despite a slight pause on some construction projects (PA) management believe they are on track to achieve their capital spending plan for the year of $1.1 billion (water $550mm/gas $400mm). WTRG continues to see potential capital spending opportunities totalling $2.8 billion through 2022.

Valuation:

The unique nature of 2020 guidance and reporting format make interpretation difficult, however, investors should take comfort in the operating performance of the company.

Equities

Americas
Water Utilities

12-month rating	**Neutral**
12m price target	**US$43.00**
Price (06 May 2020)	**US$40.67**

RIC: WTRG.N **BBG:** WTRG US

Trading data and key metrics

52-wk range	US$54.07-32.65
Market cap.	US$7.26bn
Shares o/s	178m (COM)
Free float	100%
Avg. daily volume ('000)	455
Avg. daily value (m)	US$19.7
Common s/h equity (12/20E)	US$2.25bn
P/BV (12/20E)	3.2x
Net debt / EBITDA (12/20E)	5.1x

EPS (UBS, diluted) (US$)

	12/20E	
	UBS	Cons.
Q1E	0.62	0.60
Q2E	0.35	0.20
Q3E	0.47	0.27
Q4E	0.13	0.52
12/20E	1.58	1.51
12/21E	1.68	1.65
12/22E	1.79	1.78

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Highlights (US$m)	12/17	12/18	12/19	12/20E	12/21E	12/22E	12/23E	12/24E
Revenues	810	838	881	921	956	995	1,033	1,072
EBIT (UBS)	329	337	370	399	425	454	482	512
Net earnings (UBS)	240	251	265	281	299	319	342	365
EPS (UBS, diluted) (US$)	1.35	1.41	1.48	1.58	1.68	1.79	1.92	2.05
DPS (US$)	0.79	0.88	0.94	1.00	1.07	1.15	1.23	1.32
Net (debt) / cash	(2,121)	(2,376)	(2,676)	(2,840)	(2,994)	(3,135)	(3,263)	(3,378)

Profitability/valuation	12/17	12/18	12/19	12/20E	12/21E	12/22E	12/23E	12/24E
EBIT margin %	40.6	40.3	42.0	43.3	44.5	45.6	46.7	47.7
ROIC (EBIT) %	8.4	7.9	8.0	8.0	8.1	8.3	8.4	8.6
EV/EBITDA (core) x	17.0	17.6	18.7	18.0	17.3	16.6	15.7	15.3
P/E (UBS, diluted) x	24.8	25.0	27.3	25.8	24.3	22.7	21.2	19.9
Equity FCF (UBS) yield %	(1.6)	(1.6)	(1.8)	0.2	0.5	0.9	1.3	1.7
Net dividend yield %	2.4	2.5	2.3	2.5	2.6	2.8	3.0	3.2

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US$40.67 on 06 May 2020 19:34 EDT

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Forecast returns

Forecast price appreciation	+5.7%
Forecast dividend yield	2.5%
Forecast stock return	+8.2%
Market return assumption	5.2%
Forecast excess return	+3.0%

Valuation Method and Risk Statement

Risks include, but are not limited to: rising interest rate; regulatory and policy risks; operational risks; construction risks; water quality, safety and contamination risk; physical risk to the water sources, treatment or delivery systems; cybersecurity risk; drought and extreme weather events.
Our price target is premised upon a 3% discount to the 2021 average UBS water P/E multiple. The discount reflects the sum of: a 5% discount to reflect Water group over-valuation relative to the S&P 500, 5% premium to reflect high quality regulatory jurisdiction ranking, 6% premium to reflect operations in six Fair Market Value states, and 9% discount to reflect impact of lower P/E associated with gas earnings.

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12-Month Rating	Definition	Coverage[1]	IB Services[2]
Buy	FSR is > 6% above the MRA.	48%	32%
Neutral	FSR is between -6% and 6% of the MRA.	40%	28%
Sell	FSR is > 6% below the MRA.	13%	20%
Short-Term Rating	**Definition**	**Coverage[3]**	**IB Services[4]**
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 31 March 2020.
1:Percentage of companies under coverage globally within the 12-month rating category.
2:Percentage of companies within the 12-month rating category for which investment banking (IB) services were provided within the past 12 months.
3:Percentage of companies under coverage globally within the Short-Term rating category.
4:Percentage of companies within the Short-Term rating category for which investment banking (IB) services were provided within the past 12 months.

KEY DEFINITIONS:Forecast Stock Return (FSR) is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months. In some cases, this yield may be based on accrued dividends. **Market Return Assumption (MRA)** is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium). **Under Review (UR)** Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation. **Short-Term Ratings** reflect the expected near-term (up to three months) performance of the stock and do not reflect any change in the fundamental view or investment case. **Equity Price Targets** have an investment horizon of 12 months.

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UBS Securities LLC: Daniel Ford, CFA; Paul Cole.

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Company Name	Reuters	12-month rating	Short-term rating	Price	Price date
Essential Utilities Inc[16]	WTRG.N	Neutral	N/A	US$40.67	06 May 2020

Source: UBS. All prices as of local market close.
Ratings in this table are the most current published ratings prior to this report. They may be more recent than the stock pricing date
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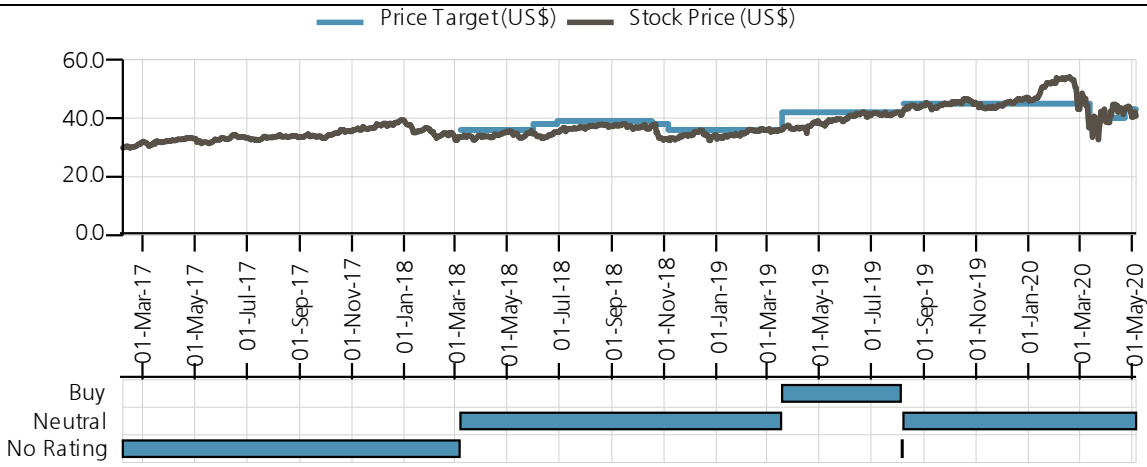
Essential Utilities Inc (US$)



Date	Stock Price (US$)	Price Target (US$)	Rating
2017-02-06	29.86	-	No Rating
2018-03-08	33.52	36.0	Neutral
2018-06-01	34.71	38.0	Neutral
2018-06-29	35.18	39.0	Neutral
2018-10-18	37.23	38.0	Neutral
2018-11-06	32.59	36.0	Neutral
2019-03-19	36.12	42.0	Buy
2019-08-06	41.15	-	No Rating
2019-08-08	42.47	45.0	Neutral
2020-03-13	38.43	40.0	Neutral
2020-04-23	42.62	43.0	Neutral

Source: UBS; as of 06 May 2020

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WELLS FARGO SECURITIES

Essential Utilities, Inc.

WTRG: M&A In Focus – Close Pending Wastewater Deals w/ New Ones Imminent

Overweight/$47

Water Utilities

Price Target Change

- **Key Points.** WTRG reported solid Q3'20 results aided by higher residential water usage due to favorable weather and COVID has FY2020 EPS trending towards top end of the $1.53-1.58 guidance range. In addition, management indicated roughly $70M of additional tuck-in deals were expected to be announced by YE2020. For our part, we increase our 20E EPS accordingly to $1.58 from $1.56 and bump up our '22 & beyond M&A placeholder to $75M/year of deals rather than $60M given the continued positive momentum on that front. Our 2021-24E EPS of $1.65, $1.78, $1.91 & $2.03 reflects a mid-'21 DELCORA close and results in a 6.6% CAGR off the '19 base of $1.47. If we were to strip out the DELCORA deal, it only has a modest $0.03-0.05 impact (less than 3%) on our '22 & beyond EPS. We reiterate our Overweight rating and increase our 12-18 month price target to $47/share (26.4X our 22E EPS) from $45.
- **Water/Wastewater M&A Update.** In addition to getting the $363M of pending deals closed (represents $0.07 of incremental EPS power), management indicated a handful of new deals are expected to be announced by YE'20 representing $70M of rate base and roughly 10,000 customers. Overall, WTRG is actively pursuing (i.e. having dialogue) municipal acquisition opportunities representing 360,000 customers, the majority of which are wastewater. Management expects the level of discussions/deals to be positively impacted by COVID as municipalities face additional financial and operational challenges and we remain optimistic that efforts could start to bear meaningful fruit in WTRG's states that have more recently adopted fair market value legislation (NC, OH, TX & VA) – we note that WTRG is the deepest-pocketed IOU in NC, OH & TX.
- ***DELCORA – The Latest.*** Much investor attention on the Q3 call was understandably on the pending $277M DELCORA wastewater deal that is potentially at risk due to a court challenge by Delaware County's County Council. Hearings were recently completed on the legality of the trust aspect DELCORA's plan and the more important hearings related to the enforceability of the asset purchase agreement (does WTRG have a valid deal?) are expected in the next few weeks. A ruling from the judge in the Court of Common Pleas of Delaware County is expected within 60 days of the hearing. That said, the judge continues to encourage parties to reach a settlement. ***While WTRG management was unable to confirm whether or not settlement discussions are taking place, the company remains confident in the ability to close the deal perhaps by late March or April.*** This is consistent with the PaPUC approval process were evidentiary hearings are scheduled next week and the statutory deadline for a decision is 3/26/21. ***(comments continue on p. 2.)***

$ EPS	2019A	2020E Curr.	2020E Prior	2021E Curr.	2021E Prior
Q1 (Mar.)	0.28	0.60 A	NC	NE	
Q2 (June)	0.37	0.29 A	NC	NE	
Q3 (Sep.)	0.48	**0.23 A**	**0.20**	NE	
Q4 (Dec.)	0.34	**0.46**	**0.47**	NE	
FY	1.47	**1.58**	**1.56**	1.65	NC
CY	1.47	1.58		1.65	
FY P/EPS	28.0x	26.1x		25.0x	
Rev.(MM)	890	1,931		2,052	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
V = Volatile
Adjusted EPS excludes items considered non-recurring.
WTR expects 2020 adjusted EPS at the top end of the $1.53-1.58 range and targets a 5-7% EPS CAGR through 2022 off the 2019 adjusted base of $1.47.

Ticker	WTRG
Price Target/Prior:	**$47/$45**
Price (11/04/2020)	**$41.19**
52-Week Range:	$30-55
Shares Outstanding: (MM)	245.2
Market Cap.: (MM)	$10,099.8
S&P 500:	3,443.44
Avg. Daily Vol.:	1,162,150
Dividend/Yield:	$1.00/2.4%
LT Debt: (MM)	$5,277.4
LT Debt/Total Cap.:	53.2%
ROE:	9.0%
3-5 Yr. Est. Growth Rate:	6.0%
CY 2020 Est. P/EPS-to-Growth:	4.4x
Last Reporting Date:	11/03/2020 After Close

NC = No Change
Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Together we'll go far

- ***DELCORA – The Latest (continued…).*** While the DELCORA deal is highly supportive of WTRG's growth aspirations and management continues to express confidence in the ability to close the transaction, we consider the future to be bright without it driven by elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends. We believe relatively low risk, regulated EPS growth of at least 6% is achievable – that rate of growth would simply be enhanced if DELCORA closes, particularly in the later part of our 5-year forecast and beyond, given the $700M of required investment needed in the system by 2028 as well as potential further municipal wastewater deals in the region.

- ***Lower Makefield Township.*** An agreement to acquire the 11,000 connection wastewater system in Bucks County, PA for $53M was announced on 9/24. The deal is subject to PaPUC approval – which we expect will be received – and therefore closure probably is not likely until Q4'21. We view the deal as highly supportive of our EPS outlook as it essentially fills in our full year '21 M&A placeholder of $60M.

Other Q3 Call Nuggets.

- **No Gas M&A** – Management made it clear that all M&A efforts are focused on the water/wastewater platform. No M&A expansion on the gas utility side is being contemplated. That said and despite gas utilities being largely out of favor with investors given anti-gas sentiment (existential threat?) in some parts of the country, management defended the Peoples deal and outlined the why the future is bright for the Western PA utility (and brighter than most other gas LDCs). We largely agree with management's arguments and our positive investment thesis and price target reflect it.

- **ESG** – Appealing to ESG investors/rating agencies is a priority. Management believes the company has made great strides in recent years with plans to further improve and therefore has a good story to tell. WTRG plans to establish credible, meaningful and attainable emissions reduction goals for Peoples within 6 months.

- **Peoples Repairs Tax** – No real updates on this front since WTRG filed in early August for PaPUC treatment of the catch up portion of the Peoples repairs tax deduction election. The filing outlined a $381M catch up deduction and proposed to share the benefits between customers (40%, via a 2% bill surcredit over 2021-24) and shareholders (60%, via an increasing income tax expense offset over 2023-25). If approved, a base rate increase would not be needed prior to 1/1/2026 while supporting the elevated pace of capex deployment.

  WTRG had communications with regulators and other key parties prior to making this filing which makes us hopeful that the proposal will be positively received and that a constructive outcome will ensue. The timing of a potential settlement could be before the evidentiary hearings in late January take place. Whether WTRG settles or the hearings occur and the proceeding is fully litigated, management believes a final decision is likely an early Q2'21 event.

  Approval of the shareholder benefit aspect of the request would increase our confidence in the gas utilities' ability to achieve our forecast – we assume gas utility earned ROEs of 10-10.3% which we believe is reasonable and consistent with Peoples 2019 rate order. On the flip side, if the PaPUC decides to go a different direction with the catchup benefits, we still believe our 2023 & beyond EPS levels are reasonable within the backdrop of the constructive PA regulatory framework. It could simply necessitate filing for a base rate increase sooner which would bring with it associated regulatory risk.

Acronyms:
DELCORA – Delaware Country Regional Water Quality Control Authority
ESG – Environmental, Social, Governance
FMV – Fair Market Value
IOU – Investor Owned Utility
LDC – Local Distribution Company
PaPUC – Pennsylvania Public Utility Commission

Price Target

Price Target: $47 from $45

Our $47/share price target reflects both a P/E multiple and DDM analysis. In terms of P/E, we apply a 70% water/30% gas utility hybrid multiple to our 2022E of $1.78. For WTRG's water utility multiple, we ascribe a 5-10% discount to the 21E multiple we use for AWK (31.5-32X, which is a 5-10% premium to the pure play water peer group median). We consider AWK to be WTRG's closest peer on the water side based on scale, key states/regions and municipal consolidation strategies. The 5-10% discount reflects a modestly lower earnings growth rate (we forecast 6-7% for WTRG's water business vs. 8% for AWK) as well as lower ESG appeal (primarily due to the Peoples gas utility). For WTRG's gas utility multiple, we utilize the 21E pure play gas LDC median of 18X (based on ATO, NWN, OGS & SR) and then apply a 5-10% premium to it. We believe a premium is warranted as (1) Peoples is at the early stages of a multi-year accelerated pipeline replacement effort which is expected to drive healthy rate base growth for the foreseeable future (WTRG's 3-year guidance is 8-10%), (2) we believe Western PA, which sits above the prolific Marcellus and Utica shale plays, is largely immune to the anti-gas sentiment impacting some areas of the country and (3) most of Peoples falls under the constructive PA regulatory framework. Key risks relate to regulatory, Peoples gas deal integration and M&A strategy execution.

Investment Thesis

Our Overweight rating is premised on our belief that WTRG shares do not fully reflect the company's strong fundamentals which include a proven EPS growth strategy, a rate base that is growing at a mid-to-upper single digit CAGR, constructive regulatory treatment (particularly in PA where roughly 70% of earnings are derived and near-term regulatory risk is low as both the water and gas utilities completed rate cases in 2019), an efficient operating model and a solid financial profile. We believe relatively low risk, regulated EPS growth of at least 6% is achievable driven by the timely rate recognition of elevated pipeline infrastructure investment needs for the foreseeable future supplemented by water/wastewater municipal M&A trends.

Company Description

Headquartered in Bryn Mawr, PA, Essential Utilities (WTRG) - formerly Aqua America - is one of the largest U.S.-based investor-owned regulated water and wastewater utilities. The company serves approximately 3 million residents (1 million customer connections) in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Indiana and Virginia. WTRG's largest subsidiary, Aqua Pennsylvania, accounts for approximately half of the company's total water customer base and nearly 70% of consolidated water rate base. Going forward, the company has expressed a desire to accelerate customer growth through a more active and focused acquisition strategy across its entire portfolio.

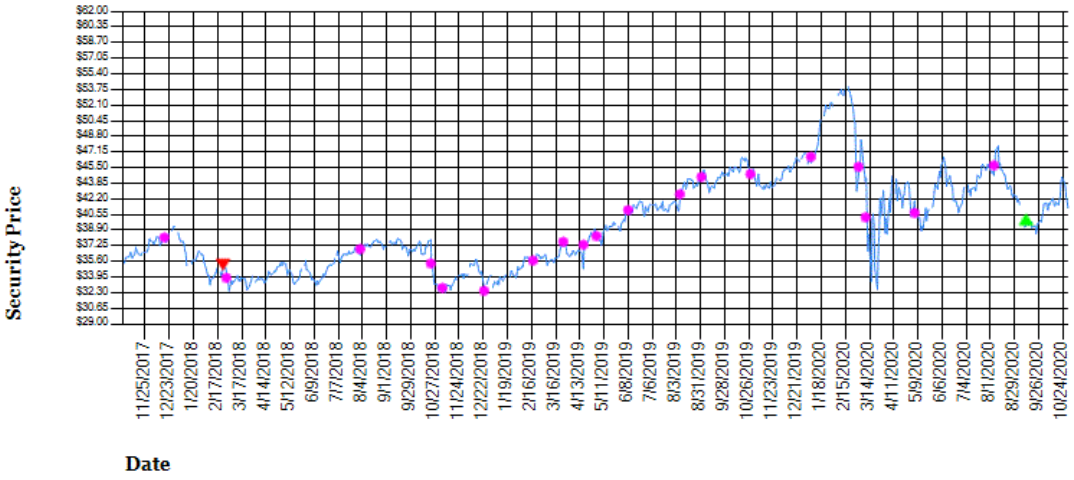
In March 2020, WTRG closed on the acquisition of Peoples - a predominately Pennsylvania-based gas utility serving 740k customers - from SteelRiver Infrastructure Partners for an enterprise value of $4.275B (includes $1.3B of assumed debt). From a price perspective, WTRG paid 1.9-2.0X rate base, 14.8X EV/EBITDA and nearly 25X P/E - lofty multiples but not that dissimilar to other gas utility transactions at the time. Management expects the deal to be EPS accretive in the first full year after close (2020) but stressed this is a strategic-driven, not synergy-driven, transaction.

Regulated operations account for more than 99% of consolidated revenues. Consolidated EPS is expected to be driven roughly 70% by water utility operations with the gas utility contributing the remaining 30%.

In February 2020, the new name Essential Utilities, Inc. and new ticker WTRG became effective. Prior, the company was known as Aqua America Inc. and traded under the ticker WTR.

Required Disclosures

Essential Utilities, Inc. (WTRG) 3-yr. Price Performance



	Date	Published Price ($)	Rating Code*	Price Target	Val. Rng. Low	Val. Rng. High	Close Price ($)
	10/30/2017		Reeder				
	10/30/2017	NA	1	40	NE	NE	35.42
●	12/18/2017	38.14	1	43	NE	NE	38.03
▼●	2/25/2018	35.00	2	37	NE	NE	35.00
●	3/1/2018	34.19	2	36	NE	NE	33.66
●	8/2/2018	36.70	2	38	NE	NE	36.70
●	10/24/2018	35.01	2	37	NE	NE	35.29
●	11/6/2018	32.70	2	35	NE	NE	32.59
●	12/24/2018	33.87	2	34	NE	NE	32.38
●	2/19/2019	35.54	2	36	NE	NE	35.52
●	3/26/2019	37.52	2	39	NE	NE	37.52
●	4/18/2019	36.52	2	38	NE	NE	37.15
●	5/3/2019	37.85	2	39	NE	NE	38.09
●	6/9/2019	40.84	2	42	NE	NE	40.84
●	8/8/2019	42.06	2	44	NE	NE	42.47
●	9/2/2019	44.29	2	47	NE	NE	44.29
●	10/29/2019	44.90	2	46	NE	NE	44.68
●	1/8/2020	46.51	2	48	NE	NE	46.51
●	3/2/2020	43.01	2	45	NE	NE	45.44
●	3/11/2020	44.41	2	48	NE	NE	40.03
●	5/7/2020	40.49	2	42	NE	NE	40.53
●	8/6/2020	45.56	2	45	NE	NE	45.56
▲	9/14/2020	39.35	1	45	NE	NE	39.82

*Effective December 7, 2019, Wells Fargo Securities' Equity Research modified its ratings definitions. Complete definitions of current ratings can be found below. For information related to prior ratings definitions, please contact equityresearch1@wellsfargo.com.

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

- ▼ Rating Downgrade
- ▲ Rating Upgrade
- ● Price Target/Val Range Change
- ◆ Initiation, Resumption, Drop or Suspend
- ■ Analyst Change
- ❒ Split Adjustment

Rating Code Key

1	Overweight/Buy	SR	Suspended
2	Equal Weight/Hold	NR	Not Rated
3	Underweight/Sell	NE	No Estimate

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2=Equal Weight: Total return on stock expected to be 0-10% over the next 12 months. HOLD
3=Underweight: Total return on stock expected to lag the Overweight- and Equal Weight-rated stocks within the analyst's coverage universe over the next 12 months. SELL

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Essential Utilities Inc WTRG (NYSE) | ★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Capital Allocation	Industry Group	ESG Risk Rating Assessment[1]
48.86 USD	39.00 USD	Low	Narrow	Stable	Standard	Utilities - Regulated	

Essential Utilities Combines Growing Water Business With Stable Gas Utility

Travis Miller
Strategist
Morningstar

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Research as of 11 Jun 2021
Estimates as of 11 Jun 2021
Pricing data through 11 Jun 2021 00:00
Rating updated as of 11 Jun 2021 00:00

[1]The ESG Risk Rating Assessment is a representation of Sustainalytics' ESG Risk Rating.
Rating as of 02 Jun 2021 00:00

Currency amounts expressed with "$" are in U.S. dollars (USD) unless otherwise denoted.

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Business Strategy and Outlook 11 Jun 2021

For more than 50 years, Essential Utilities--formerly Aqua America--was one of the few pure-play water utilities in the United States. But its $4.3 billion acquisition of Peoples Gas in March 2020 made the company nearly 50% larger and diversified its earnings mix.

The acquisition hasn't changed Essential's core investment proposition. Essential's gas and water utility earnings remain mostly rate regulated, and we expect management to run it like most other regulated U.S. utilities, prioritizing infrastructure investment growth and a robust dividend. Our outlook for 8% earnings growth during the next five years is a little higher than our growth outlook for most other U.S. utilities.

Although core retail water use has been falling steadily as a result of efficiency savings for several decades, Essential has been able to grow earnings and the dividend for many years. Like many utilities, Essential is replacing and upgrading infrastructure that is decades old across its system, resulting in organic rate base growth. We also expect Essential to grow by acquiring small, typically municipal-owned water systems. In the U.S., 85% of the population is served by a municipal water utility, offering a long runway of acquisition growth opportunities.

Similarly, we expect little natural gas usage growth at Peoples Gas, which had been owned by a private equity group. But the gas business still should produce steady earnings growth as Essential replaces and upgrades the system infrastructure.

Fair market value laws in several states support Essential's water business acquisition strategy. These laws require Essential to pay municipalities at least the assessed value of the system it acquires and allow Essential to add these assets to rate base at the assessed value rather than historical cost. The municipalities benefit by ensuring they get fair prices, and Essential shareholders benefit by ensuring the company doesn't overpay for growth. In many cases, these deals are immediately value-accretive. Recent FMV legislation in Kentucky and West Virginia opens acquisition opportunities near areas Essential already serves.

Vital Statistics

Market Cap (USD Mil)	12,002
52-Week High (USD)	48.93
52-Week Low (USD)	38.28
52-Week Total Return %	14.5
YTD Total Return %	4.4
Last Fiscal Year End	31 Dec 2020
5-Yr Forward Revenue CAGR %	11.2
5-Yr Forward EPS CAGR %	8.6
Price/Fair Value	1.25

Valuation Summary and Forecasts

Fiscal Year:	2019	2020	*2021(E)*	*2022(E)*
Price/Earnings	31.9	29.9	*28.9*	*27.3*
EV/EBITDA	23.0	24.7	*20.4*	*17.4*
EV/EBIT	33.6	39.3	*30.5*	*25.3*
Free Cash Flow Yield %	-2.0	-2.8	*-6.2*	*-2.2*
Dividend Yield %	—	—	*2.1*	*2.3*

Financial Summary and Forecasts (USD Mil)

Fiscal Year:	2019	2020	*2021(E)*	*2022(E)*
Revenue	890	1,463	*1,800*	*1,962*
Revenue YoY %	6.2	64.4	*23.0*	*9.0*
EBIT	340	435	*581*	*702*
EBIT YoY %	5.3	27.8	*33.7*	*20.8*
Net Income, Adjusted	317	402	*435*	*469*
Net Income YoY %	65.3	26.8	*8.1*	*7.9*
Diluted EPS	1.47	1.58	*1.69*	*1.79*
Diluted EPS YoY %	36.6	7.5	*7.0*	*6.1*
Free Cash Flow	-73	-143	*-525*	*-13*
Free Cash Flow YoY %	-345.3	97.3	*266.0*	*-97.5*

Historical/forecast data sources are Morningstar Estimates and may reflect adjustments.

Profile

Essential Utilities is a Pennsylvania-based holding company for U.S. water, wastewater, and natural gas distribution utilities. The company's water business serves 3 million people in eight states. Nearly three fourths of its water earnings come from Pennsylvania, primarily suburban Philadelphia. It also has a small market-based water business that provides water and water services to third parties, notably natural gas producers. Its $4.3 billion Peoples Gas acquisition that closed in March 2020 adds 750,000 gas distribution customers in Pennsylvania, West Virginia, and Kentucky.

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Essential Utilities Inc WTRG (NYSE) | ★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Capital Allocation	Industry Group	ESG Risk Rating Assessment[1]
48.86 USD	39.00 USD	Low	Narrow	Stable	Standard	Utilities - Regulated	

Morningstar Analysis

Initiating Coverage of Essential Utilities With Narrow Moat, $39 Fair Value 11 Jun 2021

We are initiating coverage of Essential Utilities with a $39 per share fair value estimate, narrow moat rating, and stable moat trend.

We consider the stock 23% overvalued based on the $48 stock price as of June 11. The stock trades at 28 times our 2021 earnings estimate, a 30% premium to the current median U.S. utilities P/E. Although we think Essential deserves a premium valuation relative to electric and gas utilities because of its higher returns on capital and growth potential in the water business, we think investors should wait for a pullback. Its closest peer, American Water Works, trades at a 30% premium to our fair value estimate and 38 P/E.

Essential, formerly Aqua America, was one of the few pure-play U.S. water distribution and wastewater utilities before acquiring Pennsylvania-based Peoples Gas in 2020. The company now gets two thirds of its earnings from its water business and one third of earnings from gas distribution.

The $4.3 billion Peoples Gas acquisition doesn't change Essential's core regulated utility business model, but we think it was a setback for investors. Essential paid more than double book value for the business, which has good near-term growth potential but long-term uncertainty as the U.S. moves away from fossil fuels. We think that capital would have been better spent growing its water businesses.

Our five-year, 8% annual earnings growth outlook tops most other U.S. utilities' outlooks. We think the water business has long, attractive runway of growth mostly through acquisitions of municipal utilities. Fair market value laws in some states allow Essential to mark up book value on its water acquisitions, eliminating the risk of overpaying.

We expect Essential to continue its impressive dividend growth track record. The company has paid a dividend every year since 1945 and has raised the dividend by 5% or more every year for the last 25 years. We consider management's 65% payout target more attractive than its peers.

Fair Value & Profit Drivers 11 Jun 2021

We are initiating coverage of Essential Utilities with a $39 per share fair value estimate.

We expect earnings to grow 8% annually during the next four years, which is above management's 5%-7% annual earnings growth target. Our growth rate is based on $1 billion of annual capital investment and $150 million of water utility acquisitions per year, on average. Our growth rate is higher than management's target range primarily due to our assumption that Essential will find more acquisition opportunities than it has in the past. We think the spread of fair market value legislation and increasing need for system investments will lead more municipal utilities to consider selling their systems.

Apart from acquisitions, the combination of surcharges and base rate increases support our earnings growth outlook. This includes favorable outcomes for likely base rate reviews in Pennsylvania, its largest service territory, in 2022-23.

In our discounted cash flow valuation, we use a 6.0% cost of capital based on a 7.5% cost of equity. This is lower than the 9% rate of return we expect investors will demand of a diversified equity portfolio, reflecting Essential's lesser sensitivity to the economic cycle and lower degree of operating leverage. We incorporate $5 per share of incremental value to better recognize the benefits accruing to shareholders from Essential having issued debt at coupon rates far below our long-term cost of debt assumption.

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Scenario Analysis

In our bear case, a 20% annual reduction in our 2021-24 capital expenditure forecast would lower our fair value estimate by $2 per share. A 50-basis-point cut in our long-term allowed regulatory return on equity assumption would reduce our fair value an additional $3 per share.

In our bull case, a 20% increase in our capital spending assumption would raise our fair value estimate by $2 per share, assuming full regulatory support at current allowed returns. A 50 basis-point increase in our long-term allowed regulatory return on equity assumption would add another $3 per share.

A 50-basis-point change in our cost of equity assumption would lead to a $2 per share change in our fair value estimate.

Economic Moat

We have greater than 50% confidence that Essential can generate economic profits on a consolidated basis for at least the next 10 years based on its efficient scale competitive advantage for its water, wastewater, and natural gas distribution businesses. Essential Utilities' consolidated returns are the foundation for our narrow moat rating.

We have strong confidence that Essential's returns on invested capital will remain at a healthy spread over its weighted average cost of capital for the foreseeable future, leading us to assign the company a narrow moat rating. Essential owns a difficult-to-replicate network of water, wastewater, and natural gas distribution infrastructure that provides essential energy sources to customers. In exchange for a service territory monopoly, state and federal regulators set rates for Essential's water distribution, wastewater, and natural gas distribution utilities at levels that aim to keep customer costs low while providing adequate returns for capital providers. This implicit contract between regulators and the utilities should, in the long run, allow Essential to earn a consistent spread over its cost of capital. Rate-setting mechanisms in the states that Essential serves are mostly constructive, leading to ROICs modestly above its WACC.

In the water distribution and wastewater businesses, Essential enjoys fair market value legislation in seven of the eight states where it has operations. This allows Essential to ensure its growth acquisitions are value-accretive by allowing it to adjust its regulated earning asset base to reflect the deal value based on a third-party valuation. This effectively eliminates the drag on returns created by goodwill and the risk of cost overruns for organic growth investment. Essential made 57 water system acquisitions between 2015 and 2019, and goodwill represented only 1% of Essential's net asset base. Thus, Essential's earned ROICs tend to track very closely its regulatory allowed ROICs, the foundation of an economic moat for regulated utilities.

As with all regulated utilities, we think regulatory caps on revenue and returns preclude Essential from establishing a wide economic moat.

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Essential derives about 1% of earnings from businesses that have few competitive advantages, particularly its water and wastewater services. Essential exited some of these businesses in 2017, and we expect these businesses' share of earnings will continue to shrink as management focuses on growth at the regulated distribution utilities.

Moat Trend

We think Essential's moat trend is stable. We do not expect the regulatory rate structures that support earnings and ROICs for Essential's water or gas utilities to change substantially, given state laws that demonstrate the political and regulatory support for maintaining Essential's financial health, stability, and investments. We believe regulators will rely on state legislation and constructive rate plans to uphold the implicit contract with capital providers that allows Essential to earn above its cost of capital on balance, in the long run. Fair market value legislation ensures Essential's growth-by-acquisition strategy is value-accretive for shareholders.

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Bulls Say/Bears Say

Bulls Say

- Constructive regulation allows Essential to raise rates through surcharges or rate cases to reduce regulatory lag and enhance cash flow available to pay the dividend and invest in growth projects.
- Fair market valuation state laws allow Essential to make municipal water utility acquisitions immediately value-accretive for shareholders.
- Essential has raised its dividend 30 times in the last 29 years, including 29 consecutive increases of more than 5%.

Bears Say

- Essential Utilities paid a peak market price for Peoples Gas, which will probably drag on consolidated returns for many years.
- Essential's capital investment plan likely means annual rate increases for most of its customers, which could cause regulatory pushback that would slow earnings growth.
- Rising interest rates could raise financing costs for Essential to fund its investments and make its dividend yield less attractive for income investors.

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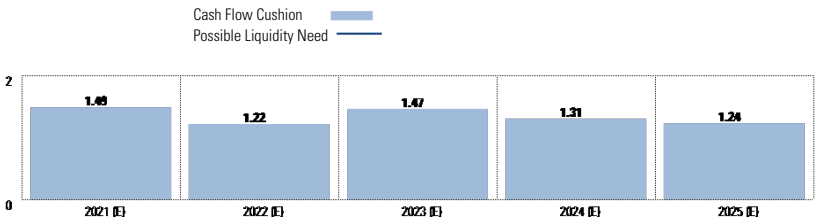
Five Year Adjusted Cash Flow Forecast (USD Mil)

	2021(E)	2022(E)	2023(E)	2024(E)	2025(E)
Cash and Equivalents (beginning of period)	5	277	339	351	425
Adjusted Available Cash Flow	893	1,528	638	1,171	716
Total Cash Available before Debt Service	898	1,805	977	1,523	1,141
Principal Payments	-406	-1,257	-425	-902	-653
Interest Payments	-197	-220	-242	-261	-266
Other Cash Obligations and Commitments	—	—	—	—	—
Total Cash Obligations and Commitments	-603	-1,477	-667	-1,163	-919

Cumulative Annual Cash Flow Cushion



Adjusted Cash Flow Summary

	USD Millions	% of Commitments
Beginning Cash Balance	5	0.1
Sum of 5-Year Adjusted Free Cash Flow	4,946	102.4
Sum of Cash and 5-Year Cash Generation	4,951	102.5
Revolver Availability	—	—
Asset Adjusted Borrowings (Repayment)	—	—
Sum of Cash, 5-Year Cash Generation, Revolver and Adjustments	4,951	102.5
Sum of 5-Year Cash Commitments	-4,828	—

Financial Strength

Essential maintains a capital structure in line with its regulatory allowed capital structure for ratemaking purposes and leverage metrics in line with high investment-grade credit ratings. We don't expect that to change.We expect Essential to issue new debt to fund growth investments and acquisitions in the coming years. We don't expect any material new equity needs once it completes its $300 million equity forward sale in August. With constructive regulation, we expect Essential will be able to use its cash flow to fund most of its equity investment needs during the next five years.Essential has paid an annual dividend since 1945 and increased it at least 5% for each of the last 25 years. We think Essential will be able to continue growing the dividend at this rate or higher while staying below management's 65% maximum payout ratio threshold, which is in line with Essential's peer utilities.

Risk & Uncertainty

The biggest uncertainty for Essential is rate regulation in the states it serves. Although Essential has a long history of constructive rate regulation, customers and regulators remain sensitive to rate increases that drive Essential's earnings growth. Deterioration of regulatory relations and policies could jeopardize Essential's growth potential.Customer growth and value-accretive water acquisitions have kept earnings growing even while water use has fallen steadily for several decades. Unlike many utilities that have lobbied to decouple rates from usage trends, Essential has maintained usage-based rates to avoid potential pushback from regulators. Customer growth, tax benefits, and constructive rate regulation have more than offset unfavorable usage trends.Essential's ability to make annual rate adjustments in states it serves offsets some of the regulatory ratemaking uncertainty. These surcharges effectively eliminate regulatory lag and improve cash flow to support capital investment and dividends.Essential's large capital investment plan will require good execution to

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keep projects on time and on budget. Delays or cost overruns could reduce shareholder returns.Essential also faces environmental, social, and governance risk, given its water and natural gas distribution businesses. At the water business, Essential must meet strict quality measures. It faces the risk of supplying contaminated drinking water for its customers if it has an operational failure, although we think this risk is low. Essential has invested in monitoring technology that allows it to supply water that is far cleaner than government requirements and reduces per- and polyfluoroalkyl substances, or PFAS.At the natural gas business, there is a long-term risk that policymakers will move retail customers away from gas heating, but we think that's unlikely in the near future, given the technical and economic hurdles in the colder climate where Essential operates.

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Management & Ownership

Management Activity

Name	Position	Shares Held	Report Date*	InsiderActivity
CHRISTOPHER H. FRANKLIN	Chief Executive Officer	175,702	27 Feb 2021	—
ROBERT A. RUBIN	Chief Accounting Officer	74,025	27 May 2021	—
MR. CHRISTOPHER P. LUNING	Sr. VP, General Counsel & Sec	49,911	16 Mar 2021	—
MR. DANIEL J. SCHULLER	Executive Vice President	40,634	16 Mar 2021	—
MS. ELLEN T. RUFF	Director,Director	32,198	31 Mar 2021	—
MR. RICHARD S. FOX	Chief Operating Officer	29,566	16 Mar 2021	—
MR. MATTHEW R. RHODES	EVP, Strategy & Corp Dev	23,069	16 Mar 2021	—
MR. DANIEL J. HILFERTY	Director,Director	20,678	31 Mar 2021	—

*Represents the date on which the owner's name, position, and common shares held were reported by the holder or issuer.

Fund Ownership

Top Owners	% of Shares Held	% of Fund Assets	Change (k)	Portfolio Date
Liberty One CAPSTONE	21.83	2.49	53,581	31 May 2021
Vanguard Total Stock Market Index Fund	2.80	0.03	-4	31 May 2021
Vanguard US Total Market Shares ETF	2.80	0.03	-4	31 May 2021
iShares Core S&P Mid-Cap ETF	2.48	0.45	1	31 May 2021
Vanguard Small Cap Index	2.45	0.21	17	31 May 2021
Concentrated Holders				
Ecofin Global Water Composite	0.01	8.39	4	31 May 2021
AAM UBS Lgr Tm Inv Ser Envir Trd 19-2	0.00	5.12	—	31 May 2021
Lyxor World Water (DR) ETF	0.48	4.73	—	31 May 2021
Pramerica Sicav Clean Water	0.11	4.59	25	31 May 2021
Invesco S&P Global Water ETF	0.36	4.54	4	31 May 2021

Institutional Transactions

Top 5 Buyers	% of Shares Held	% of Fund Assets	Shares Bought/ Sold (k)	Portfolio Date
Royal Bank of Canada	2.82	0.09	4,992	31 May 2021
NORGES BANK	1.77	0.05	4,357	31 May 2021
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BlackRock Inc	9.55	0.04	935	31 May 2021
Mariner Value Strategies, LLC	1.17	2.41	865	31 May 2021
Top 5 Sellers				
Pictet Asset Management SA (Junked)	—	—	-7,080	31 May 2021
Washington Crossing Advisors, LLC	—	—	-1,685	31 May 2021
Invesco Capital Management LLC	1.29	20.66	-1,427	31 May 2021
BMO Capital Markets Corp.	0.51	0.18	-1,120	31 May 2021
Bank of Montreal	0.56	0.04	-1,103	31 May 2021

Capital Allocation 11 Jun 2021

We give Essential Utilities a Standard capital allocation rating, balancing the company's long history of shareholder-friendly capital allocation in the water business with what we think was an ill-advised move into the gas business.

Essential has an impressive record of paying a dividend every year since 1945 and raising it 30 times in the last 29 years. While returning this cash to shareholders, Essential still found ways to invest in organic growth and acquisitions.

We think Essential overpaid for Peoples Gas. The equity dilution from the $4.3 billion cash price will be difficult to overcome even if everything goes perfectly. The $2.3 billion of goodwill on its balance sheet following the acquisition will remain a drag on returns. Goodwill was nearly equal to the book value of the assets.

Essential also gave up its premium market valuation with the Peoples acquisition. As one of the few pure-play water utilities, Essential was a staple in portfolios focused on environmental, social, and governance issues, especially water. Adding fossil-fuel exposure with the gas business could turn off some ESG investors. We think this would be an overreaction based on natural gas' low-carbon profile, but that's not likely to persuade strict environmentally focused investors to continue holding Essential.

CEO and chairman Chris Franklin has been in his role since 2015 and with the company for 28 years. CFO Dan Schuller joined the company in 2015.

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The $4.3 billion Peoples Gas acquisition doesn't change Essential's core regulated utility business model, but we think it was a setback for investors. Essential paid more than double book value for the business, which has good near-term growth potential but long-term uncertainty as the U.S. moves away from fossil fuels. We think that capital would have been better spent growing its water businesses.

Our five-year, 8% annual earnings growth outlook tops most other U.S. utilities' outlooks. We think the water business has long, attractive runway of growth mostly through acquisitions of municipal utilities. Fair market value laws in some states allow Essential to mark up book value on its water acquisitions, eliminating the risk of overpaying.

We expect Essential to continue its impressive dividend growth track record. The company has paid a dividend every year since 1945 and has raised the dividend by 5% or more every year for the last 25 years. We consider management's 65% payout target more attractive than its peers.

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Essential Utilities Inc WTRG (NYSE) | ★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Capital Allocation	Industry Group	ESG Risk Rating Assessment[1]
48.86 USD	39.00 USD	Low	Narrow	Stable	Standard	Utilities - Regulated	

Morningstar Analyst Forecasts

Financial Summary and Forecasts

Fiscal Year Ends in December

Growth (% YoY)	3-Year Hist. CAGR	2018	2019	2020	Forecast 2021	Forecast 2022	5-Year Proj. CAGR
Revenue	*21.8*	3.5	6.2	64.4	*23.0*	*9.0*	*11.2*
EBIT	*9.2*	-3.2	5.3	27.8	*33.7*	*20.8*	*20.4*
EBITDA	*13.7*	-0.2	5.7	39.3	*25.9*	*17.4*	*16.9*
Net Income	*18.8*	-19.9	65.3	26.8	*8.1*	*7.9*	*9.5*
Diluted EPS	*5.5*	-20.0	36.6	7.5	*7.0*	*6.1*	*8.6*
Earnings Before Interest, after Tax	*13.2*	20.1	-20.8	52.6	*48.4*	*-1.0*	*14.1*
Free Cash Flow	—	-232.5	-345.3	97.3	*266.0*	*-97.5*	—

Profitability	3-Year Hist. Avg	2018	2019	2020	Forecast 2021	Forecast 2022	5-Year Proj. Avg
Operating Margin %	*35.5*	38.6	38.2	29.7	*32.3*	*35.8*	*38.9*
EBITDA Margin %	*53.1*	56.1	55.8	47.3	*48.4*	*52.1*	*55.3*
Net Margin %	*28.7*	22.9	35.7	27.5	*24.2*	*23.9*	*24.3*
Free Cash Flow Margin %	*-4.8*	3.5	-8.2	-9.8	*-29.2*	*-0.7*	*-0.8*
ROIC %	*6.3*	9.8	5.0	4.2	*5.1*	*4.9*	*5.4*
Adjusted ROIC %	*6.6*	9.9	5.1	4.8	*6.3*	*5.9*	*6.4*
Return on Assets %	*3.6*	5.5	2.8	2.5	*3.0*	*3.0*	*3.2*
Return on Equity %	*11.1*	19.1	7.6	6.7	*8.8*	*8.8*	*9.3*

Leverage	3-Year Hist. Avg	2018	2019	2020	Forecast 2021	Forecast 2022	5-Year Proj. Avg
Debt/Capital	*0.52*	0.56	0.44	0.55	*0.56*	*0.56*	*0.56*
Total Debt/EBITDA	*6.61*	5.45	6.19	8.20	*7.54*	*6.92*	*6.27*
EBITDA/Interest Expense	*4.13*	4.74	3.96	3.67	*4.43*	*4.65*	*5.02*

Valuation Summary and Forecasts

	2019	2020	2021(E)	2022(E)
Price/Fair Value	—	—	—	—
Price/Earnings	31.9	29.9	*28.9*	*27.3*
EV/EBITDA	23.0	24.7	*20.4*	*17.4*
EV/EBIT	33.6	39.3	*30.5*	*25.3*
Free Cash Flow Yield %	-2.0	-2.8	*-6.2*	*-2.2*
Dividend Yield %	—	—	*2.1*	*2.3*

Key Valuation Drivers

Cost of Equity %	7.5
Pre-Tax Cost of Debt %	5.3
Weighted Average Cost of Capital %	6.0
Long-Run Tax Rate %	27.0
Stage II EBI Growth Rate %	5.0
Stage II Investment Rate %	55.6
Perpetuity Year	15

Additional estimates and scenarios available for download at http://select.morningstar.com.

Discounted Cash Flow Valuation

	USD Mil	Firm Value (%)	Per Share Value
Present Value Stage I	-26	-0.2	-0.10
Present Value Stage II	2,970	21.1	11.38
Present Value Stage III	11,125	79.1	42.62
Total Firm Value	**14,069**	**100.0**	**53.90**
Cash and Equivalents	5	—	0.02
Debt	-5,670	—	-21.72
Preferred Stock	—	—	—
Other Adjustments	1,548	—	5.93
Equity Value	**9,952**	**—**	**38.12**
Projected Diluted Shares	261		
Fair Value per Share (USD)	**39.00**		

The data in the table above represent base-case forecasts in the company's reporting currency as of the beginning of the current year. Our fair value estimate may differ from the equity value per share shown above due to our time value of money adjustment and in cases where probability-weighted scenario analysis is performed.

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Morningstar Analyst Forecasts

Income Statement (USD Mil)

Fiscal Year Ends in December	2018	2019	2020	*Forecast* 2021	*Forecast* 2022
Revenue	**838**	**890**	**1,463**	***1,800***	***1,962***
Cost of Goods Sold	—	—	166	*300*	*303*
Gross Profit	**838**	**890**	**1,297**	***1,500***	***1,659***
Selling, General & Administrative Expenses	308	333	529	*550*	*555*
Other Operating Expense (Income)	60	60	77	*79*	*81*
Other Operating Expense (Income)	—	—	—	—	—
Depreciation & Amortization (if reported separately)	147	156	257	*290*	*320*
Operating Income (ex charges)	**323**	**340**	**435**	***581***	***702***
Restructuring & Other Cash Charges	—	—	—	—	—
Impairment Charges (if reported separately)	—	—	—	—	—
Other Non-Cash (Income)/Charges	—	—	—	—	—
Operating Income (incl charges)	**323**	**340**	**435**	***581***	***702***
Interest Expense	99	125	188	*197*	*220*
Interest Income	-46	-3	19	*14*	*10*
Pre-Tax Income	**178**	**212**	**265**	***398***	***493***
Income Tax Expense	-14	-13	-20	*-36*	*23*
Other After-Tax Cash Gains (Losses)	—	—	—	—	—
Other After-Tax Non-Cash Gains (Losses)	—	—	—	—	—
(Minority Interest)	—	—	—	—	—
(Preferred Dividends)	—	—	—	—	—
Net Income	**192**	**225**	**285**	***435***	***469***
Weighted Average Diluted Shares Outstanding	178	216	255	*257*	*262*
Diluted Earnings Per Share	**1.08**	**1.04**	**1.12**	***1.69***	***1.79***
Adjusted Net Income	192	317	402	*435*	*469*
Diluted Earnings Per Share (Adjusted)	**1.08**	**1.47**	**1.58**	***1.69***	***1.79***
Dividends Per Common Share	—	—	—	*1.04*	*1.11*
EBITDA	**470**	**497**	**692**	***871***	***1,022***
Adjusted EBITDA	**470**	**497**	**692**	***871***	***1,022***

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Morningstar Analyst Forecasts

Balance Sheet (USD Mil)

Fiscal Year Ends in December	2018	2019	2020	Forecast 2021	Forecast 2022
Cash and Equivalents	4	1,869	5	*277*	*339*
Investments	—	—	—	—	—
Accounts Receivable	66	67	155	*138*	*145*
Inventory	16	18	58	*38*	*38*
Deferred Tax Assets (Current)	—	—	—	—	—
Other Short Term Assets	62	61	162	*160*	*160*
Current Assets	**147**	**2,015**	**380**	***613***	***682***
Net Property Plant, and Equipment	5,930	6,346	9,513	*10,673*	*11,448*
Goodwill	53	64	2,325	*2,325*	*2,325*
Other Intangibles	—	—	—	—	—
Deferred Tax Assets (Long-Term)	—	—	—	—	—
Other Long-Term Operating Assets	788	876	1,363	*1,350*	*1,300*
Long-Term Non-Operating Assets	46	62	125	*125*	*125*
Total Assets	**6,964**	**9,362**	**13,705**	***15,086***	***15,880***
Accounts Payable	77	75	177	*25*	*26*
Short-Term Debt	160	131	163	*163*	*163*
Deferred Tax Liabilities (Current)	—	—	—	—	—
Other Short-Term Liabilities	162	118	264	*270*	*270*
Current Liabilities	**399**	**323**	**604**	***458***	***458***
Long-Term Debt	2,398	2,943	5,508	*6,408*	*6,908*
Deferred Tax Liabilities (Long-Term)	845	936	1,258	*1,350*	*1,400*
Other Long-Term Operating Liabilities	1,122	1,069	1,347	*1,350*	*1,350*
Long-Term Non-Operating Liabilities	191	210	305	*305*	*305*
Total Liabilities	**4,955**	**5,481**	**9,021**	***9,870***	***10,421***
Preferred Stock	—	—	—	—	—
Common Stock	91	112	124	*124*	*124*
Additional Paid-in Capital	820	2,637	3,379	*3,729*	*3,779*
Retained Earnings (Deficit)	1,174	1,210	1,262	*1,444*	*1,637*
(Treasury Stock)	-76	-78	-81	*-81*	*-81*
Other Equity	—	—	—	—	—
Shareholder's Equity	**2,009**	**3,881**	**4,684**	***5,216***	***5,459***
Minority Interest	—	—	—	—	—
Total Equity	**2,009**	**3,881**	**4,684**	***5,216***	***5,459***

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Morningstar Analyst Forecasts

Cash Flow (USD Mil)

Fiscal Year Ends in December	2018	2019	2020	*Forecast* 2021	*Forecast* 2022
Net Income	192	225	285	*435*	*469*
Depreciation	147	156	257	*290*	*320*
Amortization	—	—	—	—	—
Stock-Based Compensation	—	—	—	—	—
Impairment of Goodwill	—	—	—	—	—
Impairment of Other Intangibles	—	—	—	—	—
Deferred Taxes	-15	-10	-18	*92*	*50*
Other Non-Cash Adjustments	72	-30	40	—	—
(Increase) Decrease in Accounts Receivable	-18	-4	-35	*17*	*-7*
(Increase) Decrease in Inventory	—	—	—	*21*	*0*
Change in Other Short-Term Assets	—	—	—	*2*	—
Increase (Decrease) in Accounts Payable	1	5	-2	*-152*	*0*
Change in Other Short-Term Liabilities	-10	-3	-19	*6*	—
Cash From Operations	**369**	**339**	**508**	***710***	***832***
(Capital Expenditures)	-496	-550	-836	*-1,451*	*-1,095*
Net (Acquisitions), Asset Sales, and Disposals	—	—	—	—	—
Net Sales (Purchases) of Investments	-145	-57	-3,500	—	—
Other Investing Cash Flows	1	2	2	*16*	*50*
Cash From Investing	**-640**	**-605**	**-4,334**	***-1,435***	***-1,045***
Common Stock Issuance (or Repurchase)	4	1,946	743	*350*	*50*
Common Stock (Dividends)	-151	-189	-233	*-253*	*-276*
Short-Term Debt Issuance (or Retirement)	12	10	-129	—	—
Long-Term Debt Issuance (or Retirement)	418	361	1,546	*900*	*500*
Other Financing Cash Flows	-12	3	34	—	—
Cash From Financing	**271**	**2,131**	**1,962**	***997***	***274***
Exchange Rates, Discontinued Ops, etc. (net)	—	—	—	—	—
Net Change in Cash	**-1**	**1,865**	**-1,864**	***273***	***62***

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48.86 USD	39.00 USD	Low	Narrow	Stable	Standard	Utilities - Regulated	

Comparable Company Analysis

These companies are chosen by the analyst and the data are shown by nearest calendar year in descending market capitalization order.

Valuation Analysis

		Price/Earnings			EV/EBITDA			Price/Free Cash Flow			Price/Book			Price/Sales		
Company/Ticker	Price/Fair Value	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)
American Water Works Co Inc AWK	1.31	39.3	37.6	34.1	20.5	19.3	17.9	NM	462.3	NM	—	—	—	7.4	7.1	6.7
Eversource Energy ES USA	1.22	23.8	21.6	20.9	15.3	14.0	12.9	—	NM	NM	—	—	—	3.3	3.1	3.0
NiSource Inc NI USA	0.91	17.4	19.4	18.7	12.1	11.4	10.5	NM	NM	NM	—	—	—	1.9	2.0	1.9
Average		26.8	26.2	24.6	16.0	14.9	13.8	—	462.3	—	—	—	—	4.2	4.1	3.9
Essential Utilities Inc WTRG US	**1.25**	**29.9**	***28.9***	***27.3***	**24.7**	***20.4***	***17.4***	**NM**	***NM***	***NM***	**—**	**—**	**—**	**7.9**	***6.7***	***6.1***

Returns Analysis

		ROIC %			Adjusted ROIC %			Return on Equity %			Return on Assets %			Dividend Yield %		
Company/Ticker	Last Historical Year Total Assets (Mil)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)
American Water Works Co Inc AWK	24,766 USD	6.0	6.5	6.8	6.5	7.0	7.3	11.3	11.7	12.1	3.0	3.1	3.3	1.4	1.5	1.6
Eversource Energy ES USA	46,100 USD	4.8	4.9	4.9	5.5	5.5	5.4	9.0	9.2	9.1	2.8	2.8	2.8	2.6	2.9	3.1
NiSource Inc NI USA	22,041 USD	3.9	5.8	6.3	4.2	6.3	6.9	-1.5	10.0	9.4	-0.3	2.4	2.5	3.7	3.4	3.5
Average		4.9	5.7	6.0	5.4	6.3	6.5	6.3	10.3	10.2	1.8	2.8	2.9	2.6	2.6	2.7
Essential Utilities Inc WTRG US	**13,705** USD	**4.2**	***5.1***	***4.9***	**4.8**	***6.3***	***5.9***	**6.7**	***8.8***	***8.8***	**2.5**	***3.0***	***3.0***	**—**	***2.1***	***2.3***

Growth Analysis

		Revenue Growth %			EBIT Growth %			EPS Growth %			Free Cash Flow Growth %			Dividend/Share Growth %		
Company/Ticker	Last Historical Year Revenue (Mil)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)
American Water Works Co Inc AWK	3,777 USD	4.6	8.7	6.3	3.7	15.4	7.9	8.1	9.2	10.2	24.3	-271.2	-96.0	10.0	9.7	10.0
Eversource Energy ES USA	8,904 USD	4.4	3.1	4.7	25.0	15.8	5.8	5.5	5.2	3.5	—	—	NM	6.1	6.2	5.8
NiSource Inc NI USA	4,682 USD	-10.1	11.2	5.5	-26.3	16.8	8.3	0.4	1.3	3.5	-728.1	-67.2	-435.9	5.0	4.8	4.5
Average		-0.4	7.7	5.5	0.8	16.0	7.3	4.7	5.2	5.7	-351.9	-169.2	-266.0	7.0	6.9	6.8
Essential Utilities Inc WTRG US	**1,463** USD	**64.4**	***23.0***	***9.0***	**27.8**	***33.7***	***20.8***	**7.5**	***7.0***	***6.1***	**97.3**	***266.0***	***-97.5***	**7.0**	***7.2***	***6.7***

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Comparable Company Analysis

These companies are chosen by the analyst and the data are shown by nearest calendar year in descending market capitalization order.

Profitability Analysis

Company/Ticker	Last Historical Year Net Income (Mil)	Gross Margin %			EBITDA Margin %			Operating Margin %			Net Margin %			Free Cash Flow Margin %		
		2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)
American Water Works Co Inc AWK	709 USD	100.0	100.0	100.0	49.0	50.3	50.9	33.0	35.1	35.6	18.8	18.9	19.7	-10.5	1.5	0.5
Eversource Energy ES USA	1,237 USD	66.5	66.5	67.0	33.4	36.5	37.8	22.3	25.1	25.3	13.9	14.4	14.3	—	-6.3	-10.0
NiSource Inc NI USA	508 USD	76.3	70.0	70.0	36.0	35.0	36.1	20.5	21.6	22.1	10.8	10.7	11.2	-14.0	-10.9	-14.4
Average		80.9	78.8	79.0	39.5	40.6	41.6	25.3	27.3	27.7	14.5	14.7	15.1	-12.3	-5.2	-8.0
Essential Utilities Inc WTRG US	**402** USD	**88.7**	***83.3***	***84.6***	**47.3**	***48.4***	***52.1***	**29.7**	***32.3***	***35.8***	**27.5**	***24.2***	***23.9***	**-22.4**	***-41.1***	***-13.4***

Leverage Analysis

Company/Ticker	Last Historical Year Total Debt (Mil)	Debt/Equity %			Debt/Total Cap %			EBITDA/Interest Exp.			Total Debt/EBITDA			Assets/Equity		
		2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)
American Water Works Co Inc AWK	10,940 USD	169.4	154.3	147.8	62.9	60.7	59.6	4.7	4.8	5.2	5.9	5.1	5.0	3.8	3.7	3.6
Eversource Energy ES USA	17,428 USD	122.6	125.8	127.6	55.1	55.7	56.1	5.5	5.3	5.2	5.9	5.6	5.5	3.2	3.2	3.2
NiSource Inc NI USA	9,746 USD	169.4	128.3	133.1	62.9	56.2	57.1	4.6	4.9	5.1	5.8	5.1	5.2	3.8	3.3	3.4
Average		153.8	136.1	136.2	60.3	57.5	57.6	4.9	5.0	5.2	5.9	5.3	5.2	3.6	3.4	3.4
Essential Utilities Inc WTRG US	**5,670** USD	**121.1**	***126.0***	***129.5***	**54.8**	***55.8***	***56.4***	**3.7**	***4.4***	***4.7***	**8.2**	***7.5***	***6.9***	**2.9**	***2.9***	***2.9***

Liquidity Analysis

Company/Ticker	Market Cap (Mil)	Cash per Share			Current Ratio			Quick Ratio			Cash/Short-Term Debt			Payout Ratio %		
		2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)	2020	2021(E)	2022(E)
American Water Works Co Inc AWK	29,100 USD	3.01	0.20	0.19	0.66	0.58	0.59	0.65	0.58	0.59	0.34	0.04	0.03	55.0	55.3	55.2
Eversource Energy ES USA	28,442 USD	0.31	0.34	0.38	0.64	0.56	0.54	0.58	0.50	0.49	0.05	0.05	0.06	64.0	63.0	64.4
NiSource Inc NI USA	10,202 USD	0.33	0.82	0.75	0.73	0.88	0.87	0.55	0.68	0.67	0.24	0.68	0.67	-444.0	65.8	66.4
Average		1.22	0.45	0.44	0.68	0.67	0.67	0.59	0.59	0.58	0.21	0.26	0.25	-108.3	61.4	62.0
Essential Utilities Inc WTRG US	**12,002** USD	**0.02**	***1.08***	***1.30***	**0.63**	***1.34***	***1.49***	**0.53**	***1.26***	***1.41***	**0.03**	***1.71***	***2.09***	**—**	***61.5***	***61.9***

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Research Methodology for Valuing Companies

Qualitative Equity Research Overview

At the heart of our valuation system is a detailed projection of a company's future cash flows, resulting from our analysts' research. Analysts create custom industry and company assumptions to feed income statement, balance sheet, and capital investment assumptions into our globally standardized, proprietary discounted cash flow, or DCF, modeling templates. We use scenario analysis, in-depth competitive advantage analysis, and a variety of other analytical tools to augment this process. We believe this bottom-up, long-term, fundamentally based approach allows our analysts to focus on long-term business drivers, which have the greatest valuation impact, rather than short-term market noise.

Morningstar's equity research group ("we," "our") believes that a company's intrinsic worth results from the future cash flows it can generate. The Morningstar Rating for stocks identifies stocks trading at an uncertainty-adjusted discount or premium to their intrinsic worth—or fair value estimate, in Morningstar terminology. Five-star stocks sell for the biggest risk-adjusted discount to their fair values whereas 1-star stocks trade at premiums to their intrinsic worth.

Four key components drive the Morningstar rating: (1) our assessment of the firm's economic moat, (2) our estimate of the stock's fair value, (3) our uncertainty around that fair value estimate and (4) the current market price. This process ultimately culminates in our single-point star rating.

1. Economic Moat

The concept of an economic moat plays a vital role not only in our qualitative assessment of a firm's long-term investment potential, but also in the actual calculation of our fair value estimates. An economic moat is a structural feature that allows a firm to sustain excess profits over a long period of time. We define economic profits as returns on invested capital (or ROIC) over and above our estimate of a firm's cost of capital, or weighted average cost of capital (or WACC). Without a moat, profits are more susceptible to competition. We have identified five sources of economic moats: intangible assets, switching costs, network effect, cost advantage, and efficient scale.

Companies with a narrow moat are those we believe are more likely than not to achieve normalized excess returns for at least the next 10 years. Wide-moat companies are those in which we have very high confidence that excess returns will remain for 10 years, with excess returns more likely than not to remain for at least 20 years. The longer a firm generates economic profits, the higher its intrinsic value. We believe low-quality, no-moat companies will see their normalized returns gravitate toward the firm's cost of capital more quickly than companies with moats.

When considering a company's moat, we also assess whether there is a substantial threat of value destruction, stemming from risks related to ESG, industry disruption, financial health, or other idiosyncratic issues. In this context, a risk is considered potentially value destructive if its occurrence would eliminate a firm's economic profit on a cumulative or midcycle basis. If we deem the probability of occurrence sufficiently high, we would not characterize the company as possessing an economic moat.

To assess the sustainability of excess profits, analysts perform ongoing assessments of the moat trend. A firm's moat trend is positive in cases where we think its sources of competitive advantage are growing stronger; stable where we don't anticipate changes to competitive advantages over the next several years; or negative when we see signs of deterioration.

Morningstar Research Methodology for Valuing Companies

2. Estimated Fair Value

Combining our analysts' financial forecasts with the firm's economic moat helps us assess how long returns on invested capital are likely to exceed the firm's cost of capital. Returns of firms with a wide economic moat rating are assumed to fade to the perpetuity period over a longer period of time than the returns of narrow-moat firms, and both will fade slower than no-moat firms, increasing our estimate of their intrinsic value.
Our model is divided into three distinct stages:

Stage I: Explicit Forecast

In this stage, which can last five to 10 years, analysts make full financial statement forecasts, including items such as revenue, profit margins, tax rates, changes in working-capital accounts, and capital spending. Based on these projections, we calculate earnings before interest, after taxes, or EBI, and the net new investment, or NNI, to derive our annual free cash flow forecast.

Stage II: Fade

The second stage of our model is the period it will take the company's return on new invested capital—the return on capital of the next dollar invested ("RONIC")—to decline (or rise) to its cost of capital. During the Stage II period, we use a formula to approximate cash flows in lieu of explicitly modeling the income statement, balance sheet, and cash flow statement as we do in Stage I. The length of the second stage depends on the strength of the company's economic moat. We forecast this period to last anywhere from one year (for companies with no economic moat) to 10–15 years or more (for wide-moat companies). During this period, cash flows are forecast using four assumptions: an average growth rate for EBI over the period, a normalized investment rate, average return on new invested capital, or RONIC, and the number of years until perpetuity, when excess returns cease. The investment rate and return on new invested capital decline until the perpetuity stage is reached. In the case of firms that do not earn their cost of capital, we assume marginal ROICs rise to the firm's cost of capital (usually attributable to less reinvestment), and we may truncate the second stage.

Stage III: Perpetuity

Once a company's marginal ROIC hits its cost of capital, we calculate a continuing value, using a standard perpetuity formula. At perpetuity, we assume that any growth or decline or investment in the business neither creates nor destroys value and that any new investment provides a return in line with estimated WACC.

Because a dollar earned today is worth more than a dollar earned tomorrow, we discount our projections of cash flows in stages I, II, and III to arrive at a total present value of expected future cash flows. Because we are modeling free cash flow to the firm—representing cash available to provide a return to all capital providers—we discount future cash flows using the WACC, which is a weighted average of the costs of equity, debt, and preferred stock (and any other funding sources), using expected future proportionate long-term market-value weights.

3. Uncertainty Around That Fair Value Estimate

Morningstar's Uncertainty Rating captures a range of likely potential intrinsic values for a company and uses it to

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Research Methodology for Valuing Companies

assign the margin of safety required before investing, which in turn explicitly drives our stock star rating system. The Uncertainty Rating represents the analysts' ability to bound the estimated value of the shares in a company around the Fair Value Estimate, based on the characteristics of the business underlying the stock, including operating and financial leverage, sales sensitivity to the overall economy, product concentration, pricing power, exposure to material ESG risks, and other company-specific factors.

Analysts consider at least two scenarios in addition to their base case: a bull case and a bear case. Assumptions are chosen such that the analyst believes there is a 25% probability that the company will perform better than the bull case, and a 25% probability that the company will perform worse than the bear case. The distance between the bull and bear cases is an important indicator of the uncertainty underlying the fair value estimate. In cases where there is less than a 25% probability of an event, but where the event could result in a material decline in value, analysts may adjust the uncertainty rating to reflect the increased risk. Analysts may also make a fair value adjustment to reflect the impact of this event.

Our recommended margin of safety widens as our uncertainty of the estimated value of the equity increases. The more uncertain we are about the estimated value of the equity, the greater the discount we require relative to our estimate of the value of the firm before we would recommend the purchase of the shares. In addition, the uncertainty rating provides guidance in portfolio construction based on risk tolerance.

Our uncertainty ratings for our qualitative analysis are low, medium, high, very high, and extreme.

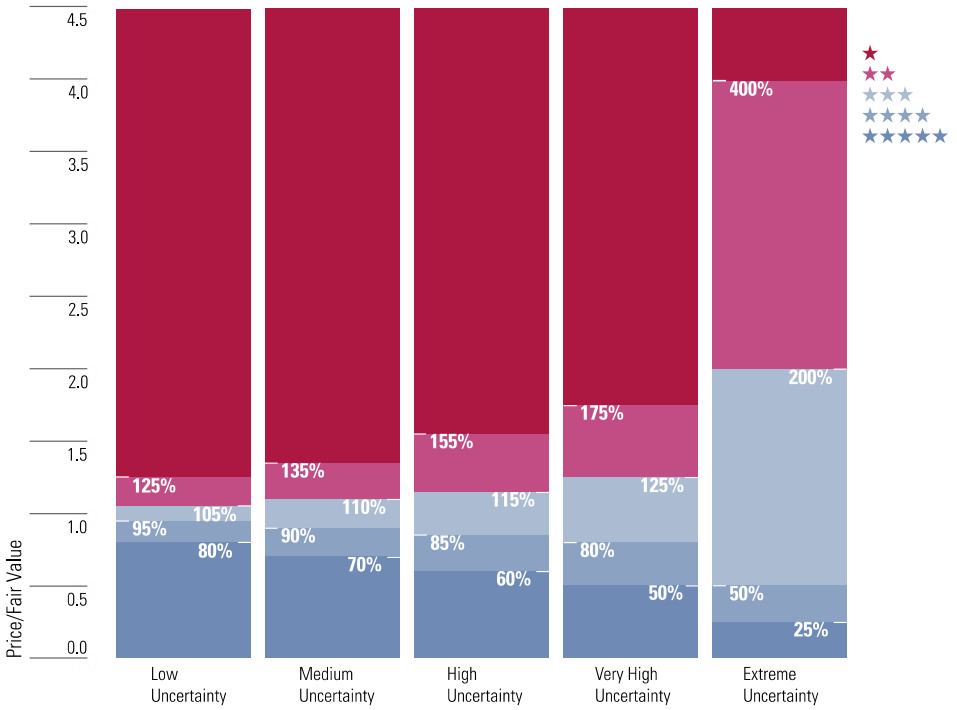
- Low–margin of safety for 5-star rating is a 20% discount and for 1-star rating is 25% premium.
- Medium–margin of safety for 5-star rating is a 30% discount and for 1-star rating is 35% premium.
- High–margin of safety for 5-star rating is a 40% discount and for 1-star rating is 55% premium.
- Very High–margin of safety for 5-star rating is a 50% discount and for 1-star rating is 75% premium.
- Extreme–margin of safety for 5-star rating is a 75% discount and for 1-star rating is 300% premium.

4. Market Price

The market prices used in this analysis and noted in the report come from exchange on which the stock is listed, which we believe is a reliable source.

For more details about our methodology, please go to https://shareholders.morningstar.com.

Morningstar Equity Research Star Rating Methodology



Morningstar Star Rating for Stocks

Once we determine the fair value estimate of a stock, we compare it with the stock's current market price on a daily basis, and the star rating is automatically re-calculated at the market close on every day the market on which the stock is listed is open.

Please note, there is no predefined distribution of stars. That is, the percentage of stocks that earn 5 stars can fluctuate daily, so the star ratings, in the aggregate, can serve as a gauge of the broader market's valuation. When there are many 5-star stocks, the stock market as a whole is more undervalued, in our opinion, than when very few companies garner our highest rating.

We expect that if our base-case assumptions are true the market price will converge on our fair value estimate over time, generally within three years (although it is impossible to predict the exact time frame in which market prices may adjust).

Our star ratings are guideposts to a broad audience and individuals must consider their own specific investment goals, risk tolerance, tax situation, time horizon, income needs, and complete investment portfolio, among other factors.

The Morningstar Star Ratings for stocks are defined below:

★★★★★ We believe appreciation beyond a fair risk-adjusted return is highly likely over a multiyear time frame. The current market price represents an excessively pessimistic outlook, limiting downside risk and maximizing upside potential.

★★★★ We believe appreciation beyond a fair risk-adjusted return is likely.

★★★ Indicates our belief that investors are likely to receive a fair risk-adjusted return (approximately cost of equity).

★★ We believe investors are likely to receive a less than fair risk-adjusted return.

★ Indicates a high probability of undesirable risk-adjusted returns from the current market price over a multiyear time frame, based on our analysis. The market is pricing in an excessively optimistic outlook, limiting upside potential and leaving the investor exposed to Capital loss.

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Research Methodology for Valuing Companies

Other Definitions

Last Price: Price of the stock as of the close of the market of the last trading day before date of the report.

Capital Allocation Rating: Our Capital Allocation (or Stewardship) Rating represents our assessment of the quality of management's capital allocation, with particular emphasis on the firm's balance sheet, investments, and shareholder distributions. Analysts consider companies' investment strategy and valuation, balance sheet management, and dividend and share buyback policies. Corporate governance factors are only considered if they are likely to materially impact shareholder value, though either the balance sheet, investment, or shareholder distributions. Analysts assign one of three ratings: "Exemplary", "Standard", or "Poor". Analysts judge Capital Allocation from an equity holder's perspective. Ratings are determined on a forward looking and absolute basis. The Standard rating is most common as most managers will exhibit neither exceptionally strong nor poor capital allocation.

Capital Allocation (or Stewardship) analysis published prior to Dec. 9, 2020, was determined using a different process. Beyond investment strategy, financial leverage, and dividend and share buyback policies, analysts also considered execution, compensation, related party transactions, and accounting practices in the rating.

Sustainalytics ESG Risk Rating Assessment: The ESG Risk Rating Assessment is provided by Sustainalytics; a Morningstar company.

Sustainalytics' ESG Risk Ratings measure the degree to which company's economic value at risk is driven by environmental, social and governance (ESG) factors.

Sustainalytics analyzes over 1,300 data points to assess a company's exposure to and management of ESG risks. In other words, ESG Risk Ratings measures a company's unmanaged ESG Risks represented as a quantitative score. Unmanaged Risk is measured on an open-ended scale starting at zero (no risk) with lower scores representing less unmanaged risk and, for 95% of cases, the unmanaged ESG Risk score is below 50.

Based on their quantitative scores, companies are grouped into one of five Risk Categories (negligible, low, medium, high, severe). These risk categories are absolute, meaning that a 'high risk' assessment reflects a comparable degree of unmanaged ESG risk across all subindustries covered.

The ESG Risk Rating Assessment is a visual representation of Sustainalytics ESG Risk Categories on a 1 to 5 scale. Companies with Negligible Risk = 5 Globes, Low Risk = 4, Medium Risk = 3 Globes, High Risk = 2 Globes, Severe Risk = 1 Globe. For more information, please visit sustainalytics.com/esg-ratings/.

Ratings should not be used as the sole basis in evaluating a company or security. Ratings involve unknown risks and uncertainties which may cause our expectations not to occur or to differ significantly from what was expected and should not be considered an offer or solicitation to buy or sell a security.

Quantitative Valuation: Using the below terms, intended to denote the relationship between the security's Last Price and Morningstar's quantitative fair value estimate for that security.

- Undervalued: Last Price is below Morningstar's quantitative fair value estimate.
- Fairly Valued: Last Price is in line with Morningstar's quantitative fair value estimate.
- Overvalued: Last Price is above Morningstar's quantitative fair value estimate.

Risk Warning

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Essential Utilities Inc WTRG (NYSE) | ★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Capital Allocation	Industry Group	ESG Risk Rating Assessment[1]
48.86 USD	39.00 USD	Low	Narrow	Stable	Standard	Utilities - Regulated	

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Essential Utilities Inc WTRG (NYSE) | ★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Capital Allocation	Industry Group	ESG Risk Rating Assessment[1]
48.86 USD	39.00 USD	Low	Narrow	Stable	Standard	Utilities - Regulated	

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Essential Utilities Inc WTRG (NYSE) | ★★

Last Price	Fair Value	Uncertainty	Economic Moat™	Moat Trend™	Capital Allocation	Industry Group	ESG Risk Rating Assessment[1]
48.86 USD	39.00 USD	Low	Narrow	Stable	Standard	Utilities - Regulated	

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AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR23. If applicable, supply a listing of all common equity infusions from the parent to the company over the past 5 years. In each case, identify date and dollar amount.

A.	2016	$20,000,000
	2017	$0
	2018	$0
	2019	$0
	2020	$20,000,000

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR24. If applicable, identify the company's common dividend payments to its parent for each of the last 5 years.

A.	2016	$30,000,000
	2017	$50,000,000
	2018	$80,000,000
	2019	$100,000,000
	2020	$50,000,000

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR25. Provide the latest year-by-year financial projections for the company for the next 5 years. Also, please indicate the date these projections were prepared; whether approved by management; and whether the projections have been submitted to bond rating agencies. The information will be treated in a confidential manner, if requested by the company in writing, as set forth in 52 Pa. Code § 5.423.

A. Please refer to Exhibit 1-A, Schedule A-1 for water and Exhibits 1-B through 1-G, Schedule A-1 for wastewater for the Company's most recent financial projections. Financial projections beyond what is projected in Exhibits 1-A through 1-G have not yet been approved by company management.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR26. Provide the company's 5-year construction budget.

A. Please see the attached.

AQUA PENNSYLVANIA, INC. **RR26 - Attachment**
2021 RATE CASE
FILING REQUIREMENTS

COMPANY'S BOARD APPROVED CAPITAL BUDGET @ 12/31/2020

	2021	2022	2023	2024	2025
301100-Organization-WA Total	(100,000)	(100,000)	(100,000)	(100,000)	(100,000)
303000-Land & Land Rights-WA Total	-	100,000	-	-	-
304000-Structures & Improvements-WA Total	20,240,300	21,432,800	9,453,002	7,210,098	10,451,100
305200-Collect & Impound Res-WA Total	2,011,900	4,015,000	3,245,600	8,216,200	11,086,800
306200-Lake, River & Other Intak-WA Total	225,000	25,000	125,000	1,025,000	25,000
307200-Wells & Springs-WA Total	3,639,000	3,029,000	1,481,000	3,255,000	3,090,000
309200-Supply Mains-WA Total	1,080,000	2,200,000	-	-	-
310000-Power Generation Equip-WA Total	1,159,000	2,003,000	3,682,000	2,886,000	2,747,000
311000-Pumping Equipment-WA Total	6,722,500	4,581,000	2,333,000	1,073,000	2,118,000
320300-Water Treatment Equip-WA Total	17,436,000	15,842,000	11,873,000	9,373,000	7,493,000
330400-Distrib Res & Standpipe-WA Total	7,479,500	6,076,000	4,169,000	4,916,000	4,140,000
331400-T & D Mains-WA Total	157,225,181	144,719,146	151,528,056	165,824,896	139,786,590
333400-Services-WA Total	26,140,052	26,736,140	26,108,400	27,267,800	25,654,480
334400-Meters-WA Total	10,783,300	6,934,699	11,330,202	10,364,806	11,946,520
335400-Fire Hydrants-WA Total	4,373,026	4,170,880	3,757,450	4,354,800	4,324,960
336400-Backflow Prevention-WA Total	2,000	2,000	2,000	2,000	2,000
339000-Other Plant & Misc Equip-WA Total	166,820	143,010	47,670	47,670	47,670
340500-Office Furn & Equip-WA Total	23,408,421	21,995,325	16,658,620	4,873,730	10,461,080
341500-Transport Equip-WA Total	3,994,000	4,052,000	4,081,500	4,667,100	5,009,300
342500-Stores Equip-WA Total	385,100	249,300	379,800	247,100	397,900
343500-Tools, Shop & Garage Eq-WA Total	1,047,100	1,355,400	945,400	953,800	884,800
344500-Laboratory Equip-WA Total	489,000	957,500	563,000	539,000	745,500
346500-Communication Equip-WA Total	4,826,800	5,608,800	3,188,400	3,329,100	2,915,800
347500-Misc Equip-WA Total	4,000	4,200	4,400	4,600	4,800
353000-Land & Land Rights-WW Total	-	-	-	14,000	-
354000-Structures & Improvements-WW Total	2,447,300	794,500	2,259,700	599,900	2,925,100
355000-Power Gen Equip-WW Total	315,000	1,015,000	15,000	65,000	365,000
360200-Collection Mains Force-WW Total	508,000	173,000	123,000	223,000	123,000
361200-Collection Mains Gravity-WW Total	6,797,900	17,288,200	18,676,100	12,016,800	9,167,500
363200-Services To Customers-WW Total	592,900	572,900	574,400	519,400	519,400
364200-Flow Measuring Devices-WW Total	25,900	25,900	25,900	25,900	25,900
371000-Pumping Equip-WW Total	729,200	680,700	1,571,700	1,145,200	587,700
380000-Treat & Disp Equip-WW Total	16,760,800	8,402,600	14,873,200	6,814,100	11,260,100
382400-Outfall Lines-WW Total	-	-	-	-	200,000
390700-Office Furn & Equip-WW Total	10,000	-	-	-	-
391700-Transportation Equip-WW Total	120,000	90,000	84,500	176,000	124,000
393700-Tools, Shop & Garage Eq-WW Total	245,000	140,000	200,000	100,000	300,000
394700-Laboratory Equip-WW Total	70,000	70,000	80,000	70,000	70,000
396700-Communication Equip-WW Total	640,000	615,000	660,000	500,000	500,000
Grand Total	322,000,000	306,000,000	294,000,000	282,600,000	269,400,000

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR27. Identify the company's and, if applicable, its parent's capital structure targets (percentages of capital types). Provide the complete basis for the capital structure targets.

A. The Company strives to maintain close to a 46/54 long term debt/equity capital structure over time. Please refer to the direct testimony of Paul R. Moul and the accompanying Exhibit 4-A for the target structure at March 31, 2023.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR28. For each month, of the most recent 24 months, supply the company's:

a. Short-term debt balance.

b. Short-term debt interest rate.

c. Balance of construction work in progress.

d. Balance of construction work in progress which is eligible for AFUDC accrual:

A. Please see the attached.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
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Seq.	Month	Short-Term Debt Balance	Short-Term Interest Rate	Balance in CWIP	CWIP Balance AFUDC Eligible
1	June-21	41,848,737	0.7500%	148,236,855	139,807,061
2	May-21	40,000,000	0.7500%	143,550,230	134,967,997
3	April-21	30,000,000	0.7700%	139,418,988	130,492,537
4	March-21	64,893,072	0.7630%	128,207,002	119,838,181
5	February-21	60,000,000	0.7670%	131,613,756	123,130,847
6	January-21	70,000,000	1.1330%	121,533,878	109,561,576
7	December-20	49,197,904	0.8030%	116,176,936	106,752,340
8	November-20	30,000,000	0.8000%	120,767,206	111,088,002
9	October-20	54,668,542	0.7320%	132,270,173	122,930,584
10	September-20	47,185,434	0.6780%	114,618,762	105,324,204
11	August-20	40,000,000	1.1240%	105,598,676	94,789,536
12	July-20	16,723,703	0.7940%	102,323,277	90,427,911
13	June-20	15,000,000	0.8500%	86,200,642	75,171,329
14	May-20	0	0.1230%	73,768,760	61,851,833
15	April-20	53,834,257	1.3130%	73,221,901	61,313,577
16	March-20	42,505,058	1.3500%	67,157,842	55,151,828
17	February-20	41,871,836	2.1830%	125,767,532	116,845,768
18	January-20	40,000,000	2.3100%	113,714,342	105,616,099
19	December-19	25,724,392	4.2380%	117,792,514	109,986,376
20	November-19	13,277,870	2.6190%	137,868,226	130,203,007
21	October-19	10,000,000	2.6400%	144,138,075	135,617,380
22	September-19	10,000,000	2.7100%	145,229,351	136,724,857
23	August-19	23,597,283	2.8430%	135,599,609	128,675,567
24	July-19	18,150,631	2.9600%	133,346,927	127,018,369

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR29. Fully identify all debt, other than instruments traded in public markets, owed to all shareholders, corporate officers, or members of the board of directors, its affiliates, parent company, or subsidiaries.

A. None.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR30. Provide a summary statement of all stock dividends, splits, or par value changes during the 2-year calendar period preceding the rate case filing.

A. There have been no splits or par value changes during the 2-year calendar period preceding the rate case filing.

There have been the following stock dividends during the 2-year calendar period preceding the rate case filing.

9/1/2019	$0.2343
12/1/2019	$0.2343
3/1/2020	$0.2343
6/1/2020	$0.2343
9/1/2020	$0.2507
12/1/2020	$0.2507
3/1/2021	$0.2507
6/1/2021	$0.2507

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR31. If a claim of the filing utility is based on utilization of the capital structure or capital costs of the parent company and consolidated system, the reasons for this claim must be fully stated and supported.

A. The Company's claims are not based on the capital structure of its parent company.

AQUA PENNSYLVANIA, INC.
2021 RATE CASE
FILING REQUIREMENTS

G. Rate of Return

RR32. To the extent not provided elsewhere, supply financial data of the company, and its parent, if applicable, for the last 5 years.

a. Times interest earned ratio—pre- and post tax basis.

b. Preferred stock dividend coverage ratio—post tax basis.

c. Times fixed charges earned ratio—pretax basis.

d. Dividend payout ratio.

e. AFUDC as a percent of earnings available for common equity.

f. Construction work in progress as a percent of net utility plant.

g. Effective income tax rate.

h. Internal cash generations as a percent of total capital requirements.

A. Please refer to the direct testimony of Paul R. Moul and the accompanying Exhibit 4-A for the Company's financial data, including the details requested in items (a) through (h).